as a “Bolshevik threat.”[18] In American eyes, Mexico had committed multiple sins. It had nationalized church property and closed Catholic schools, defaulted on foreign debt, insisted that oil companies trade in property titles for government concessions, and confiscated American-owned land without compensation. Newspapers were calling Mexico America’s foremost foreign-policy problem.

The Morrow appointment was an inspired choice. Coolidge was under pressure to do something dramatic, and he did it. Walter Lippmann hailed it as the “most extraordinary appointment made in recent years” and helped to shepherd it through the Senate Foreign Relations Committee.[19] As a specialist in Latin American loans and an opponent of dollar diplomacy, Morrow had moderated Wall Street’s often truculent attitude toward Latin American debtors. When Cuba threatened to default on foreign bonds during the 1921 sugar debacle that nearly collapsed Guaranty Trust, Morrow was credited with keeping out the marines. “Is there any one who thinks that if a man owes him money and cannot pay it, there is profit in going out and killing him?” he wrote.[20] Morrow favored diplomacy over armed intervention, an enlightened attitude for the time.

Betty Morrow expressed both elation and bitterness at the appointment. The Morrows had just decided to build a new home in Englewood, and she didn’t want their lives disrupted. *She* didn’t see Coolidge as a transcendental philosopher: “The blow has fallen! President Coolidge wrote to Dwight today asking him to be Ambassador to Mexico and Dwight is going to do it. It is a hard job, and not much honor, and it comes late. . . . Coolidge won’t run again, but Dwight goes and does a hard job for him when there is no chance of reward. How characteristic![21] Betty sarcastically told friends that Coolidge was like a father who had given away valuable gifts and thrown Dwight a little tin whistle at the end.

Morrow was sufficiently pessimistic about Mexico to say privately that the best he could do was get Mexico off the front page. Lamont advised him against taking the post, saying the turmoil of a pending presidential campaign made it an inauspicious time for action. Friends concurred and were aghast that Dwight would surrender a Morgan partnership for such a risky position. Even Lindbergh was dubious: “From what little I have seen at our border stops, I am afraid that the position will be a difficult one.”[22]

The Mexicans were also wary of Morrow, believing he would function as a collection agent for the New York banks. They chanted, “First Morrow, then the marines.” The fear was unjustified. The Lamont-led bankers’ committee for Mexico was less interested in military action than in peaceful negotiations to get Mexico to resume debt repayment. They wanted stability, not further turmoil, in Mexico. In the end, it would be the Mexicans who would be

pleasantly surprised by Dwight Morrow and the House of Morgan that would feel embittered and betrayed.

AS ambassador to Mexico, Dwight Morrow patented a new style for a *gringo* emissary in Latin America—warm and voluble, treating Mexicans as peers, not wayward children. Soon after his arrival, he told the local U.S. Chamber of Commerce that it should respect Mexican sovereignty. (With slight embarrassment, he had to write the White House and ask for a photograph of Coolidge to hang above his desk—another telltale sign of the distance between the two.) Morrow developed a close rapport with President Calles and would casually drop in on him, like an old friend. They would breakfast at Calles's ranch or tour Mexican dams and irrigation works together. Morrow's friendly, trusting manner contrasted with that of his predecessor, James R. Sheffield, who had treated nonwhites patronizingly, taken a pro-invasion stand toward Mexico, and studiously served the interests of American oil companies.

Morrow not only respected Mexican culture but liked the easygoing informality of the people. He and Betty spent weekends at Casa Mafiaña, a villa in the semitropical town of Cuernavaca. It overlooked two volcanoes and overflowed with Mexican pottery and Indian handicrafts. Morrow commissioned Diego Rivera, the left-wing Mexican muralist, to paint frescoes at the Cortes Palace, including one that depicted the revolutionist Zapata. To improve U.S.-Mexican relations, he even brought down Will Rogers to tour with him and Calles. While Rogers was there, Morrow threw a banquet complete with Mexican songs and dance. At one point, the ebullient Morrow said to Rogers with a smile, "Imagine going to war with a people like this!"[23]

Sometimes Morrow seemed more popular among Mexicans than in the American colony. The public debate about Mexico in the United States became more inflammatory in late 1927. William Randolph Hearst nursed a grudge against President Calles after the latter appropriated sections of his gigantic Babicora Ranch. That November, the Hearst newspapers ran sensational articles purportedly showing Mexican plots against the United States. Some observers thought Hearst was not only expressing pique against Calles but was deliberately fomenting trouble for Dwight Morrow; the isolationist Hearst had always disliked the Anglophile House of Morgan. On December 9, 1927, the twenty-six Hearst papers published documents that supposedly outlined a Mexican plot to bribe four U.S. senators with over $1 million. These documents were later exposed as forgeries, but in the meantime they damaged relations with Mexico.

BEFORE leaving for Mexico, Morrow had invited Charles Lindbergh to his East Sixty-sixth Street apartment. Acting on a suggestion from Walter Lippmann, Morrow proposed that the young aviator pilot *The Spirit of St. Louis* to Mexico as a goodwill gesture. Lindbergh liked the idea. He had flown to Paris on a spring day, and before donating his plane to a museum, he wanted to prove the practicality of night and winter flights. To strengthen the political message, Lindbergh suggested a flight linking Washington and Mexico City.

So on December 14, 1927, with rifle, machete, and tropical medicine on board, Lindbergh took off through stormy night skies. It was a few days after the Hearst "expose" and a perilous moment in U.S.-Mexican relations. When the sun rose the next morning, Lindbergh sailed through a cloudless Mexican morning but couldn't figure out where he was. He dipped low enough to read the names of a hotel and train stations and briefly thought all Mexican towns were named Caballeros, because he kept seeing that sign at the stations. Then he spotted a sign for Toluca, a town about fifty miles from Mexico City.

Sharing picnic sandwiches and lemonade, Morrow and President Calles awaited Lindbergh in sweltering heat at Valbuena Airport, where a special grandstand was set up for dignitaries. Morrow nervously paced up and down. When Lindbergh landed—six hours late—a crowd of Mexicans estimated at 150,000 rushed exuberantly across the field. As Lindbergh accompanied Morrow and Calles to their car, they were thronged by shouting, delirious spectators. They rode to the embassy in triumph, horns blaring, horses rearing, and crowds posted "on trees, on telegraph poles, tops of cars, roofs, even the towers of the Cathedral," as Betty Morrow recalled. "Flowers and confetti were flung every moment."[24]

Lindbergh spent Christmas at the embassy with the Morrows and took Calles on his first plane ride. He also took notice of Dwight's daughter, Anne, on vacation from her senior year at Smith College. She was a shy, pretty poetess, as slight of build as Charles was rangy and with Betty's heavy eyebrows. Lindbergh liked the fact that when he first sat next to her, she didn't ask any questions. Theirs was the strong bond of two shy people who had found each other.

Morrow hadn't especially liked the young men his daughters dated—Anne and Elisabeth having gone out with Corliss Lamont, among others. He approved of Charles Lindbergh as a "nice clean boy" who didn't drink, smoke, or see girls.[25] But when Anne announced that she and Charles wanted to get married, Morrow seemed flabbergasted. "He's going to marry Anne? What do we know about this young man?" he asked.[26] He insisted they be engaged first and get to know each other better. Despite his flustered reaction, Morrow was very fond of Charles and would beam with gee-whiz delight

when he narrated his aviation adventures.

On May 27, 1929, Anne and Charles were married at the Morrows' new Georgian mansion in Englewood, called Next Day Hill. It was an event of such fascination worldwide that the Morrows had to fool the press and bill it as a prewedding party. Even the guests were told only to drop by for lunch and a bridge game. Then Anne suddenly appeared in a white chiffon wedding gown, and a brisk ceremony took place. Only after Anne and Charles had changed clothes and escaped through the back door did Dwight and Betty broadcast the news to reporters. The young couple briefly stayed at the Leffingwell house in Oyster Bay during their secretive honeymoon, and the servants were threatened with dismissal if they mentioned the couple's presence to tradespeople in town.

It was a strong, intense match but one riddled with contradictions. Anne was the daughter of a former Morgan partner and had imbibed her father's idealism and internationalism. Charles's father, who had died in 1924, was the populist Minnesota congressman who had instigated the Pujo hearings, fulminated against the Money Trust and the Morgan cabal with the Federal Reserve Bank, and castigated the bankers who dragged America into the war. The congressman's son inherited his father's suspicion of eastern bankers and would never entirely slough it off. In the late 1930s, his isolationism would place him at odds with the House of Morgan and create a painful dilemma for Anne. But in the late 1920s, he socialized with the Morrows and Guggenheims and thrilled the Davisons by taking their beach-party guests at Peacock Point for seaplane rides.

THOSE who saw Ambassador Morrow as a proxy for the House of Morgan in Mexico were in for a rude shock. The ambassador already had a separate political agenda, Morrow having confided to Walter Lippmann that he coveted a seat in the U.S. Senate. Hence, he needed to distance himself from the bank. During the 1928 presidential campaign, he was already being toasted as a potential senatorial candidate at Republican dinners. It was now in Morrow's political interest to function as a sensitive, fair-minded arbiter in settling Mexican disputes.

Morrow had quick success with the long-running oil controversy. He developed an ingenious scheme of "perpetual concessions" for American oil companies. It gave them new concessions on pre-1917 wells, while Mexico saved face and retained theoretical ownership. This rational statesmanship delighted Walter Lippmann, who told Morrow afterward, "There is a disposition in some quarters to ascribe it to some kind of private magic which you have at your disposal."[27] For Lippmann, Morrow qualified as the most talented public man of his generation, far beyond the common run of

politicians.

Another major dispute involved the Catholic church. Calles had tried to nationalize church lands, and the violent Cristeros movement had arisen in protest. A state of war existed in parts of Mexico, with thousands of men marching under the church's banner. Morrow smuggled Walter Lippmann into the country on a secret diplomatic mission. They negotiated a compromise under which Calles agreed not to interfere with the church while Mexican priests agreed to call off their protest strike. Morrow and Lippmann sold the deal to the Vatican, and the settlement reopened the churches. One morning in Cuernavaca, Betty and Dwight were awakened by the ringing of church bells. "Betty, I have opened the churches," Dwight said, laughing. "Now perhaps you will wish me to close them again."[28]

The most frustrating area for Morrow was, ironically, the foreign debt. By 1928, Mexico had been in default for fourteen years, and its budgetary situation worsened with the lower oil revenues. In a desperate mood, bankers didn't see how Mexico could satisfy all its creditors. The country owed money to the foreign bondholders represented by Lamont as well as to western U.S. railroads and domestic lenders. Lamont thought the two hundred thousand bondholders he represented should have first claim. He argued that they had patiently waited many years for payment. Morrow, in contrast, favored a comprehensive settlement for all creditors, on the model of a bankruptcy settlement. He feared that if Mexico struck a series of separate deals, it would promise more money than it could deliver. To Lamont, the notion of one big settlement was an impractical dream that would only penalize his bondholders. And it would be so cumbersome that nobody would ever get paid.

A heated feud arose between Morrow and Lamont. Although he would never admit it, Lamont had secret reservations about Morrow. He would later eulogize him as "sparkling, brilliant, whimsical, lovable," yet he thought Morrow had an unearned reputation for sainthood. There was perhaps envy here, a feeling that Morrow threatened his own image as the leading liberal banker. Posing as Morrow's friend, Lamont gave Harold Nicolson a 125-page critique of a draft of Nicolson's biography of Morrow and reproached him for idealizing his subject. Morrow and Lamont were perhaps too much alike to be completely fooled by one another. Each was more worldly and ambitious than he cared to admit.

It's hard to know whether Lamont found Morrow's position on Mexican debt a political ploy to separate himself from 23 Wall or a quixotic plan that only an absentminded professor could espouse. In any event, by 1929 Lamont decided to break with the Morrow-inspired State Department plan for a comprehensive debt settlement. He circulated bitter memos at 23 Wall Street, sarcastically referring to Morrow as the ambassador. The ICBM, he warned,

"will be by no means content to stand by idly for a year while the ambassador is perfecting his Government claims." A few days later, Lamont informed his partners that he planned to cut a separate bargain with Mexico "despite Ambassador's attitude."[29] George Rublee, the legal adviser to the U.S. embassy in Mexico and a close friend of Morrow's, later said, "Mr. Lamont would rather take his chances and get what he could ahead of somebody else than to cooperate in a general settlement."[30]

For all his charm, Lamont could play rough when crossed. He tried to figure out an elegant way to get rid of Morrow while appearing to help him. In November 1929, he had Martin Egan hand a letter to President Hoover that recommended Morrow as secretary of war. Lamont stressed that Morrow knew nothing of the request—implying that Hoover should keep the suggestion confidential. He doubted his stratagem would work, however, owing to Hoover's insecurity in the face of Morrow's massive intellect. "Dwight was so brilliant that he would talk around [the president] in circles," Lamont said.[31] Hoover had already rebuffed an earlier request from Calvin Coolidge to appoint Morrow as his secretary of state. Hoover didn't rise to Lamont's bait. Close to Morrow—they spoke several times weekly—the president wasn't eager to advance a potential political competitor.

That month, two events made Lamont's exertions unnecessary. On November 12, Hoover appointed Morrow to represent the United States at the upcoming Naval Conference in London. Later in the month, New Jersey governor Larson asked Morrow if he would fill the brief time remaining in the unexpired term of Senator Walter E. Edge, who had just been appointed ambassador to France. A deal was struck whereby David Baird would occupy the Senate seat with the understanding that he would step aside if Morrow wanted to campaign for the Republican nomination in the spring. This provided Morrow with further incentives to oppose Lamont on the debt issue and eliminate his former Morgan partnership as a potential campaign issue.

In December, the simmering political dispute between Morrow and Lamont boiled over. By this point, Morrow, the liberal do-gooder, had moved into the position of self-appointed overlord of Mexico's finances. The man who had held back the marines now minutely reviewed Mexico's budget. When Lamont's assistant, Vernon Munroe, met with Morrow, he was shocked by the extent to which the ambassador wanted to dictate Mexican financial policy. According to Munroe, Morrow wanted to cut the Mexican budget by "eliminating the courthouse entirely, cutting 2.5 million off the education appropriation, one million pesos off the public health, 2.5 million pesos off statistics and some 4 million pesos off communications."[32] Under the guise of helping his Mexican brothers, Dwight seemed to succumb to delusions of grandeur.

During the May-June campaign for the Republican Senate nomination in New Jersey, Morrow was still serving as Mexican ambassador, and as such he followed the debt situation. Then a campaign blunder drastically reduced his influence in that post. While he was at the London Naval Conference, his military attache in Mexico, Colonel Alexander J. MacNab, made a speech in which he extravagantly praised Morrow's role in Mexican reform. He actually made Lamont's point—that Morrow was intruding more in Mexican domestic affairs than any Wall Street banker. "There is no department of government in Mexico which he has not advised and directed," MacNab said of Morrow. "He took the Secretary of Finance under his wing and taught him finance."[33] The Mexican press treated the speech as a scandal. It made Mexican officials look as if they were the ambassador's puppets, and Morrow never again had the same influence in Mexico. Nevertheless, he won the Republican nomination.

During the summer of 1930, Morrow kept flying down to Mexico to advise on the debt. The Morrow-Lamont dispute resulted in some blistering exchanges. Morrow kept urging Lamont to lecture the finance minister about the growing Mexican budget; Lamont did this, then regretted it. In a July 24 letter, his pent-up contempt for Morrow surfaced: "I have a feeling that you are a bit disgusted with our mental processes up here and are genuinely upset that we are unable to adopt in toto your point of view." He referred to a talk with the finance minister: "He retorted by telling me politely that it was really none of my business. . . . Now, my dear Dwight, you may have some means of compelling the Finance Minister to give you precise information as to his budget plans for several years ahead, but I must confess that in any such effort I, myself, am powerless." In the end, Lamont bluntly warned Morrow to stay away from his debt settlement with Mexico: "I hope you can see your way clear to letting the matter rest where it is rather than feeling called upon to defeat this plan."[34] In a cool reply, Morrow repeated that Mexico was bankrupt and should treat creditors equally. He warned Lamont that if he persisted in his course, he would ultimately have to deal with the State Department.[35]

The day after Lamont wrote Morrow—without awaiting a reply—he signed a separate accord at 23 Wall with a representative of Mexico's Chamber of Commerce. It nearly halved Mexico's debt, reducing it from $508 million to $267 million, in one stroke. True to his threats, Morrow advised Mexico to delay ratification, but his influence with President Pascual Ortiz Rubio, Calles's successor, was much diminished. As it turned out, the feud between the two Morgan men was for naught. Mexico kept postponing the date of debt repayment, and the whole farce would collapse by 1932. The outcome would have been laughable had it not consumed so much of Lamont's life and

impoverished small Mexican bondholders. By 1941, Mexican debt had shrunk to $49.6 million, or a tenth of the original amount.

Although Morrow's break with the House of Morgan was now complete, the association haunted him in the Senate race that fall. As one New Jersey paper described his opponent's strategy: "The Ambassador was to be pictured to New Jersey voters as the tool and puppet of Big Business interests, and his candidacy as a Wall Street conspiracy to capture the Presidency via the U.S. Senate route."[36]

Morrow was exhausted and dispirited. He suffered from insomnia and headaches and ran a lackluster campaign. Nicolson suggests he had a serious drinking problem. Coincidentally, Prohibition became a central topic in the campaign. Not ducking the issue, Morrow became the first federal official to favor outright repeal of the Eighteenth Amendment.

Again, he seemed driven by his ambition, and the Senate campaign produced more anxiety. Betty recorded in her diary that "Dwight is so tired; so discouraged; so *wild* that he has been trapped into this Senatorial campaign. He is exhausted, does not want it, would be glad to lose."[37] Fate, devising new ways to punish him, produced a landslide victory in November.

As senator, Morrow seemed worn from the immense burdens he had carried over the years. He immediately disappointed liberal admirers. Despite the Depression, he voted against food relief, the soldiers' bonus bill, and tougher utility regulation. This prompted one journalist to declare that in three months he had wiped away the liberal reputation of a lifetime.[38] Such remarks stung Morrow. He approached problems in his thorough, dogged way but got mired in their complexity. He passed sleepless nights reading tomes on unemployment, and Betty warned him that he was getting too little sleep. "That's nonsense," he replied. "Most people have exaggerated ideas about sleep. If I can get two solid hours I'm all right."[39] At the family Fourth of July celebration in 1931, Morrow stared sadly at the lawn of his Englewood home and said to his son-in-law, "Charles, never let yourself worry. It is bad for the mind."[40]

In September, Morrow had a minor stroke while he and Betty lunched with newspaper publisher Roy Howard on a yacht in Maine. Yet he couldn't stop his compulsive activity or moderate his exhausting pace. On October 2, 1931, after spending a sleepless night on a train from Washington to New York, he told a passenger, "I kept waking up thinking what a hell of a mess the world is in."[41] That day he attended a political reception at his Englewood home. He shook hands with four thousand people; his right hand became blistered, and he had to use his left. Three days later, then in his late fifties, Dwight Morrow died in his sleep of a cerebral hemorrhage. The man once unsettled by his dream of great wealth left a million dollars in charitable bequests alone.

And Harold Nicolson left an appropriately ambiguous epitaph: “There was about him a touch of madness or epilepsy, or something unhuman and abnormal. . . . He had the mind of a super-criminal and the character of a saint. There is no doubt at all that he was a very great man.”[42] Yet Nicolson tempered this judgment with a far less generous one: “Morrow was a shrewd and selfish little arriviste who drank himself to death.”[43]

In one respect, fate proved merciful to Dwight Morrow. Five months after Morrow died, his grandson, Charles Lindbergh, Jr., was kidnapped from his family’s home near Hopewell, New Jersey. The House of Morgan tried to help solve the famous case. Jack Morgan sounded out an underworld contact, and the bank fielded tips from several sources, including a palmist. It also bundled and numbered the ransom money that Lindbergh’s associate, Dr. John F. Condon, passed across a dark cemetery wall to the kidnapper. When the baby’s body was discovered in a wood two months later, Anne and Charles moved to Next Day Hill, the Morrow house in Englewood. Haunted by the press and bad memories, they left the United States for England in 1935. There they lived at Long Barn, a thatched Kentish house owned by Harold Nicolson, Anne’s father’s biographer.

The Lindbergh kidnapping also spread fear through the House of Morgan. Afterward, an army of 250 bodyguards protected the families of Morgan partners, and many of their grandchildren would remember growing up surrounded by opulence and armed guards.

CHAPTER SIXTEEN
CRASH

WE picture the bull market of the twenties as spanning the entire decade, when in fact it was compressed into the second half. It was largely a Wall Street phenomenon, not matched by other stock markets around the world. Germany's market had peaked in 1927, Britain's in 1928, and France's in early 1929. Why the enormous burst of Wall Street optimism? It was partly a reaction to the unsettled postwar years, with their inflation and labor strife, their bitter Red-baiting and anarchist turmoil. Financial history teaches us that the desire for oblivion is the necessary precondition for mayhem.

The euphoria was also generated by a liquidity boom of historic proportions. Cash was everywhere. In 1920, Ben Strong sharply raised interest rates to cool off an inflationary commodity boom. This created not only a recession but disinflationary conditions that lasted for several years. Money fled hard assets. As commodity bubbles burst—ranging from Texas oil to Florida land—the money poured into financial markets. Stocks and bonds floated up on a tremendous wave.

With Europe devastated by war, America's economy outpaced competitors and created a large trade surplus. The economic boom was lopsided. Commentators spoke of "sick sectors" in farming, oil, and textiles. With half of America still living in rural areas, the Wall Street rally seemed unreal and irrelevant to farmers. Nor did all banks prosper. Weakened by farming and oil loans, small-town banks failed at the rate of two a day, a fact not noticed in urban areas, where finance and real estate thrived together. For instance, in late 1928, John J. Raskob, Democratic national chairman, started plans to build the Empire State Building as a monument to "the American way of life that allowed a poor boy to make his fortune on Wall Street."[1]

Raskob and other prophets of the age espoused an ideology of endless prosperity and talked of a new economic era. Their shibboleths were readily believed by the large number of young, inexperienced people recruited by Wall Street. As the *Wall Street Journal* said after October 1929's Black Thursday, "There are people trading in Wall Street and many over the country who have never seen a real bear market."[2] If many on Wall Street were determined to forget past panics, most were too young to have ever known about them.

For many pundits, the sheer abundance of cash precluded any crash. A big

worry of the late 1920s was that America might run short of stocks. The day before the 1929 crash, the *Wall Street Journal* reported, “There is a vast amount of money awaiting investment. Thousands of traders and investors have been waiting for an opportunity to buy stocks on just such a break as has occurred over the last several weeks.”[3] The excess cash was viewed as a sign of wealth, not as an omen of dwindling opportunities for productive investment.

Riding this cash boom, the American financial services industry grew explosively. Before the war, there were 250 securities dealers; by 1929, an astounding 6,500. A critical shift in the popular attitude toward stocks occurred. Bonds had always dwarfed stocks in importance on the New York Stock Exchange. Before the war, banks and insurance companies might trade stocks, but not small investors. We recall Pierpont Morgan’s steady disdain for stocks. When asked why the market went down, he would say dismissively, “Stocks will fluctuate,” or “There were more sellers than buyers,” as if the subject weren’t worthy of analysis.[4]

In the 1920s, small investors leapt giddily into the stock market in large numbers. They frequently bought on a 10-percent margin, putting only $1,000 down to buy $10,000 worth of stock. Of a total American population of 120 million, only 1.5 to 3 million played the stock market, but their slick, easy winnings captured the national spotlight. The 1929 market disaster would be heavily concentrated among the 600,000 margin accounts.

With active securities markets, it was cheaper for big corporations to raise money by issuing securities than it was for them to raise money by paying for short-term bank credit. Many companies also financed expansion from retained earnings, continuing to wean themselves away from the banker dominance of the Baronial Age. In fact, some businesses had so much surplus cash that they engaged in stock speculation and margin lending—much as Japanese companies in the 1980s would use spare cash for *zai-tech* investment—so that the Federal Reserve’s pressure on banks to stop margin lending was offset by unregulated industrial lenders.

In this pre-Glass-Steagall era, corporate preference for securities issues posed no threat to Wall Street. The big New York banks profited through their new securities affiliates, which could also bypass limits on interstate banking. Guaranty Trust opened offices in Saint Louis, Chicago, Philadelphia, Boston, and even Montreal. The securities unit of the Chase National Bank not only operated coast-to-coast but set up offices in Paris and Rome. The world of integrated global markets was thus already foreshadowed by the 1929 crash. In 1927, Guaranty Trust invented American depositary receipts (ADRs), enabling Americans to buy overseas stocks without currency problems. This would be an extremely lucrative business for J. P. Morgan and Company

when it later took over Guaranty Trust.

There were now two securities worlds on Wall Street. One was retail-oriented and pedestrian and was typified by the National City Company, the affiliate of the bank. National City chairman Charles Mitchell lent a carnival tone to securities marketing. He would organize contests and pep talks for his nearly two thousand brokers, spurring them on to higher sales. Bankers took on the image of garrulous hucksters. Among these men, there was a fad for foreign bonds, especially from Latin America, with small investors assured of their safety. The pitfalls were not exposed until later on, when it became known that Wall Street banks had taken their bad Latin American debt and packaged it in bonds that were sold through their securities affiliates. This would be a major motivating factor behind the Glass-Steagall Act's separation of the banking and securities businesses.

By the 1929 crash, large deposit banks had vanquished many old partnerships in the securities business and originated a startling 45 percent of all new issues. The National City Bank Company sponsored more securities than J. P. Morgan and Kuhn, Loeb combined. Nevertheless, elite Wall Street survived, typified by the august House of Morgan. The bulk of prime securities business remained with the prestigious, old-line, wholesale houses. J. P. Morgan had no distribution network but originated issues distributed by as many as twelve hundred retail houses; still distant from markets, the bank allocated shares to "selling groups." It co-managed issues with its Money Trust allies—National City, First National, and Guaranty Trust—while Morgan Grenfell worked with the Houses of Baring, Rothschild, Hambro, and Lazard.

As in the days of the Pujo hearings, big bond issues were still conducted according to fixed rituals. AT&T provides an excellent example. At the Morgan Library in 1920, Jack Morgan, Harry Davison, and Robert Winsor of Kidder, Peabody worked out a secret deal to divide American Telephone and Telegraph issues. They kept identical participations throughout the decade: Kidder, Peabody, 30 percent; J. P. Morgan, 20 percent; First National Bank, 10 percent; National City Bank, 10 percent; and so on. The Gentleman Banker's Code prohibited the raiding of customers. It was thought not only bad form, but dangerous. J. P. Morgan and Kuhn, Loeb feared that if they competed for each other's clients, they would destroy each other in bloody, internecine battles.

On its marble pedestal, the wholesale House of Morgan didn't need to twist the arms of small investors. As *The New Yorker* said in 1929, "It is doubtful whether any private banker ever enjoyed the individual prestige of Morgan senior, but the firm now is vastly more powerful than it was in his day."[5] By decade's end, it would have less to repent than many other banks. Some of this was the result of tradition, as the bank profited from its Victorian disdain

for the stock market—as Pier-pont once told Bernard Baruch, “I never gamble.”[6] Jack Morgan had held a Stock Exchange seat since 1894 but never conducted a transaction. Only once, during a Liberty Bond rally, did he appear on the Exchange floor. He kept the seat only to reduce commissions from the thirty-odd brokers the bank used. In addition, common stock issues accounted for a mere 3 percent of Morgan-sponsored securities. Since the chief damage of the 1920s would be done by stock manipulation, the House of Morgan was spared involvement in some of the worst excesses.

J. P. Morgan and Company engaged almost solely in a wholesale bond and banking business. With glaring exceptions, it refused to water down standards. It recommended conservative investments, such as railroad bonds, but shied away from the tipster’s art of plugging stocks. On the notable occasion when this Morgan policy was violated, the bank was deeply embarrassed. In July 1926, Morgan partner Thomas Cochran, setting sail for Europe, entertained a reporter aboard the liner *Olympic.* (In the Roaring Twenties, even luxury liners had brokerage offices.) When Cochran was at sea, the Dow Jones ticker quoted him as saying that General Motors would eventually sell at 100 points higher than its current price. Aware of the Morgan-Du Pont interest in the company, traders drove up GM stock by 25 points in two days. Aghast at this proof of its power, the bank made sure such incidents didn’t recur.

Although the Morgan bank, as an institution, was distant from the stock market, its partners weren’t averse to speculation. They were in an excellent position to take advantage of insider trading, which was a common vice of the 1920s, and not illegal. Not only did Jazz Age Wall Street echo with rumors, but being in a position to plant false reports was considered a mark of financial maturity. Lax Stock Exchange rules and meager corporate reports made inside information more valuable, and investors milked their Wall Street friends for news. Inside tips didn’t guarantee success—many investors perished on Black Thursday clutching them—yet they were profitable enough to be considered a major perk of Wall Street employment.

In the 1930s, Morgan partners joined those favoring an end to insider trading. Lamont would say flatly, “This is a simple and unanswerable proposition in business ethics.”[7] Some had had the courage to take this stand earlier. Judge Elbert Gary, chairman of U.S. Steel, used to hold board meetings each day after the stock market closed; following these meetings, he would brief the press, denying directors an exclusive opportunity to benefit from his news. By and large, however, Morgan partners, like others on Wall Street, did benefit from insider trading, not so much on pending deals as on routine corporate information.

Edward Stettinius was a loquacious director of both General Motors and

General Electric. In 1922, Harry Davison asked whether he should buy GM preferred stock for his wife. Stettinius replied: “I hesitate . . . about buying any common stock until after the statement has been published showing the results of last year’s operations. This statement, which is now in the course of preparation, will probably show a total debit against Surplus Account of about $58 million as indicated in the memo attached hereto. I think it possible that this statement may have a depressing effect on the stock and would not favor purchases of the stock until after the statement shall have been published.”[8] Stettinius handled GM purchases for both Jack Morgan’s and Tom Lamont’s personal accounts.[9] We might call this the shooting-fish-in-a-barrel school of finance.

In passing tips, Stettinius displayed a vague sense of the impropriety of doing so. In 1923, Morgan partner Herman Harjes in Paris asked about buying General Electric shares. Note how Stettinius hesitates before spilling the news:

I would much prefer to buy than to sell the stock of the General Electric Co. at present prices, say 196. I do not feel that I can properly tell you what information has come to me as a member of the Executive Committee and Board of Directors of the Co., but I do think that I can say to you (to be treated confidentially) that it is my guess that some action will be taken within the next 6 months to still further enhance the value of the company’s shares. I shall be surprised if the shares do not sell on a basis of 225 or 230 per share, within the next six or nine months. The Co. is doing a wonderful business—and this again in confidence—profits for 11 months of 1923 show an increase of 50$$$ over the profits for the corresponding period of 1922.[10]

If Stettinius displayed scruples, it was less about revealing corporate information than in having it leak out to those beyond the inner circle of J. P. Morgan partners.

The House of Morgan was involved in another period phenomenon that belied its well-advertised repugnance toward common stock. Between 1927 and 1931, the bank participated in more than fifty stock pools, which weren’t outlawed until the New Deal. They were regarded as racy and glamorous, attracting cocktail party sophisticates, and their progress was reported in the press. These syndicates blatantly manipulated stock prices. Some would hire publicity agents or even bribe reporters to “talk up” a stock. Pools made Joe Kennedy’s reputation after he was enlisted in 1924 to defend John D. Hertz’s Yellow Cab Company against a bear raid; afterward, Hertz suspected Kennedy of carrying out such a raid against the stock himself. By October 1929, over one hundred stocks were being openly rigged by market operators.

So while Morgan partners claimed they preferred sound long-term investments, they were far from immune to the speculative atmosphere.

The 1920s were also a time of manic deal making. As Otto Kahn recalled, there was "a perfect mania of everybody trying to buy everybody else's property. . . . New organizations sprang up. Money was so easy to get. The public was so eager to buy equities and pieces of paper, that money was . . . pressed upon domestic corporations as upon foreign governments."[11] Although J. P. Morgan had no formal merger department, it informally spun many webs. It specialized in deals of strategic import, requiring sensitive contacts abroad or covert government support. Many of its deals were directed against British interests; first and foremost, 23 Wall operated as an arm of Washington.

Consider telecommunications. After the war, the United States feared the British military monopoly of undersea cable communications, which had yielded invaluable wartime intelligence. The U.S. Navy favored the use of a new private corporation, supported by Washington, to battle Britain in the emerging field of radio technology. Privately, President Wilson notified General Electric that he wanted to counter Britain's cable monopoly with an American radio monopoly. Morgan money helped GE to buy out British interests in American Marconi, which became the core of Radio Corporation of America. Washington stayed on RCA's board as a nonvoting observer.

During the 1920s, the House of Morgan also helped Sosthenes Behn to launch his worldwide empire of International Telephone and Telegraph. Again the bank's role wasn't raiding but arbitrating. A historic truce was hatched at 23 Wall, whereby AT&T ceded overseas markets to Behn, who promised, in turn, that ITT wouldn't build telephone plants in the United States. The deal, amazingly, lasted sixty years. This cartel arrangement showed that the Morgan bank still preferred collusion among big industrialists to the competitive economy *laissez-faire* ideologues.

With his taste for political intrigue, Behn and the House of Morgan were a natural match. Through Morgan partner Herman Harjes in Paris, Behn took over the Spanish telephone system, which became the crown jewel in his international empire. In the mid-1920s, J. P. Morgan and Company helped Behn to take over telephone systems in Brazil, Argentina, Chile, and Uruguay, ousting the British from their former preeminence. The bank championed Behn's cause in numberless ways. When it learned during Austrian loan negotiations that the government planned to buy telephone equipment from Siemens, it mentioned that ITT was eager to tender bids. Lamont sometimes functioned as Behn's secret plenipotentiary. In 1930, he had an audience with Mussolini solely to advance Behn's desire to build a factory in Italy. Deal making in this era was always a discreet, behind-the-scenes operation and had none of the flamboyance associated with the stock

market raiders of a later day.

IN early 1929, a sure sign of impending disaster occurred when the House of Morgan cast aside its traditional aversion and joined the flurry of stock promotion. Wall Street was being swept by new forms of leveraging. Borrowing a British concept, many brokerage houses, including Goldman, Sachs, introduced leveraged mutual funds, called “investment trusts.” A second favorite device was the holding company. Holding companies would take over many small operating companies and use their dividends to pay off their own bondholders, who had financed the takeovers in the first place. This permitted an infinite chain of acquisitions.

Adopting the vogue for utility holding companies, the House of Morgan in 1929 sponsored the United Corporation, which took over Mohawk-Hudson, the Public Service Corporation of New Jersey, Columbia Gas and Electric, and other companies that controlled more than a third of the electric power production in twelve eastern states. It was a throwback to the days when Pierpont promoted trusts, kept a large block of stock for himself, and appointed the directors. The United Corporation’s books were kept at 23 Wall, and its board was filled with Morgan friends and partners. The bank also sponsored Standard Brands, an amalgam of food-product companies that included Fleischmann, Royal Baking Powder, Chase and Sanborn, and E. W. Gillette.

The master boondoggle of 1929 was the Morgan-sponsored Alleghany Corporation, a holding company for the railroad and real estate empire of Cleveland’s Van Sweringen brothers. Oris P. and Mantis J. Van Sweringen were a queer, taciturn pair who lacked much formal education. Short, dumpy, and round-faced, they seemed as inseparable as Siamese twins. Living at Daisy Hill, their seven-hundred-acre Swiss chalet farm outside Cleveland, the bachelor brothers ate together, shared a bedroom, seldom socialized, avoided alcohol and tobacco, and dispensed with chauffeurs, valets, and other trappings of wealth. On the eve of the crash, they were worth over $100 million.

Beginning with their development of suburban Shaker Heights, the brothers had learned the art of using other people’s money. They got into railroads when they built a line from downtown Cleveland to the development. They whirled into the Morgan orbit in 1916 when the Justice Department pressured the New York Central into divesting the “Nickel Plate” railroad, which ran into Cleveland; the Van Sweringens arose as the friendly party who would take the road off New York Central’s hands for a mere $500,000 cash. Alfred Smith, president of the New York Central, took the boys into 23 Wall, threw his arms around them, and told Lamont, “I have had many experiences with

these two boys. They are very capable. . . . I want you to cooperate with them in any way you legitimately can."[12] Lamont complied.

The House of Morgan and Guaranty Trust orchestrated financing for the brothers' railroad and real estate takeovers. As masters of leverage, the Van Sweringens used each new purchase as collateral for the next. Their holding companies took control of other holding companies in an endless hall of mirrors, all supported by little cash but powerful Morgan connections. By 1929, the Van Sweringen railroads ruled America's fifth largest railroad system from atop a forty-story Cleveland tower and controlled trackage equal in length to all of Britain's railroads.

Issued by J. P. Morgan and Company in January 1929, the stock of the Alleghany Corporation was meant to be a summary achievement for the brothers—the super holding company atop their pyramid of debt. In the words of the *New York Times*, it was "the holding-company device pushed to its uttermost limits."[13] The association with the Van Sweringen brothers showed how the recklessness of the 1920s had at last infected the citadel of respectability itself—the Morgan bank. Even the mystical Morgan name couldn't hold together a pyramid built of nothing but faith. It would be four years before the public finally knew the questionable circumstances under which the Alleghany shares had been floated. In early 1929, however, the issue looked like the best buy in town.

FOR much of 1929, Jack Morgan and Tom Lamont were distracted from the coming storm by the thorny problem of Germany's reparations. They had continually warned against excess German borrowing only to find themselves subsequently making the loans. In this twilight of the businessman-diplomat, an admiring America still looked to Morgan bankers for guidance. GE chairman Owen Young and Jack Morgan were chosen as American delegates to a Paris conference that was supposed to devise an ultimate solution to the reparations issue; Tom Lamont and Boston lawyer Thomas W. Perkins were alternates. The group was technically unofficial although again in close touch with Washington. In February, they set sail on the *Aquitania*. Upon landing at Cherbourg, they were greeted by French officials, who quickly transferred them to a private railroad car for the trip to Paris.

Chaired by Owen Young, the conference took place at the plush new Hotel George V. Once again the sticking point was Germany's capacity to make reparations. As usual, the French, represented by Emile Moreau of the Banque de France, were obstinate in their opposition to lower reparations. And the U.S. refused to lower war debts. Believing reparations financially insupportable, the Reichsbank president, Dr. Schacht, disrupted the conference several times, flying into a rage and storming from the room. One

of the British delegates, Lord Revelstoke, noted that with “his hatchet, Teuton face and burly neck and badly fitting collar . . . he reminds me of a sealion at the Zoo.”[14]

At this conference, Jack Morgan had difficulty hiding his intense dislike of the Germans. Dr. Schacht made the mistake of buttonholing him about the House of Morgan’s financing of Germany’s railways. Jack was scornful. “From what I see of the Germans they are 2nd-rate people,” he cabled New York, “and I would rather have their business done for them by somebody else.”[15] He grumbled about how the conference was ruining his plans for a *Corsair* cruise on the Mediterranean, not to mention those for shooting in Scotland; Dr. Schacht noted Morgan was the first to slip away. This was a rare occasion when Jack let his feelings surface in public, and Lord Revelstoke compared him to “a wild bison in a shop that sells Dresden china.”[16]

In Paris, Dr. Schacht hoped to win substantial decreases in reparations and was irate at French intransigence. He shocked the Allies, in turn, by proposing that Germany get back the Polish corridor and take overseas colonies in exchange for the high cost of reparations. To help break a diplomatic logjam, Owen Young responded to a suggestion by his young assistant, David Sarnoff, shortly to be president of RCA, that he attempt informal negotiations with Schacht. Lamont told Sarnoff, “Good luck. If anyone can do this job, you can.”[17] On May 1, the Russian-Jewish immigrant and the German Hjalmar Schacht had their first dinner at Schacht’s room at the Hôtel Royal Monceau. There was instant rapport. Schacht had once studied Hebrew, a language Sarnoff learned while studying for the rabbinate, and they ended up talking about everything from German opera to the Old Testament. They also discussed reparations, and the first dinner turned into a marathon, eighteen-hour negotiating session. Sarnoff later took credit for selling a “safeguard clause” to Schacht that related reparations to German economic performance. This idea reconciled Schacht, however briefly, to the plan.[18]

Jack was so delighted by Sarnoff’s initiative that he brought him a big bunch of ripe French strawberries. He also told Sarnoff, “David, if you actually bring back a signed agreement, you can have anything you ask for that is within my gift.”[19] After another lengthy bargaining session in late May, Sarnoff brought an agreement back to the Ritz Hotel. Jack, amazed, tipped his black homburg to Sarnoff. “I doff my hat to you,” he said with a bow. “And I propose to stick to my promise. Ask for anything you want, and it will be yours.”[20] Sarnoff asked for a meerschaum pipe of the sort Jack smoked. It was made by an elderly London pipemaker, who first made Pierpont’s. Jack chartered a plane so someone could fly to London and fetch the pipe for Sarnoff.

The Young Plan reduced the schedule of reparations payments from that

designated by the earlier Dawes Plan, stretching them over a fiftynine-year period. It also attempted to depoliticize German debt by converting it into tradable bonds. Instead of paying the Allies directly, Germany would pay bondholders through a new Bank for International Settlements. This would free Germany from political interference and lift the yoke of the hated agent general's office. The boyish Parker Gilbert left Berlin to become a J. P. Morgan partner, a move that didn't surprise the Germans. When Gilbert warned the Germans against seeking any foreign loan beyond the Young loan, Karl von Schubert of the German Foreign Office spied an ulterior motive. J. P. Morgan was about to float a big loan for France, and a German loan "would be seen [by Gilbert] as a disagreeable competitor for the project of the House of Morgan, to which he is known to be close," said von Schubert.[21]

Set up in a hotel off the main square of Basel, Switzerland, the new Bank for International Settlements fulfilled Montagu Norman's dream of a place where central bankers could forge international monetary policy without political interference. Norman lovingly called it a confessional. A provincial U.S. Congress didn't like the word *international* and refused to let the Federal Reserve join, although several private American banks bought shares in it. The BIS would outlast the Young Plan and develop into a central bank for central bankers, just as Monty Norman had envisioned.

In June 1929, the German debt settlement was announced. Newspapers showed Dr. Schacht leaning across Owen Young to shake hands with Emile Moreau of France's central bank. No sooner were the documents signed than a window curtain caught fire and burst into flames—a lurid omen suggesting the Young Plan's fate in Germany, where it would prove no more popular than the Dawes plan. Dr. Schacht signed the document with strongly felt ambivalence, insisting that the German Cabinet take responsibility. Before long, he would denounce it and become a Nazi favorite. The $100-million portion of the Young loan, sponsored by the House of Morgan in June 1930, would be its second and final effort for Germany. Unlike the robust reception given to the Dawes loan, the Young loan aroused scant enthusiasm. Nevertheless, in 1929 the Paris conference gave a sense of closure to the era's most intractable problem and helped spur the final upward rise of the stock market in New York City. Owen Young was even mentioned as a possible presidential candidate.

WHILE Jack stayed behind for the grouse season, Lamont returned to New York. As a rule, Morgan partners didn't belong to the select group of financiers who could later point out their apocalyptic warnings about the stock market. (Joe Kennedy later said he sold stocks after hearing his bootblack touting them.) Lamont was an exponent of the new economic era

and thought only a business downturn could derail stocks. George Whitney thought the Federal Reserve Board a "set of damn fools" for tightening credit in 1929. The only Morgan seer was Russell Leffingwell, the former assistant Treasury secretary who had come to the Corner in 1923 from the law firm of Cravath, Henderson, Leffingwell, and de Gersdorff. An entertaining and courtly man, Leffingwell had a long pointed nose and a shock of premature white hair that gave him an air of wisdom. He was a liberal and sometime Democrat. In his combative, curmudgeonly intellectual style, he pilloried ideologues of both the left and the right. A perpetual worrier, he was withering in his view of the optimistic Andrew Mellon: "Meanwhile, the greatest Secretary of the Treasury since Alexander Hamilton grows richer on paper and thinks that all is for the best possible in the best of possible worlds."[22]

Leffingwell subscribed to the cheap-money theory of the crash; that is, he blamed excessively low interest rates for the speculation in stock. In 1927, Monty Norman had visited New York and asked Ben Strong for lower interest rates to take pressure off the pound. Strong obliged by lowering his discount rate. Leffingwell believed this had triggered the stock market boom. In early March 1929, when Leffingwell heard reports that Monty was getting "panicky" about the frothy conditions on Wall Street, he impatiently told Lamont, "Monty and Ben sowed the wind. I expect we shall all have to reap the whirlwind. . . . I think we are going to have a world credit crisis."[23] Later he held the two directly responsible for the Depression. It may be recalled that Jack Morgan and others at 23 Wall had favored England's return to gold in 1925, but only with the proviso that Monty raise rates, not that Ben lower them.

Benjamin Strong didn't live to see the crash. He went through a hellish series of illnesses—tuberculosis, influenza, pneumonia, and shingles—and was shot full of morphine when he died, at age fifty-five, in October 1928; Montagu Norman, disconsolate, mourned Strong's death for years. During the spring and summer of 1929, Strong's hand-picked successor, George Harrison, pleaded with the Federal Reserve Board in Washington to increase interest rates. Instead, the board vetoed rate hikes in New York. Russell Leffingwell saw a Greek tragedy unfolding. He feared that Harrison had inherited the antagonism left by Strong and that "the immense resistance offered by the Washington Board may be partly the result of ten years of bottled up bitterness against poor Ben's domination."[24] At the worst possible moment, the system was undercut by bureaucratic feuding. When the discount rate was belatedly raised in August 1929 from 5 to 6 percent, it was too late to cool off the boom.

On September 5, 1929, the tragedy of that Black Thursday was

foreshadowed when an obscure economist named Babson repeated a warning he had been making for years: “Sooner or later a crash is coming, and it may be terrific.”[25] In ordinary times, the remark would have been ignored. Instead, circulated on news wires, it briefly cracked the stock market. Professor Irving Fisher of Yale, high priest of academic hope, rallied the faithful: “Stock prices have reached what looks like a permanently high plateau.”[26] But the American economy had peaked in August and was falling even as Fisher spoke.

By mid-October, the stock market gyrations so worried Hoover that he sent an emissary, Harry Robinson, to consult Lamont, his chief adviser on Wall Street. Hoover, the first president with a telephone on his desk, frequently rang Lamont before breakfast. Despite Hoover’s closeness to the House of Morgan, many partners secretly ridiculed him as cold, pompous, and pigheaded. Parker Gilbert once called him “Secretary of Commerce and Under-Secretary of all the other departments.”[27] During the 1928 campaign, the Democrats had released a memo written by Leffingwell in his Treasury days that said, “Hoover knows nothing about finance, nothing about exchange and nothing about economics.”[28] Hoover was petulant because the bank hadn’t done more to aid his reelection. Before the primary, he sent a threatening note to Lamont, accusing him of working for Charles Dawes.

To his credit, however, the president wasn’t heedless of the Wall Street peril. In early 1928, while commerce secretary, he was flabbergasted by Coolidge’s cavalier lack of concern about the stock market. And in March 1929, as president, he summoned to the White House Richard Whitney, vice-president of the New York Stock Exchange and brother of Morgan partner George Whitney. Hoover wanted the Exchange to curb speculation—a plea that was ignored. Hoover also blamed the Fed for low interest rates and providing banks with ample reserves, which were then used to finance buying on margin.

Now Hoover’s messenger, Harry Robinson, wished to know the answers to two questions: Were the increasing number of stock mergers grounds for concern? And should the federal government take action to stop speculation on Wall Street? Five days before Black Thursday, Lamont wrote Hoover a memo in which he whitewashed the practices of an era. He blandly waved away Hoover’s well-founded worries: “First we must remember that there is a great deal of exaggeration in current gossip about speculation. . . .” He paid tribute to the self-correcting forces of the marketplace. Citing industries that had lagged in the rally—automobiles, lumber, oil, paper, sugar, and cement—he declared that the market hadn’t overheated. With a nod to United Corporation and Alleghany, he praised the new holding companies that now dominated railroads and public utilities. His rousing peroration set all fears to

rest: “Since the war the country has embarked on a remarkable period of healthy prosperity. . . . The future appears brilliant.”[29] The only fault he found was with the Federal Reserve Board in Washington—for blocking higher interest rates at the regional reserve banks.

Martin Egan brought the memo to the White House. The president was so eager to hear Lamont’s report that he held up a parade for ten or fifteen minutes in order to talk to Egan, who found him generally confident about his presidency, if edgy about Wall Street. The satisfaction didn’t last long. On October 22, the president sent a frantic messenger to Lamont expressing concern about the “speculative situation which seemed to him to be running very wild,” as Lamont relayed the message to Jack.[30] Hoover was correct—if a little late. The next day, panic selling hit selected blue chips, with Westinghouse dropping 35 points and General Electric 20. The balloon was about to burst.

The following morning, Winston Churchill stood in the visitors’ gallery of the New York Stock Exchange. Two weeks earlier, he had lunched with the Morgan partners who had helped him to restore England to the gold standard in 1925. Now he looked down on a scene that many would circuitously trace to that 1925 decision, with its need for lower U.S. interest rates. Within the first two hours of trading, almost $10 billion was lost on paper. The drops posted were so sharp and the resulting shrieks so fearful that the gallery was closed by late morning.

As in 1907, desperate men stood on the steps of Federal Hall, hands in their pockets, their hats pulled low, staring grimly ahead. Their shocked silence is almost palpable in the photographs taken that day. They stood six deep outside the Stock Exchange. Having bought on margin, many investors were ruined outright. Newspapers noted a strange noise filtering through the canyons of the Street—a roar, a hum, a murmur. It was the cumulative sound of thousands of stunned people giving vent to their feelings. Violence was in the air. When a workman appeared atop a building, the crowd assumed he wanted to leap and was impatient with his hesitation. A dozen suicides were reported, some poetically apt. “Two men jumped hand-in-hand from a high window in the Ritz,” Galbraith noted. “They had a joint account.”[31] Only the Stock Exchange pages, who lacked investments, savored the ruin of their bosses.

Around noon, the master bankers of Wall Street marched briskly up the steps of 23 Wall. These were the men whose exploits had thrilled America—Charles Mitchell of National City, Albert Wiggin of Chase, Seward Prosser of Bankers Trust, William Potter of Guaranty Trust. They represented $6 billion in assets, perhaps the world’s greatest pool of wealth. For the last time, they enjoyed the heroic stature that the Jazz Age had conferred upon them. To

Street veterans, it came as no surprise that the meeting was chaired by fifty-eight-year-old Tom Lamont. The Morgan role in rescues was now automatic. Whatever its flaws, it was the banker's bank, the arbiter of disputes, the statesmanlike firm that offered confidentiality no other house could match. In the words of B. C. Forbes, "Thomas W. Lamont, foremost Morgan partner, stepped into a role on Thursday which the original J. P. Morgan used to take in past panics."[32]

Even in a crisis, Lamont was debonair, his sangfroid now legendary. He was Wall Street's mystery man, and Black Thursday would be his celebrated moment. He was a strange candidate for the part. In his youth, he had lost a year's salary by selling short and thereafter forswore stock speculation. He was also the banker who had advised a skittish Hoover to take a posture of benign indifference toward Wall Street.

The bankers' rescue on Black Thursday proved longer on symbolism than on substance. The men knew they couldn't prop up a collapsing stock market, so they tried to introduce liquidity and engineer an orderly decline. There had been terrifying moments that morning when no buyers appeared. So they pledged $240 million to buy up assorted stocks and stabilize the market. (The Guggenheims joined this pool.) It was just a finger in the dike, but it was the best they could manage.

Because the president of the Stock Exchange was in Honolulu, the acting president, Richard Whitney, was agent for the bankers' rescue. He seemed an ideal choice because his brother was a Morgan partner and his own firm was a Morgan bond broker. Richard Whitney was also a great pretender, and his cool demeanor masked the fact that he and his wife, an heiress, were absorbing stock losses that would amount to $2 million.[33] So when he took his jaunty stroll across the Exchange floor at 1:30 P.M., it was an extraordinary performance. He went to the trading booth for U.S. Steel and bid 205 for twenty thousand shares—topping the previous bid by several points. As news of his purchase spread, the market seemed to steady for a time.

The choice of U.S. Steel, a Morgan ward, was no accident: as gentleman bankers, Lamont and the others felt they should support companies they had sponsored. It later turned out Whitney had bought only two hundred shares of Steel and pulled his order when others jumped in. At another fifteen or twenty trading posts, he repeated his bidding, placing almost $20 million in orders. By day's end, only half the bankers' money was actually spent. Yet their lingering magic was such that the market briefly rallied that afternoon. It was the last conjuring trick of the 1920s.

At the end of the trading day, the bankers regrouped for a second meeting and designated Lamont their spokesman. He was mobbed by newsmen

shouting questions. Dangling his pince-nez, he came up with the most memorable understatement in American financial history: “There has been a little distress selling on the Stock Exchange.”[34] Although often mocked, the line was actually a reply to a sarcastic reporter who asked whether Lamont had noticed the selling on the Exchange that day. Lamont blandly blamed the decline on a “technical condition” and spoke of “air pockets” in the market. In a phrase of incomparable ambiguity, he said the market was “susceptible to betterment.”[35] These hand-holding sessions with reporters continued for weeks and made Lamont a celebrity. He leapt to the cover of *Time* magazine.

Almost at once, Wall Street began to issue bravely hopeful statements. The silver-lining specialists appeared in force. That night, the retail brokers met at the brokerage house of Hornblower and Weeks and pronounced the market “technically in better condition than it has been in months.”[36] The headline in the *Wall Street Journal* the next morning featured not the crash but the rescue: “BANKERS HALT STOCK DEBACLE: 2-HOUR SELLING DELUGE STOPPED AFTER CONFERENCE AT MORGAN’S OFFICE: $1,000,000,000 FOR SUPPORT.’[37] The bankers asked Hoover to plug stocks as a cheap buy. Instead, he disgorged his well-known platitude: “The fundamental business of the country, that is production and distribution of commodities, is on a sound and prosperous basis.”[38] The market staggered through Friday and Saturday morning trading without a fresh crisis.

The 1929 crash unfolded in two stages, with a weekend in between. On Sunday, the mood was grim as tourist buses made ghoulish swings through Wall Street to see where the crash had occurred. Those who pondered Hoover’s statement over the weekend apparently rushed to sell on Monday. American Telephone and Telegraph dropped 34 points, and General Electric 47 points. Both the market and public faith in bankers were collapsing.

On Tragic Tuesday, October 29, investors looked back on Black Thursday as a halcyon time. On this worst day in market history, the ticker lagged two and a half hours behind. More than sixteen million shares changed hands—a record that would stand for forty years. By day’s end, the two-day damage had dragged share prices down by nearly 25 percent. Buying didn’t dry up this time: it simply disappeared. At the rally’s peak, White Sewing Machine sold for 48, then slumped to 11 on Monday. On Tuesday, when no buyers surfaced, an alert messenger bought shares at $1 apiece. When commuters entered Grand Central Terminal that evening, newsboys hawking papers shouted, “Read ’em and weep!”

Unlike Black Thursday, Tragic Tuesday exposed the bankers’ frailty. They were little men standing before a tidal wave. The *New York Times* wrote, “Banking support, which would have been impressive and successful under ordinary circumstances, was swept violently aside, as block after block of

stock, tremendous in proportions, deluged the market."[39] Where rumors on Black Thursday were hopeful—men winked and talked of the "organized support" taking control—Tragic Tuesday was marked by reports of bankers dumping stocks to save themselves.

Lamont now faced a more hostile group of reporters. He had to deny reports that his group was sabotaging the market for profit. "The group has continued and will continue in a cooperative way to support the market and has not been a seller of stocks."[40] With his usual cunning phraseology, he said the situation "retained hopeful features."[41] In a vain effort to bolster confidence, U.S. Steel and American Can declared extra dividends.

As if expressing a new bunker mentality, the Stock Exchange governors met on Tragic Tuesday in a basement room under the Exchange floor. When Lamont and George Whitney tried to slip in unnoticed, they were briefly detained by guards. The main topic was whether to shut the market. Richard Whitney thought a closing would unsettle the public and create a black market on the curb, as happened at the outbreak of World War I. He also feared it would create chaos among banks with heavy call loans to brokers. At various points in 1929, Morgans had $100 million outstanding in such loans, with stocks pledged as collateral. How would Wall Street banks and brokers function with stock collateral frozen?

As in 1987, the group decided to shorten Exchange hours instead. An excuse was at hand: overworked clerks were haggard from lack of sleep; shorter hours would let them catch up on paperwork. Instead of ringing at ten o'clock, the opening gong would sound at noon on Thursday, and the Exchange would be shut Friday and Saturday. Richard Whitney left a graphic impression of the basement meeting: "The office they met in was never designed for large meetings of this sort, with the result that most of the governors were compelled to stand or to sit on tables. As the meeting progressed, panic was raging overhead on the floor. . . . The feelings of those present were revealed by their habit of continually lighting cigarettes, taking a puff or two, putting them out and lighting new ones—a practice which soon made the narrow room blue with smoke."[42]

In the weeks after Tragic Tuesday, rumor mills produced tales of clandestine lunchtime meetings in the Stock Exchange basement. One version had Lamont and Richard Whitney spying on traders through a periscope. Whitney continued to walk about with a rakish air, exuding confidence, although he later spoke of the "war atmosphere" of those days. Before emerging into public, he would exhort his associates, "Now get your smiles on boys!"[43] As it happens, the real remedial action that was taken came not from the old Wall Street club but by a force new to financial panics—the Federal Reserve.

In late October, Jack, back from Europe, chaired a meeting at the Morgan Library with George Harrison, Ben Strong's successor at the New York Fed. Son of an army officer, a graduate of Yale and Harvard Law School, Harrison was a handsome, pipe-smoking man who limped as a result of a boyhood accident. An activist in the Strong mold, Harrison lowered interest rates and pumped in billions of dollars in credit to buoy banks with heavy loans to brokers. "The Stock Exchange should stay open at all costs," Harrison announced. "Gentlemen, I am ready to provide all the reserve funds that may be needed."[44] Rebuked by Fed governor Roy A. Young in Washington, Harrison courageously replied that the world was "on fire" and that his actions were "done and can't be undone." He bought up to $100 million in government bonds per day and made sure Wall Street banks had adequate reserves with which to deal with the emergency. In scale and sophistication, his postcrash actions made Pierpont's in 1907 look antediluvian in comparison, for he could expand credit as needed. Harrison confirmed the principle of government responsibility in financial panics.

The days after the crash were a great time for pep talks and false bravado. The redoubtable Irving Fisher found it consoling that weak investors were shaken from the market and that stocks now rested in stronger hands. He described the postcrash market as a bargain counter for shrewd investors.[45] From the fastness of his Pocantico Hills estate, John D. Rockefeller issued an oracular statement: "Believing that fundamental conditions of the country are sound . . . my son and I have for some days been purchasing sound common stocks."[46] Rockefeller's words were relayed to Eddie Cantor, then starring in *Whoopee* on Broadway and a victim of the collapse of the Goldman Sachs Trading Corporation. Cantor replied, "Sure, who else had any money left?"[47]

Eddie Cantor later filed a $100-million suit against Goldman, Sachs. This was probably less damaging to the firm's future than his new vaudeville routine. In it, a stooge walked out on stage violently wringing a lemon. "Who are you?" Cantor asked. "I'm the margin clerk for Goldman, Sachs," the stooge replied. So many suits were filed against Goldman, Sachs that during listless Depression days brokers with a taste for black humor would call up the firm and ask for the Litigation Department. From now on, even humor would puncture Wall Street's pretensions. The age had come to an abrupt, calamitous end. The crash was a blow to Wall Street's pride and its profits. As Bernard Baruch later said, "The stereotype of bankers as conservative, careful, prudent individuals was shattered in 1929."[48]

CHAPTER SEVENTEEN
DEPRESSION

AFTER the crash, Herbert Hoover wasn't quite as passive or impotent as legend suggests. He announced tax cuts and public works programs and asked utilities to embark on new construction. Bringing business leaders to the White House, he extracted pledges to maintain wages and thus avert an erosion of purchasing power. Henry Ford cut car prices and boosted workers' wages to $7 a day. Meanwhile, the New York Fed orchestrated a swift series of interest-rate cuts that more than halved its discount rate, to 2½ percent, by June of 1930. Clearly, the principle of government action to ease economic misfortune was enshrined before the New Deal.

Wall Street tried to face the crash with stoic fortitude and treat it as a stern but salutary lesson. Everybody sounded philosophical. In late 1929, Lamont described the crash as an unpleasant warning of no lasting harm: "I cannot but feel that it may after all be a valuable lesson and the experience gained may be turned to our future advantage. . . . There has never been a time when business as a whole was on a sounder basis."[1] This reasonable approach reflected a belief that the financial trouble had ended; in fact, it had just begun.

Never entirely comfortable with the radical, tax-cutting Republicanism of the twenties, Morgan partners hoped the crash presaged a return to more conservative economics. They had been uneasy with the speculative debauch of the twenties and welcomed a return to thrift and hard work. Dwight Morrow, then a New Jersey senator, agreed that "there is something about too much prosperity that ruins the fiber of the people."[2] Russell Leffingwell viewed the slowdown as a "healthy purge" after a seven-year bacchanalia: "The remedy is for people to stop watching the ticker, listening to the radio, drinking bootleg gin, and dancing to jazz . . . and return to the old economics and prosperity based upon saving and working."[3] Such comments savored of puritans punishing the wicked. Treasury Secretary Andrew Mellon, who had ducked a leadership role after the crash, now said of the downturn, "It will purge the rottenness out of the system. People will work harder, live a more moral life."[4] Keynes, however warned that such austerity would only deepen the Depression.

Many of the people who voiced these soothing statements were living off

the riches of the 1920s. Although Morgan partners suffered huge losses, they still boasted wealth of embarrassing proportions. At Christmas 1928, each partner had received a bonus of $1 million. In 1929, Jack's son Junius moved into Salutation, a forty-room stone mansion on an island beside his father's island estate. Even as stock brokers jumped from building ledges in October, workmen in Bath, Maine, rushed to complete *Corsair IV*, a six-thousand-horsepower yacht, 343 feet long, with gross tonnage of 2,181. Reputed to be the biggest private yacht of all time, a floating palace with elevators, beamed ceilings, India teak paneling, mahogany armchairs, and fireplaces, it required a crew of over fifty and cost Jack an estimated $2.5 million. If the price tag was stupendous, it amounted to only about half the annual income that Jack took from the bank in the late 1920s.

Jack Morgan spent the Christmas of 1929 with his fifteen grandchildren at Matinicock Point, and it was a warm, happy time. "It really resembled nothing so much as some of the families of pigs I have seen on the farm," he said.[5] In the new year, he looked forward to a cruise to Palestine with his friend Dr. Cosmo Lang, the archbishop of Canterbury.

What made the postcrash lull tolerable on Wall Street was that a political backlash hadn't yet gathered force. Nobody yet demanded radical overhauls of the system. That December, learning of proposed staff cuts at the American Museum of Natural History, Jack covered the budget shortfall; the munificence of rich men still meant something. Soon, though, the Depression would unleash a popular fury against bankers that would rage for years.

Wall Street perhaps had better excuses for postcrash complacency in 1929 than in 1987. America boasted a trade and budget surplus and was finishing the most triumphant economic decade in its history. In the world economy, it was the ascendant power and the leading creditor nation. J. P. Morgan and Company was so flush with cash that it was giving large gifts to its less fortunate London and Paris partners in the late 1920s. The age can be forgiven some of its hubris.

The speculative mood didn't immediately disappear. Those with money who rushed in to buy stocks were at first vindicated: by early 1930, the market had regained much lost ground. People chattered about a little bull market. Business investment rose, accompanied by an upturn in car and home sales. On March 7, 1930, President Hoover proclaimed: "All the evidence indicates that the worst effects of the Crash upon unemployment will have passed during the next sixty days."[6]

In April, however, the stock market began to slide, then dropped in May and June with each new Hoover expression of hope. Unlike the spectacular downward swoops of the previous October, the deterioration in prices was small and steady but unrelenting. In mid-1932, the market would bottom out

at one-tenth of its September 1929 peak. So the yokels who sold in terror after the Crash fared better, in the long run, than the canny traders who scouted for bargains.

We shall never know whether wise economic management might have averted the Great Depression. But two events led to a frightful, downward momentum. On June 17, 1930, ignoring the pleas of over a thousand American economists, President Hoover took up six gold pens and signed the Hawley-Smoot Tariff Act. Its heavy tariffs would account for more than half the price of some imports. The day before Hoover signed the bill, the stock market, in nervous anticipation, suffered its worst day since Tragic Tuesday.

As a major sponsor of foreign loans, the House of Morgan was naturally dismayed. If debtors couldn't export goods to the United States, how would they ever earn foreign exchange and pay off loans? "I almost went down on my knees to beg Herbert Hoover to veto the asinine Hawley-Smoot tariff," Lamont declared.[7] He soon referred to the world trading system as an insane asylum.[8] Apprehensively, America's most international bank watched the rise of a new economic nationalism. It would dismantle the structure of free trade and free flow of capital that the House of Morgan, along with Montagu Norman and Ben Strong, had struggled to create in the twenties. Within two years, two dozen countries would retaliate against the Hawley-Smoot tariff by raising their own tariffs and slashing U.S. imports. The age of "beggar thy neighbor" economics had begun.

The second great mid-1930 blunder was made by the Federal Reserve Board in Washington: it ended the liberal provision of credit and shrank the money supply. This was part of an attempt to rein in the New York Fed and end its backdoor diplomacy with European ministries. Treasury Secretary Andrew Mellon wanted higher interest rates to stop the flow of gold to Europe. Many at the Fed saw austerity as a bitter but necessary medicine. "The consequences of such an economic debauch are inevitable," said the Philadelphia Fed governor. "Can they be corrected and removed by cheap money? We do not believe that they can."[9] By the second half of 1930, the postcrash calm was gone. That fall, Hoover complained to Lamont about bear raids, short selling, and other unpatriotic assaults against national pride. The following year would be the worst in stock market history.

While the Fed had assumed responsibility for the health of the entire financial system after the 1929 crash, the House of Morgan still played a part in specific, smaller crises. The Fed had no obligation to rescue individuals, banks, or companies; its concerns were more general. The crash's aftermath revealed much about Morgan priorities. While claiming to represent the public interest, the firm actually represented its clients, cronies, and fellow bankers. Part of its power had always stemmed from its fidelity to Wall Street

friends, its generosity in making loans to bankers and other financial houses. This was strikingly demonstrated after the crash.

Take, for instance, the case of Charles E. Mitchell, chairman of the National City Bank. Right before the crash, Mitchell had put together a deal to merge with the Corn Exchange; if he had succeeded, he would have produced the world's largest bank, surpassing even the Midland Bank in London. Since the deal was to be effected with National City shares, Mitchell needed to maintain their price at $450. During the crash, the price plunged through this floor, and even furious buying by the National City Company, the bank's securities affiliate, couldn't sustain it. On his way to work, Mitchell stopped by 23 Wall and walked out with a $ 12-million personal loan, secured by his own National City stock. When he later failed to meet payments, the House of Morgan temporarily became the second largest stockholder in National City. Later Mitchell said of Morgans, "That firm stood at the very peak as to ethics, understanding, and leadership."[10] Yet however laudable in terms of loyalty, it was a reckless loan from a financial standpoint.

Loyalty to clients was always the vice of the House of Morgan. Sometimes it got in so deep it couldn't get out. After the crash, the Van Sweringen brothers, those financial acrobats of the 1920s, suddenly lost their balance. Their overly indebted railroads were among the worst crash performers. Much like William C. Durant with General Motors in 1920, the Van Sweringens kept buying Alleghany stock on its way down. Using borrowed money, they only augmented their losses. They ignored polite warnings from Morgans to stop their rash purchase of more railroads, including the huge Missouri Pacific. Buying on credit had become a Van Sweringen habit.

The Alleghany shares feverishly bid up in the frothy days of early 1929 now led the market down in the autumn of 1930. They fell from 56 to 10 in just two months. On the evening of October 23, 1930, Oris and Mantis Van Sweringen met at Tom Lamont's East Seventieth Street townhouse along with representatives of Guaranty Trust. The short, moon-faced brothers were $40 million in hock to their broker. Having sponsored $200 million in securities in their behalf, Morgans and Guaranty felt bound to prop them up. Lamont was pessimistic about the prospects of railroads. He was already telling Hoover how two hundred affluent passengers were arriving daily by air in New York City. Yet he also feared a domino effect among Wall Street brokers who dealt with the brothers.

The two banks led a syndicate that furnished a $40-million rescue loan for the Van Sweringens. The rescue was handled with a delicacy and secrecy that seldom accompanies personal bankruptcy. The Van Sweringens would remain as figureheads so that nobody would suspect their true plight. They were rewarded for their profligacy with a personal allowance of $ 100,000 a year. In the words of Matthew Josephson, "The Van Sweringens' personal

insolvency during 5 years was one of the best kept secrets in Wall Street."[11] The following year, when the brothers missed payments on their loans, Morgans and Guaranty Trust foreclosed on their Alleghany Railroad empire. Ultimately Alleghany stock would fall to 37½ cents per share.

As a lender of last resort, the House of Morgan favored like-minded institutions of similar character and background. Kidder, Peabody was just such a firm. It didn't hustle business or steal clients and always played by Morgan rules. In 1930, it was hit by multiple blows. The Italian government removed $8 million in deposits, and the new Bank for International Settlements instructed Kidder to switch big sums to a Swiss bank. This led to another rescue at Jack Morgan's home, chaired by George Whitney, who had started his career as a Kidder clerk. The House of Morgan arranged a $10-million line of credit. Under Whitney's tutelage, the old Kidder, Peabody was folded. Whitney brought in his friends Edwin Webster, Chandler Hovey, and Albert H. Gordon to take over the company's name and goodwill. "Incidentally, we are slowly making the grade socially," Gordon reported to the elder Webster. "Yesterday for the first time Morgan invited us to tea on our way out from the almost daily conference."[12]

Unstinting in serving its friends, the House of Morgan could be heart-less to those whose image didn't fit the preferred profile. This became apparent with the failure of the Bank of United States on December 11, 1930. With 450,000 depositors, it was New York's fourth largest deposit bank. In general, the crash and subsequent deflation had damaged the collateral behind bank loans. From a rate of 60 bank failures a month in early 1930, the figure snowballed to 254 in November and 344 in December of 1930. There were over a thousand bank failures for the year. The failure of the Bank of United States was the largest thus far and threatened more general ruin.

But this bank wasn't a high-class operation. Its Jewish owners had chosen its grand name in an effort to fool its Jewish immigrant customers into thinking it had government support. In the lobby hung a large oil portrait of the U.S. Capitol, reinforcing the misleading message. A proposed rescue plan for the Bank of United States got a cool reception on Wall Street, even after Lieutenant Governor Herbert H. Lehman, the state banking authorities, and the New York Fed all pleaded for it. The regulators wanted to merge the Bank of United States with three other banks, backed by a $30-million loan from the Wall Street banks.

At an emotional meeting, Joseph A. Broderick, the state banking chief, warned that if the bankers rejected the rescue plan, it might drag down ten other banks. One in ten New York families using bank accounts would be stranded. As the Wall Street bankers sat stony-faced, Broderick reminded them how they had just rescued Kidder, Peabody and how they had banded

together years before to save Guaranty Trust. But they refused to save the Jewish bank, pulling out of their $30-million commitment at the last minute. “I asked them if their decision to drop the plan was still final,” Broderick recalled. “They told me it was. Then I warned them they were making the most colossal mistake in the banking history of New York.”[13] The biggest bank failure in American history, the Bank of United States bankruptcy fed a psychology of fear that already gripped depositors across the country.

The failure of the Bank of United States has been attributed to anti-Semitism among Wall Street bankers. At the time, there were few commercial banks owned by Jews, Manufacturers Trust being the only other important one in New York. It is impossible to verify whether anti-Semitism stopped the bankers from rescuing the Bank of United States. But Morgan records show that its clientele’s Judaism was very much in the partners’ minds. When informing Morgan Grenfell of events in New York, Lamont’s son Tommy noted that it was patronized largely by foreigners and Jews.[14] Russell Leffingwell described it as “an uptown bank with many branches and a large clientele among our Jewish population of small merchants, and persons of small means and small education, from whom all its management was drawn.”[15] Their attitude was shortsighted, for the bank’s failure shook confidence across America. It was a failure that could have been easily avoided by the proposed merger.

Had it not been for the large number of depositors, the Bank of United States would not have deserved to survive. Its securities affiliate had sponsored shoddy stocks and issued misleading prospectuses, and had been manipulated by the bank’s own offices. Two of its owners were jailed for loose banking practices. One, bank president Bernard K. Marcus, was the uncle of Roy Cohn, who always blamed the bank’s failure on an anti-Semitic plot. Even banking superintendent Broderick was indicted for not having shut the bank sooner. (He was acquitted, after two trials.) To have to bail out such a bank undoubtedly grated on the patrician bankers. But with so many Morgan rescues occurring in those years, all backed up with high-flown rhetoric about saving the banking system, it’s hard to believe religion wasn’t a major factor behind Wall Street’s refusal to act. Hundreds of thousands of Jewish depositors were not worth one Charles Mitchell. Jews were always a blind spot in the Morgan vision, no less than in the days when Pierpont Morgan had vied with Jacob Schiff.

THE City of London had reacted to the New York crash with alarm, but also with some quiet satisfaction and *schadenfreude*, After Black Thursday, the *New York Times* reported that the “selling left London’s ’City’ in a comfortable position saying ’I told you so.’ It had been expected for a long

time. ”[16] In many ways, London profited from the crash as investors switched funds from New York, easing the strain on British gold reserves. In 1930, there was even a brief spurt in foreign lending as London became a safe haven for investors. At the same time, the deeper prognosis for Britain remained grim. Its industry languished, its unemployment rose, and London’s port was vulnerable to spreading protectionism. Several Commonwealth countries dependent on agricultural exports—Australia, Canada, and India—were hit early by the Depression, and this hurt the City.

England’s real crisis, however, originated in Central Europe, just as Montagu Norman had always suspected it would. Reparations continued to burden Germany’s economy and polarize its politics. In March 1930, Dr. Schacht submitted his resignation as Reichsbank president to protest additional German debt mandated by the Young Plan. Germany’s day of reckoning—so feared and so long predicted—was at hand. In the elections of September 1930, the National Socialists and the Communists scored sizable gains, and Chancellor Heinrich Brüning adopted an antireparations policy. The right wing capitalized on the reparations issue. On January 5, 1931, Dr. Schacht attended a dinner party thrown by Hermann Göring. For his tough stand on reparations, Schacht had become a great favorite of the National Socialists. At the dinner, he met Hitler and Joseph Goebbels and became a critical link between the Nazis and German big business. That spring, as political street fights broke out in Germany, pressure mounted to cast off the Versailles burden.

Into this already volatile situation came the powerful jolt of a major bank failure. On May 11, 1931, the Credit Anstalt failed. It was not only Austria’s largest bank but probably the most important bank in Central Europe. A rescue plan announced by the Austrian National Bank and Rothschilds only served to alert the world to trouble and brought on a run. The disaster spread through Central Europe, collapsing Austrian and German banks. In June, Norman gave emergency credit to Austria’s central bank to prop up the schilling—his swan song as a global lender of last resort. Along with an emergency loan to Germany, it marked the end of British financial leadership in the 1930s.

It was against this backdrop that Lamont telephoned Hoover on June 5, 1931, to propose a holiday on payment of war debts and reparations. Without it, he warned, there might be a European crash that could prolong America’s Depression. As Lamont’s files show, Hoover reacted in a grumpily defensive manner: “I will think about the matter, but politically it is quite impossible. Sitting in New York, as you do, you have no idea what the sentiment of the country at large is on these inter-governmental debts.” A banker of the Diplomatic Age, Lamont didn’t merely couch his argument in economic terms: he made an unashamedly political appeal. “These days you hear a lot

of people whispering about sidetracking the Administration in the 1932 Convention," Lamont told Hoover. "If you were to come out with such a plan as this, these whisperings would be silenced overnight."[17] In closing, Lamont said that if the plan ever reached fruition, the bank would hide its role and let Hoover take the credit: "This is your plan and nobody else's." What a cunning fellow Lamont was when he whispered in Hoover's ear!

Treasury Secretary Mellon tried to spike the idea and dismiss the debt as Europe's mess, but Hoover had now had enough with myopic isolationism. On the evening of June 20, 1931, he telephoned Lamont at Torrey Cliff, his home on the Palisades, to say that he had just announced a one-year moratorium on war debt and reparations payments. He knew France would be indignant at the mercy shown toward Germany and asked whether Lamont could sell the plan to the French. Lamont expressed sympathy for the French position but also reminded Hoover that they were the world's most difficult people to deal with—a recurring theme in his letters. Finally, though, he agreed to lobby the French government through the Banque de France. True to Hoover's predictions, the French thought the moratorium an Anglo-American plot to let Germany escape reparations.

The Hoover moratorium was a belated response to a crumbling world financial system. The Danat Bank, one of Germany's largest, failed on July 13, 1931. A teary-eyed Chancellor Briining rejected a New York rescue out of fear that a bad loan to President Hindenburg's son Oskar might surface in such an operation. After the Danat failure, Germany had to shut the Berlin bourse and the city's banks. Around the world, creditors were calling in German loans. The Morgan-led bond issues for Germany and Austria, heralded with trumpet peals in the 1920s, plummeted with frightening speed. All the laborious work of that decade was coming apart.

Now the crisis shifted to London, as investors traced financial ties between Germany and England. During the summer of 1931, investors dumped sterling in massive amounts. Even without Germany, the pound was already in a parlous state. In late July 1931, a committee of bankers and economists, the May Committee, had predicted that Britain's budget deficit would widen to £120 million, with no end of red ink in sight. The committee recommended higher taxes and a 10-percent cut in the dole. A few days later, sterling cracked on world markets. The Bank of England told Philip Snowden, the chancellor of the Exchequer, that Britain had almost exhausted its foreign exchange. Despite the need for stringency, Ramsay MacDonald's Labour government was stymied in coping with the problem. With 2.5 million unemployed, the unions wouldn't surrender unemployment benefits.

A few days before the May report was published, Monty Norman left the bank "feeling queer." A year before, tired and wrung out, he had taken a two-month vacation in South America. Now haggard from overwork, the high-

strung Norman was ordered to bed by doctors. When he was again ambulatory, it was recommended that he travel abroad to recover from his nervous collapse. Norman was temporarily replaced by his deputy governor, Sir Ernest Harvey. As a sterling crisis loomed, Jack Morgan and Teddy Grenfell decided to smuggle Norman out of England. Fearing he might break, the House of Morgan plotted with British authorities to place him in temporary exile. After clearing Norman's removal with Edward Peacock, a Bank of England director, Grenfell reported to New York, "M.N. has not made any progress and it has been intimated to him that he should keep away and leave No. 2 to run the show."[18] It is unclear whether the doctors were part of this scheme or whether they were invoked as a cover for the operation.

One marvels at both Morgan's imperial hauteur and the tender solicitude for Norman. The bank wished to banish him with dignity. Jack telegrammed with a gesture of royal magnanimity: if he wished, Norman could take the *Corsair IV* anywhere in Europe, North Africa, or the Far East, attended by a doctor of his own choosing. "There are rooms for six beside himself," Jack told Grenfell, "and for all the servants he could want."[19] Norman was steaming to Quebec when Jack's message came by radio, and he declined the "glorious offer." To scotch rumors of a bankers' cabal, he wanted to avoid the United States altogether. He recuperated at the Chateau Frontenac, where he also conferred with George Harrison. In exile, Monty was spared the need to take the ax to his beloved gold standard, and Grenfell said afterward he wouldn't have been able to withstand the strain.

The House of Morgan had helped Britain back onto the gold standard in 1925 and now underwrote a last-ditch effort to save it. Prime Minister Ramsay MacDonald and Philip Snowden knew the pound couldn't be defended without a foreign loan. New York and Paris owned most of the world's gold, and George Harrison suggested a joint U.S.-French loan. It fell to 23 Wall to keep MacDonald informed of Wall Street opinion *vis-à-vis* British chances for a credit. The messenger was Teddy Grenfell, who had triple authority—as a Bank of England director, a Conservative member of Parliament from the City, and the senior Morgan Grenfell partner. Pitiless toward Labour politicians and staunchly opposed to their program of nationalizing industry, he had a scathing opinion of MacDonald, whom he found coarse and gutless. "The only white thing about him is his liver, and the only portion of him that is not red is his blood."[20] In early August, Grenfell warned MacDonald that halfway measures wouldn't do and that a British loan from Wall Street would be dimly received unless he took courageous action and cut the budget deficit. Sensing a crisis in the offing, Grenfell tracked down the Conservative leader, Stanley Baldwin, then in France, and suggested he return to England at once.

Depending on one's viewpoint, Ramsay MacDonald's story in 1931 is either that of a farsighted prime minister who nobly sacrificed ideology to the national good or that of a blackguard who betrayed his party and platform to satisfy the foreign bankers. (There are striking parallels between MacDonald's actions and Grover Cleveland's alienation from his Democratic followers during the 1895 gold crisis.) A fiery, opinionated socialist, MacDonald had taken office in 1929 promising to fight unemployment, and he enacted unemployment benefits that became sacred to the trade unions. For all his rabble-rousing, however, he had a true-blue Englishman's faith in sterling as the medium of world finance. So his dilemma was stark in August 1931. Foreign bankers insisted that he close the budget gap as the precondition for a loan. But any such austerity talk brought outcries from Labour ministers, who saw it as a betrayal of their followers to appease rich bankers.

Speaking for Wall Street, Grenfell talked bluntly to MacDonald. "We are all getting tired of promises," he warned in mid-August."[21] Grenfell watched MacDonald warily, suspecting he would opt for expediency. As with Churchill in 1925, the Morgan partner took a rather mordant view of his target: "The P.M. is at last alarmed but he is so conceited and fluffy headed that it will be difficult to keep him up to the scratch."[22] He greatly underestimated MacDonald. When trade unions proved intransigent about cuts in unemployment benefits, MacDonald, angered by their obstinacy, was converted to Grenfell's cause. Many of his own ministers dug in their heels and resisted cuts in the dole.

The next steps in the crisis were intricate. The Bank of England sounded out the New York Fed on whether Chancellor Snowden's compromise plan for budget cuts would guarantee a Wall Street loan. MacDonald was afraid his cabinet would be offended by the idea of consulting New York bankers and wanted to test opinion covertly. George Harrison of the New York Fed referred the Bank of England to Morgans.

Throughout the crisis, J. P. Morgan and Morgan Grenfell had a secret back channel with the Bank of England. As Grenfell explained, "If the Prime Minister were to tell his Cabinet that he had already exposed his plan to foreign bankers and asked for a loan his Cabinet would be much incensed. . . . You must understand that neither Prime Minister nor his Cabinet have ever seen any of the cables between J.P. Morgan & Co. and Morgan Grenfell though many of them have been shown to Governor Norman and Deputy Governor."[23] On August 22, 1931, Harrison received a cable from the Bank of England outlining the new compromise budget that MacDonald would discuss with his cabinet on Sunday, August 23. The prime minister wished to know whether they could be sure of a New York loan if the cabinet adopted it.

Harrison showed the cable to George Whitney and other Morgan partners, who had gathered at the Glen Cove home of partner Frank D. Bartow.

This backdoor intrigue set the stage for a showdown between Mac-Donald and his cabinet. That Sunday evening, the cabinet ministers paced through a warm twilight in the garden of 10 Downing Street. They had awaited New York's verdict since noon. Morgan partners pored over figures calling for £70 million in budget cuts—including a 10-percent dole cut—and an extra £60 million in taxes. Finally, at 8:45 P.M., Sir Ernest Harvey at the Bank of England called Downing Street to announce a telephone message from New York. He offered to carry it right over.

For MacDonald, the suspense must have been excruciating: his political career hinged on the message. When Harvey arrived, MacDonald tore the cable from his hand and rushed back to the cabinet. This split-second action was fraught with historic consequence, for MacDonald didn't stop to screen the contents of the message or even ascertain the sender's identity. He introduced it as being from nameless New York bankers. The cabinet ministers assumed, wrongly, that the message came from the New York Fed. It actually came from George Whitney and was addressed to the Bank of England, not to the cabinet.

Coming upon the cable in Morgan Grenfell's files, it is disappointing to see the blandness of this government-toppling document. It briefly expresses sympathy for a British credit but stipulates no specific budget cuts. It's a sterile document, as if the bankers who penned it were being extremely cautious. But the cabinet ministers were hot and tired, and their nerves were frayed from debate. They spied sinister meaning behind its final lines: "In the foregoing we have as always given you the precise trend of our thought. Let us know promptly as indicated above what the Government's desires are and within 24 hours we shall be able to give you our final judgment. Are we right in assuming that the programme under consideration will have the sincere approval and support of the Bank of England and the City generally and thus go a long way toward restoring international confidence in Great Britain?"[24]

When MacDonald read these words aloud, there was such a commotion in the cabinet room that Sir Ernest Harvey heard it outside, and he later recalled that "pandemonium had broken loose."[25] This last paragraph, clearly, was intended for the Bank of England alone. To those present, it awakened old fears of dark dealings between private banks in London and New York. The other stumbling block was MacDonald's apparent mention of a 10-percent dole cut. This wasn't mentioned by Morgans. Later, in reconstructing events, Grenfell told Lamont that "the Cabinet have gone on repeating . . . that the American Bankers insisted on a 10$$$ cut. . .. If he made mention of a 10$$$ cut as a condition MacDonald must have invented it as it does not appear in

your cable."[26] The cable supports Grenfell.

MacDonald felt that he lacked the cabinet mandate to proceed with the emergency budget cuts required to restore foreign confidence in sterling. The bickering grew so fierce that at 10:20 P.M. he arrived at Buckingham Palace and laid his resignation before King George V. Looking wild and distracted, he told the king that "all was up."[27] In insisting upon the budget cuts, MacDonald set himself against powerful segments of his own party, and he now knew he had crossed some personal Rubicon. The king asked him to return to Buckingham Palace the next morning along with the opposition leaders—Stanley Baldwin of the Conservatives and Sir Herbert Samuel of the Liberals. To spread political risks and ensure passage of the cut in unemployment benefits, the king invited the three to form a coalition government. MacDonald would remain prime minister of a government that was Tory at heart.

The new government cut the budget deficit with higher taxes on gasoline, beer, tobacco, and income and lower salaries for civil servants. J. P. Morgan and Company provided a $200-million revolving line of credit, and another $200 million came from France. Unfortunately, it proved impossible to restore confidence in the pound. Many Labourites now regarded MacDonald as a traitor and were vitriolic in their criticism of him. In September, the Communists marched on Parliament and insisted that a cold-blooded bankers' "ramp," or conspiracy, had imposed unfair hardship on British workers. Unemployed workers rioted in Battersea and mounted police charged demonstrators on Oxford Street. It was widely believed that the New York Fed had brought down the government. London's *Daily Herald* featured a photograph of George Harrison on the front page, charging that a New York-led conspiracy had plotted against the British welfare state. "The *Daily Herald* to-day discloses a startling and apparently successful attempt by US bankers to dictate the internal policy of Great Britain," the headline read.[28]

One can picture Grenfell's sardonic smile as he followed this misunderstanding. To operate in the political shadows, to pass wraithlike through a crisis and exert an unseen influence on large events—for Grenfell, these were the perfections of his art. When he was pumped for information in Parliament, he played the "village idiot," he said. He confided to Lamont, "I believe it is the opinion of the late Cabinet that George Whitney's long telephone message. . . . was a message from the Federal Reserve Bank. For the present, therefore, the fall of Ramsay MacDonald will be put down to the domineering action of poor George Harrison, who will not I imagine lose his sleep in consequence."[29]

Did the House of Morgan bring down the Labour government? MacDonald himself exonerated the bankers and stressed the need to maintain the place of

sterling in world finance. Morgan records confirm that the bank refrained from recommending specific budget cuts. Yet it was no secret that Wall Street wanted the dole cuts. And the broad body of American bankers had a veto over any big British loan on Wall Street. There was no hidden Morgan agenda, only the usual bankers' mentality of favoring austerity and cuts in spending. It was Britain's choice to defend the gold standard, which placed it in the thrall of foreign investors. Morgans merely expressed the consensus among bankers.

A few days after the Sunday cabinet meeting, Lamont spoke by phone with Hoover, who gave qualified approval to the British credit. Since the large credit would enlist 110 American banks, Hoover warned that Wall Street would be accused of funneling money to Britain at a time of American distress.[30] Not for the first time, small-town America looked askance at Morgan assistance to Britain, even as Britain's left accused American bankers of treacherous interference.

The *coup de grâce* to Britain's gold standard came in September 1931, when naval units at Invergordon, Scotland, struck against proposed pay cuts. This little mutiny terrified foreign investors, who saw it as proof that the British public would never accept an austerity budget. Sterling crashed again. Monty Norman was sailing home from Canada on September 21, 1931, when England went off gold. Hence, it would no longer redeem sterling for gold at a fixed rate: the old imperial fantasy was dead, and the pound fell a shocking 30 percent. Keynes exulted over gold's demise: "There are few Englishmen who do not rejoice at the breaking of our gold fetters."[31] But Monty Norman, arriving at Liverpool, was stunned that the edifice he built was shattered. He took the train down to Euston Station and had a temper tantrum when he arrived at the bank. Yet his associates, Harvey and Peacock, believed that he would have done the same thing had he been in charge. Twenty-five countries followed Britain off gold in a rush of competitive devaluations.

In an Associated Press interview from London, Jack Morgan applauded Britain's departure from gold. When Lamont read this in New York, he was thunderstruck. Hadn't they just enlisted over one hundred banks to save that gold standard? And wouldn't those banks now feel betrayed? Lamont, who almost never got angry, was beside himself.

Now came the moment that was destined to occur—when the power relationship at the bank was revealed and even Jack Morgan would feel the sting of Lamont's pen. They had for some time a tacit deal: Jack would be semiretired figurehead, and Lamont would retain executive control. Now in his early sixties, Jack was an absentee boss who preferred golfing and yachting; he was aging and no longer traveled on the *Corsair* without a surgeon aboard. In most banking matters, control had slipped from his grasp.

Lamont had never challenged Jack openly. Now, in his fury, he confronted him directly. So unprecedented was the accusatory letter he sent that he cosigned it with Charles Steele, the other major partner in terms of capital share and an old-timer from Pierpont's days. Steele was a friend of Jack's and was regarded around the bank as a pleasant, wise old man.

It may be said that this letter of September 25, 1931, marks the moment when the House of Morgan ceased operating as a family bank. Lamont wrote: "The point that we must make to you—a point that we fear you little realize—is to have you know fully the uncomfortable position in which the New York firm has been placed before the whole American world and the public generally. What the banks here, without exception, fail to understand, is why this enormous credit operation should have been permitted to blow up in our faces over night so to speak."

Lamont reminded Jack of the solemn pledges to preserve the gold standard that were made to participating banks:

It was upon that prophecy, made wreckage in just three weeks to the day, that we were able to complete the group for the credit. There was, as we told you at the time, great reluctance upon the part of many banks to join in the credit. . . . Now the outcome has manifestly and inevitably diminished our prestige, not only publicly but with the American banking community which has for years so largely supported us in our efforts for the preservation here of British credit. And this is a fact that every partner of the firm, which (under you and your Father before you) has built up its American reputation upon careful judgment and prudent dealing, must keep in the forefront of his mind for a long time to come. . . .

> Now, we have said our say about the situation over here, and will try not to allude to the subject again. But with you so far away, it has been we have thought, quite important to acquaint you with the unpleasant facts which have come to us all.[32]

Ten years before, Lamont would never have dared this. He had always dealt with Jack gingerly so that he would never lose face. Now, however, Lamont's money and position gave him incontestable power. Still, nobody confronted a Morgan without grave anxiety. At one point in the letter, Lamont gave Jack an out: he hinted that the AP quote must have come at the end of a long interview and he closed the letter "with much love from us all," signing it "Faithfully." Lamont knew the letter was uniquely candid and bare-knuckled. After posting it, he telephoned Jack to say no blame was intended and that he, Lamont, would have acted the same under the circumstances. Yet the letter showed that a palace revolution had taken place at the House of Morgan and that the Morgan family had surrendered its absolute power. From that time onward, the influence of the Morgan family would steadily diminish

within the House of Morgan and then all but disappear.

AS the political skies darkened in 1931, Tom Lamont seemed blind to the spread of political extremism and militarism around the world. This was partly a reflection of his innate optimism, his almost instinctive faith in the future. He kept thinking the Depression couldn't get any worse, that the world would suddenly return to its senses, that the dictators would be held in check. The gregarious Lamont often found it hard to credit people's malevolence and was reluctant to probe beneath their reassuring smiles.

This blind spot was especially apparent with sovereign clients, where a banker's self-interest bolstered his preference for looking on the bright side of things. Partisan in behalf of clients, he tried to keep their reputations as unblemished as that of the House of Morgan itself. Their good name was especially vital in the Depression's volatile market for foreign bonds. Unfortunately, a concern with the financial standing of foreign states could slip over into questionable dealings with them. In extreme cases in the 1930s, the House of Morgan would function as an unfettered government in its own right, conducting a secret foreign policy at odds with that of Washington.

As fiscal agent for the imperial Japanese government in the late 1920s, Lamont had devotedly served his client. For a Western banker, he had achieved remarkable, unheard-of triumphs. After the mammoth earthquake loan, he had floated loans for Tokyo, Yokohama, and Osaka, advised on a merger between Tokyo Electric Power and Tokyo Electric Light, mediated between the Bank of Japan and the New York Fed, and extended a $25-million credit that restored Japan to the gold standard in January 1930. On the eve of the crash, the House of Morgan was exploring a possible working link with the House of Mitsui, talks that enjoyed official Japanese patronage. When it came to Japanese business, Lamont took great pride in his accomplishments.

His early faith in Japan was understandable. When he first visited in 1920, Japan stood on the brink of more than ten years of liberal, pro-Western party rule. He developed distinguished and cultured friends, especially Junnosuke Inouye, the commanding figure of Japanese finance, with whom he corresponded frequently. Inouye was finance minister for a third time after 1929. Humane and courageous, he was known for his conciliatory views on foreign affairs and was often at loggerheads with the army. He represented the enlightened antimilitarist forces in Japan. At Inouye's request, Lamont would lobby the New York press and argue Japan's case. In 1928, after meeting with editors of the *New York Times*, he told his friend, "I also told them of the patient and tolerant attitude of your people toward China and the Chinese. . . . It therefore is a matter of satisfaction to me to see how fair and sound the

Times has been."[33]

The House of Morgan attained peak involvement in Japan just as that nation's experiment with liberal rule began to crumble. Following a wave of bank failures and the stock market closing in 1927, it slipped into a depression before most Western countries. That year, Japan was enraged by China's boycott of its goods in protest of foreign encroachment—a slap at national pride that Japan would invoke during the Manchurian invasion. In 1930, the Morgan-assisted restoration of the gold standard, under Inouye's aegis, proved a masterpiece of bad timing. It made exports expensive just as world trade contracted. When Depression-plagued America economized on luxury clothes, Japanese silk exports plunged. Silk was still a staple of Japan's economy, with two of every five families drawing income from it. Poverty spread throughout the countryside, breeding a vicious new strain of rural nationalism. Rice prices also tumbled. The budding Japanese export boom was blighted by Western protectionism, feeding xenophobia. These economic setbacks enhanced the power of the militarists, who blamed foreign powers for Japan's troubles. Militarism would be bloodily manifested in Manchuria.

The Japanese had long coveted Manchuria, that resource-rich north-eastern corner of China. Whenever problems beset Japanese society—whether overpopulation, too great a reliance on foreign raw materials, or the need for new export markets—militarists saw China as the solution. They claimed Manchuria almost as a matter of divine right. China was still fragmented and chaotic, with warlords ruling parts of the country, and it appeared to be easy prey for aggressors. It was weakened by a civil war that had culminated in 1927 with Chiang Kai-shek's defeat of the Communist rebels under Mao Tse-tung. By treaty with China, Japan controlled the South Manchuria Railway and even stationed a garrison in the region. This treaty gave the Japanese militarists a legitimate cover behind which to carry out their plunder. Japan's Kwantung army plotted to use Manchuria as the base for military expansion in China.

In many ways, the House of Morgan shared Japan's jaundiced view of the Chinese, a common one in Western financial circles. China was unpopular on Wall Street and in the City. It was prone to default and adept at playing foreign bankers off against each other. Ever since the abortive China consortium under Woodrow Wilson, Lamont had looked upon the Chinese as wily and duplicitous. He perceived them less as victims of foreign intruders than as two-faced opportunists.

It was an easy attitude to assume. Japan was a major Morgan client, and no business came from China, which was still in default on a substantial portion of its foreign debt. (National City Bank, on the other hand, did a thriving business in China, which generated almost one-third of the bank's profits in 1930.) So Lamont was quick to find merit in Japanese claims that Manchuria

was economically indispensable, lay well within her sphere of influence, provided a buffer against bolshevism, and had been won with Japanese blood and treasure in the Russo-Japanese War of 1905. With billions of yen invested in Manchuria and millions of Japanese living there, some nationalists saw the region as a simple extension of Japan.

In mid-1931, while the West was distracted by the Credit Anstalt failure and the sterling crisis, the Kwantung army set in motion a plot to seize Mukden and other Manchurian towns. On September 18, it launched a surprise raid against Chinese barracks in Mukden; by the next day, the city had fallen to the Japanese. As a pretext for this aggression, the Japanese military manufactured stories of Chinese assaults against the Japanese-controlled South Manchuria Railway—stories that were later exposed as fraudulent or exaggerated. Emboldened by popular support in Japan, the military flouted civilian officials, such as Inouye and Foreign Minister Kijuro Shidehara, who opposed the use of force. Japan's Foreign Office was afraid that if it tried to rein in the Kwantung Army, it might face an armed revolt in the ranks. As fifteen thousand Japanese troops swarmed across Manchuria, diplomats lamely said that the moves were temporary and that the troops would be evacuated shortly. As historian Richard Storry said, these were "weeks of public embarrassment and secret humiliation for the Wakatsuki government."[34]

Stunned by the Mukden raid, Secretary of State Henry L. Stimson swiftly protested to Japan, and Hoover later called it "an act of rank aggression."[35] Financial markets clamored for an explanation. As finance minister, the proud, dignified Inouye had to issue a statement. He was in a precarious spot, for he had spearheaded cabinet opposition to reinforcing troops in Manchuria. He was also identified with demands for cuts in the defense budget, which earned him the lasting enmity of the military (much as Dr. Hjalmar Schacht's faith in old-fashioned balanced budgets would finally doom him with the Nazis).

Inouye consoled financial markets with an amazingly artful statement about Mukden. The *New York Times* printed it verbatim on October 22 in a dispatch with a Tokyo dateline. Entitled "INOUYE SAYS JAPAN IS EAGER TO RETIRE," it became the statement that defined Japan's position for Western financial markets. Observant readers must have been struck by its clever analogies to the Panama Canal, its quoting of Daniel Webster, and its sure feel for American sensibilities:

> A clear understanding of the present state of affairs in Manchuria shows that the question is simply one of self defense. A long, narrow strip of territory, along which runs the vital nerve called the South Manchuria Railway, is and has been by treaty arrangements since the

> Russo-Japanese War of 1904-5 under the complete administration of Japan. By treaty with Russia, duly recognized and adopted by China, Japan administers this "South Manchuria Railway Zone"—polices and protects it much as the United States Government polices and protects the Panama Canal Zone.
>
> On the 18th of September last, a night attack was made on this zone by regular Chinese troops, and the railway line was destroyed. It was evidently necessary for Japan to take strong and immediate steps. When points under the protection of one's army are invaded by regular troops, and the extent of the threatened invasion is utterly unknown, the obvious means of self defense is to proceed at once to the headquarters of the offending troops. The emergency was one which, in Mr. Webster's classic words, was 'instant, overwhelming, leaving no choice of means, and no moment for deliberation.'

The middle section of the statement portrays Japan as saving Manchuria from anarchy. It brushes aside as "minor military measures" the actions taken at Mukden. The closing is forceful:

> In the final analysis, there is nothing in the situation that should create a war and the whole affair has been magnified beyond reason in being deemed an actual danger to the peace of the world. The Japanese, as repeatedly stated, have no intention whatsoever of making war on China. On the contrary, the Japanese Government and people entertain the friendliest feelings towards the Chinese. They are probably more anxious than any other nation of the earth could possibly be, to maintain friendly relations with the Chinese.[36]

The press release was actually drafted by Tom Lamont. It was issued, with only cosmetic changes, by Japan's Ministry of Finance. (The preceding is quoted from the original in Lamont's files.) The Japanese wanted Lamont to release the statement himself, but he replied that Morgans would be thought biased and might offend the Chinese—an understatement. Perhaps he also feared his reputation among American liberals would be blackened by any revelation of his authorship; as a former champion of the League of Nations, he probably didn't want to side publicly with an aggressor. To assuage the Japanese, he explained that if Inouye "will let me know what day he plans to issue the statement, I will arrange to have it gain extra publicity here."[37]

Lamont now found himself in stark opposition to Washington's policy and faced the dilemma always latent in his role as a banker *cum* diplomat. Why did he conspire with a foreign power in a military action condemned by the U.S. government and the League of Nations? Could he have accepted, at face value, Japan's story about Manchuria? Reporters in China pointed out that

versions of the Mukden incident originated with Japan's military and were suspect. There were also widespread suspicions of a staged incident, a premeditated invasion. As the London *Times* said on September 21, the Japanese army, three days before taking Mukden, had conducted "something like a dress rehearsal" for the invasion, and "though it is reported that the incident of the South Manchuria Railway was the cause of the developments, the truth is that the whole movement was on foot before the alleged incident occurred."[38] There was, in short, plenty of evidence to give a reasonable man pause. Add to this the clear public impression that the cabinet was being duped by the army, and Lamont's alacrity is puzzling.

Cynicism toward China certainly explains much of the Morgan sympathy for the Mukden attack. Russell Leffingwell, in a hot-blooded letter to Walter Lippmann, said the indignation over Mukden was entirely misplaced. "It is grotesque for the League or for America to interfere on the side of Chinese raiders and revolutionaries, who have kept their people in war and fear and misery all these long years; and on the side of red Russia; and against the side of Japan, who in pursuance of her treaty rights has been keeping order in Manchuria and maintaining the only safe-asylum open to the fear-ridden Chinese." He hoped the Japanese would "thumb their noses" at any League of Nations or U.S. protest against its action.[39]

Along with his secret work for Mussolini, the Mukden incident is probably the most disturbing episode in Lamont's career (although nobody knew about it then). Was he trying to impress the Japanese with elite Morgan services? Or was he simply trying to maintain the value of Japanese securities? He undoubtedly wanted to shore up Inouye's tenuous position in the government. The finance minister had to demonstrate to the military that he wouldn't betray or work against it. In fact, in November, Lamont warned the Japanese that if Inouye were expelled from the cabinet—as the military favored—there would be a "distinct chill" on Wall Street and in the City.[40] But if Inouye felt a need to appease the military, why did Lamont join him?

As with Mussolini, Lamont was going beyond public relations to something approaching propaganda for a foreign power. It was a strange new application of the Gentleman Banker's Code of absolute loyalty to one's clients. Any banker could underwrite securities, but only Lamont could lobby politicians, shape newspaper editorials, and sway public opinion. The Mukden press release exposed the dangers in having bankers act like politicians and adopt the same proprietary feeling toward foreign governments as toward industrial concerns. It pointed up the perils of blurring politics and finance in the Diplomatic Age.

If Lamont were truly taken in by Mukden, then he was soon rudely stripped of his illusions. In December 1931, a less liberal Japanese cabinet took power,

and Inouye was replaced by Korekiyo Takahashi, who promptly took Japan off the gold standard. In late January 1932, the world was horrified by Japanese bombing of Chinese civilians in thickly populated suburbs of Shanghai. Once again, the Japanese blamed Chinese provocation. The terrorist tactics were far more naked than those used in Mukden, and the evidence of brutality more graphic and abundant. Newsreels brought shocking pictures of the carnage into American movie theaters. Lamont was so dismayed he told his friend Saburo Sonoda of the Yokohama Specie Bank that Japan could no longer raise money in American markets—so ghastly was the impression left by Shanghai.[41] For the House of Morgan, Shanghai initiated a slow process of disenchantment. A chastened Leffingwell wrote to Teddy Grenfell, "I confess to having had a good deal of sympathy with the Japanese in Manchuria, though none at all with the Japanese at Shanghai."[42]

Now Lamont was to absorb one stunning blow after another. Right-wing terrorism—which had already claimed the life of Prime Minister Hamaguchi in a 1930 shooting—turned on the world of finance. One by one, Lamont's Japanese friends were killed. During the Shanghai fighting in February, he received a telegram from Sonoda that said: "WITH SORROWING HEART INFORM YOU OF ASSASSINATION AND DEATH OF MR. I. INOUYE IT SEEMS [AS] IF A GREAT LIGHT HAS BEEN EXTINGUISHED AND MY DEAR COUNTRY IS FALLING INTO DARK DAYS."[43]

Inouye, sixty-three, was in the midst of a general-election campaign. As leader of the Minseito, he was expected to become the next prime minister. As he stepped from his car at a suburban Tokyo school, a twenty-two-year-old rural youth stepped from the shadows in a tattered kimono and black felt hat. He shot Inouye in the chest. The assassin was a member of the secretive, superpatriotic Blood Brotherhood, a group of fanatic young nationalists. At the police station, he boasted of his deed and blamed rural poverty on Inouye's deflationary policies. Speaking to reporters at the Imperial University Hospital, Inouye's somber, dry-eyed widow explained that she had readied herself for this moment while her husband was in the cabinet.

Lamont was profoundly upset; after all, it was Inouye who gave him hope that the old illustrious families and their liberal allies could keep militarism at bay. He wrote a touching letter of condolence to his friend Sonoda: "Such a gentle soul he was—it seems the more inexplicable that his end should be like this."[44]

The more Lamont resisted the truth about Japan, the more forcibly it intruded. A few weeks after Inouye's assassination came the murder of Lamont's other major Japanese friend, Baron Takuma Dan, the MIT-trained mining engineer and chief executive of Mitsui, who had hosted him at his villa in 1920. Baron Dan was shot as he emerged from his car at the white marble Mitsui Bank. Again the assassin was a rural youth and was apparently

also a member of the Blood Brotherhood. Lamont wrote to Baron Dan's family, recalling the 1920 trip: "I had thought at times of him as a poet in business and this impression came to me as he showed me his house and garden and we stood together looking at Fujiyama, a majestic picture towering above a superb landscape."[45]

Baron Dan's killing was an act of revenge against the House of Mitsui, which rightists had accused of treacherous profiteering in the so-called dollar-buying scandal. After England left the gold standard in September 1931, Mitsui and other *zaibatsu* banks expected the yen to be forced off gold, too, an effective devaluation. So they furiously sold yen and bought dollars. These foreign-exchange transactions netted Mitsui an estimated $50 million. But they also triggered a patriotic uproar about banks speculating against their country's currency. The issue proved an emotional one during the 1932 election. In the growing atmosphere of political extremism, many Japanese sympathized with Inouye's and Baron Dan's assassins, who received lenient sentences. Both were released from prison within a few years.

Lamont didn't readily admit error and didn't know how to abandon clients. By now, the strong rightward shift of Japanese politics was evident. The Kwantung army had overrun Manchuria, creating the puppet state of Manchukuo in March and installing Pu Yi, the last Manchu emperor, as its pliant figurehead. The incident at Mukden, the bombing of Shanghai, the murders of Inouye and Baron Dan—these events should have opened Lamont's eyes. He could no longer plead ignorance. His files from early 1932 do reveal a deep displeasure with the Japanese as he warned them not to repeat the Shanghai error, which had destroyed any sympathy they still had on Wall Street.

Nevertheless, that spring, in a bizarre turn, Lamont and Martin Egan drifted back to a pro-Japanese stance. The two had become close friends with Count Aisuke Kabayama, who had been educated at Princeton, was married on Long Island, and was close to Emperor Hirohito. Kabayama's grandfather had been an admiral and a governor of Taiwan. Lamont and Egan encouraged him to set up a Japanese information bureau in America on the Mussolini model and proudly briefed him on their Italian work. In the late spring, Egan went to Japan for talks about Manchuria. When he returned talking about "banditry and disorder in Manchuria" and blaming China for hostilities, he sounded like a Japanese militarist.[46]

The House of Morgan no longer knew which master it served—America or Japan. A few days later, on May 15, 1932, another political murder blackened Japan's image: the aging prime minister, Tsuyoshi Inukai, was gunned down in his official residence by nine young army officers, probably because he wanted to curb the military. He was replaced by Admiral Makoto Saito. It

would be the end of party government in Japan until after World War II.

In the fall of 1932, Lamont had to confront the unpleasant truth about Mukden, the knowledge that his press release for Inouye had been a hollow piece of propaganda. The League of Nations had dispatched an investigative commission to the Far East under Lord Lytton. Even before the Lytton report was endorsed by the League, Lamont's assistant, Vernon Munroe, dined one evening with General Frank McCoy, the commission's American member. The next morning, Munroe told Lamont, "The General said there was a grave question as to whether there was any explosion, that the Japanese had never been able to explain how the regular trains continued to run immediately after the explosion was supposed to have taken place and the more they had explained the more of a contradiction they had gotten into."[47] A month later, the Lytton report condemned Japanese aggression as violating the League's Covenant and branded Manchukuo a puppet state. Although the report was critical of Chinese provocations, Japan walked out of the Assembly of the League and brazenly tightened its grip on Manchuria.

By this point, Lamont was in a quandary. He wanted to maintain a belief in Japan's good intentions amid overwhelming, contradictory evidence. To sort out his feelings, he sat down and wrote a memo marked "Secret and Strictly Confidential." Whether he ever circulated it is uncertain, but it shows a man fleeing reality. "These are entirely my private thoughts," it starts out, then continues, "American suspicions as to Japan's motives are essentially these: that Japan has aggressive designs on the Asiatic Continent and that Japan may even be courting war with the United States—which are not true." To correct such misconceptions, he recommends a joint U.S.-Japanese declaration on trade and peaceful relations. The conclusion is a desperate pipe dream: "If such a joint declaration can be made, all war talk will immediately be silenced, the psychology of men will undergo a change and whatever question may arise between our two countries will become capable of an easy solution."[48]

It became progressively more difficult for Lamont to sustain any belief in Japan's imminent return to civil government. As lords of Manchukuo, the army built huge dams and industries to strengthen the nation's preparedness for war. The new finance minister, Takahashi, known as the Japanese Keynes, boosted military spending to almost half the Japanese budget. The liberalism of the twenties, along with its foremost exponents, was dead.

In 1934, Lamont underwent a sudden change of heart. Once his eyes were open, he felt fooled, and his trust turned to bitterness. He cut off subscriptions to Japanese cultural groups, snubbed visiting Japanese dignitaries, and warned Japan's consul general that the Japanese should not mistake America's peaceful spirit for cowardice. When he heard rumors that the British cabinet

might renew an alliance with Japan, he lobbied against the move. He sent an impassioned letter to Grenfell, which he expected to be passed around Whitehall: “In place of the fair liberal government that existed in the first twenty years of this century there has arisen a military clique which . . . if accounts from the liberal elements in Japan are true, have been conducting itself a good deal as a lot of the young German Nazis have been conducting themselves.”[49]

The Japanese army would continue to annex parts of northern China, a campaign that in 1937 would culminate in the Sino-Japanese War and the butchering of tens of thousands of Chinese civilians in the rape of Nanking. It was a dismal, ironic denouement to Morgan involvement in China, which began with Willard Straight’s dream of America acting as a buffer against Japanese encroachment in Manchuria and ended with a senior Morgan partner serving as apologist for that very action.

CHAPTER EIGHTEEN
MIDGET

THE Wall Street of 1932 was a dismal ghost town. Securities firms declared "apple days"—unpaid vacation days each month that enabled destitute brokers to go out and supplement their income by selling apples on the sidewalk. Apple vendors appeared at the Corner. Downtown real estate was so depressed that building companies defaulted; astute investors who bought their bonds became the future owners of Wall Street. The misery extended everywhere. Riverside Park was lined with Hoovervilles, and sylvan retreats in Central Park looked like ragged hillbilly hollows. On Park Avenue, ten-room apartments that had been occupied by financiers of the twenties now lacked tenants. The new, half-occupied Empire State Building was mocked as the "Empty State Building."

For aristocrats in private clubs, it was a time of often macabre mirth. The Union League Club had a room wallpapered with stock certificates that were rendered worthless by the crash. (They were peeled off by itchy fingers when the market recovered.) After falling for over two straight years, the stock market hit bottom on July 8, 1932. By that point, two thousand investment houses had failed, and new underwritings stood at 10 percent of their 1929 peak volume. On the Stock Exchange floor, listless traders invented games to kill time. Big Board seats that fetched $550,000 before the crash now sold for as little as $68,000. The major financial work was refunding old bonds at lower interest rates.

In 1932, almost thirteen million of America's 125 million people were unemployed. Two million roamed America searching for work, boarding boxcars and sleeping in hobo camps. Hoover refused to renounce economic orthodoxy and mount a vigorous attack on the Depression. Sometimes he flirted with fanciful solutions to America's despondency. At various times, he thought America needed a good laugh, a good poem, a good song. He even approached Will Rogers about writing a good joke to end panic hoarding. Hoover himself wore a funereal expression. Of a White House meeting with him, Secretary of State Henry Stimson said, "It was like sitting in a bath of ink." And sculptor Gutzon Borglum remarked, "If you put a rose in Hoover's hand it would wilt."[1] Hoover had a way of minimizing the nation's suffering. In 1932, he insisted, "Nobody is actually starving. The hoboes, for example, are better fed than they have ever been. One hobo in New York got ten meals

in one day."[2]

That spring, Jack Morgan was briefly roused to a rare act of public activism. A believer in self-reliance, he cited as his favorite biblical text Ezekiel 2:1: "And he said unto me, Son of man, stand upon thy feet, and I will speak it unto thee."[3] Jack construed this as God clucking his tongue at the welfare state. He preached the old-time religion, telling the marquess of Linlithgow that honesty, integrity, and economy were "the real solution of our troubles, most of which, in my opinion, come from greed. "[4] He rallied to Hoover's plea for private benevolence instead of government intervention. In March 1932, he participated in a fundraiser for the Block Community Organization of New York. Dressed in dinner jacket at his Murray Hill mansion—with butler Henry Physick and other servants listening at a rear-hall receiver—he broadcast a radio appeal for help. "We must all do our bit," he said, endorsing a plan by which workers contributed small weekly sums to a fund for the jobless. A shy man who dreaded public appearances, Jack's cooperation reflected a fearful mood among the rich. Lamont, meanwhile, helped the Red Cross raise money for farmers victimized by the Midwest drought.

An outdated allegiance to classical economics tipped a postcrash recession into seemingly insoluble depression. In late 1931, Federal Reserve Banks hiked up their discount rate by 2 percentage points in two weeks. To balance the budget, the Federal Revenue Act of 1932 almost doubled tax rates—again, the perfect medicine to kill the patient. Not everyone at Morgans automatically resisted experimentation. Throughout 1932, Russell Leffingwell, the resident Democratic iconoclast and self-styled curmudgeon, laughed at those who feared inflationary spending as "people who in an Arctic winter worry about the heat of the tropics."[5] Yet Leffingwell's own views spun like a weathervane in a high gust, and at moments he reverted to budget-balancing orthodoxy. He told Walter Lippmann that a public works program would only prolong the Depression, and he doggedly maintained the need for the gold standard.

The major Hoover policy initiative of 1932, the Reconstruction Finance Corporation, was a major boon to Morgan interests. It was set up to make loans to banks, railroads, and other hard-pressed businesses. The previous year, Lamont had told Hoover that the plight of America's railroads was "the principle impediment to domestic recovery." The railroads were burdened with debt from the twenties and couldn't service their bonds. When the Van Sweringens defaulted on their secret rescue loan in 1931, Morgans and Guaranty Trust invited the brothers in for a frank chat, telling them that "we are, in effect, the owners of all of their properties."[6] So the bank dropped its usual objections to government bailouts when it came to railroads. Oris Van

Sweringen said that he and Mantis were "on the doorstep waiting for them [the RFC] to open."[7] The Van Sweringens borrowed $75 million from the RFC, strengthening the case of those who saw it as a welfare agency for the rich.

Hard times didn't touch the splendor of top-drawer Morgan partners. If their drawing rights from the bank—that is, their annual percentage take as partners—were halved, they still had wealth left from the twenties. The main problem was enjoying it free of guilt. What would Jack do with his new *Corsair*, big enough to house a small village of hoboes? He decided, for decency's sake, to mothball it for a while, telling Cosmo Lang, the archbishop of Canterbury, "It seems very unwise to let the 'Corsair' come out this summer. There are so many suffering from lack of work, and even from actual hunger, that it is both wiser and kinder not to flaunt such luxurious amusement in the face of the public."[8] He offered to charter the boat to John D. Rockefeller, Jr.

With over $20 million in his partnership account, Tom Lamont had time to catch up on travel. Where Jack liked to sail with bishops and surgeons, Lamont preferred the company of writers, intellectuals, and socialites. In the spring of 1931, he and Florence went on a leisurely Aegean cruise with Walter Lippmann and his wife, and classics scholar Gilbert Murray. They were joined in Athens by the John Masefields. There are photos of this Depression party aboard the *Saturnia*. One shows Lamont in a double-breasted suit with pocket handkerchief and a jaunty striped vest. His shrewd eyes crease into crow's-feet as he gazes into the camera. Small and balding, he has appraising eyes, sympathetic but vigilant, that seem to take in everything. In another photograph, taken at the captain's table, the group is elegantly erect. Walter Lippmann looks dashing, while Lamont peers attentively down the table. Dining in this wood-paneled interior, with its fresh table linen, the group has a glitter that is remote from the American dreariness of the moment.

The Lamonts arrived at Patras with forty-two pieces of luggage. The Greeks treated them as visiting foreign dignitaries and followed protocol carefully. The provincial governor carried Florence's hatbox ashore while a Greek cabinet representative (probably wondering to what depths he had sunk) inspected every toilet on their hotel floor. Tom and Florence Lamont liked to affect a bohemian innocence. During this idyllic trip, Florence reported, "We almost always have a picnic luncheon because the hotels are most of them so bad. We sit in the sun and read poems about Greece after luncheon."[9]

If the Morgan world seemed to survive the Depression intact, the surface was deceptive. Between 1929 and 1932, the bank saw its net worth—its basic

capital cushion—drop with frightening speed, from $118 million to half that before Hoover left office. Total assets plunged from $704 million to $425 million. Even for the House of Morgan, these were staggering blows. The real casualties were junior partners, who shared in the losses without having reaped the spectacular bull market profits. The bank still recruited based on talent. As an official Morgan history says, "The alternative of seeking additional capital by recruiting new partners with more money than talent, thereby diluting the quality of the firm, was deemed unacceptable."[10]

The House of Morgan retained Pierpont's paternalism. When salaries were slashed by as much as 20 percent, the staff was told these cuts would be restored before partners resumed full drawing rights from their capital accounts. When the bank closed its employee dining room, it distributed cash allowances for lunch. Staff families also got two free weeks each year at a rustic Morgan camp in Maine. For the Morgan Grenfell staff, the Depression *ennui* was partly lifted by Jack's gift of a sports ground in Beckenham, with a cricket pitch, hard tennis courts, trimmed lawns, and a tea pavilion. These touches inspired fierce loyalty and a cultlike intimacy among employees. Their Depression suffering, if real, was extremely modest compared with the unspeakable suffering beyond the marble walls.

LET us consider 1932 politics, for the events that led to the Glass-Steagall Act—the Banking Act of 1933—and the division of the House of Morgan were rooted in that year. It was Herbert Hoover who first waged war on Wall Street and prompted hearings that led to new banking legislation. There had always been a slightly paranoid edge to Hoover's dealings with his Morgan friends. After staying at the White House in the summer of 1931, Dwight Morrow told Lamont that Hoover was blue and felt "he had been trying to carry out the views of the banks here in New York and yet had got rather cold comfort from them."[11] Lamont sent Hoover a note to cheer him up, yet there was an undercurrent of uneasiness in his relations with the president.

Hoover's relationship with the House of Morgan dated back to his days as a mining engineer. In 1917, he acted as intermediary between Sir Ernest Oppenheimer, who wanted to take public his Johannesburg gold-mining group, and Morgans. To consolidate his new Wall Street tie, Oppenheimer insisted on the word *American* appearing in the new company's name. Thus was born the Anglo-American Corporation, afterward Africa's richest company. Evidently Lamont thought this would inaugurate a series of mining ventures tapping Hoover's talents. As he told Morgan Grenfell, the Anglo-American deal was "part of a comprehensive plan involving association with Mr. Hoover in mining ventures generally."[12] But Hoover reneged on the deal, and Lamont later applauded Oppenheimer for ousting Hoover and engineer

William Honnold. “We never shall have any quarrel with [Oppenheimer] in regard to his feeling about Honnold and/or Hoover,” Lamont informed London.[13]

Beyond this history, Morgans and Hoover were doomed to have policy quarrels. Hoover felt straitjacketed by a Congress that cared little for Europe’s troubles, favored buy-America campaigns, and lacked interest in inheriting economic leadership from Britain. The House of Morgan, in turn, had European clients to protect, and its internationalism was no less problematic for Hoover than for his Republican predecessors. There were also clashing personal styles: Hoover was brusque and humorless, while Morgan partners were silky aristocrats.

In July of 1932, it looked as if the world economy might finally cast off the twin burdens of German reparations and Allied war debt. At Lausanne, European leaders reached a gentleman’s agreement that effectively ended the debt charade; if they could stop paying off war debts, they would stop asking for reparations. Lamont was jubilant, seeing this as an end to the economic warfare that had been waged since Versailles. He dispatched Martin Egan to the White House, not to advise Hoover to cancel the war debts outright but simply to reexamine them.

Returning from Washington, Egan said he had never seen the president so emotional about an issue. He had made a speech full of anger, self-pity, and impotent frustration. “Lamont has this matter all wrong,” Hoover had insisted, echoing widespread public sentiment. “If there is one thing the American people do not like and will not stand for it is a combination of this kind against them. . . . Lamont cannot appreciate the rising tide of resentment that is sweeping over the country. . . . They are trying to ’gang’ us. . . . Maybe they have settled German reparations but they did it the worst damned way they could.”[14] He wouldn’t extend his one-year debt moratorium and rejected French and British proposals for deferring upcoming payments; he forced France to default. So on the eve of Hitler’s advent, the Allies were squabbling over moldy financial issues that had bedeviled them for years.

The Morgan-Hoover feud over debt was mild compared with their debate over short selling on Wall Street. Moody and isolated, taciturn and stony-faced, Hoover now shared the average American’s view of Wall Street as a giant casino rigged by professionals. He saw the stock market as a report card on his performance, and it showed consistently failing grades. He came to believe in a Democratic conspiracy to drive down stocks by selling them short —that is, by selling borrowed shares in the hope of buying them back later at a cheaper price.

The “bear raiders” first achieved notoriety in the 1930 suicide market. The master was Bernard E. “Sell-’Em Ben” Smith, a twenties pool speculator who

was trounced by rising prices in 1929. That October, he suddenly came into his own and whooped it up on the day of the crash, shouting "Sell 'em all! They're not worth anything."[15] Such tales convinced Hoover of malevolent forces at work in the market. He began to compile lists of people in the bear cabal and even claimed to know they met every Sunday afternoon to plot the week's destruction![16] Hoover's obsession was fed by confidants. Senator Frederick Walcott of Connecticut told Hoover that Bernard Baruch, John J. Raskob, and other Wall Street Democrats were planning bear raids to defeat his reelection.

Hoover thought Stock Exchange officials should openly denounce the culprits. In January 1932, he called Stock Exchange president Richard Whitney to the White House for a verbal drubbing. He said short sellers were preventing an economic rebound and warned that unless Whitney curbed them, he would ask Congress to investigate the Exchange and possibly impose Federal regulation. Whitney refused to admit any danger in short selling. Privately Morgan partners mocked Hoover's obsession as absurd and fantastic, but they couldn't dissuade him from his vendetta.

Although fearing that public hearings would dredge up "discouraging filth" and sabotage recovery efforts, in 1932 Hoover asked the Senate Banking and Currency Committee to start an inquiry into short selling. Wall Street bankers were so upset that Lamont lunched at the White House with Hoover and Secretary of State Stimson, trying to spike the inquiry. Hoover said destructive short sellers had offset his beneficial measures, a remark that led to a heated exchange about the hearings. "I tried to make clear to the President that if such an enquiry was encouraged to run riot it would create nothing but uneasiness throughout the country and would help to defeat the very constructive ends to which he was leading us," Lamont said.[17]

In April, the first witness was Richard Whitney, who called Hoover's charges "purely ridiculous." Even as the hearings commenced, Hoover and Lamont were secretly trading barbed remarks about short selling. Hoover blamed the bears for everything—low public confidence, business stagnation, and falling prices. Lamont's reply was candid to the point of comic cruelty. Responding to Hoover's contention that "real values" were being destroyed by bear raids, he asked, "But what can be called 'real value' if a security has no earnings and pays no dividends?"[18] He blamed 99 percent of the market's decline on poor business.

The press had a dandy time ridiculing the Senate bear hunt, which never unearthed a Democratic conspiracy. Nevertheless, at the end of April, a subcommittee broadened the hearings to include pools and market manipulations of the 1920s. The machinations of the RCA pool were unfolded before the public. Walter E. Sachs of Goldman, Sachs had to explain the

losses of Eddie Cantor and forty thousand other investors in the Goldman Sachs Trading Corporation. Something curious now happened: as the hearings shifted from present to past, memories of the crash grew in the public mind. At first, Main Street smirked at the crash as a Calvinist thunderbolt hurled at big-city sinners. Only now, when the crash was seen as a forerunner of depression, did public rage against the bankers crystallize.

Amid the controversy, Hoover had to deal with a serious slump in the bond market—where short selling was prohibited. Corporate America couldn't cope with the debt accumulated in the 1920s, much of it to finance takeovers. Many bonds defaulted and in extreme cases dropped 10, 20, or 30 points between sales, threatening the banking system. If savings banks couldn't cash in bonds, they might have no money to pay off depositors, possibly causing runs and failures. The upshot was a Morgan-led operation to halt the bond market slide. Thirty-five banks pledged $100 million to buy high-quality bonds in a pool nicknamed the Stars and Stripes Forever. It was chaired by Lamont, who sported more titles than the mikado during this period. The bank touted the patriotic nature of the venture, but it was again that Morgan specialty—public service for profit. The bank considered bonds seriously undervalued and had excess cash on hand during the Depression. "If the organization of the Corporation . . . should have any degree of reassuring effect upon the public so much the better," J.P. Morgan and Company told the Paris partners.[19]

Lamont kept Hoover posted on the pool. In the bond market operation, some cynics spied a move to improve Republican prospects in the fall election—as if Hoover would field his own hard-charging bulls against the bears. If so, the strategy almost backfired on Hoover. Lamont used the pool as a bargaining chip and threatened to disband it unless the short-selling hearings were canceled. In the end, the pool went ahead and made a tidy profit. The hearings would drag on and eventually assume dimensions unforeseen in early 1932. They would finally take their name from a new subcommittee counsel, Ferdinand Pecora, appointed in January 1933. The Pecora hearings would lead straight to Glass-Steagall and the dismemberment of the House of Morgan.

IN the autumn of 1932, Hoover presided over one last humiliation—a nationwide banking crisis. Three years of deflation had eroded the collateral behind many loans. As banks called them in, the business slump worsened and produced more bank runs and failures. Before 1932, the thousands of bank closings were mostly confined to small rural banks. Then, that October, Nevada's governor shut the state's banks. There followed a frightening crescendo of state bank closings—euphemistically called holidays—climaxed

by an eight-day closing of Michigan banks in February. The contagion spread so fast that thirty-eight states had shut their banks by Roosevelt's inauguration.

Between the November election and the March 1933 inauguration was a time of paralysis and glowering hostility between Hoover and Roosevelt. Irritated, beleaguered, and resentful, the president refused to undertake new initiatives without Roosevelt's cooperation; Roosevelt, on the other hand, wanted to wait until he assumed full power. For the House of Morgan, it was a season of peril. Through three consecutive Republican terms, it had probably enjoyed better access to Washington than any other bankers in American history. Under Hoover, the president was a telephone call away. Sometimes Morgan power had seemed as awesome as crude left-wing propaganda would have it. Now the bank combated threats to its survival as the political wheel came full circle.

As early as 1929, Hoover advanced the idea of separating commercial and investment banking, a notion that now took hold. It appeared in a banking bill introduced by Senator Carter Glass as early as 1930 and formed part of the Democratic party platform in 1932. During the campaign, Roosevelt blamed Hoover for the speculative binge of 1929 and the spate of foreign loans that left a bloody trail of defaults. After Bolivia became the first Latin American debtor to default in 1931, nearly every Latin American government followed suit.

After Hoover's "bear raid" crusade, the president's departure wasn't mourned at the Corner. Russell Leffingwell and Parker Gilbert formed a Morgan minority that voted for Roosevelt. "The truth is," Leffingwell confessed to Walter Lippmann, "I can't bring myself to vote for a desperate man who wishes to continue desperate remedies for a desperate situation."[20] Nor was it self-evident that FDR would emerge as an enemy. Genial and aristocratic, he chastised Hoover as a big spender and advocated balanced budgets; he looked more bland than bold. Leffingwell almost patronized Roosevelt, calling him "a pleasant, kindly, well-meaning chap with a pleasing smile."[21]

Socially, FDR fit the Morgan mold far more than Hoover. Leffingwell—who knew Roosevelt from his own Treasury days, when Roosevelt was in the Navy Department—excitedly set down his pedigree for Vivian Smith of Morgan Grenfell. He noted Roosevelt's Groton and Harvard education, his Hudson River upbringing and old New York Dutch ancestry, and his employment at the Wall Street firm of Carter, Ledyard, and Milburn, which defended corporate clients against antitrust actions. Leffingwell ended sarcastically, "All that is the background of the man who is a peril to American institutions according to Hoover the foreign mining engineer."[22]

Lamont also knew Roosevelt, having rented his East Sixty-fifth Street house. Before the inauguration, he phoned him and busily dashed off "Dear Frank" letters.

If the winter interregnum suggested possible good relations, there were also warning signs. Late in the summer of 1932, Leffingwell and Roosevelt had an exchange that previewed, in miniature, the titanic feud to come. In August, Leffingwell sent "Frank" a note deriding the banking reforms being advanced by Carter Glass; in it, he tried to strike a note of camaraderie and shared values: "You and I know that we cannot cure the present deflation and depression by punishing the villains, real or imaginary, of the first post-war decade, and that when it comes down to the day of reckoning nobody gets very far with all this prohibition and regulation stuff."[23] Far from indulging Leffingwell, Roosevelt threw cold water in his face: "I wish we could get from the bankers themselves an admission that in the 1927 to 1929 period there were grave abuses and that the bankers themselves now support wholeheartedly methods to prevent recurrence thereof. Can't bankers see their own advantage in such a course?"[24] It would be the tragedy of the House of Morgan that it couldn't see the advantage in such a course. The public demanded a *mea culpa* for 1929, which the bankers wouldn't provide. As Leffingwell told Roosevelt, "The bankers were not in fact responsible for 1927-29 and the politicians were. Why then should the bankers make a false confession?"[25] Yet such was Leffing-well's disgust with Hoover's tariffs, isolationism, and reparations policy that he gladly voted for FDR.

The bank campaigned to slip Leffingwell into a Treasury post, which became a litmus test of Roosevelt's financial soundness. All aflutter, Monty Norman told Lamont, "I shall wait to hear that R.C.L. is established before I can rest happily."[26] When Senator Carter Glass was approached about taking the Treasury secretary job again, he said he would want to hire two Morgan men and former deputies: Leffingwell and Parker Gilbert.[27] Walter Lippmann joined the bandwagon, but Roosevelt cringed: "We simply can't tie up with 23."[28] The shorthand betrayed a knowingness that would work to the bank's disadvantage. Despite his failure to get a Treasury post, Leffingwell would remain a trusted friend and adviser of Roosevelt's and something of a black sheep on Wall Street for his partial support of the administration.

The person who probably shot down Leffingwell's trial balloon was Ferdinand Pecora, the fifty-three-year-old former assistant district attorney from New York, who took over the Senate's Wall Street probe in January 1933. Smoking a blunt cigar, his shirtsleeves rolled up, the hard-bitten Pecora captured the public's attention. For six months, the hearings had been stalled. Republicans and Democrats, with fine impartiality, had feared fat cats of both parties might be named and united in a conspiracy of silence. With Pecora as

counsel, the hearings acquired a new, irresistible momentum. They would afford a secret history of the crash, a sobering postmortem of the twenties that would blacken the name of bankers for a generation. From now on, they would be called banksters.

Even before Roosevelt's inauguration, Pecora turned his investigative spotlight on the National City Bank, showing eminent bankers in sordid poses, particularly the bank's head, Charles E. Mitchell, a member of the Black Thursday rescue squad. Through Pecora, the public got a view of bankers scheming while supposedly protecting the public. Pecora revealed that the $12-million Morgan loan to preserve National City's merger with the Corn Exchange Bank had represented more than 5 percent of Morgans' net worth, sticking the bank with a substantial loss. It was also disclosed that to buffer crash losses at National City, one hundred top officers had borrowed $2.4 million, interest free, from a special morale loan fund—loans never repaid.

Pecora also studied the operations of the National City Company, whose 1900 salesmen had unloaded risky Latin American bonds on the masses. It emerged that in touting bonds from Brazil, Peru, Chile, and Cuba to investors, the bank had hushed up internal reports on problems in these countries. After bank examiners criticized sugar loans made by the parent bank, the securities affiliate sold them as bonds to investors, an example of how commercial banks might palm off bad loans through securities affiliates. Pecora cited the case of an Edgar D. Brown of Pottsville, Pennsylvania, whose National City salesman had pushed him into "a bewildering array of Viennese, German, Peruvian, Chilean, Rhenish, Hungarian, and Irish government obligations."[29]

Another supposed hero of Black Thursday was Albert H. Wiggin of Chase, a poker-playing clergyman's son who sat on fifty-nine corporate boards. He was also exposed as being up to his ears in mischief. For six weeks in 1929, he had shorted shares of Chase stock and earned several million dollars; the speculation was backed by an $8-million loan from Chase itself. For good measure, Wiggin had set up a Canadian securities company to avoid federal taxes. The stories of Chase and National City showed the extent to which the traditional distinction between savings and speculation had disappeared in the 1920s—a distinction the Glass-Steagall Act would seek to restore.

The Pecora findings created a tidal wave of anger against Wall Street, and against this backdrop Roosevelt vetoed the Leffingwell nomination. As people followed the hearings on their farms and in their offices, on soup lines and in Hoovervilles, they became convinced that they'd been conned in the 1920s. Yesterday's gods were no more than greedy little devils. Even most of Wall Street was shocked by this phase of the hearings. Senator Burton Wheeler of Montana said, "The best way to restore confidence in the banks would be to take these crooked presidents out of the banks and treat them the

same way we treated Al Capone when he failed to pay his income tax." Even Carter Glass, a staunch Morgan friend, joked nastily, "One banker in my state attempted to marry a white woman and they lynched him."[30]

When Roosevelt took office on March 4, 1933, he ran up a flag of independence from Wall Street. That morning, Governor Herbert Lehman shut New York's banks, and Richard Whitney mounted the podium to close the Stock Exchange. The financial massacre was complete: of twenty-five thousand banks in 1929, some seven thousand had now failed. Amid this atmosphere of financial ruin, a grim Roosevelt delivered a stinging indictment of the bankers: "The money changers have fled from their high seats in the temple of our civilization. We may now restore that temple to the ancient truths."[31]

To offer advice on the banking crisis, Lamont had telephoned Roosevelt and urged him to avoid drastic measures. This counsel reflected a faith not only in market mechanisms but in political expediency. As J. P. Morgan and Company cabled London: "There is great reluctance to contemplate any form of federal action which it might be difficult later on to get rid of"[32] Roosevelt brushed aside Lamont's tepid remedies and announced a sweeping week-long bank holiday; over five hundred banks never reopened. Along with an emergency bank bill, this tough action restored public confidence and revealed a new public receptivity to emergency measures. Throughout the New Deal, the House of Morgan would repeat the same political error: it would advocate marginal reforms, which would be dismissed as self-serving. Instead of devising its own alternative reform package, it settled for scare tactics.

Despite these early Roosevelt rebuffs, Hoover's bleak record made even Morgan bankers ripe for experimentation. Jack Morgan was at first ecstatic about FDR. "Of course, it is quite possible that some of his cures may be wrong ones, but, on the whole, things were so bad that almost any cure may do some good. "[33] In correspondence from the Morgan files of March 1933, the partners sound remarkably like other frightened Americans: they, too, needed a savior. Hadn't they seen their own prescriptions fail? After Roosevelt's March 12 fireside chat and the reopening of the banks, 23 Wall reported with relief to Morgan Grenfell: "The whole country is filled with admiration for President Roosevelt's actions. The record of his accomplishment in just one week seems incredible because we have never experienced anything like it before."[34] The Stock Exchange soared and posted a 54-percent gain for 1933.

The House of Morgan couldn't see that, like a black speck on the horizon, the Pecora hearings were a hurricane heading in its direction. During this false honeymoon, the House of Morgan committed a famous act of apostasy: it

applauded Roosevelt for taking America off the gold standard in April. It was hoped this would devalue the dollar, raise commodity prices, and reverse the lethal deflation. A radical measure in ordinary times, it was less controversial in 1933. Harking back to greenback currency (currency with no metal backing) and free-silver coinage, farmers and other debtors were reviving old inflationary nostrums from the days of William Jennings Bryan. Roosevelt was under pressure to choose *some* inflationary expedient. Gold was moving abroad in large quantities, and there was fear it would contract the monetary base, feeding deflation.

The House of Morgan provided intellectual support for leaving gold. Russell Leffingwell lunched with Walter Lippmann and advised him on a newspaper column favoring an end to a rigid gold standard. Leffingwell saw the need for higher commodity prices. He also felt the downward drift of European currencies had led to an overvalued dollar, hurting U.S. exports. After lunch, Leffingwell said, “Walter, you’ve got to explain to the people why we can no longer afford to chain ourselves to the gold standard. Then maybe Roosevelt, who I’m sure agrees, will be able to act.”[35] Lippmann let Leffingwell vet the article and sharpen its fine points.

Leffingwell had great intellectual stature among the New Dealers. When Roosevelt later accused Treasury Secretary Henry Morgenthau, Jr., of sounding like Leffingwell, Morgenthau retorted, “I wish I had half his brains.”[36] One of the more radical brain trusters, Columbia professor Rexford G. Tugwell, noted Leffingwell’s influence on Roosevelt in the gold decision. “Consulting widely among New York acquaintances he regarded as public-minded—Russell Leffingwell of the House of Morgan was perhaps the most trusted—he had concluded that gold must be sequestered entirely, hoarding forbidden, and shipment abroad prohibited.”[37] The day after Walter Lippmann’s column appeared, Roosevelt publicly advocated an end to gold. Through a series of executive orders, he prohibited gold exports and hoarding. Congress in June abrogated the clause in bond issues that mandated compulsory payment in gold coin. Even Jack Morgan smilingly applauded the move. For those who remembered Pierpont’s 1895 rescue of the gold standard and Morgan efforts to put countries back on gold throughout the twenties, such statements were wondrous to behold, proof that the safe nineteenth-century world of neoclassic economics had been turned topsy-turvy.

Many financial experts were in a state of shock, as if the ship of state’s rudder had been violently torn off. Budget Director Lewis Douglas intoned, “This is the end of Western civilization.”[38] Bernard Baruch felt a similar alarm at this sudden turn in financial policy: “It can’t be defended except as mob rule. Maybe the country doesn’t know it yet, but I think we may find that we’ve been in a revolution more drastic than the French Revolution.”[39] The

perplexity was greater in Europe, where bankers wondered why the United States had cheapened its currency despite a trade surplus and an adequate gold store. When informed that Monty Norman thought the move would plunge the world into bankruptcy, Roosevelt—who called him Old Pink Whiskers—just laughed. The gold embargo showed that both the United States and England had renounced world leadership in favor of domestic ends. The world was adrift in a full-blown war of economic nationalism, fought with competitive currency devaluations.

For people schooled in the old economic verities, it was a disorienting new world. Bernard S. Carter, a Morgan et Compagnie partner in Paris, told J. P. Morgan partners how a Romanian banker walked into Morgans' place Vendôme office and launched into the following diatribe:

Here are the 3 great financial countries of the world, who have been preaching the sanctity of contracts to us ever since the war, and who have now all resorted to repudiation of one kind or another in their turn. First England goes off the gold standard, then France refuses to pay her debts to America, and now America goes off the gold standard. I guess we Roumanians are not such crooks after all![40]

By summer, Roosevelt was chiding the gold standard and other "old fetishes of so-called international bankers" and praising the brave new world of managed national currencies.[41] Although by background an internationalist and a strong supporter of the League of Nations, FDR pursued domestic recovery at the expense of global economic leadership. More cosmopolitan than Hoover, he had a vestigial fear of British finance. He ended British war-debt payments, as Leffingwell had advised, but couldn't suppress a view of British bankers as a devious bunch out to trick the Yanks. "The trouble is that when you sit around the table with a Britisher he usually gets 80$$$ of the deal and you get what's left," Roosevelt explained.[42]

So the early New Deal threatened the House of Morgan in two ways: the Pecora hearings were exposing practices that could bring fresh regulation to Wall Street. And the White House attitude toward European finance augured an end to the House of Morgan's special diplomatic role of the 1920s. After an incestuous relationship with Washington in the twenties, the bank would suffer the curse of eternal banishment.

THAT spring, FDR urged the Senate Banking Committee to adopt a broader, more amorphous mandate to investigate "all the ramifications of bad banking." It was nothing less than a license for a comprehensive inquest into Wall Street. The committee turned to private bankers—whom Pecora defined as men "who make their own rules and are not subject to examination"—with

J. P. Morgan and Company topping the list. It was too much to expect America's richest bankers to get off scot-free. What retrospective of the twenties would be complete without the bank that epitomized the decade's power? As a former Republican party chairman said, "Never before in the history of the world has there been such a powerful centralized control over finance, industrial production, credit, and wages as is at this time vested in the Morgan group."[43] It was time for Washington to storm the Bastille of Wall Street.

In Ferdinand Pecora, the committee's $255-a-month counsel, history provided a perfect foil for Morgan bankers. A Sicilian-born, anti-Tammany Democrat, he had thick, wavy black hair mixed with gray, a jaunty grin, and an assertive chin. A devoted Bull Mooser in 1912, he had switched to Wilson's progressive Democrats in 1916. As assistant district attorney in New York, he took on tough assignments—from bucket shops to crooked banks, the Police Department to bail bondsmen—posting an 80-percent conviction rate. Even when his prosecutorial manner was mild, he had a talent for taunts and withering asides. He was also fearless and incorruptible and had rejected several offers from Wall Street law firms. When he took over the Senate probe, he thought he would be through before Roosevelt took office. Instead, the investigation went on until May 1934, producing ten thousand pages of testimony that filled up eight fat tomes.

At first, the House of Morgan snickered at the Pecora hearings, seeing them as a circus. Lamont thought they were a political ploy "designed to acquaint a curiosity-loving public with the nature and extent of our own banking institutions."[44] With its fetish for secrecy, the bank tried to limit the inquiry's scope. On March 22, 1933, Lamont and counsel John W. Davis—the 1924 Democratic presidential candidate, dubbed the Morgan prosecuting attorney—visited Pecora at his shabby, temporary offices at 285 Madison Avenue. Davis had assiduously protected the House of Morgan's rights as a private bank and had written a New York State statute that exempted private banks from state inspection. Pecora was striking at an ancient privilege of gentleman bankers—keeping their capital position secret. On Davis's advice, Lamont refused to give a statement of Morgan capital, opposed examination of the bank's records, and insisted on the confidentiality of client accounts. As a close friend and near-neighbor of Jack Morgan's and a fellow vestryman of Saint John's of Lattingtown, Davis was in high dudgeon at any insinuation of Morgan dishonesty. He quickly elevated the affair into a matter of honor and constitutional rights. Two days later, he told Pecora he was "very chilly" to his request for five years of J. P. Morgan and Company balance sheets.

Along with Parker Gilbert, Lamont visited George Harrison of the New York Fed and tried to enlist his influence for withholding the annual

statements. Not only did Harrison refuse, but in his diary he registered shock at the request. Pecora interpreted the Morgan refusal to answer his questions as barefaced defiance and waged war against the bank in the press and on Capitol Hill. He got the Senate to pass a resolution enabling the committee to investigate private banking—a timely reminder to Morgans that it remained unregulated only at government sufferance. Pecora had won. For over six weeks, his sleuths worked in a room at 23 Wall, sifting through records no outsider had ever before seen. In the sole concession to Morgan eminence, investigators stopped at six each evening, while their colleagues worked until midnight elsewhere on the Street.

As bank image maker, Lamont tried to soften any impression that he was obstructing the investigation. On April 11, he wrote a clever letter to Roosevelt vowing cooperation; the bank would make political hay by yielding to the inevitable: "So far as this particular item is concerned, we haven't the slightest hesitation at any time in showing our balance sheet to members of the Committee, and I may add that I think you would regard it as a highly satisfactory one."[45] This last remark alluded to shared values, as if Lamont were reminding Roosevelt of his patrician background.

Jack Morgan was especially enraged by Pecora. He believed implicitly in Morgan integrity and interpreted any investigation, by definition, as a vendetta. He unpacked a colorful array of ethnic epithets; at age sixty-six, he wasn't about to learn tolerance. Pecora was degraded to a "dirty little wop," "a sharp little criminal lawyer," and "a 2nd-rate criminal lawyer."[46] It never occurred to Jack that Pecora might uncover anything amiss; he, too, thought the hearings were cooked up to pander to public voyeurism. He told the marquess of Linlithgow: "The risk of finding anything crooked in our affairs, honestly looked at, is nil; but it is taking a large part of the time of all the partners, and one whole firm of lawyers, to go through all the bank history and get ready to answer [the committee's questions]."[47] Lamont told his friend Lady Astor that he deplored the "Spanish Inquisition" in Washington and the conduct of the "young native Sicilian counsel, Ferdinand Pecora."[48] With such an inflated sense of virtue, the Morgan partners marched blindly into the hearings.

As the partners prepared for their May appearance, the hearings took on a new urgency. Sponsored by Senator Carter Glass of Virginia and Representative Henry Steagall of Alabama, a bill was working its way through Congress to separate commercial and investment banking. This would force large commercial banks to give up their securities affiliates; deposit-and-loan business would be severed from securities work. The political movement to punish Wall Street was becoming a juggernaut. Nobody had expected securities reform to dominate the early New Deal. But Pecora's

sensational findings pressured the Roosevelt administration to take action against Wall Street.

Amid an upsurge of populist feeling in 1933, demagogues of the left and right found the House of Morgan a convenient idol to smash. Responding to the Pecora inquiry, Louisiana's Huey P. Long gave a speech entitled "Our Constant Rulers." In it, he argued, against all evidence, that Roosevelt had stacked the Treasury Department with Morgan men. Roosevelt, claimed Long, was no less beholden to 23 Wall than Hoover: "Parker Gilbert from Morgan & Company, Leffingwell . . . what is the use of hemming and hawing? We know who is running the thing."[49]

Threats to the bank went far beyond redneck demagogues or professors in Roosevelt's brain trust: they came from the banking community itself. In 1930, the Chase bank had merged with the Equitable Trust to form the world's largest bank of its time. Winthrop W. Aldrich, a brother-in-law of John D. Rockefeller, Jr., had succeeded the disgraced Albert Wiggin as Chase president in early 1933 and wanted to refurbish the bank's image. To this end, he got behind the push to divide commercial and investment banking. In March 1933, he took steps to spin off the Chase securities affiliate, Chase Harris Forbes. Similarly, James Perkins, who succeeded Charles Mitchell at National City, believed that its reckless stock affiliate had nearly ruined the bank, and he, too, favored a sequestration of financial functions. The bankers' unity of the 1920s was breaking down into furious backbiting and jockeying for advantage. According to Arthur Schlesinger, Jr., "Aldrich's action was interpreted as a Rockefeller assault on the House of Morgan; and for a time he achieved almost the dignity of a traitor to his class." The counterattack came from William Potter of Guaranty Trust, who criticized Aldrich's proposals as "quite the most disastrous . . . ever heard from a member of the financial community."[50] This division within the realm of banking sped the passage of the Glass-Steagall Act.

The House of Morgan was the first private bank investigated by Pecora. After three months of nonstop preparation, the Morgan entourage swept into a $2,000-a-day suite of rooms at the Carlton Hotel attended by a small army of Davis, Polk lawyers. Jack was to be the first witness. The night before, John Davis rehearsed him with biting questions. Believing that Pierpont's arrogance before the Pujo Committee had harmed the House of Morgan, Davis advised the men not to be coy, argumentative, or defensive. "I lined up the partners and held school every day," he later recalled.[51] As star witness, Jack was awaited with feverish anticipation. That morning, crowds ringed Capitol Hill to get seats in a sweltering, overflowing Senate Caucus Room. On the way, Jack confided to his chauffeur that he was afraid he would lose his temper. Charles Robertson sniffed, "Oh, you would not lose your temper

with the likes of them."[52] Restored to his senses, Jack decided not to stoop to their level. No, he would conduct himself with honor. He entered the Capitol accompanied by several tough-looking bodyguards.

Shortly before ten o'clock on Tuesday morning, May 23, guards cleared the way for Jack Morgan to enter the hearing room; he was flanked by Tom Lamont and John Davis. Flashbulbs exploded and spectators buzzed as the world's most famous private banker stepped beneath the chandeliers and Corinthian pilasters. Despite his legendary name, Jack, age sixty-six, was a mystery man to most Americans, ghostly and insubstantial. He didn't look fearsome. Over six feet two with broad shoulders and an egg-shaped head, he was a balding, white-haired old man with dark eyebrows. Within himself he might feel sheepish, but he had a kindly smile and radiated a well-tailored poise in his three-piece suit and gold watch chain. He and Pecora typified contrasting images—the imperturbable Bourbon and the assertive immigrant.

Nobody was less eager than Jack to be dragged from his semiretire-ment. At this moment of crisis, he reverted to the tradition upheld by three generations of Morgans, the Gentleman Banker's Code, first pounded into Pierpont's head by Junius sixty years before. Jack's opening statement harked back to Pierpont's statement at the Pujo hearings, that character was the basis of credit:

The private banker is a member of a profession which has been practiced since the middle ages. In the process of time there has grown up a code of professional ethics and customs, on the observance of which depend his reputation, his force and his usefulness to the community in which he works . . . if, in the exercise of his profession, the private banker disregards this code, which could never be expressed in any legislation, but has a force far greater than any law, he will sacrifice his credit. This credit is his most valuable possession; it is the result of years of faith and honorable dealing and, while it may be quickly lost, once lost cannot be restored for a long time, if ever.

> If I may be permitted to speak of the firm, of which I have the honour to be the senior partner, I should state that at all times the idea of doing only first class business, and that in a first class way, has been before our minds.[53]

This was as clear a statement of principles as Jack could muster: this was his birthright, what it meant to be a Morgan banker. Yet his attempt at candor sounded strangely anachronistic to American ears. Jack was an old-school banker, as out of place as an alchemist in the atomic age. Historian William E. Leuchtenburg has said, "On the witness stand, Morgan appeared to have been resurrected from some Dickensian countinghouse."[54] This was literally true,

for Jack was trained in late Victorian London and never abandoned its banking folkways.

His black hair swept up in a pompadour, his chin jutting, Pecora jabbed the air and posed aggressive questions; sometimes he even pointed his cigar at Jack. Abiding by Davis's advice, Jack didn't joust with the attorney. He smiled nervously, called Pecora "Sir," and hardly seemed a world-devouring tycoon. He breathed no fire, hurled no thunderbolts. The public saw the figure well-known to friends and associates but seldom, if ever, seen in public—the bluff, genial, but shy and vulnerable banker. "I should like it if the stuttering part were cut out of my answer to that question," Jack asked at one point. "I am not used to this form of examination, Mr. Pecora, and I do not get my words quite straight always."[55]

Like Samuel Untermyer at the Pujo hearings, Ferdinand Pecora focused on the House of Morgan's standing as the banker's bank. Jack saw nothing wrong with Morgan partners sitting on the boards of Guaranty Trust and Bankers Trust. Nor was he ashamed of the Morgan bank making loans to sixty officers and directors of other banks, including Charles Mitchell of National City, Seward Prosser of Bankers Trust, and William Potter of Guaranty Trust. Denying that this afforded any special advantages, Jack said, "They are friends of ours, and we know that they are good, sound, straight fellows."[56] Far from regretting the Morgan role as the Wall Street clubhouse, Jack boasted that a private bank offered neutral territory, where incorporated banks might "meet and discuss the general problems without rivalry or competition."[57]

Jack's testimony exposed Depression America to a form of wholesale, private banking that it had never known existed. When Pecora asked for the firm's partnership agreement, John Davis protested such public revelation. So in executive session, Pecora unrolled the agreement: a magnificently hand-lettered scroll that even some Morgan partners had never seen. It disclosed Jack's absolute powers to arbitrate disputes, allocate undivided profits, and even dissolve the bank. Jack was proud of the bank's secrecy. "Our relations with our clients are much more confidential, in my opinion, than the relations with an incorporated bank can be," he said.[58]

In a culture that worshiped the hard sell, the reticent J. P. Morgan and Company was a puzzling curiosity. As a private New York bank, it couldn't advertise, solicit deposits from the general public, or pay interest on deposits of less than $7,500. Apparently, getting a Morgan account was like being accepted at an exclusive country club. Even Senator Duncan U. Fletcher of Florida, the Chairman of the Senate Banking and Currency Committee, was perplexed by this:

Fletcher: But you are serving the public?

Morgan: Yes; but we are serving only our own clients who are our clients by our own choice.

Fletcher: But you do not turn a man down, you do not select your clients; you do not give them tickets and pass on them?

Morgan: Yes, we do.

Fletcher: You do?

Morgan: Yes, indeed; we do.

Fletcher: I suppose if I went there, even though I had never [seen] any member of the firm, and had $100,000 I wanted to leave with the bank, you would take it, wouldn't you?

Morgan: No, we should not do it.

Fletcher: You would not?

Morgan: No.

Fletcher: I'm quite sure then you would not . . .

Morgan: Not unless you came in with some introduction, Senator.[59]

Then who banked at this place? Pecora outlined a list of companies that kept million-dollar balances at Morgans—AT&T, Celanese, Du Pont, General Electric, General Mills, Ingersoll-Rand, ITT, Johns-Man-ville, Kennecott Copper, Montgomery Ward, New York Central, Northern Pacific, Standard Brands, Standard Oil of New Jersey, Texas Gulf Sulphur, and U.S. Steel. Their executives often chose J. P. Morgan for their personal bank accounts as well. Pecora had charts showing that Morgan partners held 126 directorships in 89 corporations with $20 billion in assets. He later called this "incomparably the greatest reach of power in private hands in our entire history."[60] He seemed incredulous when Jack said partners went on boards only at the "earnest request" of a company.

If Jack entered the hearings with serene confidence, he was soon engulfed in an issue that would shadow him throughout the New Deal—income taxes. Pecora revealed that Jack had paid no income tax for 1930, 1931, and 1932, and all twenty Morgan partners paid nothing for 1931 and 1932. (Jack had

paid taxes in England for these years.) Pecora also showed that by making Parker Gilbert a partner on January 2, 1931—instead of December 31, 1930, as would have been customary—the firm claimed a $31-million capital loss for 1931. Bumbling and flustered, Jack couldn't recall the details of his tax picture; such vagueness was plausible to his associates, suspicious to the public. Although Jack and most of the partners hadn't violated the law and had simply taken sizable write-offs from stock losses, their failure to pay taxes was politically explosive in the Depression. Tax shelters had not yet become a favorite American pastime, and the government desperately needed money. The next day, headlines trumpeted the Morgan partners' "tax evasion."

There were further embarrassing disclosures. Lamont's son Tommy, now a Morgan partner, had created a $114,000 capital loss by selling depressed shares to his wife, then buying them back three months later—a practice known as a wash sale. The young Lamont had to pay $3,949 in back taxes to remedy the problem. It turned out that the Internal Revenue Service had been curiously lax in examining Morgan tax returns; so sterling was the bank's reputation—or so feared was its power—that agents never closely inspected tax returns prepared there. As Pecora later said: "The Bible tells us that a good name is rather to be chosen than great riches. But it was vouchsafed to the members of J. P. Morgan and Company to enjoy both."[61]

As Jack's testimony took on a carnival atmosphere, Kentucky senator Alben W. Barkley told the doorkeeper to shut the rear door and asked photographers to stop setting off the blinding flashbulbs. The cacophony from voices and chairs scraping in the gallery sometimes drowned out Jack's soft voice. The pugnacious Carter Glass—who considered it a waste of time to interrogate upstanding Morgan partners—experienced mounting indignation. A small man with a shock of disheveled hair and a spare face, he thought the hearings a "Roman holiday" that were distracting attention from his banking bill. He sniped at Pecora for his treatment of the Morgan partners. "I do not intend to see any injustice done to the House of Morgan," he said, reddening with anger. "That is my attitude."[62] Fed up with the commotion over Jack's appearance at the hearings, he blurted out, "We are having a circus, and the only things lacking now are peanuts and colored lemonade."[63]

This gibe would change Jack Morgan's life. Overnight it echoed in the mind of Charles Leef, a Ringling Brothers press agent. The next morning, he brought to Capitol Hill a thirty-two-year-old midget named Lya Graf. She wore a blue satin dress and red straw hat. Only twenty-seven inches tall, she had a Kewpie-doll face with bright eyes and round cheeks. To enliven a delayed start to the hearings, Ray Tucker, a Scripps-Howard newsman, went out into the corridor and shepherded Leef and Lya into the Senate Caucus

Room to meet the celebrated banker. “Mr. Morgan, this is Miss Graf,” Tucker said. “She works for the circus.” Graf blanched, but Jack stood and shook her hand with instinctive ceremony. When he sat down, Leef, emboldened, plunked Graf on his lap, to the horror of Morgan partners and lawyers. Jack apparently thought at first she was a child.

“I have a grandson bigger than you,” Jack said in the sudden glow of dozens of flashbulbs.

“But I’m older.”

“How old are you?”

“Thirty-two,” interjected Leef.

“I’m not,” Graf protested. “Only twenty.”

“Well, you certainly don’t look it,” Jack replied. “Where do you live?”

“In a tent, sir.”

“Lya,” said Leef, “take off your hat.”

“No, no,” she said.

“Don’t take it off,” Jack said. “It’s pretty.”[64]

The most powerful men on Wall Street—Tom Lamont, John Davis, Richard Whitney—bitterly watched what they saw as a vulgar stunt, even a cruel attempt to embarrass Jack. When the senators filed in, they were outraged by what had happened and appealed to the press not to print the pictures, a request honored only by the *New York Times.* The next day, pictures of Jack and Lya Graf appeared on front pages across America. They would rank as some of the best-known of all Depression photographs.

They are actually lovely shots, bright with whimsy, and they probably accomplished more for Jack’s image than anything since the 1915 shooting. Between the portly businessman and the ringleted midget on his knee, there was an electric chemistry. While Graf steadied herself, Jack watched with fascinated amusement; he was tender with the midget and resembled a proud grandfather. For a generation of Americans, this would be their indelible image of Jack Morgan. The pictures were widely credited with starting a new age in financial public relations.

When his testimony was over, Jack dozed through the appearances of the other Morgan partners. At one point, he awoke abruptly to ask what year it was. In the sultry hearing room, a senator suggested they take off their coats. The old-fashioned Jack balked prudishly, then slipped off his light gray jacket, showing his white suspenders. He laughed and joked with guards and asked one if he needed his gun as protection against the senators. He showed reporters the famous bloodstone Pier-pont had worn. Yet he was not nearly as calm or relaxed as he appeared. When a newsman told him he hadn’t seen such hoopla since the Lindbergh kidnapping, Jack said privately that he “felt quite sick” at the comment.[65] His seeming aplomb contrasted with his deep

mortification at being held up to public scrutiny.

Jack could have used the episode with Lya Graf to capitalize on goodwill. Instead, he was embittered by the hearings and sulked over the incident. His New England pride wouldn't let him admit what the photographs suggest—that he had enjoyed the impromptu encounter. He didn't want to be made human in such a sordid way and said the incident had been "very unusual and somewhat unpleasant."[66] With the press, he tried to react to the episode with faint sarcasm. When asked why he hadn't removed the woman from his lap, he replied, "Well, you see, I didn't know but what she might be a member of the Brain Trust or one of the Cabinet."[67]

Everyone noted the uncanny parallels between the Pujo and Pecora hearings. Newspaper commentary favorably contrasted Jack's cooperation with Pierpont's truculence and Will Rogers even forecast a brilliant career for Jack. In milder moments, Jack conceded that Pecora hadn't been as taxing as Untermyer. But he was still unforgiving in his general appraisal. "Pecora has the manners of a prosecuting attorney who is trying to convict a horse thief. Some of these senators remind me of sex suppressed old maids who think everybody is trying to seduce them."[68]For someone as bashful as lack, a public grilling was a gruesome affair. He declared, "To have stood before a crowd of people and attempt by straight answers to crooked questions, to convince the world that one is honest, is a form of insult that I do not think would be possible in any civilized country."[69]

Sometimes Jack could laugh about the experience. One day on the golf fairway, he was lining up a shot when his caddy, Frank Colby, said he should think of the ball as Pecora's head. When Jack hit a splendid shot, they both laughed appreciatively.[70] But most of the time, Jack brooded about the hearings, which ended up alienating him from the New Deal. Afterward, he got a visit from William Jay Schieffelin, son-in-law of Dr. Markoe, who was trying to win support for a scheme enabling poor people to buy life insurance from savings banks. Jack not only refused to help, but made a revealing comment: "I only wish I had the capacity you have, a capacity for indignation at outrages. I've been so outraged that it leaves me cold when I hear of somebody else being outraged."[71] This sense of his own victimization would close Jack's mind toward the Roosevelt programs. More and more, he would feel a revulsion from America, a sense of being abandoned by his own country, and profound anger at the tarnishing of his bank's reputation.

The story of Lya Graf ends sadly. As sensitive as Jack, she was traumatized by the endless jokes about the episode—so much so that in 1935 she decided to return to her native Germany, even though she was half Jewish: her real name was Lia Schwarz. Two years later, she was arrested by the Nazis as a "useless person" and sent to Auschwitz, where she died in the gas chambers.

All this was learned only after the war when Nate Eagle, the Ringling Brothers manager who cared for the midgets, traced her history. Jack Morgan never knew what became of her, nor that her extreme distress over their brief encounter set in motion events that led, ultimately, to her death.

AS Pecora adroitly exposed their subterfuges, the other partners fared no better than Jack. When George Whitney read a statement favoring disclosure of commissions in security offerings, Pecora sarcastically noted that the legislation had just been passed. Returning in his questioning to 1929, Pecora lobbed another grenade over to the Morgan side. That year, the bank had joined the craze for creating new holding companies and had sponsored Alleghany Corporation as a vehicle for the railroad and real estate interests of the Van Sweringen brothers; United Corporation, an electric-utility holding company; and Standard Brands, a merger of four food and consumer-products companies.

Instead of placing shares only with dealers, Morgans borrowed a British precedent and placed shares with scores of friendly individuals. These shares came from a block of stock the bank kept as its underwriting fee. On Wall Street in the 1920s, it wasn't uncommon to have company officers or well-heeled individuals serve as underwriters. By allocating shares of the three holding companies to rich investors, Morgans claimed, it had tried to strike a compromise with its usual policy of not enticing individuals into risky stock transactions. As George Whitney said, they chose only those customers whom they knew were "competent financially and mentally to undertake the risks, whatever the risk may be."[72]

Such self-serving descriptions didn't capture the reality of 1929. In the souped-up bull market, shares offered to Morgan intimates before the public issue were already selling on a when-issued basis at a steep premium. (When-issued sales occur before a public offering and anticipate the price that will prevail when trading begins.) Between the Morgan price for lucky friends and this provisional market price lay a wide gap, an instant windfall. For instance, the bank was giving Alleghany shares to friends at $20 apiece; these could soon be cashed in for $35; United shares at $75 would soon go for $99; and Standard Brands shares bought at $32 could be redeemed just sixty days later at $41. In the soaring 1929 market, there was no great risk in carrying these shares before public issue, and the potential rewards were colossal. The shares seemed almost to be outright gifts—the sort of royal bequest only the House of Morgan could bestow. In Alleghany stock alone, the bank had over $8 million in profits to distribute. The setup was dubbed the gravy train.

The revelation of the House of Morgan's so-called preferred list of friends confirmed Main Street's cynicism of Wall Street as a place of easy riches and

loose morals. For Morgan critics, this was at last the smoking gun, the tangible proof of corruption. The stunning list of recipients encompassed the American business and political elite. It started at the very top. After leaving the White House, Calvin Coolidge had been advised on finances by Morgan partner Tom Cochran and received three thousand shares of Standard Brands; somewhat ashamed at this revelation, he told friends that it saddened him to appear on the preferred list while they were on the welfare list.[73] Other Republican beneficiaries included Charles O. Hilles, chairman of the Republican National Committee, and Charles Francis Adams, Hoover's secretary of the navy and the father-in-law of Jack's younger son, Harry.

Hedging its bets, Morgans also cultivated Democrats. This side of the ledger was even more embarrassing to its recipients, among them William G. McAdoo, the former Treasury secretary, a mentor of Russell Leffingwell. What made McAdoo's plight especially mortifying was that as a senator, he now sat on the Pecora committee. Also on the list was John J. Raskob, chairman of the Democratic National Committee. The list reached straight into the New Deal itself. When he was president of American Car and Foundry Company in 1929, William H. Woodin, now FDR's Treasury secretary, had taken up Morgans on an offer.

Beyond politics, the preferred list exposed an astonishing range of Morgan corporate contacts. There were business chieftains—Owen Young of General Electric, Myron Taylor of U.S. Steel, Walter Teagle of Standard Oil of New Jersey, Walter Gifford of AT&T, and Sosthenes Behn of ITT; financiers—Albert Wiggin of Chase, George F. Baker of First National, Richard Whitney of the New York Stock Exchange, and Bernard Baruch; a war hero—General John Pershing; a national hero—Charles Lindbergh; distinguished lawyers—John W. Davis and Albert G. Milbank; and distinguished families—Guggenheims, Drexels, Biddies, and Berwinds.

The House of Morgan was shaken by the disclosures and the imputation of dishonesty. When hiring partners, both Pierpont and Jack had always made the same statement; they would say, "I want my business done up there"—holding their hands in the air—"and not down here"—pointing to the ground.[74] Jack would tell people that at the first sign of unethical conduct, they should come straight to him. Now the bank had to face charges that it had unscrupulously curried favor with a broad spectrum of business and political leaders. How to defend the indefensible?

The task fell to George Whitney, whose Brahmin good looks and lacquered black hair made him the prototypically handsome Morgan partner of his generation. He had enjoyed Alleghany bounty himself, netting $229,000 on the sale of eight thousand shares. A tough, unyielding witness, Whitney stuck to the line that the bank was shielding small investors from risk. "They took a

risk of profit," Whitney said of the preferred customers; "they took a risk of loss." Pecora later rejoined: "Many there were who would gladly have helped them share that appalling peril!"[75] At moments, even the self-assured Whitney seemed confused, stammering at one point, "I don't know, Senator Couzens. It is hard to say why we did things. It is even harder to say why we didn't."[76]

Even as Morgan partners denied that shares were distributed to influence people, Pecora released subpoenaed bank records that confirmed a less than angelic intent. In 1929, Morgan partner William Ewing had written to William Woodin coyly acknowledging the bonanza being offered:

I believe that the stock is selling in the market around $35 to $37 a share, which means very little, except that people wish to speculate. We are reserving for you 1,000 shares at $20 a share, if you would like to have it. There are no strings tied to this stock, and you can sell it whenever you wish. . . . We just want you to know that we were thinking of you in this connection and thought you might like to have a little of the stock at the same price we are paying for it.[77]

Other documents suggested that the operation was conducted secretly. Partner Arthur Anderson told lawyer Albert Milbank, "It probably is unnecessary for me to add that I hope you will not make any mention of this operation."[78] Some correspondence resorted to sly hints. Golfing in Palm Beach, John J. Raskob, a former Du Pont treasurer and General Motors director, thanked George Whitney for his shares with the sincere hope that "the future holds opportunities for me to reciprocate."[79]

Lamont was indignant at charges of influence peddling. Yet his own files contain a February 1929 memo that may be the most damaging of all. In a postscript written to Arthur Anderson, it shows how the distributed shares were discussed internally: "It occurred to me this morning to make inquiry from you whether in our distribution of Al-leghany common we had allotted anything to Frederick Strauss. He was so exceedingly helpful and at considerable sacrifice to himself in going over to Washington to testify in the matter of the stock issues, that I am not at all sure that we ought not to try to do something for him even at a date as late as this."[80] Clearly, the preferred list had less to do with protecting small investors than with rewarding important friends.

The preferred list came at a particularly inopportune time both for the Roosevelt administration and the Morgan bank. High finance was on trial, and congressional hoppers bulged with securities-reform bills. The cabinet spent an hour deciding whether Woodin should remain in his post as Treasury secretary. Vice-President John Nance Garner favored his resignation to

establish that the administration was free of Morgan influence, but Roosevelt feared abandoning a friend under fire. “The President took the position that many of us did things prior to 1929 that we wouldn’t think of doing now; that our code of ethics had radically changed,” Interior Secretary Harold Ickes wrote in his diary.[81] Woodin remained in the cabinet until November 1933, when, gravely ill, he was replaced by Morgenthau. The cabinet was also disturbed by the appearance of Norman Davis, its roving ambassador, on the preferred list. Some feared that if the Roosevelt administration moved closer to the League of Nations or the British government, the public would impute the action to Morgan influence over Davis. Despite this, Davis represented Washington at several high-level European conferences in the 1930s.

The public reacted to the preferred list scandal with extreme disillusionment: the brightest angel on Wall Street had fallen. The bank had avoided the flagrant abuses of other banks—even Pecora called Morgans a “conservative” firm—but the preferred list cast it in the mud with other banks. A stunned Walter Lippmann told Morgan friends that no group of men should have such private power without public accountability. It was a bitter pill for Lippmann, who had often dined at Lamont’s table. His biographer, Ronald Steel, suggests that he and other journalists were lulled to sleep by Lamont, whose “charm and familiarity with the trade enabled him to persuade many journalists to look upon the activities of the Morgan firm no more critically than he did himself.”[82]

Lippmann wasn’t the only shocked journalist. As if some mighty public trust had been betrayed, the *New York Times* wrote an elegiac editorial: “Here was a firm of bankers, perhaps the most famous and powerful in the whole world, which was certainly under no necessity of practicing the small arts of petty traders. Yet it failed under a test of its pride and prestige. . . . They have given their warmest friends cause for feeling that somehow the whole community, along with numbers of men whom all had delighted to honor, has been involved in a sort of public misfortune.”[83]

Reading this, Lamont became distraught. Of the Morgan partners, he had the most personal need for admiration. He wrote his friend Adolph Ochs, publisher of the *Times*, trying to extenuate the scandal. He said Morgans hadn’t expected people on the list to serve in public office again. He cited the risks of owning common stock and made it sound as if the list were made up only of family and friends. The explanations sounded strained: “We naturally turned in part to individuals who had ample means and who understand the nature of common stock—men who are prepared to take a chance with their money.”[84] All his arts couldn’t hide what had become a certifiable scandal, setting the stage for the bill that would dismember the House of Morgan.

THE Glass-Steagall Act was sponsored by a Virginia senator who felt more warmly toward 23 Wall than any of his Senate Banking Committee colleagues. Small and peppery, Carter Glass was a former Lynchburg newspaper editor with little formal education. As a congressman, he had helped to write the Federal Reserve Act and had espoused strong banker control. As Wilson's Treasury secretary, he had been Russell Leffing-well's boss. In early 1933, he was a mass of contradictions. After supporting Roosevelt's election, he quickly emerged as an articulate critic of FDR. He rebuffed the president's offer to become Treasury secretary and attacked New Deal activism from a Jeffersonian standpoint; he was the sole Democratic senator to oppose the gold devaluation. Glass sponsored his famous bill with no personal animus toward Wall Street. In fact, he and Leffingwell often exchanged nostalgic, syrupy notes about their years in the Treasury Department. Although Leffingwell described their friendship as one of his most cherished, he was frustrated in his efforts to capitalize on it that spring: when subcommittee members working on the bank-reform bill swore not to talk to outsiders about it, Glass had to abide by the decision.

Glass-Steagall evolved in a way that owed much to fate. Huey Long and other congressional populists wanted federal deposit insurance in the bill, as well as restrictions on interstate branching. Both features were anathema to Roosevelt, who favored a national banking system that would put small-town Republican bankers out of business, not prop them up. Like Hoover, he feared that deposit insurance would pull strong banks down with the weak and thought it "puts a premium on sloppy banking and penalizes good banking."[85]

Roosevelt kept the press guessing whether he would support Glass-Steagall. The Pecora hearings certainly contributed to public support of the bill. But what sealed its fate was the flood of mail to Congress favoring deposit insurance. The inclusion of deposit insurance was also important because nobody wanted to insure the securities affiliates of banks; if they had federal insurance, they would be obliged to stick to conservative loan-and-deposit banking. Finally, the bill set ceilings on savings interest rates. The Glass-Steagall Act was signed on June 16, 1933, by a president who didn't even think the public was particularly eager for banking reform. From now on, banks would either take deposits and make loans or merchandise securities—but not both.

A surprise last-minute insertion in the bill was a provision endorsed by Chase president Winthrop Aldrich that forced private banks to choose between deposit and securities businesses. This was the *coup de grâce* for the House of Morgan. Later Carter Glass told Leffingwell that Aldrich drafted this provision and that Roosevelt foisted it on him. Pecora's disclosure about the Morgan partners' avoidance of income taxes made it impossible to delete

this provision, so strong was public wrath.[86] Adding to the pressure was Chase's decision to disband its securities affiliate, whose refugees joined with renegades from the First National Bank of Boston to form First Boston, the first modern American investment bank.

The Glass-Steagall Act took dead aim at the House of Morgan. After all, it was the bank that had most spectacularly fused the two forms of banking. It had, ironically, proved that the two types of services could be successfully combined; Kuhn, Loeb and Lehman Brothers did less deposit business, while National City and Chase had scandal-ridden securities affiliates. The House of Morgan was the active double threat, with its million-dollar corporate balances and blue-ribbon underwriting business.

What was the theory behind the Glass-Steagall Act? Foremost, it was meant to restore a certain sobriety to American finance. In the 1920s, the banker had gone from a person of sober rectitude to a huckster who encouraged people to gamble on risky stocks and bonds. As Pecora noted, small investors identified commercial banks with security, so that National City stock salesmen "came to them clothed with all the authority and prestige of the magic name 'National City.' "[87] It was also argued that the union of deposit and securities banking created potential conflicts of interest. Banks could take bad loans, repackage them as bonds, and fob them off on investors, as National City had done with Latin American loans. They could even lend investors the money to buy the bonds. A final problem with the banks' brokerage affiliates was that they forced the Federal Reserve System to stand behind both depositors and speculators. If a securities affiliate failed, the Fed might need to rescue it to protect the parent bank. In other words, the government might have to protect speculators to save depositors.

Ultimately, Glass-Steagall was as much an attempt to punish the banking industry as it was a measure to reform it. It was Main Street striking back at Wall Street, rounding out the 1929 disaster. The bill also had supporters among small investment banks eager to exclude large commercial banks from their domain. Many economic historians have pointed out the tenuous links between the crash and the subsequent bank failures. Bank failures were concentrated among thousands of country banks across America, while big Wall Street banks with securities affiliates withstood the Depression relatively well. Yet Glass-Steagall and other New Deal reform acts were directed at Wall Street and insulated little crossroads banks from big-city competition. This made political, but not economic, sense. The speculative fever of the 1920s had infected *all* securities houses, whether or not they were subsidiaries of deposit banks. The Jazz Age on Wall Street might have been no less effervescent if a Glass-Steagall arrangement had already been in place.

The House of Morgan had trenchant arguments to make against the bill, but

nobody listened. After the Pecora hearings, even well-reasoned arguments by the financial elite resembled self-serving blather. Lamont pointed out that the flagrant scandals of the 1920s had involved retail-investment affiliates. Why, then, couldn't wholesale banks, such as J. P. Morgan, distribute securities not to individuals but to dealers and large institutions? The Morgan partners also argued that disclosure requirements in the new Securities Act of 1933 would force banks to identify any loans outstanding to countries or companies whose bonds they issued—safeguards for bond investors lacking in the 1920s.

Lamont contended that size wasn't to blame for America's fragile banking system so much as fragmentation. The country had over twenty thousand banking institutions, resulting in a financial history peculiarly checkered with panics, failures, and runs. England, France, and Canada, by contrast, had a small number of large national banks, and these had passed through the Depression in far better shape. Then why not bigger, better-capitalized banks? To free banks from reliance on a single industry—whether Texas oil or Kansas farming—Lamont favored interstate banking. Russell Leffingwell contended as well that removing big commercial banks from underwriting work would produce capital-short investment banks—a prophecy not fully appreciated until decades later.

In 1933, however, such a perspective was bootless. The public wanted to see the giants slain and didn't care about the dusty little banks that had faltered from bad luck or mismanagement. America's atomized banking system might have contributed to its stormy financial history, but the political response was always to segment it further. With the Glass-Steagall Act, America experienced the catharsis awaited since Black Thursday. As Leffingwell said, "There is so much hunger and distress that it is only too natural for the people to blame the bankers and to visit their wrath on the greatest name in American banking."[88] All the while, Morgan partners felt that they suffered for sins committed by others. George Whitney later remarked that "we never retailed while I was in our office, but that's where the trouble started, and the New Deal was smart enough to realize that if they could cut the security business up in pieces, they would take this power away and they did."[89]

CHAPTER NINETEEN
CRACK-UP

AFTER passage of the Glass-Steagall Act, there was a grace period, during which the House of Morgan had to choose between deposit and investment banking. The partners still hoped the measure would be repealed. But after its unrivaled political influence in the 1920s, the bank seemed paralyzed, unable to exercise influence. As Arthur Schlesinger, Jr., has noted, no group lost more in public esteem, or more keenly lamented its exclusion from Washington, than the bankers. They became a caste of untouchables right at the start of the New Deal. For the House of Morgan, there were moments when the rout by enemy troops seemed terrifyingly complete. Its old foes were entrenched in Washington. For the new securities-disclosure law, the White House had asked Samuel Untermyer, of Pujo fame, to prepare a draft. Untermyer lost standing with Roosevelt, however, when he bragged too much about his supposed intimacy with the president.

The intellectual mentor of much legislation was that scourge of the New Haven Railroad, Louis Brandeis, now a Supreme Court justice. In May 1933, the precepts he had expounded to Lamont at the University Club twenty years before became law in the Securities Act. This truth-in-securities law required the registration of new securities and full disclosure of information about companies and underwriters. *Caveat vendor* replaced *caveat emptor* as the regulatory philosophy. When FDR spoke in favor of the bill, he alluded to Brandeis's book about the New Haven railroad, *Other People's Money;* the law, said Roosevelt, would embody "the ancient truth that those who manage banks, corporations, and other agencies handling or using other people's money are trustees acting for others."[1]

For the House of Morgan, Louis Brandeis was more than just a critic; he was an adversary of almost mythical proportions. In early 1934, Leffingwell told Lamont he should read a new edition of *Other People's Money* and blamed Brandeis for the Glass-Steagall provision pertaining to private banks: "I have little doubt that he inspired it, or even drafted it. The Jews do not forget. They are relentless. . . . The reason why I make so much of this is that I think you underestimate the forces we are antagonizing. . . . I believe that we are confronted with the profound politico-economic philosophy, matured in the wood for twenty years, of the finest brain and the most powerful personality in the Democratic party, who happens to be a Justice of the

Supreme Court."[2] Despite the separation of powers, Brandeis advised Roosevelt through an emissary—his daughter, Elizabeth Raushenbush. Roosevelt referred to Brandeis by the code name Isaiah.

In 1934, the House of Morgan joined with New York Stock Exchange president Richard Whitney in a zealous lobbying effort to defeat the Securities Exchange Act. Operating from a Georgetown townhouse nicknamed the Wall Street Embassy, they warned that federal regulation would convert the Street into "a deserted village."[3] It was a campaign of such harrowing intensity that despite the anti-Wall Street mood, the bill's authors were surprised by their victory. One of them, Thomas G. Corcoran, exulted, "Rayburn and I stood alone against all the batteries of lawyers sent by Morgan's and the Stock Exchange—and we won out!"[4] Another Morgan hobgoblin, Joseph Kennedy, snubbed by Jack before the crash, became the Securities and Exchange Commission's first chairman. Ferdinand Pecora, who worked on the bill, was named a commissioner. The money changers had indeed been chased from the Temple, by the Irish, the Italians, and the Jews—the groups excluded from Wasp Wall Street in the 1920s.

The Morgan partners resorted to hyperbolic criticism when they should have been conciliatory. Jack Morgan inveighed against "absurd" federal deposit insurance and warned of dying capital markets if securities laws were enacted. Faced with the decline of the bank's power, he emitted an air of subdued defeat. He complained to friends that he was a punching bag for every political propagandist. Like other partners, he felt muzzled in contesting the New Deal—perhaps the reason why he didn't join his friend and lawyer John Davis in forming the anti-New Deal Liberty League in 1934. "If anybody lifts his voice in protest . . . he is at once held up to public scorn as a totally selfish, grasping individual, wholly unresponsive to the new thought,"[5] he declared. He was an easy butt for critics. He often antagonized reporters by curtly refusing interviews: "I do not think my opinion is worth a damn." Other times, he would talk and denounce progressive income taxes or take other inflammatory stands. Either way, his popularity declined.

Teddy Roosevelt had been Pierpont's tormenter, and now another Roosevelt served the same role for Jack. At moments, the Roosevelt family seemed one big throng of Morgan-hating harpies. When somebody mentioned TR, Jack spluttered: "God damn all Roosevelts!"[6] He was fond of quoting Richard Hooker, the English Renaissance divine, that to live by one man's will was every man's misery. For Jack, that man was FDR, whom he saw as a frightening left-wing charlatan out to destroy his own class. In 1934, he said, "I am gradually coming to the opinion, which I did not have at first, that the United States will probably outlive even the attacks upon it by Franklin Roosevelt and I am particularly satisfied to see the rising tide of opposition to

his fierce methods and his wholesale slaughter of reputations."[7] The Roosevelt hatred became obsessive. When Jack developed a heart condition, his grandchildren were instructed not to mention the president's name in his presence. Other accounts tell of retainers snipping Roosevelt photos from Jack's morning paper, in deference to the master's high blood pressure.

Rather than bending with the time, Jack's conservatism grew crustily defensive. The old swipes at Congress lapsed into ugly diatribes against democracy and universal suffrage. Congressmen were "wild men" who controlled his destiny, while the intelligent, propertied class were subjected to the whims of a fickle, emotional majority. He regarded the New Deal less as a set of economic reforms than as a direct, malicious assault on the social order, aimed at the "extinction of all wealth and earning power."[8] Notwithstanding a 25-percent jobless rate, he wanted balanced budgets and low taxes. "The more I see of the New Deal," he said, "the more I realize that there is nothing new about it except its name."[9]

As chief bank lobbyist, Lamont wasn't reflexively antagonistic to the New Deal and applauded measures to combat deflation, such as open-market operations (the purchase and sale of government securities) by the Fed. At moments in the 1930s, Morgans supported easy-money policies while hidebound Wall Street fretted about inflation. But even Lamont never presented a reform program that would steal the bank critics' thunder; Wall Street let its enemies write the new laws.

As was his wont, Lamont used different voices as he spoke to different people. At a private dinner in 1934, he told relief administrator Harry Hopkins, "Well, if the country was willing to spend thirty billion dollars in a year's time to try to lick the Germans, I don't see why people should complain about its spending five or six billion dollars to keep people from starving."[10] Here he sounded like a free-spending liberal. Yet in chatting with Chancellor of the Exchequer Neville Chamberlain that year, he praised Britain for overcoming the Depression through sound, old-fashioned policies, not deficit spending. He joked, "I suppose I mustn't hold you personally responsible for having sent Keynes over and to have made our President spend another *Vi* billion dollars in public works."[11]

The best weapon the Morgan bank had for changing New Deal policy was Russell Leffingwell. With his pure white hair and Pinocchio nose, he looked like a sage or an elder statesman. He was an omnivorous reader, a man of wide vision who could offer cogent opinions on any subject. Leffingwell had the most balanced view of the New Deal and often told friends Roosevelt had saved America from revolution in 1933. He wasn't afraid to scandalize Wall Street by consorting with the president. Sometimes he used his friend Morris Ernst, a liberal lawyer, as an intermediary to the White House, so that Walter

Winchell and other columnists wouldn't get wind of his influence. Yet even Leffingwell couldn't make the intellectual adjustment required by the economic emergency. When Roosevelt brought him to the White House in October 1934 to discuss a new public works program, Leffingwell rejected the plan with ritual assertions that it would cause inflation and crowd out private capital from financial markets. Yet deflation was the major problem, and far from being overcrowded, capital markets were empty. Leffingwell was a nineteenth-century liberal and found it hard to approve of many forms of government intervention in the economy.

In many ways, the House of Morgan was a muscle-bound giant, afraid its lobbying efforts would be twisted by opponents into proof of insidious power. By late 1933, the airwaves were filled with demagogic voices that ascribed the Depression to Wall Street-inspired monetary policy. Father Charles E. Coughlin, the radio priest, stoked the old prairie fires once lighted by William Jennings Bryan. From his Shrine of the Little Flower near Detroit, he incited his nationwide audience with tales of a bank that had enslaved America to the gold standard, had long colluded with the British crown, and had forced debt and deflation on farmers. That the same bank had hailed Britain and America's departure from gold mattered not a whit. In a November 1933 broadcast entitled "Thus Goeth the Battle!" Coughlin dredged up old myths about the House of Morgan: "Who in God's name ever accused the Morgans of having patriotism to this country? Who doesn't know that they have been playing the British game for years; that they pay taxes to England and none to America?"

He then evoked a football team of politicians—Morgan stooges all—who had pushed America into the Depression:

> And on the sidelines there sits J. Pierpont Morgan—the Knute Rockne of the grand old guard—the scout in the pay of England, the master mind of tax-dodging, the strategist of the financial huddle. . .
>
> There are two powerful generations of Morgans—the elder who sold guns to the Civil War soldiers—guns that couldn't shoot—and the younger who arranged money for more guns that shot to no avail in the last war. . . . Now where do you stand? Choose between Roosevelt and Morgans! Choose between these anointed racketeers of Wall Street . . . and the "new deal"![12]

Father Coughlin would ask his listeners to mail in dollar bills. It later was revealed that he used some of the money to speculate in silver futures through a personal account at Paine Webber.

In these scurrilous attacks by Coughlin, the Hearst press, and other

isolationist organs, a powerful theme emerged—that World War I and the Depression had been instigated by the same Wall Street bankers. The argument was that the bankers drew America into the war to safeguard their Allied loans and that the debts and reparations produced by the war led to the Depression, *ergo*, Morgans and other international bankers were to blame for American participation in the war and for the Depression. For Anglophobic populists, this was a convenient equation. They could exploit discontent with Wall Street to argue against closer ties with Britain, and they could tap isolationist sentiment to press for tougher bank controls. The House of Morgan was the natural target for this attack.

ROOSEVELT was as perplexed and annoyed with the Wall Street bankers as they were with him. He saw himself as saving the patient with radical surgery, not killing him. His talent for experimentation, for latching onto new ideas, was profoundly disturbing to bankers who had lived by sacred, immutable laws. To try to patch up relations, FDR invited Morgan loyalist George Harrison, Ben Strong's successor at the New York Fed, for a weekend cruise aboard his yacht, the *Sequoia*. Commenting on the bankers' mistrust, Roosevelt said ruefully, "They oppose everything I do, even though it is with the intention of helping them."[13]

Eager to mediate, Harrison arranged for FDR to address a meeting of the American Bankers Association in Washington. Lamont and Parker Gilbert attended, the first time Morgan partners ever graced an ABA meeting. The effort at mediation only worsened matters. Jackson Reynolds of the First National Bank of New York delivered a keynote speech lauding FDR. But when it was discovered that Roosevelt himself had vetted the speech, the bankers felt cheated, and the New Deal-bankers truce was ended. Both sides retreated into a bitter standoff.

Perhaps the most sophisticated foray against the House of Morgan came from those who sought changes in the Federal Reserve System. A little-noticed provision of the Glass-Steagall Act forbade the New York Fed to conduct negotiations with foreign banks. This was Washington's response to the elaborate connivance between Ben Strong and Monty Norman—a relationship so important for the House of Morgan. The seemingly innocuous measure was one of Washington's canniest moves against the bank.

Then in 1934, a young Utah banker, Marriner Stoddard Eccles, advised the Roosevelt administration on revisions to the Federal Reserve Act. Eccles wanted to emasculate the New York Fed and shift power to the Federal Reserve Board in Washington so as to purge the influence of Wall Street bankers from the system. Leffingwell was especially incensed at this move because he blamed the 1929 crash on the Washington board's interference

with the New York Fed, which had wanted to raise interest rates and arrest speculation. George Harrison tried to marshal enough conservative senators to defeat the Banking Act of 1935, but his efforts were in vain. Under the Eccles legislation, the district banks lost much of their autonomy; power was now lodged in the seven-member Washington board. In two symbolic steps underscoring the Fed's new independence, the Treasury secretary was removed from the board, and the Fed, which had operated from Treasury premises, got its own building.

Later Eccles tried to put Parker Gilbert on the reorganized Fed board, but Morgan partners dismissed the move as a sop, knowing that the Fed now responded to new political masters. In many ways, the Eccles reforms belatedly accomplished the aims of the Fed's progressive supporters, who had wanted an American central bank to curb Wall Street power. The 1920s Republican abdication of an international role had permitted Ben Strong and the House of Morgan to subvert that intention. Now, over twenty years later, the ghost of the Money Trust was finally exorcised.

AMONG Wall Street banks, none agonized more than the House of Morgan over whether to choose deposit or investment banking. It postponed a final decision until the summer of 1935. By that point, it had been legally barred from securities work for a year. Disturbed by the paucity of industrial issues on Wall Street, Carter Glass inserted an amendment into the proposed Banking Act of 1935 that restored limited securities powers to deposit banks. The partners rested their final hopes on this peg.

George Whitney, as head of corporate underwriting, was under mounting pressure to inform Morgan clients of the bank's decision. With interest rates down, many companies wanted to refund maturing bonds at lower rates. They kept asking Whitney what to do. In late July, Charles Mitchell, former chairman of the National City Bank and now a partner in Blyth and Company, found Whitney still hoping for a last-minute reversal of Glass-Steagall. "I think they are waiting . . . to see if the underwriting amendment in the banking bill will pass," Mitchell told a partner, "and regarding this they are more optimistic than they have been."[14] In late August, the banking amendment reached a House-Senate conference committee. But President Roosevelt—bringing down his fist in one last blow to the House of Morgan—interceded to kill the amendment. He refused to consider any modification of Glass-Steagall.

As if too depressed to face the truth, Jack had kept assuring Teddy Grenfell that the amendment would pass. Yet mysterious doings in the art market of early 1935 betrayed his underlying pessimism. Citing inheritance taxes and a desire to put his estate in order, Jack sold six magnificent paintings for $1.5

million. To Fritz Thyssen, the German steel magnate, went Domenico Ghirlandajo's portrait of Giovanna Tor-nabuoni while the Metropolitan Museum got a Fra Filippo Lippi triptych and Rubens's Anne of Austria. Through Christie's in London, Jack auctioned seven cases of coveted miniatures amassed over thirty years. In oppressive July heat, with a nurse in attendance in case anyone fainted, Christie's sold a portrait by Hans Holbein the Younger, a gold pendant with Queen Elizabeth's profile, and other rarities. Only astute press commentators connected this sudden need for cash with a pending decision about the House of Morgan. As he had demonstrated after his father's death, Jack was ready to pare his art collection ruthlessly if he needed to conserve the bank's capital.

Before J. P. Morgan and Company made its decision, a new arrangement was devised with Morgan Grenfell in June 1934 to comply with Glass-Steagall. The British house became a limited company in which the New York firm held a one-third stake. This was designed to buffer the new commercial bank, J. P. Morgan and Company, from British securities work, a structure preferred by the Bank of England as well. New York would now be a passive investor. "It was definitely a hands-off situation," noted Tim Collins, a later Morgan Grenfell chairman.[15] There remained a close, familial feeling between 23 Wall and 23 Great Winchester, and the London *Times* called it only a "slight technical alteration."[16] Yet for a firm that had always been subordinate to New York, the change represented a new level of British autonomy. It also occurred at a time when the City could no longer float huge foreign loans, as it had before the war, except for the British Empire. Morgan Grenfell and London's other merchant banks concentrated instead upon securities and merger work for domestic companies.

In August 1935, Tom Lamont gathered the J. P. Morgan chieftains at his island farm off the Maine coast. The group included Morgan partners Leffingwell, Whitney, S. Parker Gilbert, and Harold Stanley, and Lansing Reed of Davis, Polk, and Wardwell. At this secret meeting, the House of Morgan decided irrevocably to remain a deposit bank and spin off an investment bank called Morgan Stanley. No minutes survive from this summit, thus leaving unanswered several essential questions. Why did Morgans—nonpareil of underwriters—opt for "commercial" rather than "investment" banking? Why the preference for deposits and loans rather than securities and brokering? Why an action that, in retrospect, seems a failure of vision?

Fifty years later, the choice seems strange. Between 1919 and the Pecora hearings, Morgans had sponsored $6 billion in securities for blue-chip companies and foreign governments. The Morgan cachet on bond issues brought in collateral banking business, such as the payment of dividends on

bonds. As Russell Leffingwell had told Lamont, “I believe further that our securities business is a necessary feeder to our banking business, and that without it the banking business would in time dry up.”[17] Except for Brown Brothers Harriman, most distinguished partnerships—Kuhn, Loeb; Goldman, Sachs; and Lehman Brothers—opted for “investment banking” (a misnomer for the securities business the term denotes). The world of commercial banking—with its letters of credit, loans, foreign exchange, and stock-transfer work—seemed prosaic for a bank of such rarefied tastes and as active in secret diplomacy as J. P. Morgan and Company.

The choice was heavily influenced by the moribund state of the securities markets. Securities underwriting had become the firm’s least profitable activity, and new securities laws strapped underwriters with large potential liabilities. Stung by the preferred-list scandal, perhaps Jack Morgan favored commercial banking as more stable and consistently profitable than investment banking. In urging repeal of Glass-Steagall, Leffingwell wrote a letter to Roosevelt that shows the way in which securities work was regarded during the Depression:

> The business of underwriting capital issues is and should be a byproduct business. It is occasional and sporadic. Nobody can afford to be in the business unless he has a good bread and butter business to live on. A house exclusively in the underwriting business is under too much pressure to pay overhead and living expenses to pick and choose the issues it will underwrite.
>
> One reason why our record is so good . . . may be . . . that we have no salesmen, very little overhead attributable to the underwriting business and that we have a good bread and butter banking business. So we could and did say no to half of Europe and of South America.[18]

This approach of keeping overhead low, not having salesmen, and selecting only prime clients would shape Morgan Stanley’s philosophy for the next forty-five years.

The human factor was undoubtedly also significant in choosing commercial banking. In 1935, about 20 percent of American workers were unemployed. It would have been hard to renounce the labor-intensive activities on the commercial-banking side. To have entered investment banking would have meant wholesale firings—an egregious betrayal for a paternalistic firm. Says an official Morgan history: “At the time of that decision the partnership, J.P. Morgan &. Co., had a staff of about 425 people. If the firm had chosen to remain solely in the securities business, a large part of this staff probably would have become surplus. . . . Approximately 400 people were busy in

commercial banking and other activities and remained with the firm; about twenty left to form Morgan Stanley & Co."[19]

There were also less benign motives. Morgan partners wanted to retain the option of someday recreating the House of Morgan without losing its clients. In late 1934, Lamont wrote to his partner Charles Steele: "We all feel, I think, that ways and means will be found to get us back into the securities business, either through the amendment of the existing laws or through *some separate corporate plan* or otherwise. We are considering all these matters now, but have by no means accepted the idea that . . . we are to be eliminated from the security business"[20] (italics added). The reference to a separate corporate plan hints at Morgan Stanley's genesis. Lamont, it seems, believed they could stay in securities without changes in Glass-Steagall, suggesting he had a trick or two up his sleeve.

Both at 23 Wall and elsewhere, Morgan Stanley was regarded as a branch of the main trunk, a successor firm. As a cable to Morgan Gren-fell explained, "The fact it is a segregation is apparently well understood. At the same time, everyone looks to the new company to carry on the traditions of the firm."[21] The House of Morgan probably wanted to create a firm that later, under a friendly Republican administration, could be cleanly folded back into J. P. Morgan and Company. Lamont may have recalled the birth of Bankers Trust as a "captive" bank, one that would politely return customers referred to them for trust business. If Morgans had chosen investment banking and released 90 percent of its staff, it would have been impossible to rebuild the House of Morgan if Glass-Steagall were rescinded.

At four o'clock on the afternoon of September 5, 1935, the eve of Jack Morgan's sixty-eighth birthday, the House of Morgan was officially divided. Lamont, Whitney, and Stanley stood before the fireplace at the end of the long narrow partners' room, below the oil portrait of Pierpont. They announced to two dozen newsmen that several people from the Morgan Bond Department would leave to form Morgan Stanley. The new firm would have three J. P. Morgan partners—Harold Stanley, who had joined the firm in late 1927, after Dwight Morrow was appointed ambassador to Mexico; Jack's younger son, Harry; and William Ewing—and two Drexel partners, Perry Hall and Edward H. York. Lamont said the new firm would conduct a securities business "of the character formerly handled by our firm."[22]

Jack and Harry Morgan were absent from the conference, refusing to forgo the pleasures of grouse shooting, even on this historic occasion. It was a mournful moment. One reporter, noting the solemn faces, observed, "The segregation of the old firm was taken as seriously as a separation of any private family."[23] Yet however lugubrious for Morgans, the new Morgan Stanley was cheered as a sign of returning prosperity, a tonic to Wall Street's

mood.

Morgan Stanley looked less a distant cousin than a richly endowed stepson of J. P. Morgan and Company, which financed it almost fully. Morgan Stanley officers owned virtually all the $500,000 of common stock, and they retained voting control. But the real start-up capital was $7 million in nonvoting preferred stock, $6.6 million of it held by J. P. Morgan partners. Jack and his family held about 50 percent of the preferred shares; Tom Lamont and his family, over 40 percent. Small wonder the new offshoot caused grumbling from some competitors, a feeling that J. P. Morgan and Company had honored the letter, but violated the spirit, of Glass-Steagall.

On September 16, 1935, Morgan Stanley opened for business at 2 Wall Street, about a hundred yards from 23 Wall. The office of this splendid bastard had a view of the Trinity Church steeple and its decor evoked its blue-blooded parentage. Prints of old New York adorned the walls, and signature rolltop desks were lined up in the manner of 23 Wall. It had something of the mood of a J. P. Morgan branch office. “My first job in the bank was going to Morgan Stanley,” recalled Ellmore C. Patterson, later chairman of Morgan Guaranty. “They were short-handed. It got very busy and they borrowed two of us for about a year.”[24]

September 16 was one of the most bizarre opening days in American business history: it didn’t resemble that of a new business. The night before, Perry Hall asked the janitor to set out a table in case anybody sent flowers. When he reported to work, he found two hundred floral displays. “In fact, the entire length of our office was just one row after another of these magnificent flowers in vases. . . . Nearly every one of them was from our competitors and associates on the Street.”[25] One reporter said it resembled a flower show. The *New York Times* noted the eerie sense of continuity: “The inauguration of business proceeded as if it were just the beginning of another week in any old-established firm.”[26] One Morgan Stanley legend, perhaps apocryphal, claims that so many companies came for business the first week that when one utility chairman arrived to discuss financing, Stanley said, “Tell him to come back next week.”[27]

At the new firm, the leading personalities were recognizable Morgan types. The press, as if covering the debut of a new country club, showed them golfing or emerging from the surf. Harold Stanley, a utility-bond expert, was handsome and distinguished looking with thick, prematurely gray hair, a long face, and steady eyes. Now nearly fifty, he was president and senior statesman of the firm and a figure of enormous stature on Wall Street.

Son of a General Electric engineer—the inventor of the Thermos bottle—Stanley had a very Morgan pedigree: he was a Massachusetts Episcopalian, a star hockey and baseball player at Yale, and a Skull and Bones member. He

owned a home in Greenwich, Connecticut, and an apartment on Sutton Place. As a negotiator, he was tough and stubborn but honest. “While others banged conference tables he sat shyly by; but he seldom budged in an argument,” reported *Newsweek*.[28] Coolly diplomatic, he was well suited for the political attacks that would shadow Morgan Stanley for twenty years.

Absent from the opening-day festivities was the firm’s new treasurer, Harry Morgan, thirty-five, then returning from England aboard a cruise ship. Harry’s aloofness from the affairs of the firm foreshadowed later developments. Yet it would be important for the new firm to have not only the Morgan name and money, but a real, breathing Morgan on the premises.

Harry Morgan had shiny, pomaded hair, a sharp chin, and electrically intense eyes. He was brusque and aggressive like his grandfather and with some of Pierpont’s flamboyance. He bought up the Eaton’s Neck peninsula on the North Shore and commuted by seaplane to Wall Street. As had happened with Jack in relation to Pierpont during the Pujo hearings, Harry became deeply embittered by the Pecora hearings’ treatment of his father. It would be the formative event of his life, making him fanatically private and aloof from any public role other than in the world of yachting. It would likewise make Morgan Stanley far less prone than the old House of Morgan to dabble in politics or seek publicity. In 1935, the press portrayed Harry as the real heir to the Morgan business talents, and he shone in comparison with his more languid, gentle older brother, Junius, who remained with J. P. Morgan and Company. Harry would function more as the conscience of Morgan Stanley, the custodian of its traditions, than as a day-to-day executive. He also had important business contacts through his friendship with European banking families, including the Wallenbergs and the Ham-bros. He explained his role thus: “My father, as my grandfather got older, brought into his firm some very brilliant and desirable new partners. He built a team, and he was immensely successful in doing that and in acting as a moderator and team captain. In many ways when this firm was started, I thought that there was a place for me to act in such a capacity.”[29]

The founders of Morgan Stanley romanticized their early days, stressing the perils they braved. “We were going out into a rough sea in a little tiny rowboat,” said Perry Hall. “We didn’t know how we would be received.”[30] They were, in fact, received like members of a Renaissance court in exile. There were many links between J. P. Morgan and the new firm. Morgan Stanley closings—that is, payments for and deliveries of securities—took place at 23 Wall. And George Whitney, acting as “family physician” to clients, steered them to Morgan Stanley. Morgan Stanley started out with only a few spillover deals from the Corner—but what deals! George Whitney steered such clients as Wendell Willkie, chairman of Consumers Power, to

Harold Stanley; before September 1935 was over, Morgan Stanley had its first big electric utility issue. Early in the summer, Walter Gifford of AT&T had asked Stanley about rumors that Morgan partners would form a securities firm. When Stanley confirmed this, Gifford said, "That solves my problem." He then put on his hat and left.[31] AT&T needed to do some new financing, and the Securities and Exchange Commission was eager for AT&T to return to capital markets to prove their health under the new regulations. In a historic issue for Illinois Bell Telephone, Morgan Stanley published the first newspaper prospectus conforming to New Deal securities laws, following consultations in Washington between Stanley and SEC chairman Joseph P. Kennedy.

Despite predictions from the House of Morgan that the New Deal would kill capital markets, they boomed in 1935, and underwritings jumped fourfold. In its first year of operation, Morgan Stanley handled an astounding $1 billion in issues, sweeping a quarter of the market. *Forbes* hailed a wonder: "Most firms, institutions and companies start off modestly. Unique is the record of Morgan Stanley & Co. . . . never remotely approached by any other newly created organization."[32] The firm originated issues but generally wouldn't participate in others' issues. SEC rules limited the size of underwriting stakes relative to a firm's capital, and so syndicates grew huge. On telephone issues, Morgan Stanley might marshal up to one hundred underwriters and five hundred or six hundred distributors. Its power to exclude firms from issues made it feared. Gradually much of J. P. Morgan's clientele—lovingly referred to as the Franchise—shifted to the new firm. By the late 1930s, New York Central, AT&T, General Motors, Johns-Manville, Du Pont, U.S. Steel, and Standard Oil of New Jersey, as well as the governments of Argentina and Canada, had come for securities work. Morgan Stanley was strong in the same areas as the pre-Glass-Steagall unified bank—utilities, telephone companies, railroads, heavy industry, mining, and foreign governments.

The rest of Wall Street assumed that Morgan Stanley had inherited its parent's mantle of authority. Charles Blyth and his partner, Charles Mitchell, sought to ingratiate themselves with the new leaders. "Our main job is to get under the covers and as close to them as possible," Blyth told Mitchell.[33] To cultivate Morgan Stanley, he suggested opening an account at J. P. Morgan and Company. "It is true our account won't be very important," he told Blyth, ". . . but it would show that our hearts are in the right place."[34] Such was the persisting faith in any firm bearing the Morgan name.

For New Deal reformers, it was also hard to believe that J. P. Morgan and Company didn't lurk somewhere in the shadows. That Morgan Stanley assumed so many former J. P. Morgan clients bred suspicion. One powerful

enemy who resolutely tracked Morgan Stanley conquests was Interior Secretary Harold L. Ickes. After the firm's formation, he wrote in his diary, "Meanwhile, taking advantage of the depression, the Morgan people have extended their financial domination. Ordered to put a stop to the underwriting business of their bank, they have organized a separate company which is doing even more business than was done by the bank itself along this line."[35] Ickes and other enemies bided their time. But they would soon strike back in a sustained attack, through Congress and the courts.

For J. P. Morgan partners down the street, the sudden boom in the securities market was bitterly ironic, for the parent firm was sleepy in the late 1930s. Almost the entire bank was squeezed into 23 Wall, with some scattered offices in 15 Broad Street, next door. With $430 million in total resources, J. P. Morgan and Company still ranked as the biggest private bank in the world. But Glass-Steagall had meant more than a loss of business, money, and power. It robbed the bank of some ineffable mystery that had surrounded it. With the Pecora hearings, the bank had published a balance sheet for the first time. Now the firm had to publish statements and submit to government examination. Likewise in London, Monty Norman asked Teddy Grenfell for the firm's balance sheet for the first time in 1936. Slowly, gradually, the gentleman bankers' world was being bureaucratized, and the financiers were emerging, dazed and blinking, into unaccustomed sunlight.

CHAPTER TWENTY
WIZARD

IT was now the twilight of the Diplomatic Age for the House of Morgan. Far from enjoying privileged access to the White House as it had in the twenties, it bore a special stigma. This new detachment from Washington was most apparent as the bank wrestled with the fate of the huge German loans from the 1920s—the celebrated 1924 Dawes loan and 1930 Young loan. Although these appeared under quasi-governmental auspices, Washington now dodged responsibility for their repayment and even showed a cavalier indifference. The New Dealers didn't want to jeopardize trade and security interests to enforce debt repayment, and the Morgan partners felt cheated. After all, dating back to the first China consortium, they had cooperated with the government on the assumption that they would receive official support in negotiating with defaulting debtors. That was the *quid pro quo*. Now the House of Morgan, after carrying out the bidding of its political masters, felt abandoned as Germany threatened default with Hitler's advent as chancellor in 1933.

To follow the saga of the Morgan involvement with the German reparations payments, it is helpful to retrace the odyssey of Dr. Hjalmar Schacht, who alternately posed as friend and foe of the House of Morgan. In 1930, he had resigned from the Reichsbank to protest the final terms of the Young Plan. After the Nazi election success in 1932, he sided with that party and prodded fellow bankers at the Deutsche and Dresdner banks to lend financial support. Among the German industrial class, Dr. Schacht conferred legitimacy on Hitler's thugs. At Hermann Göring's home in early 1933, he helped Hitler raise M 3 million from businessmen, a meeting climaxed by Gustav Krupp von Bohlen und Halbach's pledge, on behalf of the rich guests, to give staunch support to the Nazis. Schacht even consented to a request from Hitler that he administer the new campaign fund.

Hindenburg, yielding to Hitler's wishes, restored Schacht to his post as Reichsbank president. After 1934, Schacht was also the minister of economics. As financial overlord of the Third Reich, Schacht would supervise public works, including construction of the Autobahn, his services winning him a reputation as the evil wizard of Nazi finance, the mountebank who could make financial magic for the Fuhrer. According to William Shirer, "No single person was as responsible as Schacht for Germany's *economic*

preparation for the war which Hitler provoked in 1939."[1] In one panegyric, Hitler said that Schacht had accomplished more in a three-year period than had the entire Nazi party combined.

As a Nuremberg war criminal, Schacht would portray himself as an early foe of Hitler's, a beleaguered man trying to stop the mad progress of the war machine. He never joined the Nazi party and claimed that he had opposed the persecution of the Jews. But there was a great deal of humbug about Schacht, who liked to pretend his pure intentions were being subverted by unscrupulous German politicians. In his duplicitous style, he would tell Jewish bankers that Hitler was a temporary evil needed to restore order, and he would vocally oppose persecution of the Jews. (He feared that such persecution would tarnish Germany's image in overseas banking circles.) Then he would boast privately to Hitler that he had blocked Jewish bank accounts and channeled the money into German rearmament. Because there was some truth to his self-defense, his story is more complex than that of his unreservedly diabolic associates. In the words of Nuremberg prosecutor Telford Taylor, "This self-righteous and stiff-necked individual was and remains the most enigmatic and controversial person of the pre-war years."[2]

Dr. Schacht was an anomaly among high German officials. He remained a gentleman banker of the old school, giving Nazi finance a patina of dignity. Sporting rimless spectacles, parting his fine, white hair down the middle, smoking cigars, and wearing pinstripes and suspenders, he was indispensable to Hitler, not only for the ingenious way in which he harnessed German banking to a war economy, but for the respectability he won abroad. Having slain the 1923 hyperinflation, Schacht could fool international bankers into thinking they had a friend in Berlin who adhered to their own financial standards. And he had already won the lasting friendship of Montagu Norman. Where others saw a Nazi collaborator, Norman saw a courageous central banker fighting inflation and combating German rearmament for its incompatibility with sound finance. Schacht once told Hitler, "Only two things can bring about the downfall of the National-Socialist regime, war and inflation."[3] This was the Hjalmar Schacht that Monty Norman preferred to see. The Morgan partners were more quickly disillusioned, believing that Schacht never wanted to pay reparations and had misled them into thinking he did.

Unlike the many flunkies who surrounded Hitler, the arrogant Schacht exercised real power; finance was an area beyond the pale of the Fiihrer's obsessions. At first, he gave Schacht *carte blanche* in running the Reichsbank. "He understood nothing whatever about economics," Schacht later explained. "So long as I maintained the balance of trade and kept him supplied with foreign exchange he didn't bother about how I managed it."[4]

Bullheaded and conceited, Schacht wouldn't hesitate to yell at Hitler and took liberties that would have cost others their heads. Once the Fiihrer gave him a painting as a gift; Schacht returned it, saying it was a forgery. Nothing fazed him, and the cocksure banker had Hitler a bit bamboozled. Albert Speer noted of Hitler, "All his life he respected but distrusted professionals such as . . . Schacht."[5]

From a political standpoint, no instant alarm sounded at the House of Morgan when Hitler took office in 1933 and gained the power to rule by decree. Jack Morgan still nursed the old grudges against the Hun, but his reservations about Hitler were less moral than nationalistic. As he told his friend the Countess Buxton, "If I could feel more easy about your friends, the Boche, I should feel myself that we were all going to get along pretty well; but, except for his attitude toward the Jews, which I consider wholesome, the new Dictator of Germany seems to me very much like the old Kaiser."[6]

Nevertheless, a shift in Germany's policy toward foreign debt appeared quickly. In May 1933, Hitler dispatched Schacht to Washington for eight days of talks. To divert him on his transatlantic crossing, Lamont sent biographies of Napoléon and Marie-Antoinette—volumes that perhaps contained their own tacit message about the corruption of absolute power. Meeting with Roosevelt and Secretary of State Cordell Hull, Schacht boisterously insisted that stories about the harassment of Jews were grossly exaggerated and said that foreign protest would only backfire. He also warned that Germany was running short of foreign exchange to service the $2 billion in debt held by American investors. This White House meeting occurred during the Pecora hearings, and Schacht recorded this curious reaction from the president: "Roosevelt gave his thigh a resounding smack and exclaimed with a laugh: 'Serves the Wall Street bankers right!' "[7] Afraid that Schacht might take this literally, Roosevelt's advisers warned the president of the potential damage of his little jest. The next day, Hull rushed to tell Schacht that Roosevelt was actually shocked by the default threat. "It occurred to me that the President had not expressed any shock until twenty-four hours had elapsed," observed Schacht.[8] Roosevelt's attitude may well have emboldened Schacht in his determination to repudiate German debt held in America.

That June, Schacht announced a moratorium on long-term overseas debt. The big German loans had been multinational—the Young loan, for instance, had appeared in nine markets and currencies—but the various creditor countries didn't mount a united defense. Rather, they behaved like panicky creditors in a crowded bankruptcy court, each trying to get Germany to pay off his own bonds first. Articles appeared in the U.S. press reporting that European creditors wanted to strike separate deals with the Nazis. As a lever to pry open foreign markets to German goods, Schacht favored deals with

countries running trade surpluses with Germany. The implicit message was buy more from us, and we might look more favorably upon your bonds. It was a policy of selective default, a clever divide-and-conquer strategy that broke down creditors' unity and set them against each other. Schacht hoped that by stalling the creditors and driving down the price of the German bonds, he could buy them back at a price significantly lower than their face value—a tactic that apparently pleased Hitler.

When Lamont learned that Schacht was contemplating selective repudiation in 1934, he reminded him that Morgans had supplied over half the Dawes funds and a third of the Young funds. With pardonable overstatement, he said the bank had always advocated moderation toward Germany. Most of all, Lamont appealed loftily to international law, promises made to investors that these loans superseded all others and enjoyed special political protection. Lamont was speaking reasonably to a man already hip-deep in diabolic machinations: "Of course, we expect to see the Reich obligations on [the Young Loan], as on the Dawes loan, carried out. Otherwise all international agreements might as well be torn up."[9]

From Dr. Schacht's reply, it was clear that the usual norms of business behavior no longer applied in Germany. Written in an extravagant, hysterical style, it was not the sort of letter people usually sent to the sedate precincts of 23 Wall. Schacht began by saying Germany's problem was not default but a transfer difficulty resulting from a lack of foreign exchange. Then he veered off into bombast and mad whimsy:

> Whether you may threaten me with death or not will not alter the situation because here is the plain fact that I have no foreign valuta [foreign exchange], and whether you may call me immoral or stupid or whatever you like it is beyond my power to create dollars and pounds because you would not like falsified banknotes but good currency. . . .
>
> I would be willing to sell my brain and my body if any foreigner would pay for it and would place the proceeds into the hands of the Loan Trustees, but I am afraid that even the proceeds of such a sale would not be sufficient to cover the existing liabilities.[10]

Schacht may have wanted to drive a wedge between England and America, perpetuating tensions over war debts and reparations. By threatening to strike a separate bargain by which British bondholders received some payments (albeit at lower interest rates) and Americans didn't, he delivered a blow to Anglo-American amity. (Schacht argued that Germany's trade surplus with England allowed it to make the interest payments.)The fight over unequal treatment, first with German, then with Austrian, debt, would prove the most

divisive issue ever between J. P. Morgan and Company and Morgan Grenfell.

There had always been a latent contradiction at the heart of the Anglo-American Morgan empire. So long as U.S. and British interests coincided, it could be straddled. When those interests diverged, however, British and American partners were obliged to follow the wishes of their respective governments. They were too deep in politics to do otherwise. With J. P. Morgan and Company now a minority stockholder rather than a partner in Morgan Grenfell, there was also a new structural distance between the two firms.

For more than twenty years, Teddy Grenfell had been the Morgan ambassador to the British government. Now, somewhat unwillingly, he conveyed stiff protests from his New York partners to Whitehall. With rumours of a separate German deal with England swirling around Wall Street, Lamont drafted a letter to the British government, demanding that it take responsibility for American bondholders of German debt. Morgan Grenfell partners argued against its testy wording, but Lamont and Leffingwell refused to back down. Biting his tongue, Grenfell duly delivered the cable to Prime Minister Ramsay MacDonald. For a letter to a chief of state, it struck a faintly arrogant chord, a tone of mild menace:

Prior to the issue of the External Loan of 1924, we had not been associated with German finance, public or private, and we venture most respectfully to remind you that in your then capacity as Prime Minister you did us the honor of addressing our firm . . . by which you conveyed to us the requests of His Majesty's Government that we should undertake the placing of the Dawes Loan in this country. . . . Meanwhile, however, for the reasons indicated above, we believe that His Majesty's Government . . . will wish to use its good offices in every way possible for the protection of interests of all holders of these loans irrespective of nationality. . . .[11]

Two weeks later, Lamont followed this up by meeting with Neville Chamberlain, then chancellor of the Exchequer. It was a vintage Lamont performance—tough resolve beneath suave civility. He said Morgans had become involved with Germany only because the Bank of England wanted to put Weimar Germany back on its feet and enable it to make reparations. Affable and noncommittal, Chamberlain asked what he would recommend. Lamont asked whether Chamberlain would scuttle a separate accord with Germany if no justice were done to American investors.

Chamberlain: I should not feel justified in going so far as to cancel my British arrangements if they fail to accede to my request re U.S.A.

Lamont: No, I agree, nor should I expect you to do so. I believe that the representations you make will be so clear and strong as to go far toward getting similar treatment accorded to us.[12]

The British never rode to the rescue. What made this so galling to Lamont was that he always believed Britain had initiated the side deal with Schacht. Morgan partners were thunderstruck by what they saw as British cynicism and the end of financial leadership they had always associated with the City. Schacht himself didn't seem to dispute Lamont's version of events. When George Harrison went to Germany with Roosevelt's encouragement, Schacht professed dismay over discrimination against American bondholders. He said the British had blackmailed him into their deal and kept telling Harrison "God bless you!" for protesting to the foreign minister. Harrison came back to New York very disturbed. "He utterly disagrees with Monty about Hitler and Hitler-ism," Leffingwell told Lamont about Harrison's visit. "He didn't see a smile on any face in Germany in two days."[13]

To press his case, Lamont got Secretary of State Cordell Hull worked up about the discriminatory treatment of American bondholders. As he told Grenfell, "The American Government feels very strongly that the American investment community was had."[14] Jack Morgan appealed to Monty Norman, whom he believed to be the one person outside Germany with any influence over Schacht.

Norman wasn't so upset by the German actions and was willing to make allowances for the Nazis. He continued to harbor more hostility toward France than toward Germany. In July 1934, he arrived in New York looking sickly and dispirited. He immediately telephoned Russell Leffingwell and took a cab down to 23 Wall. Leffingwell summarized their meeting for Lamont: "Monty says that Hitler and Schacht are the bulwarks of civilization in Germany and the only friends we have. They are fighting the war of our system of society against communism. If they fail, communism will follow in Germany, and anything may follow in Europe."[15] This high regard for German culture had led Norman to back the 1924 Dawes loan in the first place. But the admiration now persisted under altered circumstances. As we shall see, most Morgan partners took a relatively benign view of German intentions, although there were skeptics from the start. The cynically acute Grenfell first penetrated Schacht's disguises, already believing in 1934 that he was building up stocks of raw materials with which to prepare Germany for war.

Meeting with Schacht at Baden-Baden in 1935, Lamont worked out a debt settlement that provided about 70 percent of the interest due on the two large German loans. After this meeting, Lamont and Schacht continued to perform

a strange duet by mail. They pretended to be normal bankers in normal times, although Schacht's behavior seemed increasingly erratic. In 1936, Morgan Grenfell partner Francis Rodd visited Schacht in Berlin and found him in a crazily jocular mood. He rather giddily instructed Rodd to "send his love" to Lamont and praised Morgans as the world's premier bank. Schacht even invited Lamont to attend the Olympic Games, held that year in Berlin.

In a power struggle, Schacht finally lost out to his arch rival, Göring. His downfall began when he balked at buying foreign exchange for Nazi propaganda efforts abroad and tried to limit military imports of raw materials to what could be obtained by barter arrangements. In the last analysis, Schacht was too orthodox a banker, favoring slower growth and civilian production rather than a permanent war economy. In 1936, sitting on the terrace at Berchtesgaden, Albert Speer overheard Schacht arguing with Hitler in his office. As Speer recalled: "Some time around 1936 Schacht had come to the salon of the Berghof to report. . . . Hitler was shouting at his Finance Minister, evidently in extreme excitement. We heard Schacht replying firmly in a loud voice. The dialogue grew increasingly heated on both sides and then ceased abruptly. Furious, Hitler came out on the terrace and ranted on about this disobliging, limited minister who was holding up the rearmament program.[16]

Göring was put in charge of raw materials and foreign exchange. Although Schacht soon relinquished the economics ministry to Göring, he retained the Reichsbank presidency until January 1939.

Schacht will reappear in the Morgan saga at the time of the Austrian Anschluss. At this point, however, suffice it to say that the German debt quarrel left deep wounds on both sides of the Atlantic and dredged up the old issue of war debts. The British felt the United States should have canceled old war debts; Americans, even Morgan partners, believed Britain could have made a more determined effort to pay. Now that the Depression had finally retired lingering issues of debt and reparations, a new set of issues over the settlement of default debt would tear at Anglo-American financial harmony. The tension would last right up until the war.

THE mid-1930s resounded with charges that to protect Allied loans the House of Morgan had led America into the First World War. Isolationists exploited this canard to try to ensure American neutrality in any future European war. They rallied the country against Wall Street, propounding a simplistic view of history that equated big business with bloodlust for war profits. A Wisconsin congressman, Thomas O'Malley, introduced a bill requiring the richest Americans to be drafted first—a foolproof way, he thought, to end wars. "It will be Privates Ford, Rockefeller, and Morgan in the

next war," he said.[17]

Portents of war were visible everywhere—for those who cared to see them. In March 1935, Hitler tore up the Versailles treaty and reintroduced obligatory military service. He boasted to Sir John Simon, the British foreign secretary, that the Luftwaffe had attained parity with the Royal Air Force. A year later, the Fiihrer occupied the Rhineland without any military rebuke from the Allies. Yet Sir Anthony Eden, secretary of state for foreign affairs, thought the best way to keep Germany from war was to strengthen Hitler's economy. In 1936, Charles Lindbergh, at the invitation of Hermann Göring, toured Germany and marveled at its aircraft factories and technology, later urging Britain and France to retreat in self-defense behind a string of British dreadnoughts and the Maginot Line.

Isolationists might portray the Morgan partners as warmongers, but they weren't alarmed by developments in Germany. In fact, they were strangely sanguine. After the Rhineland occupation, Lamont told Dr. Schacht, "The American public has to a considerable extent gotten the idea that Europe is about to plunge into the midst of another general war. . . . I may be too much of an optimist, but I do not share this view."[18] Even while espousing cooperation with England, the bank steadfastly refused to interpret Axis rearmament as the prelude to a new European conflict. For all the rhetoric about mercenary bankers, the Morgan partners were more prone to appeasement than hawkishness.

In early 1936, the ghost of World War I was revived by a Senate munitions investigation chaired by Senator Gerald P. Nye, a North Dakota Republican and adherent of Father Coughlin. With his pugnacious face and thrusting chin, Nye, like Pecora, formed a picturesque contrast to the stately Morgan partners he subpoenaed. He set out to prove that J. P. Morgan and other banks had dragooned America into war to safeguard loans and perpetuate a booming munitions business. Once again, the timid Jack Morgan was transmogrified into a venal, snarling monster. As *Time* magazine said, "Before the Committee for settlement was a scandalous question: should J. P. Morgan be hated as a war-monger second only to Kaiser Wilhelm?"[19] For Jack, who so earnestly hated the Germans, it was a mortifying comparison.

Once again, a Morgan retinue departed for Washington, occupying an entire eighth-floor wing of the Shoreham Hotel and remaining barricaded behind a phalanx of plainclothes guards. (That same year, Polaroid founder Edwin H. Land visited Jack at 23 Wall and found him guarded by men with machine guns.) As if to show their sublime contempt for the hearings and disdain for the follies of petty men, the partners dressed in dinner jackets for their nightly meal. Newspapers showed George Whitney, legs folded, elegantly reading a newspaper in a smoking jacket, bedroom slippers, and

bow tie before retiring for the night. Once again, Morgan staffers were sidetracked by a government inquiry. From a Brooklyn warehouse, they disinterred the bank's wartime documents—twelve million of them, enough to fill up forty trucks.

The Nye hearings were a flop. Unlike the Pecora hearings, where partners were defensive and stammered their way through sometimes incoherent answers, the Nye committee invited them to relive their proudest hour. "We were pro-ally by inheritance, by instinct, by opinion," Lamont boasted, admitting that partners were glad to see America enter the war.[20] At that dawn of the Diplomatic Age, he contended, the bank had scrupulously heeded Washington's wishes, waiting until Robert Lansing had replaced William Jennings Bryan and approved Allied credits.

Far from seeming bellicose, Jack looked like a sleepy, avuncular old man. When Lamont said money was the root of all evil, Jack slyly interrupted: "The Bible doesn't say 'money,' " he grinned. "It says, 'The *love* of money is the root of all evil.' "[21] And while Lamont parried questions, Jack dozed or chatted with newsmen during breaks. Indeed, he had been appalled by the outbreak of war and had issued appeals to belligerents in 1914 to stop the combat. When it came to supporting the Allies, he was proudly secure in his position. "The fact that the Allies found us useful and valued our assistance in their task is the fact of which I am most proud in all my business life of more than 45 years."[22] His personal defense was bluntly effective: "Do you suppose that because business was good I wanted my son to go to war? He did, though."[23]

The hearings had as much to do with the Depression as with the war, and there was an uproar over Jack's classic blooper: "If you destroy the leisure class, you destroy civilization." Asked by reporters to define this class, Jack stumbled: "By the leisure class I mean the families who employ one servant, 25 million or 30 million families."[24] Critics from the Housewives League of America gleefully pointed out to newspaper editors that there were fewer than thirty million families in the United States, and only two million of them had cooks or servants. As an amateur sociologist, Jack left something to be desired.

Although Morgan partners considered the controversy a sideshow, it had an enduring influence, helping to muzzle their pro-Allied views and making them gun-shy of political controversy as World War II approached. In 1934, California senator Hiram W. Johnson, an isolationist, had sponsored the Johnson Act, which forbade loans to foreign governments that were in default on their dollar obligations. Neutrality Acts were also passed that blocked warring countries from purchasing arms or raising loans in the United States. This was part of an attempt to forestall any repetition of the Morgan Export

Department or the Anglo-French loan in the event of war and to induce a steady American disengagement from Europe's affairs.

Even as America debated its position in a hypothetical European war, Mussolini launched a full-scale invasion of Ethiopia in October 1935. II Duce had a megalomaniac vision of merging this territory with the colonies of Eritrea, Italian Somaliland, and Libya to forge an East African empire. Some five hundred thousand Ethiopians were sacrificed in a campaign infamous for its savage use of mustard gas. Like the Japanese in Manchuria, Mussolini's army pretended to act in self-defense and had the effrontery to denounce Ethiopian aggression. Fifty League of Nations states condemned the violation of Ethiopian sovereignty and voted economic sanctions. Relying on voluntary compliance by American business, Secretary of State Cordell Hull asked for a "moral" embargo on sales of war materiel to Italy—shipments of oil, metal, and machinery. These exhortations were often ignored by American industry. Although Britain went along with the League's economic sanctions, it stopped short of more extreme measures, such as cutting off all supplies of oil. Prime Minister Stanley Baldwin instructed his foreign secretary, Sir Samuel Hoare, "Keep us out of the war, Sam. We are not ready for it."[25]

By the mid-1980s, the House of Morgan's enthusiasm for il Duce had cooled, as had Wall Street's in general. One student of U.S. business support for Mussolini describes the post-1934 attitude as one of "a clamorous repudiation of the whole Fascist experiment."[26] Not only did the Johnson Act block new Italian loans, but Mussolini's behavior scared away American investors. There was apprehension about the dictator in high Anglo-American circles. Visiting Stanley Baldwin at 10 Downing Street in July 1935, Jack Morgan found him "terribly disturbed and apprehensive, as all are here, about Mussolini and Abyssinia."[27] Lamont warned the bank's Roman agent, Giovanni Fummi, that the rumored African campaign would jeopardize any renewal of credits to the Banca d'Italia.

As before, the Morgan bank portrayed Giovanni Fummi as a non-Fascist who happened to have extraordinary access to Mussolini. They paid him handsomely for his services—some $50,000 a year, or the same salary Parker Gilbert received as agent general for Germany. But Fummi wasn't upset by the Ethiopian bloodshed and praised the country's economic potential. He relayed a message to 23 Wall saying that Mussolini hoped U.S. capital could be funneled into the area. To dim such expectations, Lamont replied that Ethiopia would hurt Italy's financial prospects abroad for a long time. In 1936, Mussolini sent a new Italian ambassador, Fulvio Suvich, to New York to drum up support for an Italian loan. When Italy sent troops to fight alongside Franco's insurgents in the Spanish Civil War that summer, the effort was doomed (though Lamont supported Franco—and had heated quarrels

with his son Corliss about the war). That fall, Hitler and Mussolini joined together in a Rome-Berlin Axis.

After Ethiopia, relations between Mussolini and Lamont remained in abeyance for a time. In April 1937, Lamont visited Rome, ostensibly on a pleasure trip. There was a hidden agenda behind the holiday, however. Lamont had contacted British officials, who expressed hope that Mussolini could be weaned from Hitler. He also conferred with Cordell Hull about the latter's program of lower global tariffs. In 1934, Congress had passed the Reciprocal Trade Agreements Act, an attempt to end the economic nationalism of the Depression by cutting tariffs to half their 1930 levels so long as other governments reciprocated with U.S. exports. Along with Germany, Italy was now on the road to autarky—that is, economic self-sufficiency—and Hull was alarmed by its retreat from the world economy. He thought that if the United States could conclude trade agreements with Axis powers, it might avert war. Lamont promised that in his talks with England, France, and Italy, he would promote Hull's pet notion of lower tariffs. For Lamont, it was a momentary reversion to his heady Republican missions of the 1920s.

Operating behind veils of mystery, Tom Lamont often had several reasons for his actions. He undoubtedly wanted to prevent a war and destroy the beggar-thy-neighbor spirit symbolized by the Hawley-Smoot Tariff Act of 1930. But he was also ready to forgive Mussolini his violent excesses and return to the *status quo ante.* Recently he had begun to meditate on ways of rehabilitating Mussolini in Anglo-Saxon eyes, telling a correspondent two weeks before his April trip to Italy, "I must say I prefer, of two foul evils, the fascists who make war, to the communists who seek to overthrow our governments. . . . The Duce should be presented to the public not as a warrior or in warlike attitudes, but in pastoral, agricultural, friendly, domestic and peaceful attitudes."[28] This would have been news to the half a million Ethiopian dead.

Soon after Lamont arrived in Rome, Vincenzo Azzolini, governor of the Banca d'Italia, learned of his visit. II Duce—ever eager to flaunt his popularity with world business leaders—then invited Lamont and Fummi in for a private audience. It occurred amid press reports that Mussolini would visit Hitler in late summer or early fall. It was Lamont's first chat with the Italian leader since 1930. A transcript of the April 16, 1937, meeting has survived in Lamont's papers. Mussolini began by spouting hysterical pleas for sympathy:

Duce: We have made a great conquest in Africa—that is finished now—I am for Peace, I am for World Peace—I am very strong for Peace. I

need Peace—I need Peace—I am very strong for Peace. We are satisfied.

Lamont: I believe you, Excellency, when you say that, I know it must be so, but the impression in America is very different. There you are pictured as a man who wants war rather than peace; that impression should be corrected. It is very important that in America your real attitude should be understood.[29]

As he had promised Hull, Lamont touted free-trade policies, and Mussolini hinted he would like a generous helping of American money in exchange: "America, Mr. Lamont, holds the key to economic cooperation. You see, Mr. Lamont, America has enormous quantities of gold, too much gold for the world's good."[30] Mussolini also expressed a wish for better relations with Britain, toward whom his policy had been wildly contradictory. He would talk about new agreements one day, then broadcast anti-British radio propaganda the next. In fact, the month before, he had secretly informed his army officers that he planned to destroy Britain. (Later it turned out he kept posted on British diplomacy by having his aids sift through the wastebaskets at the British embassy in Rome.) Mussolini's plea for improved Anglo-Italian relations was marred by a comic slip:

Duce: I am doing everything I can to increase the friendship with Great Britain, everything, but Great Britain is always suspicious of what we say or do, and attributes wrong reasons to our speech and actions.

Lamont: It pleases me immensely to have you say you are doing all you can to increase the friendship with England. In London last July I heard important expressions along the same line. It happened that when there I dined with the then King Edward VIII, and he said to me "now that sanctions are to be ended we must get back to the basis of our traditional friendship with Italy." Mr. Neville Chamberlain, the Chancellor of the Exchequer, who is to succeed Mr. Stanley Baldwin as Prime Minister voiced to me the same sentiments. (For a moment the Duce seemed to think that I alluded to the late Sir Austen Chamberlain whose friendship for Italy was well-known, but he remembered, and corrected himself with "Oh yes, I know that Mr. Neville Chamberlain is well disposed toward us.)"[31]

The interview had started uneasily, as if Lamont wished to register his

moral disapproval for the record. Then he warmed appreciably and resorted to the old courtier's mode, saying that Italians and Americans shared traits of industry, thrift, and imagination. He extolled Rome's tuberculosis sanatorium and regretted that Americans missed such wonders. "We spend too much time gazing at what the Romans were doing in 100 A.D., and not enough time in looking at what the Romans are doing in 1937 A.D."[32] In a vaguely surreal moment, he told Mussolini that tourism to post-Ethiopia Italy could be tremendously expanded. In a telling reminder of the old days, Lamont said he had jotted down fresh points on how Mussolini might handle public opinion. "Ah yes," said Mussolini, "I am very grateful for your counsel . . . do not hesitate to advise me direct in regard to these matters. One of my mottoes is 'advice from everyone, collaboration by many, decision and responsibility by a few.' "[33] Lamont and Fummi applauded this formulation.

Toward the close, perhaps afraid that things had gotten too friendly, Lamont returned to American fears of Italian aggression. He said—with perhaps an icy smile—"The American people, Excellency, have unbounded admiration for the marvellous achievements you have accomplished for Italy since 1922, unbounded admiration for these great material developments, but as regards yourself, Excellency . . . they are really afraid of you."[34] Smiling, Mussolini said the impression must be corrected. He urged Lamont to make a statement to the Italian press—which Lamont declined to do. Afterward, Lamont briefed William Phillips, the American ambassador in Rome, who seemed delighted by the talk.

Clearly, part of Lamont's Italian agenda was to curb Mussolini's warlike tendencies and nudge him closer to the United States and Britain. His visit enjoyed official encouragement. Yet soon afterward, Lamont reverted to propaganda work that could hardly have been sanctioned by Washington and was reminiscent of his relationship with il Duce in the twenties. True to his pledge, Lamont forwarded a memo designed to help Mussolini "enlighten American and British opinion" about his peaceful intentions. It paralleled the memo drafted for funnosuke Inouye after Japan's 1931 invasion of Manchuria, drawing specious analogies between Mussolini's actions and American history, trying to convert the story of Ethiopian slaughter into a comforting tale of Italians conquering a wilderness. How should Mussolini quiet concern? By likening the Ethiopian campaign to America's westward expansion: "In previous speeches in the last few months the Duce has spoken of the growth of new empire in Africa. His Government's ends have been achieved. There now remains the task of agricultural and economic development in Ethiopia. There is a vast and fertile region as yet largely uninhabited and uncultivated. It would yield to the hard work and intelligent cultivation of Italian emigrants, just as a half century or more ago the vast

resources of Western America were developed by American emigrants."[35]

What exactly was Lamont's purpose here? Was he trying to push Mussolini toward a new policy, or merely generating clever lines to hoodwink English and American opinion? Did he have any qualms about equating pioneers settling the American West with Italian troops hurling mustard gas? It is hard to imagine that the State Department or the British Foreign Office would have condoned this, notwithstanding *pro forma* lines about the need for world economic cooperation. After Libya, Corfu, Ethiopia, and Spain, these attempts at coaching Mussolini seem terribly misplaced. Lamont's slick publicity lines were now as empty as the dictator's own speeches:

It is true that each of the great nations of the world must have adequate defences. But preparation to that end is approaching completion on every side, including Italy's own defences; so that now the primary end today and tomorrow must be the maintenance of world peace. . . . Italy was immeasurably the leader of the Renaissance, that great revival of the arts and learning that set the whole world upon a new path of enlightenment and progress. It is that same eager vitality that marks the Italian race today. . . . Italy welcomes the study of its past and is aware what attractions its galleries, its monuments, its cities, have for friends from abroad. They should study also the modern Italy, the material development of the past fifteen years, the public works, the reclamation projects, the industrial and agricultural policies, and perhaps above all the social and welfare system with its wonderful work as shown in hospitals, sanatoria, etc. Then indeed would Italy's friends be impressed with what has been accomplished here.[36]

Lamont's last fling with Mussolini again reveals his willingness to renounce principle for convenience. The most polished man on Wall Street, known for his thoughtful gifts and exquisite courtesies, was now a victim of his own disguises. Nothing mattered any longer but surfaces; his moral center had eroded and slipped away over the years. The bullying dictator and the eloquent banker no longer seemed as antithetical a pair as they had at the start of their friendship, when Lamont was fresh from his tutelage under Woodrow Wilson. The *New York Times* once said that Lamont "was a man who hated to see a friendship come to an end."[37] His relationship with Mussolini perversely confirmed that insight.

There was, however, yet another ongoing aspect of Morgan involvement in Italy—the Vatican account, which prospered even as government business stagnated. Lamont and other Morgan partners fed portfolio advice to Fummi, who in turn advised the Vatican on American securities holdings. The bank held papal securities in custody. (Fummi occasionally bungled the signals from Wall Street, advising the Vatican in 1938 to sell American stocks just as

Lamont sent an updated report urging purchases. The Vatican then loaded up on American stocks, expecting that the Neutrality Act would be repealed, triggering a bull market on Wall Street.) Morgan judgments were always respectfully considered. As Fummi once told Lamont, “I hope you will approve of my above line of reasoning for there is no doubt that it has influenced the decision taken by the Amministrazione Speciale della Santa Sede a good deal.”[38]

Lamont conducted his own personal diplomacy to restore traditional Anglo-Italian amity. Through his friend Lady Astor, he lobbied Lord Halifax, the foreign secretary, in April 1938 and argued the need to recognize the Ethiopian conquest as a *fait accompli.*[39] He apparently didn’t worry that tossing Ethiopia to Mussolini might embolden him. Meanwhile, Neville Chamberlain dispatched his sister-in-law Ivy—the widow of Sir Austen Chamberlain—to Rome to speak with her friend Mussolini in the hopes of drawing him away from Hitler. In early 1938, the British recognized Italy’s Ethiopian conquest in exchange for Italian troop withdrawals from the Spanish Civil War. Russell Leffingwell, who had denounced the Ethiopian invasion as a “predatory war,” told Lamont he thought Britain was “throwing Ethiopia to the wolves.”[40] The British diplomatic triumph was fleeting: in 1939, Mussolini would seize Albania and sign a “pact of steel” with the Nazis.

CHAPTER TWENTY-ONE
EMBEZZLER

EMBITTERED by the New Deal, Jack Morgan didn't age gracefully or happily and divided his time between apathy and rage. He was a lonely man who had never recuperated from his wife's death. He didn't remarry and continued to tend Jessie's gardens. At his Gannochy Lodge shooting parties, he would invite the Queen Mother's sister or some comparable dowager to serve as hostess. Whether attending Yale-Harvard regattas in his boater or browsing in the Morgan Library, he gave off a solitary air. This sense of loneliness was accentuated by the grandeur of his surroundings. At Matinicock Point, he lived alone in a forty-five room house. Although a widower for nearly ten years, he refused to shut his English or American estates or vary the annual ritual that called for Camp Uncas in the Adirondacks in the spring or Gannochy Lodge in August. At exorbitant expense, he maintained butlers, housekeepers, and gardeners, as well as the fifty-man crew of *Corsair IV.* This unchanging structure provided emotional solace and support but also frittered away much of the fortune that would have gone to his heirs.

Jack took inordinate pride in his grandchildren, sixteen strong by 1935. When a four-year-old grandson asked why locomotive engineers blew whistles at grade crossings, Jack assigned high-priced Davis, Polk lawyers to find the answer. Yet he often seemed closed and aloof to his grandchildren. Once a week, he hosted a black-tie dinner for the entire family at Matinicock Point. Extremely punctual, he would stand at the door checking his watch and start exactly on time. Everybody lived in fear of being late. When he took five of his grandchildren across the Atlantic on the *Corsair*, he allowed them to read or play solitaire but not to enjoy deck games. If sensitive within, he seemed cold and distant without.

Jack still reported regularly to the Corner, taking his spot at the far end of the double row of rolltop desks, beneath Pierpont's portrait. He was an archaic figure in a world mad with reform. Change and experimentation were so alien to his nature that the crash and Depression produced no evolution in his philosophy. In 1936, he enunciated his business creed this way: "Do your work; be honest; keep your word; help when you can; be fair."[1] Another favorite saying was "Keep your mouth shut and your eyes and ears open."[2] His philosophy showed no scuff marks of the time, only a somber faith that

with sufficient patience and fortitude traditional values would prevail.

Jack didn't travel in circles likely to challenge his views. He told U.S. Steel chairman Myron Taylor that he knew nobody in favor of the 1935 Wagner Act, which sanctioned collective bargaining; and he probably didn't. Never attempting to broaden his outlook, he came to typify the New Deal stereotype of the "economic royalist." In 1935, for the first time, he instituted personal economies. He trimmed living expenses to $60,000 annually and halved his contributions to Saint John's of Lattingtown, the millionaire's church whose burial ground was so liberally graced with Morgan partners. Such economies, if arduous for Jack, still left him with a life style inconceivably majestic to ordinary citizens.

The Nye "merchants of death" hearings in early 1936 confirmed Jack's suspicion that he was the eternal target of demagogues and left him feeling depressed. During the hearings, his friend King George V died. He wrote a British friend: "the death of the King has caused a great feeling of sadness in this country as well as in yours."[3] As if they were the unconquerable curses of his house, the combined strain and fatigue of Pecora and Nye had the same effect on Jack as the Pujo hearings had on Pierpont. In mid-June 1936, while visiting Jessie's sister, Mrs. Stephen Crosby, in Massachusetts, he had his first heart attack, complicated by a severe neuritis attack, which made it difficult for him to walk.

The Morgan family wanted to transport him back to Glen Cove with minimal publicity, and he was moved by stretcher to a private railroad car. His sons, Junius and Harry, waited for him at the Mill Neck Station on Long Island. They paced the platform anxiously, smoking pipes, their hats pulled low, trying to dissuade photographers from taking pictures. As the train pulled in, Jack, in blue silk robe and white scarf, saw the photographers and lowered his window shade, his old disgust for the press welling up. An ambulance hidden in the bushes moved toward the train, and four men lifted Jack in a chair to the ground. A photographer rushed to the ambulance window for a last shot of Jack inside and Harry went white with fury. A less inhibited Morgan guard smashed the photographer in the jaw.

That winter, Jack spent two weeks cruising the South Seas, convalescing with a heart specialist on board. By now, his views of the world were etched with a corrosive anger. In late 1936, King Edward VIII abdicated, and Jack saw nothing romantic or pitiable in his plight, merely a betrayal of trust. He told Lord Linlithgow: "What a pity that the little king had not the guts enough to do his job."[4] The gutless action would prove highly advantageous for the House of Morgan. Only a year earlier, Jack had entertained the duke and duchess of York—now to be King George VI and Queen Elizabeth—at Gannochy for the Glorious Twelfth. They would continue to be guests at

Gannochy and aboard the *Corsair*. In late April 1937, Jack sailed for Plymouth *en route* to the coronation, bearing a special invitation to sit in the royal family's box. As the squire of Wall Hall, he invited two thousand guests, mostly local farmers, to celebrate the occasion at his estate. But he suffered a second heart attack and missed the Westminster Abbey coronation. He had to listen to the ceremonies over the radio.

When he returned to America aboard the *Queen Mary*, his physician advised him not to talk to reporters, lest his blood pressure rise again. (Trying to be more affable, Jack had taken to granting shipboard interviews.) As the ship docked in a thick Manhattan fog, reporters dashed all over the ship trying to find Jack. They finally tracked him down in a stuffy little room and got him talking on the subject that was his invariable downfall during the New Deal—taxes. He had already inflamed public opinion in 1935 by saying that "everybody who makes any money in the United States actually is working eight months of the year for the government."[5] When he said this, a fifth of the work force was idle and many people relied on relief or public works programs for survival. Now Jack put his foot in his mouth once again. While he was in England, Roosevelt and Treasury Secretary Morgenthau had started a campaign against tax evasion by the rich to reverse declining federal revenues. Jack didn't know how incendiary the topic had become. He told reporters: "Congress should know how to levy taxes, and if it doesn't know how to collect them, then a man is a fool to pay the taxes. If stupid mistakes are made, it is up to Congress to rectify them and not for us taxpayers to do so."[6]

Once again, Jack was flabbergasted by the public outrage that ensued; he never ceased to be a political naif. Lamont had to explain to him patiently how inflammatory such remarks might sound in the current political atmosphere. Lamont said of Jack to Walter Lippmann's wife, Faye, "You see, as a matter of fact, he is as simple as a child, and when he once gets started with newspaper men he talks with them just as carelessly as he would with his own partners."[7]. Even though Jack rushed to retract his statement, stressing that he had no sympathy for tax dodgers, the damage was already done. Two weeks later, the Treasury released the names of sixty-seven wealthy taxpayers who had used legal schemes to avoid taxes. Jack's name didn't appear on this list, but Lamont's did.

For New Dealers, Jack Morgan symbolized the self-destructive complacency of America's rich, those unable to adjust to changing times. Reading Jack's shipboard comments, Felix Frankfurter seized on them as proof of the decadence of business leaders who couldn't see that their real self-interest lay in New Deal reform. "What a temper of mind J.P. Morgan revealed in this morning's press," Frankfurter wrote to President Roosevelt. "I

nearly exploded. . . . When the most esteemed of financiers discloses such a morally obtuse, anti-social attitude, one realizes anew that the real enemy of capital is not Communism but capitalists and their retinue of scribes and lawyers."[8]

Jack was far more affected by criticism than politicians realized. The public assumed that all tycoons were crusty, unemotional, and immune to public wrath. J. P. Morgan had become less a person than a political symbol for the rich and reactionary who opposed social justice. Yet Jack had been emotionally unhinged since Jessie's death, and he remained terribly shy and unsure of himself. This tended to make him gruff, aloof, and elusive. Unsophisticated, he could be easily baited by clever reporters. A lonely widower in retirement, he poured out his grief to assorted duchesses, old college chums, and selected archbishops. He still found it hard to cope without Jessie's emotional support.

Over time, Jack had come to see the Roosevelt administration as one giant conspiracy out to hound him. Gnashing his teeth, he told Monty Norman, "The state of affairs might be so satisfactory and helpful so easily if we did not have a crazy man in charge and my chief feeling is one of resentment at what he is putting us through."[9] To Owen Young of General Electric, we owe a startling vignette that shows how dangerously frayed Jack's nerves were in early 1938. The two men were chatting at 23 Wall when Jack erupted into a tirade. He lost all control of his emotions. Young was so thunderstruck that he recorded his impressions immediately afterward, together with strict instructions not to publish them until both were dead. Young recalled Jack saying:

"I just want you to know, Owen Young, that I don't care a damn what happens to you or anybody else. I don't care what happens to the country. All I care about"—and he became vehement, almost passionate—"all I care about is this business! If I could help it by going out of this country and establishing myself somewhere else I'd do it—I'd do anything. In all honesty I want you to know exactly how I feel. And if things go on this way much longer I won't put up with 'em. I'll take the business and get out." His hand trembling—under great emotional strain.

Attempting to calm him, Young put his arm around Jack and reminded him gently of Pierpont's faith in America, the talents the Morgans had contributed to their bank. Then he tried to rouse his spirits: "You'll stay right here and outface these passing discouragements, because if you ran away you wouldn't be Jack Morgan. You owe it to the future and you owe it to yourself.' When I was finished," Young wrote, "he was silent, and I was startled to find that his eyes had filled. 'Well, Owen,' he said, 'I guess I needed some one to talk to

me like that. And I guess you're the only one who could have done it.' "[10]

Jack never found peace under Franklin Roosevelt, at least not until the Second World War dissolved the feuds of the 1930s in a warm bath of patriotic fervor. Only when the focus of national attention switched from the Depression and domestic economic inequities to foreign menace did the Morgan bank and the New Deal again find any common ground.

EVEN as the House of Morgan fended off assaults from Franklin Roosevelt, it experienced the ire of his successor, Senator Harry S. Truman of Missouri. In his first Senate term, Truman later said, he spent more time on railroad finance than any other single subject. This led to a collision with the House of Morgan, which, with Kuhn, Loeb, still dominated railroad issues in the 1930s. Struggling to compete with new truck and air traffic, the railroads were an intractable Depression problem, with bankers blamed for their mismanagement. In 1935, Truman joined a subcommittee chaired by Burton K. Wheeler, a progressive Montana Democrat, investigating banker influence over railroads. The Wheeler hearings studied the manacles that bound railroads to exclusive relations with traditional bankers. From the time of Louis Brandeis's campaign against Morgan domination of the New Haven Railroad, reformers had urged an arm's-length distance between bankers and clients. Now they again espoused competitive bidding to allow all bankers to compete for a given issue.

By a curious historical freak, Max Lowenthal, counsel to the Wheeler subcommittee, introduced Truman to that ubiquitous Morgan demon, Louis Brandeis, who was now a Supreme Court justice. In the late 1930s, justices still received visitors for tea one afternoon a week. At teas held at his California Street home, Brandeis would leave other visitors and buttonhole Truman for hours, quizzing him on the hearings and arguing for stricter regulation of railroads and a severing of their Wall Street links. Truman was converted to Brandeis's gospel of a competitive economy based on small business and zealous antitrust regulation. This philosophy exerted a powerful hold during Roosevelt's second term and naturally exacerbated the clash with that apostle of big-business planning and economic concentration, the House of Morgan.

Anticipating the onslaught of Senator Wheeler and his committee, the Morgan partners in 1935 acted to jettison that great embarrassment from the Jazz Age—the bankrupt Van Sweringen brothers. For five years, Morgans had secretly propped them up with a $40-million "rescue" loan, even though they owed $8 million in back interest charges. When the brothers again defaulted in May 1935, the bank decided it would be political suicide to take control of their collateral—the vast Alleghany railroad and their real estate empire.

Political expediency demanded they cut their losses and sell off Alleghany stock. This need to propitiate Washington was a striking sign of diminished Morgan power and prestige. The bank placed a small newspaper ad announcing plans to sell off the collateral at an auction. It was a shabby anticlimax to the bank's once-glamorous relationship with the Van Sweringens.

On September 30, 1935, the remnants of the Van Sweringen empire went under the gavel at the securities auction room of Adrian H. Muller and Sons. Mullers was known as the securities graveyard, and its offices had an appropriate view of the cemetery of Saint Paul's churchyard. Beneath bare electric bulbs, in a drab room strewn with dusty paintings and worthless junk, George Whitney sat with legs crossed on a cheap folding chair. Smart and well tailored, he smiled blandly and tried to look blase at this moment of Morgan disgrace. The House of Morgan's handsome, blond attorney, Frederick A.O. Schwarz of Davis, Polk, and Wardwell, brought along the Alleghany securities in two rich-looking leather portfolios. It was a packed house. In the rear, like a resurrected ghost of the 1929 crash, a tense, pale Oris Van Sweringen flitted about. With twenty-eight thousand miles of track, or a tenth of the entire American railroad system, Alleghany fetched only $3 million, exposing a loss of $9 million apiece for both Morgans and Guaranty Trust. And it turned out that the indestructible Van Sweringens had repurchased the railroads by creating one last holding company and getting two associates to advance the cash.

Afterward, George Whitney—with a tight-lipped smile—shook hands with a happy, flushed Oris Van Sweringen. "I would rather have paid the bill," Oris whispered to Whitney. The funereal auction room provided a fitting end to the fiasco. But following the strange copycat pattern of their lives, the Van Sweringens died in quick succession. Mantis died that December. Eleven months later, Oris arrived in Hoboken for a meeting at Morgans and died of a coronary thrombosis while still in his private sleeping car. He left an estate consisting of hardly much more than Mantis's life insurance. The Van Sweringen railroads, meanwhile, remained heavily in hock to the banks.

The auction didn't pacify the Wheeler investigators. Even Glass-Stea-gall and the creation of Morgan Stanley hadn't modified Senator Wheeler's belief that J. P. Morgan and Company controlled the railroad securities business. He asked one witness, "But generally in the Street is it not conceded that Morgan Stanley & Co. is the same thing, or is just as much dominated by Morgan, as before?"[11]

For six months in 1936, Wheeler investigators pored over records at 23 Wall Street: once sacred, confidential documents were becoming increasingly smudged with the fingerprints of government investigators. Committee counsel Max Lowenthal became the new Morgan bogeyman, and George

Whitney complained to Jack about the “Jewish lawyer element” behind the investigation.[12] Whitney thought the Van Sweringens the real object of their investigation, with the bank serving as their proxy after they died. In 1937, Senator Wheeler, distracted by the battle over Supreme Court reform, appointed Truman as acting chairman of the railroad investigation. At this point, the committee turned to the Van Sweringen’s 1930 purchase of Missouri Pacific, bought with proceeds from the Alleghany underwriting of 1929, made notorious by the preferred list.

A future president was now educated in the Wall Street plunder of the 1920s. As Margaret Truman recalled, “It was my father’s investigation of the Missouri Pacific that really enraged him and convinced him for all time that ’the wrecking crew,’ as he called Wall Street financiers, were a special interest group constantly ready to sacrifice the welfare of millions for the profits of a few.”[13] Under Alleghany—and ultimately Morgan control—the Missouri Pacific had become an open scandal. The railroad was milked for dividends while management fired thousands of workers, abandoned improvements, and made no provision for an emergency fund. There were also malodorous political dealings with Missouri legislators, one state senator having received $1,000, which he itemized as “covering services in the Alleghany-Missouri Pacific matter.”[14]

The feisty Truman dug in his heels against tremendous Wall Street pressure to desist from the investigation. He blamed the House of Morgan for his troubles. As he wrote his wife, Bess, “It is a mess and has created a terrible furor in New York. Guaranty Trust and J. P. Morgan have used every means available to make me quit. I’m going to finish the job or die in the attempt.”[15] Truman saw himself as the upright country boy who wouldn’t be hoodwinked by smart-alecky New York types, and he had a cultural as well as a political aversion to the bank. Even as a young man, he had considered Pierpont a snob who consorted with decadent European royalty, and he was quick to pick up on George Whitney’s air of superiority, his disdain for little midwestern senators. “Mr. Whitney is very much inclined to feel his position,” he told Bess. “He came to my office at about a quarter to ten and told me what he was going to do. I simply asked him who the chairman of the committee happened to be and he immediately dismounted and went along like a gentleman.”[16] Truman’s experience left him with an enduring view of Wall Street bankers as smart, greedy, and oblivious to the hazards of concentrated wealth. The ordinary government bureaucrat, he declared, was no more a match for Wall Street lawyers than a lamb for a butcher.

The Wheeler hearings spawned a Morgan enemy who would plague both J. P. Morgan and Company and Morgan Stanley for twenty years. Robert Young was a self-styled Texas populist who had worked for General Motors in New

York and made a fortune selling short in the 1929 crash. He left to form his own investment firm, buying for himself, GM president Alfred P. Sloan, Jr., and other auto company executives. After buying a major block of Alleghany stock in the early 1930s, he and his clients were rebuffed by Morgans and Guaranty Trust in securing a board seat. Young would never forget this insult.

After the Van Sweringens died, Young and his associate, Allen Kirby, an heir to the Woolworth fortune, bought control of the bankrupt Alleghany empire, still heavily mortgaged to J. P. Morgan and Company and Guaranty Trust. But rather than being a pliant client, Young decided to use Alleghany as a springboard for an assault on the House of Morgan itself. While other businessmen bucked the New Deal, Young cleverly mouthed its slogans and cast himself as a plucky outsider, proclaiming his mission as "saving capitalism from the capitalists." He said he wanted to diffuse the power of Morgans and its associates. Lamont was outraged by Young's testimony before the Truman subcommittee and called him on the carpet at 23 Wall. It was a dressing down that stung for the rest of Young's life. When he told Lamont that he intended to keep him informed about his Alleghany rehabilitation plans, Lamont replied, "You don't understand me. I want not only to be informed, but I want to help guide you in your policies."[17]

For Young, all was revealed in a flash of light. He often repeated the story, the way sinners retell their moments of conversion. Lamont had made him feel "just like a country boy" and had "literally put me on the carpet, spanked me and raked me over the coals for having the temerity to be developing a . . . plan without discussing it with Morgan's."[18]

Inflamed by Lamont's high-handed manner and emboldened by the Wheeler hearings, Young led a revolt against Morgan hegemony in railroad finance. His main target was the exclusive relations that gentleman bankers demanded from clients. The House of Morgan had managed issues for the C&.O railroad, which was part of the Alleghany empire. Young and his banking associates, Harold Stuart of Halsey, Stuart in Chicago and Cyrus Eaton of Otis and Company in Cleveland, laid a trap for the Morgan interests in November 1938. Young traveled out to Cleveland in a private railroad car with Harold Stanley of Morgan Stanley and Elisha Walker of Kuhn, Loeb for a meeting of the C&O finance committee. The New York bankers expected to negotiate a new $30-million bond issue in private.

Stanley and Walker must have known something was afoot, for they had been asked to submit sealed bids for the issue. It was unprecedented for a Morgan Stanley partner to travel to a board meeting in this way. In what he doubtless thought a great concession, Stanley told the meeting that he would allow Kuhn, Loeb's name to appear alongside Morgan Stanley's as co-manager. At this point, Young delivered his bombshell: "Mr. Stanley, we are

not interested in the advertising, or whose name appears above whose. . . . What we are interested in is what C&O is to get for the bonds."[19] Young suddenly disclosed that he had brought a competitive bid from Otis and Halsey, Stuart that would net the C&O $3.5 million more than the terms proposed by Morgans and Kuhn, Loeb. Some old Van Sweringen loyalists on the board still wanted to accept the traditional Wall Street bankers. Young threw them into confusion by threatening to sue them if they rejected the lower bid. He pranced about the room singing, "Morgan will not get this business! Morgan will not get this business! "[20] The flustered directors recessed, conferred with lawyers, then came back and accepted the lower bid.

Young's palace coup inaugurated a brand-new era on Wall Street. Instead of having gentleman bankers privately negotiate issues with clients, more issues would be opened up to competitive bids. This typically meant smaller "spreads" between the price paid to the company and the price at which the issues were resold to the public. With smaller profit margins for the investment bankers, more money, in theory, would remain for the issuer.

During the next two years, the *troika* of Young, Eaton, and Stuart got two other railroads to accept competitive bids. In 1941, the SEC promulgated Rule U-50, mandating competitive bidding for public utility holding company issues. In 1944, the Interstate Commerce Commission enacted a similar ruling for railroads. However notable these victories for anti-Wall Street forces, they didn't touch the far more lucrative industrial issues outside of railroads and utilities. The major proponents of old-fashioned banking would be Harold Stanley and his firm. Stanley would argue against the "casual intermittent connections" between bankers and issuers produced by competitive bidding, warning that companies would receive poor advice and sell issues at improper prices. If the argument were transparently self-serving, industrial America would willingly submit to its logic. For another forty years, blue-chip America would agree to exclusive relations with Morgan Stanley, an alliance unbroken until IBM rebelled in 1979.

CLEARLY, if there were going to be a rapprochement between the House of Morgan and the New Deal, it wouldn't come from Jack Morgan, whose implacable bitterness made him politically valueless. It also wouldn't come from George Whitney, the very model of the patrician banker that the reformers abhorred. Any new approach to the White House would have to involve Tom Lamont, who yearned to return to the political game and chafed under his Washington exile.

The turbulent year of 1937 presented a possible opening for the bank. After drifting from spring to late summer, the economy and the stock market nose-dived in September. So steep was the fall in stock and commodity markets

that October 19 was dubbed Black Tuesday. Markets slumped almost halfway to their 1932 lows. Investment banks took such a severe beating on two issues—Bethlehem Steel bonds and Pure Oil preferred stock—that there was talk of closing the Stock Exchange. Assuming the Morgan role of Wall Street leadership, Harold Stanley called in the heads of several investment banks and took an informal survey of their condition. In return, he offered them a rare, confidential look at Morgan Stanley's books. Glass-Steagall had left an investment banking field of small, poorly capitalized banks, and the inevitable shakeout now began. Suffering heavy underwriting losses, the firm of Edward B. Smith and Company—the successor to Guaranty Trust's securities affiliate—merged with Charles D. Barney and Company to form Smith, Barney, a firm that fell into the Morgan group. The confidence of the New Deal was shaken by this sudden reversion to the unsettled financial markets of the early 1930s.

The industrial sector was also in turmoil. In January and February of 1937, the fledgling United Auto Workers paralyzed General Motors with sit-down strikes. In Flint, Michigan, police fired on strikers armed only with slingshots. From 14 percent in 1937, unemployment would zoom to 19 percent the following year. These events not only created a sense that the New Deal had stalled, but they intensified conflicts between the two chief administration factions. One group—inspired by Louis Brandeis and identified with Felix Frankfurter, Thomas G. Corcoran, and Benjamin V. Cohen—blamed big business for America's failure to shake off the Depression and advocated more competitive markets. Their ally, Robert H. Jackson, chief of the Justice Department's antitrust division, argued that monopolists had "priced themselves out of the market, and priced themselves into a slump."[21] Echoing this theme, Interior Secretary Harold Ickes warned of the pernicious influence of America's sixty ruling families. Roosevelt was fond of experimentation, and his political church had many pews. For the moment, he favored the antitrust faction and told brain truster Rexford G. Tugwell that it might "scare these people [i.e., business] into doing something."[22]

There was another wing of brain trusters who had been influential during the so-called First New Deal, from 1933 to 1935. They admired the technological efficiency of big business and regarded the Brandeis view of a small-scale, competitive economy as a fanciful wish for a bygone America. They accepted the inevitability of economic concentration and advocated public control of the large economic units rather than vainly trying to break them up. They denounced the Jackson-Ickes speeches as demagogic and counterproductive. By late 1937, they were emboldened to mount a counterattack when FDR told Tugwell that "perhaps a message addressed to him by a mixed group of labor and business leaders would be one way in

which he could find means for retreat and a change of policy."[23]

In fashioning their group, these left-wing New Dealers found common cause with Morgans. This wasn't as contradictory as it sounded. From Pierpont's day, the House of Morgan had supported industrial planning, albeit under private control. What were the railway associations and U.S. Steel if not planned economic systems? (We recall the covert ideological link between the bank and the Progressives, epitomized by the friendship between Teddy Roosevelt and George Perkins.) At the same time, the partners were by no means hostile to all federal intervention to stop the Depression. If they hewed to the balanced-budget dogma and opposed higher taxes, Lamont, Leffingwell, and Parker Gilbert also advocated cheaper money to combat deflation. By contrast, the American Bankers Association attacked Roosevelt's policy of low interest rates. The obscurantism of their fellow bankers sometimes bothered the Morgan men. "I sometimes wonder whether we ought to continue to give our silent sanction to the American Bankers Association by continuing our membership in it," Leffingwell said, blaming tight Fed policy in 1936-37 for that year's downturn.[24] In modern parlance, the Morgan partners were sympathetic to macroeconomic management of the overall economy, even if they deplored microeconomic regulation of specific industries.

Adolf A. Berle was an important theoretician of government planning, and in 1932, with economist Gardiner Means, he co-authored a classic text, *The Modern Corporation and Private Property.* Berle and Means insisted that the large corporation was an ineradicable fact of modern economic life and that government had to adjust to it. Disturbed by Robert Jackson's speeches, Berle started to correspond with Lamont, who, of course, spoke kindly about big business, which he asserted had higher ethical standards than small business. He also stressed his allegiance to Roosevelt's foreign policy and a good portion of his domestic policy as well. There was considerable poetic embellishment here. Not long before, Lamont had complained to his close friend Lady Astor about the "extravagance, waste, and loose administration" of Roosevelt's White House.[25] But whatever license he took, Lamont was at least willing to talk and bargain with the New Dealers—a vast improvement over the fruitless rage of Jack Morgan and the rest of diehard Wall Street. Lamont struck a deal with Berle: he would support relief payments and deficit spending in exchange for a repeal of the surplus profits and capital gains taxes. At the same time, political attacks against business, especially utilities, had to end. This was the sort of political horse-trading so conspicuously absent from previous Morgan efforts to affect the New Deal.

On the afternoon of December 22, 1937, eight members of a new Advisory Group met at New York's Century Club, with Berle as chairman. Lamont and

Owen Young of General Electric represented big business; Rexford Tugwell and Charles Taussig spoke for the New Deal; and Philip Murray, president of the steelworkers' union, John L. Lewis of the Congress of Industrial Organizations, and CIO counsel Lee Pressman were there for the labor movement. In a decade badly polarized by class conflict, it was a unique moment. The eight men jointly opposed the antitrust prosecutions of Robert Jackson and endorsed the broad outlines of an agreement that had already been worked out by Berle and Lamont. At the end, Tugwell promised to set up a meeting with Roosevelt to discuss the pact.

As a creature of the shadows, Lamont imagined the meeting with Roosevelt on January 14, 1938, would be a private, discreet affair. Instead, the participants had to run a gauntlet of photographers and reporters. There were press gibes about "Mr. Berle's economic zoo" and front-page coverage supplied by unsympathetic White House leaks.[26] Nevertheless, it was a productive meeting, with the conferees approving expanded purchasing power through federal spending rather than the old deflationary shaving-wages approach to hard times. Despite Roosevelt's desire for more meetings, the experiment was stillborn. Brandeis-influenced regulators in the administration—such as Thomas Corcoran and Ben Cohen, who drafted the securities law—opposed such overtures to business. And a far-left faction in the CIO was equally bent on spiking this nascent business-labor-government triumvirate.

For his part, Lamont regretted that the White House meeting had degenerated into cheap political theater and that the cooperation offered by him and Owen Young "had been used to make third rate politics."[27] At a time of political invective, it was a missed opportunity that demonstrated the potential benefit of practical discussions between business and labor. For the House of Morgan, it was an especially irretrievable chance, because the White House meeting occurred on the eve of a Morgan scandal that would turn the clock back to the dark days of 1933, calling into question the partners' view of themselves as enlightened, public-spirited financiers.

FOR the House of Morgan, the winter of 1937-38 turned into a time of debacle and mourning. In February 1938, worn by responsibility and the labors of a precocious early adulthood, forty-five-year-old S. Parker Gilbert died. The prodigy who ran the Mellon Treasury Department in his twenties had suffered from hypertension; his death was caused by heart and kidney problems, but many thought he had worked himself to death. The years of staying till two in the morning at the Treasury and the years in Weimar Berlin, where the Germans noted his unrelenting devotion to work, had taken their toll. Earlier, Gilbert and his bride, Louise, a Kentucky belle whose racy sayings were repeated around Wall Street, had postponed their honeymoon for

five years. After joining the bank in 1931—Parker hadn't asked for a set salary, waving it aside as a detail—the Morgan partners protected him, always urging him to vacation and conserve his strength. His prodigious work and dedication earned him decorations from France, Belgium, and Italy and honorary degrees from Harvard and Columbia. A year after he died, the pretty, round-faced Louise married Harold Stanley, whose first wife had died in 1934. This not only created a novel link between J. P. Morgan and Morgan Stanley but meant that Louise's son, S. Parker Gilbert, Jr., Morgan Stanley chairman in the 1980s, would claim a unique Morgan lineage.

Parker Gilbert's death came two weeks before scandal broke. If the House of Morgan lost its investment banking business with Glass-Stea-gall, it perhaps lost its honor in the Richard Whitney case. Where Ferdinand Pecora had exposed questionable practices—things legitimate but of dubious wisdom —the Whitney scandal was for the House of Morgan a closer brush with the law. The case became a morality play of old versus new Wall Street, of private versus public trust. It would do more than just scotch Lamont's attempt to ingratiate himself with the New Deal. It would also speed reforms of the New York Stock Exchange.

As president of the Exchange from 1930 to 1935, Richard Whitney had been the most arrogant Wall Street foe of federal securities regulation. For New Dealers, he personified the smug insolence of the *ancien régime* on Wall Street. When he testified about securities reform before the Senate Banking and Currency Committee in 1932, he lectured the senators on the need for a senatorial pay cut. Opposing creation of the SEC, he told Pecora's investigators, "You gentlemen are making a great mistake. The Exchange is a perfect institution," and he wouldn't let brokers answer the Pecora questionnaires.[28] In 1937, he met his match in SEC chairman William O. Douglas, who succeeded Joe Kennedy that year. Douglas had engaged in talks with Stock Exchange president Charles R. Gay about Exchange reform, and Whitney led a board faction opposed to such efforts. In the autumn of 1937, Douglas gave the Stock Exchange leaders a stern tongue-lashing: "The job of regulation's got to be done. It isn't being done now, and, damn it, you're going to do it or we are."[29] Resigned to the need for change, Gay appointed a committee under Carle C. Conway of Continental Can to study reforms. In January 1938 it recommended a complete revamping of the Exchange, including a full-time paid president, a professional staff, and nonmember governors. It was amid such rancorous skirmishing that the Richard Whitney scandal would unfold.

George and Richard Whitney were both tall, impressive, and patrician. Sons of a bank president, they had a Boston Brahmin upbringing and had attended Groton and Harvard. People would notice the gold watch chain with

the Porcellian pig that Richard wore from his Harvard days. Morgan partner George had developed a dislike of his Groton classmate Franklin Roosevelt that he never shed. “My brother and I went to college, and we were always comfortable,” he said. “There was no poor-boy stuff about this.”[30] George came to Morgans via Kidder, Peabody, becoming a partner in 1919.

With a ruggedly handsome face, solid jaw, and elegant hauteur, George was emblematic of the Morgan bank in those years. A British visitor later commented, “George Whitney—tall, slim, iron gray head, very goodlooking and altogether charming—Miss Macey regards him as dangerous both to men and women!”[31] He perpetuated the Morgan tradition of fashion-plate partners. By a splendid coincidence, he had married Martha Bacon, daughter of Robert, the Greek God of Wall Street who had so entranced Pierpont.

By the late 1930s, George Whitney ran the Morgan bank and was a director of Kennecott Copper, Texas Gulf Sulphur, Johns-Manville, and Guaranty Trust. As the head of domestic underwriting, he suffered more than other Morgan partners from Glass-Steagall and watched his business pass into Harold Stanley’s hands. He was greatly respected on Wall Street and, despite his reserve, very popular in the bank. Of the Morgan partners who trooped to Washington to answer questions, George Whitney often seemed the most snobbishly indignant, as if unwilling to concede the legitimacy of the proceedings. Just when it looked as if New Deal attacks might relent, the scandal that broke meant more government inquisitors trying to penetrate his polished defenses.

George grew up in the shadow of his older brother, Richard, the star of the family. Richard’s early career on Wall Street seemed to live up to his family’s high expectations. On Black Thursday in 1929, as vice-president of the Stock Exchange, he had taken the fabled stroll, placing the bid for U.S. Steel and other stocks; the following spring he was elevated to president of the Exchange, the youngest person in history to hold the position. He became popularly known as the man who halted the panic of 1929 and emerged as something of a folk hero.[32] Cold and pompous, he was Mr. Wall Street, presiding in a black cutaway in his palatial suite on the Exchange’s top floor. In the private-club atmosphere, he represented the reactionary elements, the floor traders and specialists who resisted federal regulation, against the relatively more liberal retail brokers.

Richard’s association with J. P. Morgan went beyond his brother. His firm, Richard Whitney and Company, was the major broker handling gilt-edged bonds for the bank. Even if nobody at Morgans had been involved in the scandal, it would have reflected on the bank. As journalist John Brooks has said, “When the gods of 23 Wall materialized on the earthly market across the street, the bodily form they took was that of Dick Whitney.”[33] The bank

generally stayed aloof, not involving itself in disputes at the Exchange, and was dismayed by the popular impression that Richard Whitney represented its views. By the time the scandal broke, it was too late to correct that impression.

Richard Whitney led a double life in the 1930s. As he defended pools, short sales, and other speculation from Washington attacks, he was struggling with an addiction to gambling. He was a sucker for fast-buck artists. He bought stock in a Florida fertilizer company right before that state's economy collapsed and invested in a bootleg applejack called Jersey Lightning. All the while, he lived like a country squire. Married to the heiress daughter of a former president of the Union League Club, he bred thoroughbreds at a five-hundred-acre New Jersey estate, presided over the Essex Fox Hounds, owned a Fifth Avenue townhouse, and swaggered about like a tycoon.

Chronically indebted, Richard was always borrowing and enlisting people in joint investment schemes. In 1929, he tried to lure his distant cousin, Jock Whitney, into an investment partnership. But by then Richard's reputation was already sufficiently murky that lawyer Lewis Cass Ledyard talked Jock out of it. (Later, with his friend David O. Selznick, Jock would buy the movie rights to *The Story of Richard Whitney.*) The remarkably faithful George kept Richard solvent and indulged his fantasies of financial glory. Before the crash, George lent Richard $500,000 to buy a Stock Exchange seat. After that, the loans grew more frequent, and Richard ran up a staggering $3-million debt to his brother. These loans permitted others; as Richard panhandled on Wall Street, people assumed George stood behind him. The fear and respect accorded the House of Morgan was such that throughout Richard's protracted financial crisis, nobody ever demanded repayment.

In 1931, the Morgan bank made a $500,000 loan to Richard that had to be continually renewed. The partners professed to like Richard's roguish style, but with deep, unspoken reservations. At one point, they tried to get a veteran Stock Exchange governor to merge his firm with Richard's in order to curb the latter's excesses. Several times, Lamont warned George that Richard's shrilly condescending attacks against securities reform were counterproductive. George himself knew Richard was being reckless. And when Morgans underwent its first inspection by state bank examiners in 1934, George had to supply his own securities as collateral for Richard's loan.

By the mid-1930s, in a sure sign of desperation, Richard was approaching Jewish Exchange members for loans, even though he had blackballed them from the Exchange's upper echelons. In 1936, George asked partner Henry P. Davison, Jr., Harry's son, to inspect Richard's finances. While quizzing Richard in a polite, offhand manner, Davison noticed that his loans lacked sufficient collateral. Worse, Richard was using borrowed securities as collateral for more loans—the broad and open highway to financial ruin so

memorably paved by William Crapo Durant a generation before.

At this point, Richard graduated from poor judgment to outright crime and began to loot two blue-blooded institutions. The Stock Exchange had a $2.5-million Gratuity Fund, which provided death benefits to members' families; Richard helped himself to $1 million of its securities as collateral for loans to himself and his firm. As treasurer of the New York Yacht Club, he misappropriated $150,000 in securities. The scandal was uncovered when Richard Whitney skipped a meeting of the Gratuity Fund trustees and a meek clerk divulged the missing securities. Suddenly Richard had to replace the "borrowed" shares. Among others, he tapped Averell Harriman for $50,000 but needed bigger money. On November 23, 1937, he went to George for a $ 1-million emergency loan. The bank's formal culpability began here, because Richard admitted his criminal acts to his brother. It must have been a nightmare for George, who had spent years in Washington hotly defending the House of Morgan against insinuations of impropriety. As Richard said of George, "He was terribly disturbed and aghast that it could have been done and asked me many, many times why I had done it, and just couldn't understand it—thunderstruck, as he had reason to be."[34]

Lacking ready cash, George went to Lamont and told him Richard was in a "very serious jam." ("Jam" would be the all-purpose euphemism of the scandal.) He admitted the misappropriation of Stock Exchange securities and said they had to be replaced the next day. Cool but sympathetic, Lamont said, "Well, that is a devil of a note, George. Why, Dick Whitney is all right; how could he mishandle securities even for a moment, no matter what the jam?"[35] The next day, in an extraordinary act of fear or friendship, Lamont sat down and wrote out a personal check for $1 million; George then made it over to Richard. Two weeks later, after repaying Lamont, George asked Jack Morgan if he could withdraw money from his partnership capital, vaguely referring to Richard's being in an "awful jam." Jack didn't inquire as to the reason. He later said he assumed the money was for a business matter.

Because Lamont and George didn't report Richard's crime, they were guilty of misprision of a felony. For three months, they knew Richard was a crook but told nobody at the Stock Exchange and handled the embezzlement as a matter best settled privately among gentlemen. They faced an excruciating dilemma. The Morgan partners never paid bribes and prided themselves on their integrity, but now there were strong temptations to hush up the scandal. George was naturally reluctant to expose his brother's crimes. And the bank knew the New Dealers would gladly exploit a scandal to impose further reforms on Wall Street. They didn't want to throw Richard to the liberal Democratic wolves, especially to William O. Douglas, who was ready to pounce on the House of Morgan and the Stock Exchange.

A zealous regulator with a bottomless hatred of Wall Street, Douglas was a certified Morgan-hater. He had labeled the "Morgan influence . . . the most pernicious one in industry and finance today."[36] He loathed the "goddamn bankers" and castigated the "financial termites" driven by a thirst for immediate profit. He continually plied Roosevelt with memos about the need for new regional industrial banks to "displace the Morgan influence in the various regions [with] a new and enlightened leadership in the business."[37] Douglas was also conducting his crusade against the New York Stock Exchange, which he regarded as an archaic private club. In fact, he threatened to take over the Exchange the same month Richard went to George for his emergency loan.

It is apt at this point, before examining the final act of the Whitney scandal, to relate a small anecdote that deserves a place in the Morgan annals. In February 1938, Richard took a $100,000 loan from a Walter T. Rosen. Evidently Rosen was well versed in Morgan lore, for in agreeing to the loan, he told Richard, "I have always been much impressed by the attitude of the elder Mr. Morgan who held the view that the personal integrity of the borrower was of far greater value than his collateral." With a straight face, Richard replied, "Mr. Morgan was entirely right."[38] By this point, Richard had racked up $27 million in loans.

On March 5, 1938, while George was recuperating from an illness in Florida, Richard suddenly appeared at the Links Club. He interrupted Morgan partner Frank Bartow at a bridge game. "I am in a jam," he blurted out and asked Bartow for a loan. He admitted that he had embezzled shares from the New York Yacht Club. Bartow said, "This is serious." Richard replied, "This is criminal."[39] Richard was about to appear before a Stock Exchange investigative committee and desperately needed money. Bartow refused to make a move before consulting a lawyer. The next day, he and Jack Morgan met with John Davis, who warned that any attempt to lend money to Richard could ruin the House of Morgan.[40] Their refusal to help sealed Richard's fate. When they telephoned George in Florida and told him of his brother's impending downfall, George simply gasped, "My God!"[41]

On March 7, 1938, the board of governors of the Stock Exchange voted misconduct charges against Richard Whitney. The next morning, an Exchange representative sounded the gong on the trading floor and announced the suspension of Richard Whitney and Company for insolvency. Pandemonium followed, and share prices plunged. Soon afterward, New York County district attorney Thomas E. Dewey indicted Whitney for grand larceny and securities theft, including a $100,000 theft from his wife. It came as a great shock to America's aristocracy, including President Roosevelt. With old class loyalty surfacing, the president sat teary-eyed when William O. Douglas

brought him the news as he breakfasted in bed. “Not Dick Whitney!” the president cried; “Dick Whitney—Dick Whitney. I can’t believe it!”[42] For a moment, the economic royalists seemed as unconscionable as New Deal slogans claimed.

The House of Morgan was outraged by the hastily arranged SEC investigation into the Whitney scandal. The crowded New York hearings took place at 120 Broadway, right near the Corner. Dean Acheson of Covington, Burling represented the Stock Exchange, while a young SEC lawyer named Gerhard A. Gesell led the questioning. When Ge-sell asked Jack Morgan whether he thought he had responsibilities to the Exchange in the matter, Jack replied, “No, none at all.”[43] When Gesell asked why Morgans had lent money to Richard, Jack replied that he had never inquired as to the reason. “Well, you didn’t think it was wine and women and horses, did you?” Gesell asked. When Jack said no, the sum was too large for that, everybody laughed.[44] Tired and defeated, Jack sat with eyes shut through much of the testimony, as if it were a bad dream from which he would soon thankfully awake. Gesell later praised him as a “perfectly delightful old gentleman . . . mellow and always truthful.”[45]

Lamont’s usual sangfroid deserted him. At the hearings, he admitted that it hadn’t occurred to him that Richard was a thief, that he lent the money to George, and that he assumed Stock Exchange officials knew of the share dealings. He indignantly asked, “Would you expect me, Mr. Gesell, to say to Mr. George Whitney, ’Yes, George, I will help you out to cure this default, which you believe is a perfectly isolated thing, but I must trot down to the district attorney’s office and denounce your brother forthwith?”[46] Lamont said he had done what any friend would do. Similarly, George Whitney said he had done what any brother would do.

Lamont’s papers confirm his sense of bafflement. Even to his friend Lady Astor, he felt obliged to plead his innocence:

It is all a bit like Alice in Wonderland to me. Ought we all to forget the principles on which we were trained to help one another, to try to forgive and to try to give the fellow another chance? . . .

> Of course, as the evidence proved, Dick was a thoroughgoing crook. He lied to George up to the last moment, he falsified his books, he deceived his wife and children, etc. etc. But all this was unknown to George last November at the time that he tried to help Dick undo the wrong that he had done.[47]

Although Richard Whitney pleaded guilty to grand larceny, George and Lamont escaped punishment. Prosecutor Dewey perhaps thought the rich had suffered enough. But the SEC report harshly criticized the pair and said they

had known of Richard's criminal conduct and financial difficulties. (Even before seeing the report, Jack told Lamont and George it would be another "poisonous" SEC document.[48]) Hard and relentless, William O. Douglas wanted Morgan blood. During the hearings, he summoned Gesell to his office and said, "The press tells me you're being soft on George Whitney." Gesell shot back, "Bill, that's beneath you. I've been bringing out the facts, but I'm not going to rub George Whitney's face in the dirt simply because he helped his brother. And I'm not being soft on him."[49] Whitney respected Gesell and later encouraged Covington, Burling to hire him. "But you'd better get rid of this fellow Acheson," he told Harry Covington. "He's no good."[50]

Douglas asked the Justice Department to review George Whitney's and Lamont's conduct for possible misprision of a felony. When Justice Department attorney Brien McMahon refused to prosecute them, Douglas saw a malign conspiracy at work. He later said McMahon would "cast our reports into the dustbin. . . . Somewhere in the background was a powerful figure with money and political connections."[51] When he tried to get the Exchange to pursue the Morgan partners, only University of Chicago president Robert Hutchins voted for censure.

Douglas capitalized on the scandal to push through a new constitution and reform slate at the Exchange. The embezzlement demonstrated the need for greater openness at the Stock Exchange. By mid-May, the reforms recommended by the Conway committee were enacted. The board of governors was broadened to include public members, and the thirty-four-year-old secretary of the Conway committee, William McChesney Martin of Saint Louis, was elected the first salaried president of the Exchange. Douglas thus converted the Exchange from a private club into a body responsive to SEC dictates. He also pushed another reform agenda—competitive bidding for securities issues. In December 1938, he won a partial victory when the SEC ruled that investment banks couldn't collect underwriting fees from public utilities unless they engaged in arm's-length bargaining. Other financial crusaders also took heart from Whitney's disgrace. Railroadman Robert Young later said he had the courage to persist against Lamont's opposition after reading about Whitney's arrest, which he saw as proof of decaying Morgan power.

And what happened to Richard Whitney? After his arrest he behaved like a French nobleman being dragged off to the guillotine. Determined to face down his executioners, he berated Gerhard Gesell for being five minutes late to one interrogation. He objected to being described as insolvent, saying in a huff, "I still can borrow money from my friends."[52] Meanwhile wealthy sympathizers stacked up floral wreaths in front of his East Seventy-third Street townhouse. After he was convicted of grand larceny, a circus

atmosphere attended his departure for a five- to ten-year prison term at Sing Sing. Five thousand spectators at Grand Central Terminal saw a tall bowler-hatted man being led to the train by police. He was shackled to two other prisoners—an extortionist and a man convicted of assault. Unlike these two criminals, the impassive Whitney made no attempt to hide his face from photographers. He became inmate number 94835 at Sing Sing, and the first Stock Exchange president ever to serve time there.

In the long run, the scandal's real beneficiary may have been George Whitney. For years, he profited from comparison with Richard and became the Nice Honest Whitney Brother, softening his image as a defender of privilege. His loyalty to Richard stirred even the New Dealers. Over the years, Gerhard Gesell would be touched by news photographs of George taking a glove or a bat to Richard so he could play on the prison baseball team. (Richard was also visited by his old Groton headmaster, the Reverend Endicott Peabody.) By August 1941, Richard was eligible for parole, and George drove up to meet him at the prison gate. Richard then served as superintendent of a dairy farm in Barnstable, Massachusetts. He never again entered the world of finance or public life.

CHAPTER TWENTY-TWO
APPEASEMENT

FROM its inception, the House of Morgan had been Anglo-American in spirit and character. The Great War, in particular, fused the London and New York banks in a belief in Anglo-American responsibility for world peace and prosperity. Morgan partners subscribed to an idea expressed by Walter Lippmann in 1915 that U.S. foreign policy would experience a "crowning disaster" if uninformed by "a vision of the Anglo-American future."[1] That vision was Morgan dogma, the bedrock of partners' political beliefs. Yet the Second World War—both its prelude and the early stages, before Pearl Harbor—would prove a divisive experience, exposing tensions between New York and London that had been unacknowledged or long suppressed.

The Anglo-American comradeship had always been a bit one-sided. The Wall Street partners were ardent Anglophiles who celebrated British culture and made annual trips to London. Whether renting a Scottish castle or buying Sir Joshua Reynolds paintings, they identified with the British and affected their manners. This pro-British sentiment owed much to the fact that during most partners' early adulthood, London stood supreme in world banking. The partners at 23 Wall belonged to a generation that had eagerly boarded transatlantic luxury liners in the early 1900s to partake of British sophistication. Of his first visit to London, Lamont recalled, "For me London was the most thrilling spot that I had ever known or could imagine existed."[2] The test of a true J. P. Morgan partner was whether he saw the City as his ancestral home.

Jack Morgan preferred to be in England, where he wasn't caricatured as an uncaring plutocrat. He enjoyed the secluded privacy of Wall Hall outside London and had a wood-paneled office at 23 Great Winchester Street. England respected his privacy and was an ideal sanctuary from the strident New Deal denunciations. While Franklin Roosevelt hounded him, British royalty lionized him. George V said he felt comfortable with only two Americans—Jack Morgan and Ambassador Walter Hines Page. (Jack's granddaughter Jane married Walter Page's grandson, who bore the ambassador's name and became a postwar Morgan Guaranty chairman.) After shooting at Gannochy as Jack's guest, George VI told Sir Gerald Campbell, "I consider Mr. Morgan the world's greatest gentleman. Whenever he comes

into the room, I instinctively feel that I must arise."[3] When Lamont reported this, Jack blushingly said it made him feel "a little shy; but it is naturally very pleasant to me to hear of such nice things being said by a man whom I have known for a considerable number of years."[4] Jack bounced the king's daughter, the future Queen Elizabeth, on his knee, and his friendship with the royal family was a factor in Morgan Grenfell's later handling of a significant share of Elizabeth II's personal wealth.

Morgan Grenfell partners never fully reciprocated this admiration. Despite their real affection for the New York partners, they weren't enthralled by American history and probably found the country charming but provincial. By the late 1930s, several of the London partners were exalted personages, peers of the realm—Grenfell (Lord Saint Just), Smith (Lord Bicester), and Tom Catto (Lord Catto). Their institutional ties bound them as strongly to the British power structure as to their New York brethren. Smith was governor of the Royal Exchange Assurance Company and chaired the City of London Conservative and Unionist Association. Grenfell—now suffering from heart and lung problems and laid up with a patch on his lung—was a member of Parliament and a Bank of England director and had worked a Bank of England symbol into his coat of arms.

J. P. Morgan and Company had always hired gifted outsiders—Perkins, Davison, Morrow, Lamont, and Leffingwell—who rose on the strength of their intelligence. Morgan Grenfell recruited from a smaller circle of family members and friends. This would give the firm an inbred feeling, a genteel hothouse atmosphere, and a stuffy complacency that would make it dangerously ossified by the 1950s. Lord Bicester's son Rufus became a partner, and Francis Rodd, the son of a former British ambassador to Rome, was married to Rufus's sister. Morgan Grenfell partners displayed an upper-crust insularity. The first Lord Bicester, Vivian Hugh Smith, is the best example. As squire of Tusmore Park in Oxfordshire, he indulged a mad passion for steeplechase horses. Every year he went to Ireland to buy them and was frustrated in his great ambition of winning the Grand National. In a remark that some might have deemed insulting—but Bicester doubtless treasured—Lamont told him, "It is a great life you lead. You are my ideal of the English gentleman of the Victorian Age."[5] These weren't the sort of people to be enamored of American culture.

After Glass-Steagall, J. P. Morgan and Company not only became a minority shareholder in Morgan Grenfell but became more distanced from its affairs. As Lamont explained, "Morgan Grenfell & Co. considers that business done through them is their business."[6] After J. P. Morgan chose commercial banking, New York and London couldn't issue securities together, as they had in the 1920s. And foreign lending was down throughout

the Depression. Hobbled by a weak pound and government restrictions on overseas lending, the City's merchant banks, tired and unimaginative, entered a deep sleep from which they wouldn't awaken until the aluminium war of the late 1950s.

The most serious threat to J. P. Morgan-Morgan Grenfell unity was over foreign debt, which, like a bad hangover, remained from the 1920s lending binge. The first split had occurred with German debt. The Nazi policy of selective defaults generated ill will between the Morgan houses in London and New York. Then in March 1938, it looked as if history would repeat itself. Hitler ordered his troops into Austria and made a triumphant entry into Vienna, cheered by ecstatic crowds. Fulfilling his *Mein Kampf* prophecy, he reduced Austria to a German province while the Gestapo unleashed a wave of violence against Jews and other undesirables.

The J. P. Morgan and Company partners immediately feared default on a huge 1930 Austrian reconstruction loan. No less than in Pierpont's day, the bank had a fanatic sense of responsibility toward bonds it had issued. The British portion of the loan had been managed by several London banks, including Morgan Grenfell. Would the Nazis honor Austrian debt? Or would they classify it with German reparations loans and claim it was foisted upon Austria by the Allies? Most important, would Germany again cut a separate deal with England?

Hjalmar Schacht's power had continued to wane. Increasingly disgruntled with the Nazis, he feared the inflationary consequences of Germany's military buildup: he had defiantly told his arch rival, Göring, "Your foreign-exchange policy, your policy regarding production, and your financial policy [are] unsound."[7]

After the Austrian Anschluss, Schacht said, he secretly lost all sympathy with Hitler and began to contemplate his overthrow. But his apostasy was carefully disguised. Schacht was charged with running Austria's National Bank and subordinating its financial system to German monetary policy. Two weeks after the bloodless invasion, he assembled the staff of the central bank and delivered a terrifying speech: "Not a single person will find a future with us who is not wholeheartedly for Adolph Hitler. . . . The Reichsbank will always be nothing but National Socialist or I shall cease to be its manager." After administering a loyalty oath to the Fiihrer, he led the bank staff in a brisk chanting of *"Sieg Heil!"*[8] Schacht fired Dr. Kienbock, the Austrian banker who had offered Gobelin tapestries to Morgans as loan collateral in the early 1920s. With his usual self-congratulatory bent, Schacht later explained, "I saw to it that he was able to retire on a full pension and with flying colors though he was known to be of partly Jewish extraction."[9] The old Jewish Viennese banks were torn asunder. Baron Louis von Rothschild was arrested,

jailed, and released only after signing over all Rothschild assets in Austria to the state.

The House of Morgan closely monitored German speeches about Austrian debt. Before long, Walther Funk, who had replaced Göring as economics minister just before the Anschluss, was making statements that equated Austrian loans with German loans and claiming that they, too, were made by the Allies merely to ensure reparations. He ranted about scheming bankers and craven politicians who had conspired to draw Germany into "debt and interest slavery." In New York, Lamont watched nervously for signs of a deal between England and the Nazis. On April 25, 1938, his son, Tommy, spotted an item in the London financial press that alerted them to an impending settlement. "In other words," Tommy said, ". . . our good friends in the Bank of England and the City are contemplating pulling a fast one to the disadvantage of the American holders of Austrian bonds."[10]

Lamont was furious: the man who never got angry flew into a rage. To Sir Frederick Leith-Ross, the reparations expert at the British Treasury, he wrote a letter in stiletto-sharp prose. Recalling the 1934 British deal with Germany, he said:

I am recalling all this not in a spirit, my dear Leith, of anything except good will in pointing out to you the advantage of considering American interests in connection with the 1930 Austrian loan. The new fashion in the world is that every country should develop its own nationalism to the nth degree. But over here when our people listen to polite inquiries from our British friends as to what America's attitude might be in the case of Britain's becoming involved in a general war, the inclination is to wonder a little why the British sometimes overlook these matters (like the Dawes and Young loan matter) which are small in themselves, but which constitute an unceasing cause of irritation.

Lamont ended by alluding to the State Department's "deep interest" in the Austrian loan.[11]

While Lamont's exquisite courtesy toward the British now turned into elegant taunts and insults, his warnings proved fruitless. Schacht and Monty Norman kept up their mysterious dialogue, meeting monthly at the Bank for International Settlements in Basel. In June, an Anglo-German debt settlement was announced in Parliament, and professions of British-American financial solidarity yielded to brazen opportunism. It is interesting to note that Neville Chamberlain, in his desire to appease Germany, was indifferent to reports of Schacht's secret defection from Hitler. That summer in Basel, Schacht told Norman of his decision to abandon Hitler and work for his overthrow. When Norman repeated this to Chamberlain, the prime minister retorted, "Who is

Schacht? I have to deal with Hitler."[12]

How did Britain justify its deal? Norman told Lamont that Britain tried to settle Austrian debt on a nonpartisan international basis but that the Nazis insisted on discriminatory treatment. At the same time, the British—echoing Schacht's viewpoint—said they were running a trade deficit with Germany and that Austrian debt repayments would recycle to Britain some of the money they were paying for German goods. It was a depressing reversal from the Diplomatic Age of the 1920s. Monty Norman—the man who wanted to lift finance above the muddy realm of politics and into the clear air—now submitted to nationalistic pressures. With his usual theatrics, he wrote Lamont a lachrymose explanation: "For few debtor countries nowadays are willing to treat debts from the standpoint of ethics and equity and not from the standpoint of politics and convenience. . . . You cannot answer this because I am going away for a long time to heal my wound and I only write to clear your views and my conscience!"[13]

The feud between J. P. Morgan and Morgan Grenfell lingered; that the latter had placed British interests ahead of joint Morgan interests could not be lightly dismissed. In a tone he usually reserved for the browbeating of debtors, Lamont warned the London partners not to take Anglo-American cooperation for granted in the event of war—a shockingly grave threat. He wrote, "Must we accept that the high sanction of Great Britain is to be given to the growing habit of ignoring international connections and the rights of property?"[14] This sort of reprimand would have surprised isolationists, who saw only collusion between the House of Morgan and England.

Apparently fearing the Austrian feud would imperil Anglo-American financial relations, Francis Rodd circulated Lamont's letter at the British Treasury—without consulting New York. When Lamont learned of this, he exploded, believing his letter had been sent in strict confidence and could damage Morgan relations with the Treasury and the Bank of England. He sent a stinging rebuke to 23 Great Winchester Street:

You are aware that for generations past the partners of our house have always felt it to the great advantage of both our countries that the friendliest possible relations should exist between them. . . . As you know now we never meant our letter to be filed with the British Treasury. . . . There are lots of things one can say to a man that he cannot write to him, and that is a thousand times more true with regard to governments. The priceless value of Morgan Grenfell & Co. to us . . . has been precisely in the ability of the partners of Morgan Grenfell & Co. to interpret us to the British Treasury and the British Treasury to us. We have never thought of Morgan Grenfell & Co. as a post office for the transmission of our letters to the British Government.[15]

The pitfalls of the Anglo-American Morgan relationship were here apparent: did Morgan Grenfell represent the British government to J. P. Morgan or J. P. Morgan to the British government? How could New York partners expect Morgan Grenfell to be so intimate with Whitehall yet detached at the same time? These question had never been adequately posed, much less answered, because no serious conflict had arisen during the 1920s, the heyday of financial internationalism. Now the nationalistic squabbling of the 1930s destroyed many illusions about the supposed allegiance of the London partners to J. P. Morgan and Company. The "Trojan horse" strategy followed since the early 1900s—of giving the London house a British complexion and character—had, in the last analysis, backfired on the New York house.

THE New York partners traveled in aristocratic British circles and were frequent visitors at the Astor estate at Cliveden. No less than the House of Morgan itself, Nancy Astor represented a marriage of American capital and British aristocracy. Born Nancy Langhorne in Virginia, she ended up as the first woman to hold a seat in the House of Commons (having campaigned for office in pearls and accompanied by a liveried coachman). A stylish, pretty woman with a sharp tongue and a zest for political rows, she liked to heckle, tease, and argue. Once, while visiting her adversary Winston Churchill at Blenheim, Astor said, "If I were married to you, I would put poison in your coffee." Churchill replied, "And if I were married to you, I would drink it."[16]

Nancy was married to the rich but feckless Waldorf Astor, second viscount and the grandson of John Jacob Astor III. Waldorf drew the bulk of his income from rentals of his Manhattan real estate holdings, so the transatlantic structure of the House of Morgan perfectly suited his business needs. Waldorf also consulted Tom Lamont about his personal finances, and Lamont had switched him out of American securities and into Canadian municipal bonds after the 1929 crash. The Lamonts and the Astors socialized and even vacationed together.

Lady Astor bewitched Tom Lamont, and for twenty years they kept up an abundant correspondence. There was a likeness between them. Both were romantics with a taste for *noblesse oblige*, self-invented aristocrats who had acted out extravagant dreams and confidently inhabited their stations. From government offices, Cunard staterooms, hotel rooms—even once while Astor set her hair—the two exchanged long, often effusive letters. They traded gossip, personal confessions, and political intelligence. After the Richard Whitney scandal, Lamont sent her clippings to establish his innocence and Astor replied, "Dearest Tom, I don't have to read your cuttings, or anything else for that matter, to know that you would never do wrong. Such is my

affection for you!”[17]

Their correspondence had a vaguely romantic cast. Lamont termed Lady Astor “the kindest-hearted and best friend in the world” and called her “the girl I love most.”[18] In his inimitable fashion, he showered her with gifts and favors. He could break down anybody’s resistance, conquer anyone with charm, such was his genius for cultivating friends. Golfing with him at Cliveden in 1930, she had admired a set of clubs owned by another guest, Frank Kellogg, until recently the U.S. secretary of state. Back on Wall Street, Lamont tracked down the original manufacturer and had identical clubs made for her. “I am really ridiculously excited and grateful,” she wrote back.[19] Another time, Lamont slipped away from 23 Wall, went uptown, and bought her two frocks at Saks Fifth Avenue. It was a warm friendship, indeed.

On the eve of World War II, Lamont’s friendship with the Astors took on important political dimensions. Cliveden, the Astor estate on the Thames, had become a gathering place for politicians and intellectuals who favored appeasement of the Nazis. They thought England could coexist with Hitler, feared a war would shatter the British Empire, and supported the appeasement policies of Stanley Baldwin and Neville Chamberlain. In time, the name Cliveden became synonymous with a phobic hatred of Russia, a benign or even admiring view of Fascist intentions, and a rejection of Churchill’s warnings about German rearmament.

Like his Cliveden friends, Lamont believed that Europe’s dictators could be held at bay through diplomacy and that war could be avoided. He also thought Britain and France were woefully unprepared for war. To some extent, Lamont and his partners were still cowed by the Nye committee charges that they had been “merchants of death” in World War I. They weren’t eager to stick their necks out in support of another war. “As for our dictators, Hitler and Mussolini,” Lamont wrote Lady Astor in 1937, “they don’t seem to have changed their spots very much, but I seem to think that raging at them will do no good, and if there is a possibility of methods of appeasement, these are our only chance.”[20] Earlier, Lamont had asked Lady Astor to lobby the Foreign Office in support of its recognizing Mussolini’s conquest in Ethiopia. When Hitler took over Austria, Lamont assured her that his Italian friends were “aghast” at the coup and said their view must surely reflect il Duce’s own horror. Right up to the war, he believed that Italy had sided with the Germans only under extreme duress.

Lamont took a more alarmist view of events in the Pacific. He had never fully recovered from his sense of betrayal by the Japanese militarists, and this only deepened his sense of their malevolence. During Japan’s fierce aggression against China in July 1937 and the slaughter of thousands of Chinese civilians in the rape of Nanking, he spied a design to subdue all of

East Asia. He didn't mince words with Japanese businessmen who made overtures to the bank. In September 1937, he assured the Japanese consul general that he would not "find one American in one hundred thousand who is not shocked and distressed beyond measure" by Japanese military operations in and around Shanghai.[21] (In fact, a few weeks later Russell Leffingwell told Lamont that China would fare better under Japanese domination.[22]) In contrast with his gullible acceptance of the Mukden incident of 1931, an irate Lamont now protested to the Bank of Japan that "faked stories" about China were being circulated by Japan all over the world.[23]

In September 1938, Neville Chamberlain flew to Munich and capitulated to Hitler's demand for the Sudetenland. Hitler forswore further territorial ambitions, and Chamberlain hoped that the partition of Czechoslovakia would sate the dictator's appetite for conquest. In accepting the Munich Pact, the British cabinet wasn't completely naive about Hitler's intentions: many thought England needed time to mount an expensive rearmament program and that war with Germany would be suicidal. Returning to Downing Street talking of "peace with honour," Chamberlain received a tumultuous welcome. The London *Times* said, "No conqueror returning from a victory on the battlefield has come adorned with nobler laurels."[24] Amid a rapturous greeting in the House of Commons, Churchill was the sour, lonely voice of dissent, branding Munich a "total and unmitigated defeat." He was predictably heckled by Nancy Astor.[25]

The House of Morgan stoutly supported Munich. In a flight of fancy, Lamont predicted a new German regime within two years. Jack Morgan was sure that in the end Hitler would have to be stopped forcibly. In the meantime, he thought his friend Chamberlain had bought valuable time. "What an achievement!" he wrote to the prime minister in breathless tones. "I little thought when you were at Gannochy at tea and I said I had a hunch that there would be no war and you said hunches were the only thing to go on, and that you had the same hunch as I did, that you were going to be the one to have the imagination and courage to make that hunch come true! It never occurred to me that a single man could do so much by sheer force of courage, fairness and reasonableness."[26] With rather heavy snickering, Jack said that if Churchill or Lloyd George were in charge, the world would have been at war long ago.[27] Vivian Smith, now Lord Bicester, was more muted in his support of Munich, warning that Hitler was a "fanatic" and that Göring and Goebbels were "gangsters" using the Nazis as a cloak for their evil-doing.[28] While congratulating the Morgan Grenfell partners that Chamberlain had averted war, Russell Leffingwell privately lamented to Lamont that Britain had submitted to blackmail.[29]

Hitler was puffed up with the success of his blackmail. In March 1939, he

devoured the rest of Czechoslovakia, and the German army marched into Prague. Czechoslovakia's extinction shattered the appeasement movement. Nancy Astor's intimate friend Lord Lothian sent a despondent note to Lamont saying he had abandoned hope of decent behavior from that gangster, Hitler. Two days later, Lady Astor herself urged Chamberlain to condemn Germany. By the end of the month, Chamberlain reversed his course and guaranteed Poland's independence.[30]

The British public dealt harshly with the complacency Baldwin and Chamberlain had shown in the face of the German threat. Political adulation turned into vitriolic abuse as the British solidly closed ranks behind a determined response to Hitler. In America, however, the division of public opinion toward the European turmoil only grew more contentious. For Morgan partners in New York, it was an especially problematic dispute. As Lamont had warned Morgan Grenfell and the British Treasury, there was a residue of pent-up American hostility left over from the financial disputes of the 1930s. And the power of American isolationists was such that the bank couldn't immediately proclaim the proud, unalloyed support for Britain that it had in 1914. J. P. Morgan and Company would find itself in the uncomfortable position of antagonizing the isolationists for doing too much for Britain while disappointing the British for not doing enough.

An indirect casualty of Munich was Hjalmar Schacht, who had joined in the secret generals' plot of September 1938 to overthrow Hitler. He later claimed the conspirators were disheartened by the Allies' cowardice at Munich. Schacht's standing in Nazi Germany had grown precarious in late 1938. At the Reichsbank Christmas party, held several weeks after the burning of Jewish shops and synagogues on Kristallnacht, he deplored such actions. In early 1939, the deluded Schacht still churned out Reichsbank memos on the need to cut inflationary arms expenditures, as if Hitler cared about neoclassical economics. In London that December, he presented a plan for the emigration of fifty thousand Jews from Germany—to be paid for with all their belongings and ransom payments from the world Jewish community. In the first week of January, Monty Norman made a last trip to Germany, to attend the christening of his godson—Schacht's grandson Norman Hjalmar—named in tribute to him. When Hitler fired Schacht from the Reichsbank on January 20, Norman belatedly awoke to the full horror of the Nazi menace.

RIGHT before the outbreak of World War II came the first state visit by a British monarch to the United States—a piece of pageantry and propaganda in which the House of Morgan participated. The trip was inspired by Joseph Kennedy, who became ambassador to the Court of Saint James's in 1938. Like many Roosevelt appointments, this one infuriated 23 Wall. Several of his

biases simultaneously aroused, Jack Morgan told Monty Norman, “I share your wonder that an Irish Papist and a Wall Street punter should have been selected for the London Embassy. Of course you must expect him to have to be a New Dealer, because Franklin would not appoint anyone else.”[31] Although Norman patronized Kennedy as a social climber of inferior Irish stock, they met weekly, and Norman shared his pessimistic views about England’s prospects in a war against Germany.

What made Kennedy’s appointment doubly galling for Jack was that as ambassador the Irishman was living at Princes Gate, which Jack had given to the State Department as an ambassador’s residence in the 1920s. (Joe Kennedy had his revenge on Morgan snubs: today the blue marker outside the house commemorates John F. Kennedy’s brief residence there and says nothing of the Morgans’ original ownership of the property.) Princes Gate would enjoy only a fleeting existence as an official residence, however. After the war, Barbara Hutton, the Wool-worth heiress, donated her Winfield House in Regent’s Park, and that became the new residence of American ambassadors.

The 1939 visit came about when Queen Elizabeth one day said to Kennedy, “I only know 3 Americans—you, Fred Astaire, and J. P. Morgan—and I would like to know more.”[32] To remedy this, Kennedy suggested a goodwill trip to the United States. Through their private secretary, the royal couple sounded out Jack Morgan and John Davis, who agreed that a visit would indeed be timely. When the king and queen came to the United States in June 1939, Joe Kennedy was pointedly snubbed and excluded from attending their party.

As planned, the American trip elicited a tremendous outpouring of pro-British sympathy. The royal couple enjoyed hot dogs at Hyde Park, and Roosevelt outlined limited naval steps he could take to support Britain in case of war. But it didn’t help the House of Morgan, for it reinforced the old stereotype of the firm’s being in league with the British crown. At a garden party at the British embassy in Washington, the king and queen sat up on the porch in remote splendor with several private citizens—Jack Morgan, John D. Rockefeller, Jr., and Mrs. Cornelius Vanderbilt. Only two New Dealers, James Farley and Cordell Hull, were allowed to join them. Stranded down on the lawn with other commoners, the saturnine Harold Ickes enviously watched Morgan and the other economic royalists up on the porch and felt demeaned. He wasn’t mollified when the king and queen descended to mingle with the “common herd.”[33]

In late August 1939, Jack Morgan and King George VI were shooting together at Balmoral in Scotland, complaining about the bird shortage, when Europe suddenly mobilized for war. Like sovereigns retreating to their

respective capitals, the king returned to London and Jack to Wall Street. On September 1, Germany invaded Poland. Soon Neville Chamberlain, his voice shaking, announced that Britain was at war with Germany. The New York Stock Exchange reacted with its best session in two years, and the bond market leaped upward with the heaviest one-day volume in history. Unlike the outbreak of World War I, American investors weren't fooled as to who would profit from the conflict and foresaw an economic boom. It was the Second World War—not the New Deal—that would wipe away the vestiges of the Depression.

It dawned on the House of Morgan that the firm might dust off the World War I purchasing-agency concept. Might not the bank again aid the Allies behind a shield of neutrality? After pondering such a move, the bank informed the British, French, and U.S. governments that it wouldn't try to repeat the experience. After so many years of hearings, the bank felt politically vulnerable and feared a revival of war-profiteering charges.

The bank also contended with an anti-Wall Street faction in Washington, which was determined to block any Morgan role. This opposition was apparent when Roosevelt created a short-lived War Resources Board. In an amazing coincidence, he chose as chairman Edward R. Stettinius, Jr., son of the Morgan genius of the Export Department in World War I. A handsome man with prematurely silver hair, Stettinius had risen through the ranks of two Morgan clients, General Motors and U.S. Steel, ending up chairman of the latter. The war board included another Morgan favorite, Walter Gifford of AT&T. Roosevelt wanted to counteract charges of being an enemy of business, but his liberal subordinates smelled extreme danger in this tactical retreat. Hugh Johnson, former head of the National Recovery Administration, told Assistant Secretary of War Louis Johnson that the government did not "intend to let Morgan and DuPont men run the war."[34] Henry Wallace, then FDR's secretary of agriculture, also warned against bringing Wall Street bankers to Washington.

The assiduous Harold Ickes quickly gathered his cabal of Brandeis men, Tom Corcoran and Bob Jackson. He noted, "We wondered how far the President would go or would permit others to go in abdicating in favor of big business, as Wilson did at the time of the First World War."[35] Ickes thought Wilson's liberal credentials were tarnished by his wartime closeness to Wall Street and he hoped Roosevelt could avoid such a fate. His efforts to keep the Morgan bank out of war work dovetailed with his friend Cyrus Eaton's efforts to break up Morgan power in the financial world. In late 1939 and early 1940, the Temporary National Economic Committee investigated an alleged monopoly in the investment banking field, with Morgan Stanley its prime suspect.

These anti-Morgan maneuvers, coming from several directions, prevented the bank from resuming its World War I role, as did earlier U.S. entry into the war. In the Second World War, Washington would take charge of industrial mobilization through the War Production Board and other agencies. The federal government was vastly more powerful now than it had been in Woodrow Wilson's day, and it didn't hesitate to intervene in the economy for political ends. In fact, government resources now eclipsed those of private banking houses. By World War II, banks were no longer large enough to bankroll wars, as Barings, Rothschilds, and Morgans had done in their heydays. With their large budgets, central banks, and taxing powers, the modern nation-states no longer needed to rely on the good offices of private bankers.

The House of Morgan championed economic support for Great Britain. As a belligerent, Britain was covered by the arms embargo of the Neutrality Act (passed, *inter alia,* to prevent a recurrence of the House of Morgan's role in World War I). Lamont lobbied Roosevelt to repeal it, contending that it not only favored but emboldened Germany. In November 1939, Congress did repeal the embargo, permitting arms exports to countries at war on a "cash and carry basis": that is, they could purchase U.S. supplies so long as they paid for and transported them. Under this arrangement, American planes would fly to the U.S.-Canadian border, and Canadian pilots would then fly them to Britain.

The cash-and-carry decision created an urgent need for gold or dollars for the massive purchases. As in World War I, Britain raised money by commandeering American securities held by its nationals. The House of Morgan was charged with selling these securities in New York without triggering sharp price declines. It handled the British operation alone but shared a comparable French operation with Lazard Frères. Only a few people in each brokerage house knew the seller's identity, and Morgans warned brokers that if any information leaked out, their services would be terminated within twenty-four hours. To oversee the operation, the British Treasury sent T. J. Carlyle Gifford to 23 Wall. He was already known to Morgans as chairman of the Scottish Investment Trust of Edinburgh, which used J. P. Morgan as custodian for U.S. securities. Impressed by the House of Morgan's performance, Gifford nonetheless agreed with Roosevelt's assessment that the bank's participation was a severe political liability: "It seems the President and [Treasury Secretary] Morgenthau would much have preferred us not to go to J.P. Morgan & Co. and so have probably resented that and are now afraid it may cause difficulties when they appear [before] Congress," he reported back to London.[36]

Both for Nancy Astor's and Britain's sakes, Lamont assisted Lady Astor's great spiritual companion, Lord Lothian, who was sent to Washington as

British ambassador in April 1939. A former secretary of the Rhodes Trust and a founder of the Royal Institute of International Affairs, Lothian was shy, professorial, and, like Lady Astor, a devout Christian Scientist. Immediately after his appointment, he cabled Lamont, “Shall want all your advice and help.”[37] In Washington, Lord Lothian found the mood very much opposed to Hitler but, at the same time, resolutely opposed to war. Drawing on his Wall Street ally, he would fly up to New York on a late-afternoon flight, speak to a dinner assembled by Lamont, then take a night train back to Washington. Lothian, repenting of his Cliveden appeasement period, would prove a superbly eloquent spokesman in enlisting support for Britain.

In 1939, the most vociferous opposition to U.S. entry into the war came from the German and Italian immigrants, midwestern farmers, and labor unions. The isolationist agenda didn’t change from World War I: there was the same disgust with European broils and the same suspicion that Britain would dupe the United States into saving its own empire. Complicating matters was the still fresh memory of the Great War.

The Morgan partners flatly opposed U.S. entry into the war and were dubious about the Allies’ chances of beating Germany. As Russell Leffingwell said right before the war’s outbreak, the British and French “cannot subjugate the Germans. There are too many of the devils, and they are too competent.”[38] In May 1940, Lamont joined William Allen White in forming the Committee to Defend America by Aiding the Allies, whose outlook perfectly reflected the Morgan position. The group assailed the same nemeses—the Hearst newspapers and Senators Wheeler and Nye—that had hounded the House of Morgan for years. While fervently attacking the isolationists, it parted company from a kindred group, Fight for Freedom, which endorsed U.S. entry into the war; instead, it heeded FDR’s call for all aid short of war. (At this time, Jack’s sister Anne formed the American Friends of France and by June 1940 was sailing to that country to evacuate refugees and head an ambulance unit. She would have a special plaque dedicated to her memory in Les Invalides, the Paris war memorial, after she died in 1952.)

One of Lamont’s special committee assignments was to neutralize Herbert Hoover’s Anglophobia. Still bruised from his presidency and wishing to repeat his wartime triumph with European food relief, Hoover favored a scheme for feeding Nazi-occupied countries; Lamont supported Britain’s blockade against such activity. When Lamont and White visited Hoover, they couldn’t change his mind and vowed to fight him. Afterward, a press account popped up describing Hoover truculently pacing the room and swearing that he would tour the country and fight Britain on the issue. Lamont assured Hoover that *he* hadn’t talked to a newsman and said the account must have

been a misrepresentation. Even at the end, the Lamont-Hoover relationship—once seen as a Faustian pact between Wall Street and Washington—was tense and querulous.

The House of Morgan's pro-British views brought it into conflict with the nation's most visible isolationist, Charles Lindbergh. In late 1935, the Lindberghs had moved to England, hoping to find a tranquillity denied them in America after their son's kidnapping. At the prompting of the U.S. military, Lindbergh visited Nazi Germany in 1936 to tour German aircraft factories. He made subsequent trips in 1937 and 1938 and developed a growing admiration for German air power—admiration that he expressed to Stanley Baldwin at Downing Street and in the drawing rooms of Cliveden. Lindbergh insisted that a war against Germany was unwinnable, would destroy American democracy, and would open the way for Communist infiltration. When he accepted a decoration from Hermann Göring at a reception, it added to suspicion in some quarters that Lindbergh was not only awed by the Nazis but sympathetic to them.

By the time the Lindberghs returned to America in April 1939, Charles had a settled belief in German invincibility and French and British decadence. That fall, he began making radio speeches urging U.S. neutrality and arguing against repeal of the arms embargo. His remarks were sometimes laced with racist innuendos. On October 13, 1939, he said, "If the white race is ever seriously threatened, it may then be time for us to take our part for its protection, to fight side by side with the English, French, and Germans. But not with one against the other for our mutual destruction."[39] Whether consciously or not, Lindbergh had absorbed many Nazi doctrines. In the *Atlantic Monthly* of March 1940, he cynically saw England and France as fighting for their possessions and ethics, whereas the Germans claimed "the right of an able and virile nation to expand—to conquer territory and influence by force of arms as other nations have done at one time or another throughout history."[40]

During the debate over the war, Lindbergh increasingly reverted to his father's midwestern populism, with its reflexive hatred of the Money Trust and its dark vision of Anglo-American finance. While the younger Lindbergh might have taken comfort from following in his father's footsteps, the situation was more complicated for his wife. Anne Morrow Lindbergh was torn between her isolationist husband and the memory of her late internationalist father. She had always admired the Morgan partners, a type she saw as "keen man-of-the-world, discreet, kindly and cultured."[41] She once talked of the "whole warm rich world of my father and mother" and remembered idealistic talk over breakfast between her father and Jean Monnet, a French economist and diplomat. She cherished memories of her

father, and after reading Harold Nicol-son's biography of him, she wrote, "I suddenly feel my heritage, feel him in me. It is mine."[42]

Now Anne was in an excruciating situation. Her mother felt strongly that Dwight would have favored aid for the Allies. Most of the Lindberghs' friends on Long Island held similar views. The Lindberghs also had many French and British friends, and as soon as Germany began mobilizing for war in 1938, Anne imagined Florrie Grenfell, Lady Astor, and the rest wiped out by air raids.[43] Yet Anne shared Charles's simplistic views of European politics, albeit without the nasty overlay of racism. In 1940, she published a book called *The Wave of the Future* in which she saw the war not as a contest between good and evil but as one between the "Forces of the Past" (the Allies) and the "Forces of the Future" (Germany).

If Charles felt buoyed by his identification with his father, Anne was tormented by the ghost of hers. She told herself that Charles was as idealistic as her father but that it was the idealism of a later age. After William Allen White formed the Committee for Defending America by Aiding the Allies, Anne asked herself, "I wonder where Daddy would stand? Probably behind the committee *et al.* And yet he was among those idealists, very practical, intensely practical—that was his great gift."[44] Nevertheless, as the Lindberghs were socially ostracized by old friends—including Harry Guggenheim, who had sponsored Charles's three-month tour following the solo flight—Anne was haunted by her father's specter. She lamented that "Charles . . . has the memory of his father with him," but "I'm entirely alone."[45]

Anne's dilemma was sharpened on May 19, 1940, when Charles made a radio speech entitled "The Air Defense of America." By then, the Nazis had conquered Denmark and were overrunning Holland and Belgium. Lindbergh's speech made menacing reference to "powerful elements in America" who controlled the "machinery of influence and propaganda." These elements, he said, wanted to push America into war for profit and to serve their foreign allies.[46] The Morgan bank wasn't named, but Lindbergh's language echoed that used in attacks on the bank ever since the Nye hearings. President Roosevelt told Treasury Secretary Henry Morgenthau the next day, "I am absolutely convinced that Lindbergh is a Nazi."[47]

Betty Morrow, now acting president of Smith College (having attained the academic distinction denied Dwight), was disturbed by Charles's insinuations. Five days after the radio speech, she had an emotional lunch with Anne at the Cosmopolitan Club. Betty felt ashamed that America hadn't rushed to join England and said in anguish to Anne, "How they will *hate* us—oh, how they will *hate* us."[48] Yet despite her candor with her daughter, Morrow felt constrained in challenging her son-in-law. The day after the lunch, she secretly wrote to Lamont asking him to reason with Lindbergh: "I am in a

difficult position just now . . . but my chief worry is over Anne. She is torn in spirit and it is telling on her health."[49]

Taking the tone of a concerned uncle, Lamont wrote to the rather aloof Charles Lindbergh. He said he had hesitated to contact him and cited his affection for the Morrow family. Then he asked point-blank who those nameless conspirators in his speech were. He added that he didn't know of any such elements. Trying to recapture the personal warmth of earlier years, Lamont admonished him tactfully: "Dear Charles—It is so important that we shall have unity in our country that we must not broadcast suspicions and accusations unless we have complete basis for the charges."[50]

The return letter must have chilled Lamont. It wasn't hostile so much as cool and correct, as if Lindbergh had turned into a stranger. "I intentionally did not specify individuals, groups, or organizations in my address because I still hope that it will not be necessary to do this," Lindbergh said, claiming that to do so would only stir up dangerous class antagonisms. He warned that U.S. entry into the war would cause "chaotic conditions" and destroy American moderation. He concluded, "I have great respect for your judgment, but I am afraid that our viewpoints differ in regard to the attitude this country should take toward the war in Europe."[51] Later, when a reporter asked Lamont why he didn't visit the Lindberghs, he snapped, "I have nothing to do with them."[52]

Her secret overture through Lamont having failed, Betty Morrow decided to make public her opposition to her son-in-law. During the Dunkirk evacuation in June, she made a speech for the William Allen White committee rebutting Charles's views. She telephoned Anne first to soften the blow. "Your father would have wanted me to do it," she told Anne, who thought her mother was being exploited for the purposes of publicity.[53] Betty came to agree with this appraisal after White made a speech boasting of his "smart trick" in setting her against Charles. After that, Betty Morrow was "very humanly, unwilling to appear again in a public clash with Lindbergh," as Russell Leffingwell informed Roosevelt.[54]

THERE was a moment in the spring of 1940 when it seemed the House of Morgan might simultaneously defeat the New Deal and advance the British cause. The long-awaited middle path opened up in the Republican party. Along with the British ambassador, Lord Lothian, Lamont attended a dinner at the home of publisher Ogden M. Reid, who presented two would-be Republican presidential candidates. Robert A. Taft, son of the former president and a Republican senator from Ohio, was predictably anti-internationalist. But the other aspirant, Wendell Willkie, was a revelation. As

president of the giant utility holding company Commonwealth and Southern Corporation, he had clashed with FDR over the Tennessee Valley Authority's takeover of his generating plants. At the dinner, Willkie came out in favor of unqualified support for Britain, including the provisioning of planes and naval equipment. On the spot, Lamont and Reid championed his candidacy, and Lamont was instrumental in getting him to run. Willkie then repeated his pro-British pep talk before a dinner at Lamont's house, a gathering credited with enlisting Wall Street support for his run for the presidency.

For Morgan partners, Willkie was tailor-made. Ever since McKinley, the bank had been baffled by a Hobson's choice in American politics. It could side either with Democrats, who were too interventionist at home, or with Republicans, who were too isolationist abroad. As a major foreign lender, it favored free trade and free flow of capital at a time when big business was still mostly protectionist. On balance, the bank had opted for Republicans, but not without considerable discomfort on foreign issues.

Willkie was decidedly in the Morgan grain. A former Democrat, he was an outward-looking Anglophile, a supporter of reciprocal trade agreements, and generally attuned to FDR's foreign policy. At the same time, he was a supporter of domestic free markets and wished for a midcourse correction in New Deal policies and a more favorable environment for investment. He had plenty of Wall Street friends, including Perry Hall of Morgan Stanley (where Willkie was one of Harold Stanley's first clients in 1935), and provided a version of Republicanism they could unreservedly support.

With his broad, open face, big grin, and Indiana twang, Willkie was folksy and sophisticated and uniquely able to advance Wall Street's cause without seeming like an ambassador for the rich. *Fortune* called him a "clever bumpkin," and Harold Ickes memorably mocked him as "a simple barefoot Wall Street lawyer."[55] The verdict was too harsh, for Willkie wanted to retain many New Deal innovations—collective bargaining, minimum wages, and maximum hours—that were anathema to Wall Street bankers. Though Willkie declared his candidacy only seven weeks before the Republican National Convention in June 1940, his dark-horse candidacy galloped fast. He had to soft-pedal his Morgan support so as not to alarm the small-town, anti-Wall Street wing of the party. To foster a down-home image, he took a modest two-room suite at the Benjamin Franklin Hotel in Philadelphia, site of the convention, and Tom Lamont was expressly instructed to avoid his headquarters.

Despite this sanitary distance, the anti-Willkie troops wasted no time in fastening onto his Wall Street links in order to discredit him. Representative Usher L. Burdick of North Dakota circulated an alarmist tract to delegates that said, "I believe I am serving the best interests of the Republican Party by protesting in advance and exposing the machinations and attempts of J.P.

Morgan and the other New York City bankers in forcing Wendell Willkie on the Republican Party. Money, I know, talks."[56]

The Republicans were famished for new leaders and finally chose Willkie on the sixth ballot over prosecutor Thomas Dewey (who had indicted Richard Whitney) and Senator Taft. The following month, FDR was nominated for a third term in Chicago, with Henry A. Wallace of Iowa as his running mate. Willkie tried gamely to forge a compromise between support for FDR's foreign policy during the war emergency and moderate reform of New Deal policy. He even sounded out Roosevelt about a deal in which the president would consult him on foreign policy in exchange for a pledge to keep the war out of the campaign. Roosevelt didn't trust the Republicans enough to accede to this and was loath to confer the prestige of such a deal upon Willkie.

In November, Roosevelt won by over five million votes. Willkie's defeat didn't end charges of Wall Street machinations but only strengthened the conviction of those who saw wily bankers as having foisted him upon the party. As historian Harry Elmer Barnes afterward charged: "It is doubtful if any man was ever nominated for the Presidency on the basis of less popular knowledge and approval. There were at least a dozen or more persons in the famous 'smoke-filled room' in the Chicago hotel where Warren G. Harding was chosen for the nomination in 1920. Two men decided that Mr. Willkie should be the Republican nominee. . . . These men were Ogden Mills Reid . . . and Thomas W. Lamont."[57]

As it turned out, the House of Morgan didn't suffer as much from Willkie's defeat as might have been expected. Bolstered by his election victory, Roosevelt moved more vigorously to support Britain, and in this effort he needed the Morgan bank. With marvelous suddenness, the chill in Morgan-Roosevelt relations thawed and was replaced by cordiality from the White House of a sort that 23 Wall hadn't known since the twenties. As America's attention shifted from blistering debates over domestic policy to ways in which to deal with Europe's dictators, the power of the House of Morgan surged accordingly.

CHAPTER TWENTY-THREE
HOSTAGES

ON June 22, 1940, the new French Premier, Marshal Henri Philippe Petain, submitted to the Nazi *blitzkrieg* and signed an armistice with Hitler, leaving Britain to fight alone against the Axis powers. This left Morgan et Compagnie in a vulnerable situation. The stately *Banque Morgan*, as the French termed it, occupied an imposing mansion at 14 place Vendôme, its marble banking floor illuminated by a huge skylight. Established by the Drexels in 1868, the firm had an illustrious heritage, having stayed open during the Franco-Prussian War and World War I. It was known as Morgan, Harjes until 1926, when partner Herman Harjes died in a Deauville polo accident and the name was changed to Morgan et Compagnie. Under the interlocking partnership structure of the pre-Glass-Steagall Morgan empire, Jack Morgan was senior partner, and New York had provided most of the bank's capital.

If Morgan et Compagnie never achieved quite the renown of the New York and London banks, it still ranked as one of the largest foreign financial institutions in Paris even in the 1980s. It was a conduit for dealings between the French government and J. P. Morgan and Company and was very close to the Banque de France. Its French officers had often held high government posts. Morgan et Compagnie served the subsidiaries of most American companies in France, provided traveler's checks and letters of credit for rich American tourists, handled currency transactions for Americans in France, and had vaults brimming with securities owned by Americans and Frenchmen. It exchanged young apprentices with Morgan Grenfell and J. P. Morgan. Yet in the last analysis, the French house was always stymied by Morgan intimacy with Great Britain and France's nationalistic resistance to American business penetration.

So total was the wartime news blackout that an account of what happened to Morgan et Compagnie during the Nazi occupation wasn't known until September 1944; it can now be reconstructed from unpublished memoirs at Morgan Guaranty. The story begins with the Banque de France, which didn't trust the phony peace promulgated by the Munich Pact and in 1938 began making plans to protect its gold. It shipped gold to New York as a fund for future war purchases and took gold bullion stored at its vaults on the rue de la Vrilliere and distributed it to fifty-one strategic sites around the country.

Many Parisian banks made similar contingency plans. Morgan et Compagnie bought a run-down hotel in Niort, a town southeast of Nantes. It was redesigned as a self-sufficient unit for protecting securities, with safes in the basement and sleeping quarters upstairs for staff. After war was declared, the French government advised Morgans to set up an office in Chatel-Guyon, in unoccupied France, to protect its exchange dealings with the Banque de France. Several weeks before the Nazis stormed Paris, Morgans and other banks shipped out securities to these safe houses in south-central France and left behind skeleton staffs in Paris. Then, five days before France fell, two American partners of Morgan et Compagnie, Bernard S. Carter and Julian Allen, fled Paris along roads swollen with refugees and clogged with horse-drawn carts and bicycles. All of these acts proved wise precautions.

During the German occupation, the Nazi flag flew over the Justice Ministry and the Ritz Hôtel, Morgan et Compagnie's neighbors on the place Vendôme. Three of the American banks with Paris branches—J. P. Morgan, Guaranty Trust, and Chase National—stayed open, while the fourth—National City—shut down. In late June 1940, Leonard Rist of Morgan et Compagnie was arrested and dispatched to a German prison camp in the Sudetenland. Rist was the son of an eminent French economist, Charles Rist, and had been personally recruited by Jack Morgan. When Leonard was in New York in 1928, he recalled, Jack "asked me what the hell I was doing in any other place than Morgan's in exactly those words; whereupon I decided to apply for a job at Morgan's in Paris."[1]

Rist ended up spending eighteen months behind barbed wire while his parents worked out emergency plans to secure a Wall Street job for their younger son through Russell Leffingwell. The House of Morgan finally sprang Leonard through their old Vatican friend, Bernardino Nogara, the treasurer of the Special Administration of the Holy See. Nogara somehow convinced the Germans that Rist's release was needed to maintain French financial health. The combined force of the Morgan mystique and Rist's reputation was such that the argument worked. After the war, the French Treasury assigned Leonard Rist to the World Bank, and he ended up as head of its Economic Department.

For the rest of the war, executive control of Morgan et Compagnie fell to two stubborn, courageous Frenchmen—the elegant Maurice Pesson-Didion, a veteran wounded in the Battle of the Marne, and Louis Tute-leers, chief of the Credit Department, who limped from a wartime injury suffered while serving in the Belgian army. The two bankers had to contend with constant, hovering Nazi interference and menacing surveillance of their activities. To finance his conquests, Hitler set a policy of plundering gold and foreign currency from banks in occupied territories. As part of his revenge for Versailles, he chose to extort money from France. Like other banks, Morgan et Compagnie could

conduct business in franc accounts, but foreign-exchange transactions were outlawed. The bank had to apprise the Germans of any foreign currency it held as well as any property in safe deposit boxes.

The House of Morgan has always been proud that it operated in Nazi-occupied Paris without compromising its principles. Yet the bank may have had a secret patron: Marshal Petain, head of the collaborationist Vichy government. As a celebrated war hero in 1917, Petain had associated with many fund-raising society ladies, including Herman Harjes's wife and Anne Morgan. It was perhaps through such meetings that he came to have an account at Morgan et Compagnie. This embarrassing account was disclosed in November 1941, during a boisterous debate in the British House of Commons. It came out that Petain had signed an annuity plan with a Canadian company in 1937; even after the fall of France and the British blockade, the Canadian company duly paid £600 annually to Morgan Grenfell, which then credited Petain's account at Morgan et Compagnie. The transfers were sanctioned by a British Treasury license.

In the House of Commons, Dr. Russell Thomas protested to Chancellor of the Exchequer Kingsley Wood, "Will the right honorable gentleman consider that the payment tends to irritate the public temper, lowers the prestige of the Government, and opens up avenues of suspicion at a time when national unity is essential?"[2] In defending the transfers, Kingsley Wood noted that Canada had maintained diplomatic relations with Vichy France and that Pétain was a head of state. Nevertheless, at some point, the transfers were stopped.

After Pearl Harbor, Morgan et Compagnie was branded an enemy bank and assigned a special German overseer, Herr Caesar, who operated out of 18 place Vendôme. He insisted that the firm accept accounts from Nazi banks and businesses. To avoid this indignity, Pesson-Didion informed the Nazis that J. P. Morgan and Company had instructed him not to accept new accounts or expand old ones; if forced to break this rule, he said bluntly, he would have to liquidate the bank. This prearranged strategy worked, and the bank took no Nazi deposits.

With Jewish accounts, Morgan et Compagnie had less success. The Nazis had assembled a special administrative team to ransack Jewish securities and accounts. At Morgans and other Paris banks, they emptied the accounts and safety deposit boxes of Jewish clients and looted Fr 11.5 million in all. Morgans lodged protests to no avail. It seems doubtful whether any bank could have operated during the occupation if it had resisted these efforts too strenuously.

The most dramatic encounter with the Nazis occurred in 1944, when a Defense Corps—SS—officer marched into the bank and demanded money kept by a certain depositor. When the redoubtable Tuteleers resisted, the officer drew a gun and shoved it in his back, forcing him to limp out into the

street. Tuteleers and Leonard Rist were taken to SS headquarters on the rue des Saussaies and informed that unless the depositor's money were promptly handed over, they would be sent to a German prison camp. Prodded with gun butts and sequestered for an hour or two in a dark broom closet, the two were released when the $8,000 ransom was paid.

On another occasion, defying threats of prison or deportation, Maurice Pesson-Didion refused to hand over some French Treasury bills. A Gestapo officer then demanded to see a list of securities owned by Morgan et Compagnie and was incredulous that aside from government securities, the bank owned so little. Evidently imbued with a sense of mythical Morgan power, he swore that Pesson-Didion must be mocking him and the Reich. Citing supposed Morgan influence over other French firms, the officer expected to find lists of huge holdings of Credit Lyonnais and other bank stocks. He wouldn't abandon the belief that the House of Morgan held reams of French bank shares. Lamont later retold the story of what the German officer had said: " 'If they did not, how in the world were they able to control all the banks?' Pesson-Didion replied they held none. Then the German official asked him to explain 'the immense influence which the Morgan firms seemed to have all over the Continent and everywhere.' Pesson-Didion replied quietly that he could think of no explanation unless it lay in the character of the men who made up the Morgan institutions."[3] Lamont may have embellished the tale, but Morgan et Compagnie doubtless exercised less influence in reality than in the overheated minds of Nazi officialdom. There was always a mistaken sense that the House of Morgan principally exerted power through direct-share ownership in companies rather than through exclusive banking and advisory relations. With the full panoply of J. P. Morgan and Company power behind it, Morgan et Compagnie didn't need vast capital resources.

Morgan et Compagnie was the sole American bank in Paris to stay open throughout the war. It even turned a small profit. Leonard Rist was smart enough to see that such success might smack of collaboration, or at least of moral corner cutting. Perhaps as a result, he frequently cited his decoration from General Eisenhower for "gallant service in assisting the escape of Allied soldiers from the enemy."[4] That the U.S. government approved Morgan et Compagnie's wartime conduct was confirmed in late 1944 when the Treasury and War departments asked J. P. Morgan and Company to send senior Paris partner Dean Jay and other Americans back to the place Vendôme to restore a semblance of normality. Of the small, white-haired Dean Jay, it was said that American businessmen in France seldom made a major move without consulting him, and so his return carried symbolic weight. In the highest tribute of all, Morgan et Compagnie was assigned to handle deposits for

American troops in liberated France.

AS the lights went out across Europe in 1940, Tom Lamont made a last-ditch effort to steer Benito Mussolini away from Adolf Hitler. His faith in Mussolini had survived many atrocities. In January 1939, after Mussolini gassed villages in Libya and Ethiopia, Lamont was still reassuring the Morgan agent in Rome, Giovanni Fummi, of his “genuine admiration for the Duce’s extraordinary domestic achievements in behalf of his people.”[5] He clung to the fiction prevalent on Wall Street in the 1920s that there were two Mussolinis—the good domestic manager and the bad foreign adventurer—who somehow coinhabited the same stocky body.

By the spring of 1939, Lamont’s overtures to Mussolini were inextricably intertwined with U.S. government policy. In his last mission of the Diplomatic Age, he operated as a private diplomat for Roosevelt as he tried to pull Italy back from war. In serving the White House, Lamont had to overcome a hurdle—how to explain to FDR Fummi’s matchless access to Mussolini? However much the bank might cast Fummi as a neutral agent, for twenty years he had fulsomely praised il Duce. Fummi had predicted that Mussolini would make Italy a great Mediterranean power. Now Lamont trotted out the standard formula regarding Fummi: “While he is loyal to his Government, he is not a fascist.”[6] Whether Roosevelt believed this or not, Lamont was an uncommonly handy intermediary between the United States and Italy.

That spring, Lamont toyed with the idea of traveling to Rome and picknicking *alfresco* in the countryside. “I have every now and then a sort of longing or a nostalgia for the sunshine and brightness of Italy,” he told Fummi.[7] But he canceled a proposed trip, fearing a reporter might spot his name on a steamship list. He jovially told Joe Kennedy that “the Duce’s antics in Albania”—Italy’s April 1939 conquest of Albania—lay behind his cancellation of a scheduled stay at the American Academy in Rome, an institution subsidized by Morgan partners since Pierpont’s days.[8]

Instead of visiting, Lamont addressed a letter to the Italian government, warning that the United States would staunchly resist German—and, by implication, Italian—aggression. In the intricate ways of Morgan secret diplomacy, Fummi passed the letter to Bernardino Nogara, the Vatican’s financial secretary, who passed it to Azzolini at the Banca d’Italia. It thus arrived on Mussolini’s desk with the incontestable authority of God and money behind it.

The Vatican figured importantly in both Lamont’s and Roosevelt’s efforts to sway Mussolini. In February 1939, Roosevelt had sent Joe Kennedy to the

funeral of Pope Pius XI as a way of currying favor with the Vatican. A year later, he became the first president to assign a personal representative to the Vatican—Myron Taylor, former head of U.S. Steel and, in earlier years, an admirer of Mussolini. The Vatican feared its own political isolation if Hitler and Mussolini made an alliance, so it welcomed the Roosevelt opening, which aroused intense opposition from American Protestants.

In the spring of 1940, Lamont made a final approach to Mussolini. He sent a letter that he cleared first over the telephone with Roosevelt and that Tom Catto also showed to the British foreign secretary, Lord Halifax. Lamont tried to puncture Mussolini's delusion that in the event of war, he could count on faithful support from Italian-Americans. Lamont said that Italian-Americans were rabidly anti-Hitler and that Italy shouldn't be fooled by American isolationists. He warned against a Nazi *blitzkrieg.* Once again, Fummi handed the message to Nogara at the Vatican, who promised to transmit its contents to Mussolini. Not only did the mission fail, but it perhaps backfired, planting the notion in Mussolini's mind that Fummi, as a Morgan courier, could function as an Anglo-American spy. Lamont's maneuvers coincided with a mission to Mussolini undertaken by Undersecretary of State Sumner Welles for FDR. After a rather frigid interview with Welles, Mussolini told his son-in-law Galeazzo Ciano, "Between us and the Americans any kind of understanding is impossible because they judge problems on the surface while we go deeply into them."[9] Mussolini also rebuffed a mission undertaken by Francis Rodd of Morgan Grenfell, who believed that the British War Office was bungling the chance to co-opt il Duce. Shortly after the June 1940 evacuation of the British Expeditionary Force at Dunkirk, Mussolini permanently locked arms with Hitler.

In September 1940, Mussolini ordered the arrest of Giovanni Fummi—his way of rewarding the House of Morgan for its years of thankless loyalty. According to Morgan records, Fummi was abducted from his Roman hotel and held incommunicado at the Regina Coeli prison. Mussolini was now a financial as well as a political renegade and no longer had to flatter Lamont. Two months before, Italy had defaulted on its municipal and government loans. Officially, Fummi was charged with expressing pro-British sentiments through the mail. This was a specious, legalistic indictment that thinly veiled a political vendetta. For Fummi, it was a crushing end to twenty years of selling Mussolini to Wall Street's most powerful bankers. It was also an unmerited slap, for even after Mussolini embraced Hitler, Fummi still rationalized it as the only course left. Up until the war, both Lamont and Fummi had contended that Mussolini was driven into Hitler's arms not by madness or megalomania, but by Western diplomatic ineptitude.

Lamont, stunned and blindsided, felt personally responsible for securing Fummi's release. The two men had had a close, if curiously unequal,

relationship. Fummi would address him as Mr. Lamont, while Lamont would reply using the diminutive Nino. A professional hand-wringer, the sentimental, hypochondriacal Fummi had shared many trials with Lamont—his first wife's death from cancer in 1930, several breakdowns from overwork, and arthritis. In Morgan annals of crisp business letters, Fummi's notes stand apart as the musings of a tender, melancholic man who bared his grief in a most un-Morgan-like manner.

Whether operating from the Via Veneto in Rome or a Saint-Tropez villa—made possible by his ample Morgan retainer—Fummi was always vulnerable to charges of his being a foreign agent. For twenty years, he had performed a tightrope act, balancing patriotism with professional necessity. Most of the time, he could serve both his Wall Street masters and Mussolini. But what if their interests clashed? Fummi often told Lamont that if a conflict ever arose, the bank would take precedence over Italy. Then, in 1939, he conceded that if war came, he would serve in the Italian army. He never resolved the confusion over his national identity.

Compounding Fummi's trouble was that in 1934 he had married Lady Anne Crawford, daughter of the Earl of Crawford and Balcarres and niece of Sir Ronald Lindsay, the British ambassador in Washington. This English veneer must have excited Mussolini's suspicions. For Fummi's wedding, the House of Morgan sent the couple a pair of George II silver mugs. In 1938, Fummi chattered happily about how Anglicized he had become, with "an English wife, an English secretary and an English nannie!"[10] When war came, however, he knew he was in a ticklish situation and packed off his English wife, children, and nannie to Scotland while he stayed behind in Rome. Perhaps the arrest came as less than a total surprise.

Lamont orchestrated Fummi's release in a masterful way. First he got the State Department involved. Then, through Myron Taylor, he sent confidential messages to the papal secretary. There was good reason to expect Vatican sympathy: Fummi was a close confidant of Nogara, who headed the Vatican's investment arm, the Special Administration of the Holy See. While Pope Piux XI was alive, it had even been assumed that Fummi would someday replace Nogara as the Vatican's chief portfolio manager. It is also likely that Nogara was secretly hostile to the Germans, for neither before nor after the war would he invest Vatican funds in German securities. In addition, Lamont had once lunched with the new pope, Pius XII, in New York. Responding to Lamont's pleas, the Vatican cabled back that they were doing "utmost privately and officially in order to obtain release friend." The papacy underscored Mussolini's personal involvement in the affair: "We understand ultimate decision has to be taken by Government chief."[11]

In the end, only a personal appeal to Mussolini by Lamont would work. It

was as if the sadistic Duce wanted to extract one last tribute, one last insufferable humiliation, from his banker. Lamont had to check his anger and argue that Fummi had represented Italy to the House of Morgan and not the reverse. If there were more truth to this than Lamont would ever care to admit, it now had to be grossly overstated. He wrote:

It was Fummi, and Fummi alone, who urged my original visit to Rome in 1923 and the subsequent visits which resulted in these favorable loan operations for your Government. On every occasion he was active in the negotiation and zealous to advance the good name of his Government and to protect it at every point. While it is true that Fummi was our own representative in Italy, yet it is even truer, so to speak, that he acted broadly and wisely as a financial ambassador for your Government.

Far from evading the subject of Fummi's marriage to an Englishwoman, Lamont rather brazenly advanced it as an extra guarantee of Fummi's patriotism: "As time went on, we became more and more impressed with the fidelity which he did show and was bound to show towards his own Government and people. The fact of his having married Lady Anne Crawford only served to make him more meticulous in the manner in which he handled himself and in the correctness of his attitude toward his own Government."

It is noticeable that Lamont never directly accused Mussolini of arresting Fummi or of having prior knowledge. He wrote as if he were entreating a wise, neutral, and all-powerful arbiter. In the end, Lamont groveled one last time: "Finally, it is because of your kindly and generous attitude towards me personally in all our interviews, and perhaps especially because of the charming sense of proportion that you have always shown in such interviews, that I have ventured to address you this urgent personal appeal in Fummi's behalf."[12]

About ten days after Fummi's arrest, a cable arrived at Morgans from Vatican City. It reported that Fummi had been safely released and would be exiled to Switzerland. For Lamont, it was an ironic end to seventeen years of having scraped and bowed and hoped that Mussolini could be reformed. He wasn't left with the dignity of any comforting illusions. As he wrote in a somber letter to Fummi in Saint-Moritz, Switzerland, "Some time or other, dear Nino, a new day will dawn and America and Italy will once more be friends. But before that day comes there will be fire and flame and sword, grief for us all."[13]

In February 1941, the Morgan office in Rome was closed. Two weeks later, the irrepressible Fummi popped up in London to supervise a secret transfer of Vatican gold bullion stored in a basement room at Morgan Grenfell. Throughout the 1930s, the Vatican had bought the gold at the fixed price of $35 an ounce, never selling any. Fummi would discreetly refer to it as the

"special commodity." For security reasons, the Vatican now decided to ship the gold to New York. The wartime transfer was carried out under the official aegis of Lord Halifax, until recently Britain's foreign secretary. The gold ended up at the Federal Reserve Bank of New York. There it would dizzily appreciate in the postwar years.

In 1942, Bernardino Nogara tried to call in his IOU for his help in the release of Leonard Rist and Giovanni Fummi. The Vatican held a large stake in a South American banking group, Sudameris, which was headquartered in Paris but had branches in Argentina, Brazil, and other Latin American countries. America's wartime blacklist had produced heavy losses for the Brazilian bank, and it faced possible liquidation; Nogara wanted to get Sudameris off the list. To this end, he proposed that Morgans buy half of the company. In exchange, he said the House of Morgan would have final approval over its actions. Although Fummi was ready to go to New York to negotiate and Nogara promised to "guarantee the fullest respect of the Allied interests in the management of the South American branches of Sudameris," Lamont explained the political and legal impossibility of buying shares in foreign banks that had French and Italian backing.[14] Vatican appeals to the State Department bore no fruit, either. But the discussion reveals an interesting example of the Vatican's diplomatic independence in Axis Italy.

IN May of 1940, Neville Chamberlain resigned in favor of Winston Churchill, a man with whom the House of Morgan had always had a peevish, family quarrel. Teddy Grenfell had been blind to Churchill's merits, saying of him after the crash, "His record for thirty years has shown him to be the most unreliable of statesmen as well as the most unstable of friends . . . I wish he would change his party for the third time and go over to Ramsay MacDonald, or even further to the left."[15] During the summer of 1940, Nancy Astor grudgingly conceded to Tom Lamont that Churchill was doing a good job but regretted Lloyd George's absence from the cabinet.

In August 1940, the Battle of Britain began. Reported vividly to America by Edward R. Murrow's broadcasts, the nightly blitz drove Londoners into the Underground. Morgan Grenfell had girded for war, adding air-raid shelters and gas-proof access to street and stairways. Although 23 Great Winchester escaped a direct hit, the square mile of the City was badly bombed, and the Dutch Church across the narrow lane from Morgan Grenfell was destroyed. When a parachute mine in its rubble exploded, the blast stripped wood panels from the Morgan partners' room and blew out several doors. A nearby conflagration at Carpenters' Hall was extinguished in time to save 23 Great Winchester. Later on, a V-1 missile fell in Old Broad Street, where George Peabody and Junius Morgan had once worked. After each such pounding of

London, Harold Nicolson would send Charles Lindbergh a needling postcard, saying, “Do you still think we are soft?”[16]

As British children were evacuated from London, the House of Morgan proudly did its duty. No cause warmed Jack Morgan’s blood more than England at war. Gray and tired, he went to a West Fourteenth Street pier for the arrival of almost four hundred British children aboard two ocean liners. There he met the eleven-year-old Lord Primrose and two of Lord Bicester’s grandchildren, all with governesses and nurses in tow. They would be his wartime guests at Matinicock Point, along with three other City Smith offspring. “Jack Morgan lived in considerable Victorian splendor, with armed guards all over the place,” recalled Charles E. A. Hambro, who spent part of the war with the Harry Morgans in New York before rushing back to play on Eton’s cricket team in 1943, “and there was Lord Primrose in isolation with the old boy.”[17] In a further caretaker service for Britain, the vaults of J. P. Morgan and Company received British government rowing trophies, along with two Gutenberg Bibles.

Chartering George Whitney’s old boat, the *Wanderer*, Jack transferred *Corsair IV* to Britain for war service. He donated many of its interior decorations, from a blue rug to wicker deck chairs, to a “Bundles for Britain” benefit at Gimbel’s, and Harry Morgan sold his Grumman amphibian plane to the Canadian government for use in coastal patrols. After France fell, a British visitor at 23 Wall expressed fear for the future. “Our turn is next,” he told Jack. “The Huns will let loose on us a blitz that will be hard to withstand.” Jack brimmed with emotion. “My good friend,” he said, “you need not be downcast for a single moment. I tell you, Britain will never give in, never, never, never!”[18] His fecund imagination now had fresh cause to picture pursuing Germans. In escaping from London raids, young Luftwaffe pilots would empty surplus bombs over Wall Hall, and in October a load blew out the mansion’s windows. For safekeeping, his silver collection was brought into the 23 Great Winchester vaults that housed the Vatican gold.

Morgan Grenfell was depopulated as partners entered government service, a logical culmination of the firm’s activities during the Diplomatic Age. It was already something of a branch office for the Bank of England, the Treasury, and the Foreign Office. Francis Rodd, who had explored the southern Sahara in the 1920s and won a medal from the Royal Geographic Society, was posted to Africa, while Willy Hill-Wood spent much of the war in Washington as a U.K. censor. Lord Bicester and Lady Sybil converted their Oxfordshire estate, Tusmore, into a fifty-bed convalescent home, as other British country houses were turned into barracks or troop hospitals.

Monty Norman recommended Tom Catto for a new, unpaid position as financial adviser to the chancellor of the Exchequer, Kingsley Wood. A short,

shrewd, dignified Scot of humble background, Catto had been a Morgan Grenfell partner since 1928. Before that, he had managed the large Indian merchant house of Andrew Yule and Company, owned by Morgan partners in London and New York. He had the exotic, global connections of an empire-building entrepreneur, having done deals with Vivian Smith in the Middle East and Russia. He and John Maynard Keynes were assigned rooms on opposite sides of the chancellor's office; Keynes to represent the independent, theoretical view; Catto, the practical, banking side. They were soon dubbed Catto and Doggo, and Lord Bicester, with muted glee, reported to 23 Wall that Catto was liberally throwing out many of Doggo's impractical ideas. Monty Norman preferred dealing with Catto, who would succeed him as governor, perpetuating Morgan Grenfell's charmed access to the Bank of England.

With much of Europe under Nazi control, Churchill knew he had to woo America with all the wit, charm, and energy at his disposal. He faced a new opponent, an organization equally determined to keep America out of the war —America First. Formed by two Yale graduate students, R. Douglas Stuart, Jr., and Kingman Brewster, it was a response to the William Allen White committee and promptly recruited Charles Lindbergh. Through his America First speeches, Lindbergh destroyed the last remnants of the hero worship he once aroused. Stumping the country, he would claim that "the three most important groups which have been pressing this country toward war are the British, the Jewish and the Roosevelt administration."[19] He talked of insidious Jewish influence in the American government and media.

Despite the impact of Lindbergh's speeches, the nightly terror in London engendered a wave of sympathy for Britain. Strengthened by his November 1940 reelection, Roosevelt stepped up efforts to aid England. He and Churchill negotiated an exchange of fifty old U.S. destroyers for eight British air bases in the West Indies. By late November 1940, Lord Lothian sounded the alert regarding a looming British cash crisis, and in early December, Churchill told Roosevelt the time was coming when England would "no longer be able to pay cash."[20]

During this desperate autumn in Britain, the House of Morgan and the Roosevelt administration were reunited in a campaign to provide all aid short of war. This rapprochement produced a sense of mutual relief. After chatting with Roosevelt at the White House, Leffingwell told him on December 24, 1940, that "whatever differences there may have been about domestic affairs, I and my colleagues are heart and soul with you for unlimited material aid to Britain and for national defense."[21] That weekend, Roosevelt was broadcasting a fireside chat in support of Britain, and Leffingwell offered some pointers. "When you say 'give,' you mean give or lend goods, guns,

ships, planes, munitions and whatnot . . . you are not interested in giving England a bank account, but in giving her the things she needs."[22] In his radio address, Roosevelt exhorted Americans to make the United States "the great arsenal of democracy," and a week later he asked Congress to enact a lend-lease program that would let Washington guarantee payment for British war orders in the United States and lease supplies indefinitely. There would be no immediate cost to the Allies. Roosevelt hoped that the Lend-Lease Act would avert another war debts/reparations mess after the war. Churchill called it "the most unsordid act in the history of any nation."[23] Morgan support of the plan is notable in that it precluded any repetition of the bank's financing role in World War I.

As Lindbergh and other isolationists testified against the Lend-Lease Act, Roosevelt and Treasury Secretary Morgenthau sought a dramatic way to rebut charges that Britain had billions of dollars in idle assets salted away around the world. They decided to ask for an act of bloody public self-sacrifice—nothing less than the sale of a major British industrial holding in America to show that Britain had exhausted all options before pleading for aid. In March 1941, on the eve of congressional passage of lend-lease, Roosevelt and Morgenthau notified Whitehall that it would have to consummate an important sale at once. The White House itself selected Britain's single most valuable industrial possession in America—the American Viscose Company, a subsidiary of the Cour-taulds' textile empire. With seven plants and eighteen thousand employees, it was probably the world's largest rayon producer. Washington urged extreme haste and imposed a seventy-two-hour deadline for announcing the sale.

The British found this need to demonstrate faith to an old friend degrading. A somber delegation, including Tom Catto, broke the news to chairman Samuel Courtauld, who reacted in exemplary fashion. He asked only one question: "Was the sale essential in the national interest, whatever the hardship on him and his company?"[24] When Catto replied that it was required by the essential interests of wartime finance, the patriotic Courtauld fell on his sword. The Courtaulds' board was given thirty-six hours to make arrangements—surely the fastest such major divestment in history.

To sell American Viscose to American investors, J. P. Morgan and Company recommended to the British Treasury that Morgan Stanley and Dillon, Read manage the sale, with 23 Wall providing the necessary bank loans. The handling of the sale rankled the British for years. In unsettled, wartime conditions, it was hard to know what price might attract American investors. Textile shares had been fluctuating wildly, and underwriting tasks that normally took weeks were compressed into days. While Britain received $54 million, the seventeen-firm syndicate headed by Morgan Stanley and

Dillon, Read resold the shares publicly for $62 million, pocketing the difference. Some Britons—most notably Winston Churchill—thought they had been fleeced by the bankers. At the time, the Courtaulds' directors claimed the company's tangible assets alone were worth $128 million. Obviously, there was a fantastic discrepancy.

After the war, Churchill described the sale in dryly cynical terms: "The great British business of Courtaulds in America was sold by us at the request of the United States Government at a comparatively low figure, and then resold through the markets at a much higher price from which we did not benefit."[25] When Harold Stanley read this description in a 1949 newspaper excerpt of Churchill's memoirs, he was shocked. Through Lord Harcourt of Morgan Grenfell, he made extensive efforts to get Churchill to modify it. He even tried to draw on Churchill's old friendship with his wife, Louise (formerly Mrs. Parker Gilbert), who had aided Churchill when he had an accident in New York years before. In revising his book, Churchill agreed to delete the impression that the bankers were too richly rewarded for their services. But he wouldn't budge in his opinion that American Viscose had fetched far less than its intrinsic worth. At the time of the sale, it was agreed that the matter would be referred to a three-man arbitration tribunal. In bitter postwar litigation, Courtaulds received additional compensation from the British government.

After congressional passage of Lend-Lease on March 11, 1941, Roosevelt approved a long list of supplies to be shipped to England. The progressive wing of the isolationist movement resented not only its defeat on Lend-Lease but also Roosevelt's about-face in his attitude toward Wall Street and the House of Morgan. That April, Senator Burton Wheeler of Montana, who had pursued Morgans in the railroad hearings, castigated Roosevelt for inviting the "money changers" and "Wall Street lawyers" into his camp. He angrily noted that people such as Willkie and Lamont were suddenly portrayed as "liberals," while progressives were being styled as "Tories, Nazi sympathizers, or anti-Semites" because of their opposition to U.S. participation in the war.[26]

While attacked by progressives as warmongers, the House of Morgan was actually engaged in a hidden feud with its British friends for taking the opposite position. Tom Lamont had helped Roosevelt lobby for Lend-Lease yet insisted that the United States not enter the war. Ostensibly, this was so America could remain an arsenal for England, but there were also festering sores from the 1930s feuds. Lamont and Catto at the British Treasury shared their own diplomatic back channel, and Lamont's letters became increasingly petulant. In May 1941, he wrote a remarkable letter to Catto, full of bile and defending the U.S. failure to go to war:

If the American people have seemed sluggish in coming to Britain's aid, nevertheless, it must be acknowledged that the U.S.A. is the first nation to go all-out in their opposition to Hitler without having faced an immediate, desperate threat to its existence. On that point does not America deserve praise for such progress rather than implied criticism for its slowness? Every country in Europe, including Britain, waited almost until Hitler had his thumb on its windpipe before it waked up and got started.

> Most English people look upon America, because it was (150 years ago) a British colony, as simply a younger, perhaps more vigorous, less polished England. That picture is emphasized by our former habit of calling England 'the Mother Country.'

At this point in the letter, Lamont dredged up the quarrels of the 1930s. He recalled Britain's double cross on German debt and its unwillingness to make payments on the World War I debt, which might have won American sympathy. He recalled how in 1935 he had begged Neville Chamberlain to consider a commercial treaty with the United States to create goodwill for England in America, saying it might be needed in some future crisis. "Mr. Chamberlain smiled an icy smile and was not interested in American good will."

The letter ended by implying that British snobbery toward America was no less galling to Lamont than were the financial betrayals of the 1930s. He referred to an inequality behind the fraternal Anglo-American facade: "Meanwhile, Britain, with the exception of a few of us, has, as I have intimated, never shown any great interest in America unless or until she needed America's help desperately. Tens of thousands of Americans would journey annually to the other side. But I can number on the fingers of less than my two hands the number of eminent British persons who have ever been interested to visit America."[27]

It seemed a strange time to kick the British, who had suffered the winter bombings in London, Coventry, and Plymouth. Those radical American pamphleteers who had portrayed the House of Morgan as fawning, uncritical Anglophiles—how startled they would have been by this letter from Lamont. He showed it to Leffingwell, who actually thought it sounded too apologetic. "If I were talking to Americans, I might be saying the same things," Leffingwell confessed, "but talking to Britishers I think it unduly encourages their sense of superiority to colonials and Americans."[28]

Tom Catto replied with gallantry. To be sure, he was a high Treasury adviser and afraid to alienate an influential American. But Catto also had considerable personal skill in handling delicate matters. He wrote a letter of such dignity that it perhaps reminded the J. P. Morgan partners of why Britain's restoration as a world financial center had for decades been such an

emotional issue with them:

> I was much interested in your letter and you must never think that hitting straight from the shoulder on such matters upsets me in any way. We have known each other too many years for that. . . . Whatever our shortcomings and however short our memory may be, we are cheered and encouraged by the knowledge that your great country is with us in our struggle. We have entire confidence that in the end that will mean victory! . . . It is a long road that has no turning. When we reach that turning, I believe Hitler and his gangsters will get a surprise. . . . Do not worry about us. We are all cheerful. We have had a few knocks but we can take them, indeed one hears less of the proverbial British grousing in these times than in days of peace.[29]

LATER Lamont would tell of the time when a "heavy fire curtain" fell between J. P. Morgan and Morgan Grenfell, and the House of Morgan was internally divided.[30] One partner didn't live to see the curtain rise. Teddy Grenfell—Lord Saint Just—died ten days before Pearl Harbor. In the late 1930s, he'd had heart and lung problems and was frail and bedridden for months at a time. Doctors recommended golf at Sandwich or West Indian cruises with his wife to restore his health.

Grenfell belonged to a vanishing species—the diplomatic banker. His work was often an inseparable blend of private and public purpose. Cool and dapper, he had been a Morgan sphinx, cloaked in mystery, working unseen in the top echelons of government and finance. "English Bankers and Houses are very much more secretive than those in New York," he told Lamont, and secrecy was his unchanging creed.[31] He believed implicitly in the wisdom of his class, country, and profession and had no patience with reformers. His mind was acute, his predictions unerring, his tailoring immaculate, and his pose debonair. But his sympathies were limited and his tolerance dim. He saw bankers defending immutable truths against political folly and public ignorance. He would have been misplaced in the coming Casino Age, when governments, not private bankers, would assume financial leadership. So strong was Gren-fell's friendship with Jack Morgan that his death would weaken the tie between the New York and London houses.

EVEN with Europe at war, Tom Lamont didn't shed his Panglossian tendency to predict favorable outcomes in world affairs. He expected Japan to refrain from war against the Allies, not from any scruples, but because self-interest dictated that it be on the winning side. Three weeks before Pearl Harbor, he told Walter Lippmann that if Japan "were on the losing side she

would lose complete influence in the whole Pacific region and would sink there to the status of a second or third rate power. . . . I may be 100% mistaken, but I am really not worried at all about the Far East for the moment."[32] On December 7, 1941, Japan attacked Pearl Harbor, and yet another Lamont illusion was shattered. In the most eloquent expression of disgust with Japan, Lamont joined that year with Henry Luce in merging eight China aid groups into United China Relief. The Japanese presence on Wall Street was abolished as the New York State superintendent of banks seized the assets of the Yokohama Specie Bank, Japan's fiscal agent before the war.

U.S. entry into the war in 1941 repaired the breach within the House of Morgan. With the United States and Britain fighting side by side, Morgan partners revived the belief that their countries were destined to rule the world jointly. In a new spirit of forgiveness, Lamont took to citing English, Scottish, and Irish blood in American veins as the country's real source of strength. Vindictive toward Britain two years before, Russell Leffingwell said warmly, "To my mind the only thing worth fighting for is to save England and the British Empire. For that I would shed every drop of blood in my own veins, and let many millions of Americans shed theirs too."[33]

J. P. Morgan and Company resumed its customary role of defending the mother country. When *Life* magazine published an open letter saying the war shouldn't be fought so Britain could keep her empire, Lamont sparred with Henry Luce. The bank had known Luce well ever since his Yale classmate Henry P. Davison, Jr., became the first investor in *Time* magazine and a company director. Lamont now told him that America had its own imperialism and backed its own Latin American dictators: "Why do we yell about 'imperialism' when we are busy day and night scheming to get the whole Caribbean under our control and sweeping all of Latin America into our orbit by lavish loans and diplomatic manoeuvres?"[34]

A new rapport between Roosevelt and Jack Morgan was evident in November 1941, when labor leader John L. Lewis ordered a strike against captive coal mines owned by the steel companies. When Roosevelt appealed for patriotic restraint, Lewis said his adversary should also be restrained. "My adversary is a rich man named Morgan, who lives in New York," he declared.[35] To Roosevelt, Lamont protested this insinuation that U.S. Steel was just a tool of Jack's. Not only did Roosevelt side with Jack—a novelty in itself—but he did so with a new geniality. A class traitor no more, he told Lamont: "I was really angry at Lewis' unwarranted, untrue, and demagogic statement about Jack. . . . When you see Jack, tell him for me not to concern himself any more about Lewis' attack, for after many years of observation, I have come reluctantly to the conclusion that Lewis' is a psychopathic condition."[36]

Able to slough off divisive, prewar domestic issues, FDR and the Morgan partners became fast friends. After Lamont congratulated him for declaring war, Roosevelt wired back, “Generous words of approval from an old friend like you are heartening.”[37] They swapped jokes, anecdotes, and amusing press clips, including one citing Communist leader Earl Browder’s accusation that Roosevelt had prevailed upon Lamont and Walter Lippmann to engineer Willkie’s nomination. In early 1942, Lamont spent almost an hour at the White House speculating as to how the U.S. might use Fort Knox gold in the postwar world to stabilize currencies. Roosevelt said America was trusted more in continental Europe than was Britain. This was the relationship Lamont had craved—full of secrets, confidences, and back scratching. Turning to the subject of Churchill, FDR confided to Lamont that Winston didn’t have the economic mind they had.[38] (Yet in 1939, the British embassy in Washington filed this tart appraisal of Roosevelt: “His knowledge of certain subjects, particularly finance and economics, is superficial.”[39]) At Roosevelt’s request, Lamont appeared at a Madison Square Garden rally for Soviet-American friendship—the one time Tom appeared politically with his left-wing son, Corliss.

What strengthened ties between Roosevelt and the House of Morgan was that both felt beleaguered by the same isolationist forces. In the spring of 1942, Leffingwell told the president that the war effort required more parades, brass bands, and flag-waving. Agreeing, Roosevelt added that “the real trouble is not in the people or the leaders, but in a gang which unfortunately survives—made up mostly of those who were isolationists before December seventh and who are actuated today by various motives in their effort to instill disunity in the country.”[40] So the new concord between Roosevelt and Morgans corresponded to the old political axiom that the enemy of my enemy is my friend. War had finally made peace between the White House and the House of Morgan.

CHAPTER TWENTY-FOUR
PASSAGES

THE early war years saw the final transformation of J. P. Morgan and Company from a private partnership to a corporation. This momentous step in Morgan history was taken only after extensive deliberations at the Pierpont Morgan Library. In announcing the transformation in February 1940, Jack made an unprecedented appearance at the press conference. He would be board chairman, George Whitney chief executive, and Lamont head of the executive committee. In dropping the partnership form, Jack had to sell the New York Stock Exchange seat bought by Pierpont in 1895. As a private bank, partners had been exposed to the full risk of loss. But they had gladly accepted this risk in order to keep their capital position secret and their books free from inspection. This tradition had contributed immeasurably to the firm's mystery and power.

Why, then, the change? The bank feared rapid capital depletion as the three richest partners aged: Tom Lamont, Charles Steele, and Jack Morgan. Steele had died in Westbury, New York, in mid-1939, after spending his last years watching his grandsons play polo. If either Jack Morgan or Lamont died soon, too, there could be a serious drain on capital. A combination of the Depression and inheritance and income taxes had whittled the bank's assets down from $ 119 million in 1929 to only $39 million in 1940. By converting to share ownership, heirs could sell their stakes without disrupting the bank's capital. There was also a wish to enter the trust business, which was closed to partnerships. In 1927, American Telephone and Telegraph had funded the first big corporate retirement plan, and Morgans wanted to capture similar huge pools of capital.

There were other blows to Morgans' traditional aloofness as well. In 1942, it joined the Federal Reserve System—having been the largest holdout—in a move related to its heavy purchase of government bonds, which was Wall Street's principal wartime activity: the Corner witnessed Victory Loan rallies for which huge throngs turned out before a flag-draped Stock Exchange. Now for the first time, the House of Morgan's nearly $700 million in deposits became subject to federal deposit insurance. Also in 1942, ownership of Morgan shares spread beyond the eighty or ninety people, mostly family and friends, who had controlled it before. A syndicate led by Smith, Barney offered 8 percent of Morgan shares to the public—the first time ordinary

mortals could buy a piece of a Morgan bank. This both broadened ownership and assigned value to closely held shares. In a final affront to tradition, J. P. Morgan and Company disclosed its earnings in a prospectus.

In this period of transition, the Morgan link with its Philadelphia affiliate, Drexel and Company, also ended. The Philadelphia firm had brought the Drexels, Biddies, Berwinds, and other Main Line families into the Morgan fold. As Pierpont had told Arsene Pujo, "It only has a different name, owing to my desire to keep Mr. Drexel's name in Philadelphia."[1] In 1940, 23 Wall took over Drexel's deposits, shut the Philadelphia office, and sold the name to some Philadelphia partners who were forming an investment bank. Later on, I. W. "Tubby" Burn-ham merged his Burnham and Company with the reincarnated Drexel, so that the famous name would later grace the junk-bond operation of Drexel Burnham Lambert.

To qualify for Stock Exchange membership, Morgan Stanley became a partnership in 1941. It was now harried by the Brandeisian trustbusters who had pursued J. P. Morgan and Company and saw Morgan Stanley as simply a retooled version of the original company. Morgan Stanley's instant success had aroused suspicion, for it had managed a quarter of all negotiated bond issues since Glass-Steagall. During the Temporary National Economic Committee hearings in 1939 and 1940, the committee's chairman, Senator Joseph O'Mahoney of Wyoming, refused to believe J. P. Morgan had withdrawn from investment banking: "Now that the Banking Act has separated two functions that were formerly merged, Morgan Stanley in the investment field has succeeded to a similar dominant position that J.P. Morgan formerly held."[2] SEC counsel John Hauser advanced a conspiracy theory that dismissed Morgan Stanley as a "legal fiction" set up by J. P. Morgan partners to bypass Glass-Steagall. An exasperated Harold Stanley was repeatedly asked whether he took orders from 23 Wall after Glass-Steagall. "We were a separate, split-off organization," he insisted. "We owned and ran the business. Our money had been risked in the common stock."[3] Notwithstanding his denials, the SEC charged that J. P. Morgan and Company had used its influence over Dayton Power to obtain business for Morgan Stanley.

What weakened Morgan Stanley's claim to autonomy was that most of its preferred stock was owned by J. P. Morgan and Company officers. The SEC asserted this created "an identity of pecuniary interest" between the two Morgan houses and an "emotional" and "psychological" affiliation.[4] So Morgan Stanley began buying the preferred stock, and J. P. Morgan executives sold it to their wives, sons, grandchildren, and so forth—a transparent ruse that didn't fool anybody. To retire the bogey of J. P. Morgan control once and for all, Morgan Stanley redeemed and canceled its preferred

shares on December 5, 1941. This ended any formal link between the two firms, although a multitude of intangible links would weave them together for decades.

At this point, the campaign against Wall Street shifted to a lower gear. The investment banking business was moribund during the war as the Treasury Department asked underwriters to desist from new bond issues so as not to compete with government war-bond drives. Therefore, the drive to reform investment banking was stalled until the Medina trial of the early postwar years. In the meantime, by switching to a partnership form, Morgan Stanley retreated into the world of “mystery and dignity,” as Judge Medina later labeled it, just as J. P. Morgan was emerging into the sunlight.

AFTER initial grumbling, Jack Morgan settled amiably into his new role as board chairman. “What he had looked forward to with distaste he found not at all disagreeable,” said Russell Leffingwell.[5] On January 31, 1943, Jack presided over the first public shareholders meeting of J. P. Morgan and Company, Inc. It was a pleasant, autumnal time for him: the war had silenced New Deal charges of villainy, and everybody was saying that Jack hadn’t seemed so happy since before Jessie’s death, eighteen years before. He enjoyed serving as nanny to his English war babies and went duck shooting nearly every weekend that fall. There were gentler pursuits as well, including the new hobby of taking color photographs of cherry blossoms and other flowers.

The soft-shoe, avuncular Jack was much more in evidence. Every evening, he stopped to chat with the Pinkerton guards at Matinicock Point, thanking them as they opened the gates that guarded the estate. Playing backgammon with John Davis for a nickel a game, he had a winning streak and teased Davis’s butler that he was about to lose his wages. He observed life’s smaller details. Each morning, at the same bend in the road, he passed a young neighbor driving to work in the opposite direction; when the young man overslept one morning and they passed further down the road than usual, Jack wagged a satirical finger of rebuke.

In late February, doctors gave Jack a clean bill of health before he left for a Florida holiday, a quiet fishing trip on the Gulf of Mexico. On the train to Boca Grande, he had heart trouble, however, followed by a cerebral stroke. His steadfast valet of twenty-eight years, Bernard Stewart, managed to get him to his rented cottage at the Gasparilla Inn, a winter resort on a barrier island, and his New York heart specialist, Dr. Henry S. Patterson, came down to look after him. Jack survived less than two weeks. He died in a coma on March 13, 1943, and his body was brought north in a special Pullman car attached to the Seaboard Line.

Even in death, there were eerie parallels between Jack and Pierpont Morgan. Both died at the age of seventy-five, and again news of the death was withheld until after the stock market closed, so as not to disturb share prices. The voluminous obituaries that followed were of the full-page variety reserved for heads of state. The *New York Times* commented, "The private banking house of J.P. Morgan & Co. . . . gained a position of world-wide importance and a place in international financial affairs that not even the house of Rothschild attained in the period of its greatest power."[6] The paper called Jack the last financial titan—they had said the same thing of Pierpont —noting that for the first time since George Peabody's retirement, the Morgan bank was not headed by a Morgan. Tom Lamont ascended to board chairman.

Jack's funeral service, too, was reminiscent of Pierpont's. He lay in state at the Pierpont Morgan Library before a funeral at Saint George's Church on Stuyvesant Square. The service featured the black baritone Harry Burleigh, who had sung at the 1913 funeral. Again flags flew at half-mast over the New York Stock Exchange and the Corner. One difference was subtly apparent to the twelve hundred mourners who arrived in a heavy downpour: they were solemnly escorted to their seats by the directors of *two* banking houses—J. P. Morgan and Company and Morgan Stanley. After cremation, Jack's ashes were sent to Hartford for burial at Cedar Hill Cemetery, alongside the graves of Pierpont and Junius.

In his will, Jack perpetuated Pierpont's tradition of flamboyant generosity, including a $ 1-million trust fund for his elderly domestic employees. Henry Physick, Jack's butler of thirty-four years and the man who was so resourceful during the 1915 assassination attempt, received $25; 000. His secretary of forty years, John Axten, hired as a boy of nineteen, got $50,000, as did Belle da Costa Greene. With a paternalistic flourish in the style of Pierpont, Jack gave six months' wages to long-time bank employees and three months' to those hired more recently.

As they had been at his father's death, everybody was surprised by the relative modesty of Jack's estate—only $16 million before taxes and expenses, $4.6 million afterward. Following merchant-banking tradition, he left the bulk of his estate to his sons, Junius and Harry. His daughters' families, the Nichols and the Pennoyers, would enjoy the prestige but less of the fortune associated with the Morgan name. During his lifetime, Jack gave away an estimated $35 million, including $ 15 million to the Pierpont Morgan Library and $9 million to the Metropolitan Museum of Art. His fortune wasn't frittered away only by philanthropy. After Jessie's death, he had maintained the fantastic indulgence of the colossal yachts and the regal estates.

Opinion of Jack's place in history was immediately divided. Clearly, his

business career had been a personal triumph. When he took over the bank, Wall Street rumor mills had patronized him as a bungler. Yet under him, the House of Morgan had amassed power beyond that of the bank under Junius or even under Pierpont. It had taken on extraordinary international breadth, winning many governments, finance ministries, and central banks as clients and capitalizing on the merger of politics and finance in the Diplomatic Age. The building at 23 Wall now seemed less a smoky clubhouse of banking cronies than a gathering place for the world's financial elite. With some glaring exceptions—such as the Van Sweringen escapade and the Richard Whitney scandal—Jack had preserved the bank's reputation for fair, conservative dealings.

He had also put in place a superlative team and allowed its members to employ the full scope of their energies. He was a good "successor" figure who knew how to delegate power and take disinterested pleasure in his partners' feats. If the Morgan bank moved like a well-oiled machine and was free of internal warfare, it had something to do with Jack's reputable stewardship. A more self-centered boss might have regretted his own absence during the 1929 crash, yet Jack took fatherly pride in his partners' behavior: "I . . . was made very happy by the absolutely magnificent conduct of all my partners during the 'late unpleasantness' in Wall Street. The Firm showed that it could behave just as well when I was not there, as it could have done had I been there."[7] Unlike his father, he was never a prisoner of his ego.

Of Jack's public role, a far less flattering judgment must be rendered. The *New Republic* acidly observed that Jack had "added nothing creative or humanizing to American life, and . . . his passing subtracts nothing."[8] In the Victorian age, he would have been a model banker, cherishing honor, integrity, and Christianity. Such values, however, were inadequate during the worldwide Depression, when many people went hungry while still abiding by them. It was a harsh Providence that dropped such a hidebound, frightened man into an age of radical upheaval and experimentation. He asked for privacy in an era that demanded accountability. Increasingly the Morgan bank operated as an adjunct of government. It couldn't accept the benefits of public service without also accepting its burdens. Fleeing his political troubles, Jack kept aloof from his countrymen and never understood plain Americans the way he did English aristocrats. The *New Yorker* once said with justice, "One feels he could both teach and learn if he would cross the Mississippi frequently and meet the people that largely make up America."[9]

At a time that demanded fresh thinking, Jack could only reiterate ancient economic verities and brood over affronts to his dignity. Rather than giving new ideologies a fair hearing, he found them evil and insidious. For a man of such delicacy, who reported late to work so he could watch the tulips bloom,

he could be heartless with his supposed enemies—Jews, Catholics, Germans, liberals, reformers, and intellectuals—whom he lumped together into a single nefarious plot. "The world knew him only as a somewhat mysterious colossus of finance," said The *New York Herald Tribune*.[10] If the world saw remarkably little of his compassion, he had himself to blame for it. He never gave of himself freely to the public. At bottom, he didn't believe in common humanity and imagined his foes driven by motives unlike his own. Instead of accepting change as a fact of life, he raged against his moment in history and suffered in the process.

That Jack Morgan was an anachronism could be seen by the fate of his possessions: only institutions could afford his boats and residences. *Corsair IV* was bought by Pacific Cruise Lines and converted into a cruise ship for eighty-five passengers. His Georgian brick mansion on Long Island was rented to the Soviet UN delegation in 1949. Soviet diplomats and their families played volleyball on a lawn that once had been owned by the czar's banker; in the mansion, they installed seventy-one beds, sixty-seven canvas chairs, and eight big cafeteria tables. The town of Glen Cove objected to this use of the property, and the Russians had to depart. For many years afterward, the estate served as a convent for the Sisters of Saint John the Baptist, who built a chapel in the courtyard between the main house and Jack's sixteen-car garage. The mansion was later torn down, and one hundred suburban houses were put up on the old estate grounds. The fifteen-hundred-acre Camp Uncas in the Adirondacks was bought by the Boy Scouts, while the United Lutheran Church paid a scant $245,000 in 1949 for Jack's forty-five-room Madison Avenue townhouse. In 1988, when the Lutherans decamped for Chicago, they sold it back to the Pierpont Morgan Library for $15 million. Wall Hall was acquired by the county council for a green belt around London. Princes Gate, once among the finest private homes in London, became headquarters of the Independent Television Authority in the 1950s (and in 1980 had as its neighbor just a few doors away the Iranian embassy, which in that year was the scene of a violent siege). The world of the grandees was over. In the post-World War II era the Wall Street and City banks would grow into vast, global institutions of a hitherto unimaginable size. But the bankers inhabiting them would, paradoxically, seem that much smaller.

FOR central bankers of the Diplomatic Age, the war proved a time of melancholy reflection. Monty Norman bemoaned the curse of modern democracy, of making decisions by "counting noses," as he scornfully phrased it. He blamed politicians for destroying the rational system of gold-linked currencies that he and his Morgan friends had created in the 1920s. All had foundered on the rocks of nationalism and politics. Finance, it turned out,

wasn't a sterile laboratory that could be run by scientific bankers in white coats. Nor could it be left to a mysterious, self-appointed priesthood. In the Casino Age, central and private banks would no longer function as sovereign states but would be linked to government entities, both national and multilateral.

Throughout the war, Russell Leffingwell sent food packages to Monty Norman. A rattled man wanting reassurance, Norman asked Leffingwell whether he was wrong about the gold standard and his attempts to refurbish the old imperial pound. Any other course of action, Norman pleaded, would "have shaken the confidence in Europe, and have produced a feeling of uncertainty, which seemed the one thing to be avoided."[11] Leffingwell agreed that only gold formed a bulwark against the modern plagues of managed currencies, budget deficits, and bloated welfare states. He, too, recognized the futility of their labors: "How we labored together, you and Ben, my partners and I, to rebuild the world after the last war—and look at the d——thing now!"[12] Monty was equally despondent: "As I look back, it now seems that, with all the thought and work and good intentions which we provided, we achieved *absolutely* nothing. . . . I think we should have done just as much good if we had been able to collect the money and pour it down the drain."[13]

There would be a day of reckoning for Monty Norman no less than there had been for Ben Strong. The Labour party had never forgiven him for his tough attitude toward the first Labour government in the 1920s, nor for the austerity imposed in 1925 on behalf of the gold standard. When the government abandoned gold in 1931, it only reinforced suspicions that financial "rules" were ruses to intimidate recalcitrant left-wing governments. The bitter 1931 gibe of Labour party veteran Beatrice Webb—"Nobody told us we could do it"—still reverberated. Now Norman's autocratic twenty-four year reign at the Bank of England would belatedly produce new government controls over British finance.

Norman's health declined in 1943 and 1944 and he was diagnosed as having pneumonia and then meningitis. Fragile and broken in his seventies, he heeded doctors' advice that he resign. For several years, Tom Catto had been mentioned as a successor, and his conscientious work at the wartime Treasury impressed Norman. Although Catto had been the sole liberal at the solidly Tory Morgan Grenfell, the Labour party feared he would perpetuate City rule at the Bank of England. As early as 1940, Hugh Dalton, minister of economic warfare, warned Chancellor of the Exchequer Kingsley Wood that "there will be much feeling against Catto as successor. He comes from the most reactionary firm in the City, Morgan Grenfell, who, I say, have a notorious record as partisan Tories."[14]

Chosen governor in 1944, Catto made a wistful pilgrimage to Norman's

country house to receive the older man’s blessing. “My dear, Catto,” Norman said, “I had been my own first choice for re-election as Governor of the Bank of England, but the doctors say ’No.’ You are my second choice. God bless you.”[15] Touched by this gesture, Catto broke down and paced the garden with Norman’s wife before he could regain his composure. Catto’s appointment was interpreted as underscoring the need for close postwar cooperation with the United States.

After the surprise defeat of Churchill’s government in the 1945 elections, Clement Attlee’s Labour government put nationalization of the bank at the top of its parliamentary agenda. Although the bank had long handled national debt, currency issues, and foreign exchange, it was privately owned by seventeen thousand stockholders. Now the central bankers were to be driven from the shadows in which they had operated. For Labour partisans, it was a long overdue act of revenge against Norman.

Die-hards in the City thought Catto should resign as a matter of honor rather than supervise a bank under government control. Monty Norman never quite overcame the feeling that Catto should have been wily enough to defeat nationalization. Catto, in fact, proved a perfect transitional figure and probably secured a better deal for the bank than Norman could have. He wasn’t regarded as a City figure hostile to Whitehall and was a shrewd, conciliatory man. He recognized that Norman’s dictum, “Never excuse, never explain,” wouldn’t suffice in the new age. Central banks could no longer be priestly or hermetic, and Catto thought it best for a sound banker to manage the transition. To preserve the bank’s independence, he won agreement that the governor be appointed for five-year renewable terms and dismissed only by act of Parliament.

In March 1946, after more than 250 years of independence, the Bank of England became a public institution. It would now be less influenced by merchant bankers, and more industrialists and union leaders would be appointed as its postwar directors. Catto told Lamont with relief, “The ship had to be steered between Scylla and Charybdis but we managed somehow!”[16] After serving as governor until his seventieth birthday, Catto in 1949 took a desk again at Morgan Grenfell but didn’t resume formal duties at the firm. His son Stephen, however, would be a postwar Morgan Grenfell chairman.

For Monty Norman, the new world embodied everything he despised. Lamenting the “socialisation at a gallop” overtaking England, he told Leffingwell that he seldom went into the City anymore and found it a sad place, reduced to refunding bonds at lower interest rates. The man who had devoted his life to maintaining London as a world financial center now saw it as a place of faded glory: “I fear that the various ancient businesses of

London have practically come to an end, or continue perhaps as shadows."[17] As foreign business shifted more decisively to New York than it had after World War I, leaving little room for London leadership, Norman seemed lost, unhinged, distraught. "I wonder what old Ben would think of all this," he said.[18] On February 4, 1950, Montagu Norman died, having suffered a stroke the year before.

AFTER the war, a hearty survivor, Dr. Hjalmar Horace Greeley Schacht, had resumed his correspondence with Monty Norman. Arrested by the Gestapo in July 1944 after participating in another plot against Hitler, he was sent to the Ravensbrueck concentration camp and ultimately passed through thirty-two prisons, including the death camp at Dachau. He formed part of a distinguished group of prisoners that included the former Austrian chancellor Kurt von Schuschnigg and Leon Blum. In the last stages of war, their captors hurried them southeast to escape the advancing American troops. On May 4, 1945, Schacht and the others were about to be executed by the Gestapo, under express orders from Hitler, when they were liberated by Allied troops in the south Tirol.

Schacht tried to visit the ailing Norman, but he hadn't been officially de-Nazified and was denied an English visa. He was a shameless, bull-headed man whose sheer arrogance seemed to preserve him in adversity. After being indicted as a war criminal by the Nuremberg tribunal, he was placed under arrest by General Lucius Clay, commander of the U.S. Army of Occupation in Germany. When Clay went to Schacht's chalet outside Berlin to take him into custody, Schacht resisted the notion that he was anti-American. As proof, he told Clay, "Look at the picture on the wall." It was a signed photograph that David Sarnoff had given him at the Young Plan conference in Paris in 1929.[19]

Awaiting the Nuremberg war trials at a prison camp, Schacht continued to behave in a bizarrely unpredictable manner. Albert Speer, Hitler's architect and minister of armaments, recalled how Schacht delivered dramatic poetry readings to pass the time. When American military psychologists delivered IQ tests to the war criminals, Schacht scored first in the group. There were many strange reunions at Nuremberg. Schacht hadn't seen Hermann Göring since losing out in the power struggle to him in 1937. "Our next meeting was in prison at Nuremberg when we were taken to a cell with 2 bathtubs where—I in one and Goering in the other—we each proceeded to soap ourselves all over," Schacht wrote. "Sic transit gloria mundi!"[20]

At Nuremberg, Schacht refused to admit responsibility for Hitler's success and denied he had made a unique contribution to the Nazi cause. He said of Hitler, "He would have found other methods and other assistance; he was not

the man to give up."[21] Schacht could document enough resistance in the late 1930s to offset the impression of collaboration with the Nazis. He cast himself as a solitary critic of the regime who was appalled by the cowardice of workers, liberals, churchmen, and scientists. So the man who rallied Krupp, Thyssen, and other German industrialists around Adolf Hitler and helped mold the robust German war economy was one of only three Nazis acquitted at Nuremberg. A German de-Nazification court afterward convicted him as a major Nazi offender, and he was sentenced to eight years in a labor camp, although he appealed and was released after a year. In the 1950s, he wrote a long-winded, self-adoring autobiography that was conspicuously short on contrition for his role in Nazi finance. He died unrepentant in 1970, at the age of ninety-three, of complications resulting from a fall.

STARTING in 1943, Tom Lamont had heart trouble and no longer reported regularly to the bank. Toward the end of the war, his handsome grandson Thomas W. Lamont II, died aboard the submarine *Snook* in the Pacific. Now in his seventies and nostalgic with age, Lamont composed a charming volume of memoirs about his boyhood in a country parsonage. His romantic nature never flagged. Throughout the war, he had sent food parcels to Nancy Astor, who even in her sixties was energetic enough to perform cartwheels in the air-raid shelters. In 1945, after she had retired from twenty-five years in Parliament, Lamont paid $3,000 in expenses for her to visit the United States. On the eve of her visit, he wrote her, "And meantime with your war cares largely removed I shall find you I know looking younger and lovelier than ever before." Then he added, forgetfully, "How proud you must be that it was Britain who in 1940 stood all alone against the entire world of barbarism and saved civilization."[22]

Unpleasant reminders of the past would intrude. In 1944, the Italian government dispatched a financial mission to Lamont. Some of the old gang wanted to crank up the Italy-America Society, but Lamont suggested that maybe they should wait awhile. When news came of Mussolini's death in 1945, Lamont said its "indecent" manner upset him but that otherwise nobody regretted it. With a new anti-Fascist mood in postwar Italy, Lamont took pains to rewrite history. In 1946, he told Count Giuseppe Volpi, the former finance minister, that the $100-million loan to Italy in 1926 was made under duress. He implied that he had frowned upon it: "I hardly have to say that the loan was not one that we were eager to arrange, nor was it sought by us. On the contrary, it was a part of the series of post-war reconstruction operations encouraged by our own Government."[23]

By war's end, Lamont came to the bank only for short periods each week. He continued to make the grandly liberal gestures that had marked his

extraordinary tenure at 23 Wall. For $2 million, he endowed an undergraduate library at Harvard—appropriately, it would be for government documents—and sent what Norman called a "whomping" check for restoring Canterbury Cathedral. He ended his banking career with a Pierpontian act of munificence: in the lean year of 1947, the firm had skipped bonus payments; Lamont decided to compensate by giving every staff member a Christmas gift equal to 5 percent of his or her salary.

Lamont had time to wonder about the hopefulness that had buoyed him between the wars, making him susceptible to the false allure of appeasement. He now saw Americans as too self-absorbed by materialism and too coddled by peace to brace for violence. In a 1945 essay, "Germany's Heartbreak House," he tried to figure out why the Allies were deaf to Churchill's pleas regarding Hitler. He wrote:

The truth is that the British and French, like us Americans, are so peace-loving that it has always been hard for them to realize that there are gangster peoples going about the world seeking whom they may devour. We have all refused to believe until the last moment that there were Dillinger nations prowling about with completely laid plans of evil portent. . . . For in the makeup of the Anglo-Saxon peoples there is . . . that extreme of humaneness that abhors cruelty and will have naught of it.[24]

The explanation omits the large measure of self-interest that had led Lamont to cling first to Japan, then to Italy.

On February 3, 1948, Tom Lamont died at his home in Boca Grande, Florida, at age seventy-seven, and Russell Leffingwell became chairman of the House of Morgan. So many friends flocked to Lamont's funeral at the Brick Presbyterian Church on Park Avenue that folding chairs were hastily arranged in the side aisles and balcony. Two veterans of Black Thursday—William Potter of Guaranty Trust and Albert Wiggin of Chase—were in evidence. Whereas at Jack's funeral the mourners sang "Onward Christian Soldiers," at Tom's passages from Milton's *Samson Agonistes* were read against a brilliant backdrop of white flowers.

Lamont's estate was so enormous that the charitable and educational bequests came to $9.5 million, including $5 million to Harvard and $2 million to Phillips Exeter Academy. Through a syndicate managed by Morgan Stanley, his estate sold off his twenty-five-thousand-share block of J. P. Morgan stock. It was the largest block in existence, with an estimated market value of nearly $6 million.

Lamont was a man of prodigious gifts, the real J. P. Morgan behind J. P. Morgan and Company. Had he lived in Pierpont's day, he might have

summoned steel mills or transcontinental railroads into being. Instead, as a man of the Diplomatic Age, he was the architect of huge state loans in the 1920s. As they defaulted in the 1930s, he had to devote his time to fruitless salvage operations, and his gifts were squandered in the general wreckage. For all his power, he seems in retrospect a tiny figure bobbing atop a gigantic tidal wave. His story is a sobering tale of human limitations.

In its front-page obituary, the *Times* said that the driving force of Lamont's life "was an unremitting search for the good, the full and the gracious life."[25] Indeed, one admires his ambition to lead a beautiful, rounded life and bring poetry into the straitlaced world of banking. He gave a literary gloss and an intellectual richness to the House of Morgan, stretching the sense of what it means to be a banker. He was a man who dealt with the large issues of the day, saw the strategic significance of his actions, and transcended a provincial concern with profit. His vision of banking was remarkably spacious.

Yet he resorted to moral shortcuts and political compromises. He was too quick to paper over conflicts with rhetoric and to settle arguments with smiles. The optimism that made him an inspiring leader also contained an element of pure opportunism. He refused to terminate business relationships until *force majeure* supervened, and his complicity with Japanese militarists and Mussolini are black marks on his record. By the end, he could no longer distinguish policy from public relations or separate means from ends. In trying to please too many people, he lost the habit of truth—a habit, once lost, that can never be regained. Perhaps the most extraordinary figure in Morgan history, Lamont was a dreamer whose reach exceeded his grasp. He fell short of the ideals that he himself articulated. After his death, Wall Street would seem grayer and more bureaucratic. As a confidant of presidents, prime ministers, and kings, he was the last great banker of the Diplomatic Age.

PART THREE
The Casino Age
1948–1989

CHAPTER TWENTY-FIVE
METHUSELAH

AFTER Tom Lamont's death, Russell Leffingwell served as chairman of J. P. Morgan from 1948 to 1950. Sucking on a long, straight pipe, he had an air of Methuselah-like wisdom, with his large pointed nose and white hair. As chairman of the Council on Foreign Relations from 1946 to 1953, he would stop by its offices on his way home to East Sixty-Ninth Street. Bookish and witty, a masterly rhetorician, he could write a trenchant essay or speak extemporaneously on any subject. His mind was promiscuously rich. Once, after delivering a fiery opinion at a board meeting, he asked, "Does anyone disagree?" Tom Lamont replied softly, "Would anyone dare, Russell?" He had a gift for comebacks. When his daughter went on her first cruise, she asked how many people she could tip. "Well," he said dryly, "if you have enough money, you can go right up to the captain."[1] The writer Edna Ferber left this impression of Leffingwell at a dinner party: "He seemed to me to be wise, tolerant, sound, liberal; and, combined with these qualities, he has, astoundingly enough, humor."[2] She couldn't imagine a Scrooge behind his "florid rather Puckish face."[3]

Leffingwell was the last of the handpicked thinkers that Morgans bred prolifically between the wars, when Wall Street still produced Renaissance men. As members of small partnerships, the elite financiers straddled all aspects of business. They had time to read, to ponder, to enter politics: the gray era of specialization hadn't dawned. Leffingwell thought that Glass-Steagall, by segmenting banking, had destroyed the most interesting jobs on the Street.

After World War II, the Morgan bank was upstaged by a new set of multilateral institutions. Between the wars, the mysterious *troika* of the Bank of England, the New York Fed, and Morgans had largely governed the international monetary order. At Bretton Woods, New Hampshire, in 1944, they were superseded by a proposed World Bank and International Monetary Fund. These twin bodies would try to lift currency stabilization and European reconstruction to a supranational plane. In the postwar era, there would also be greater collaboration among central banks and finance ministries of the major industrial countries. The upshot was that financial tasks entrusted to private bankers in the 1920s were placed irretrievably in public hands.

Bankers were distanced from politicians by a new sense of public propriety, with secret collaboration regarded as corrupting by government. The Diplomatic Age was dead.

In the new Casino Age, as we shall call it, banks would operate in a broader competitive sphere. The banker had grown powerful when capital markets were limited, with few financial intermediaries to tap them. In the post-World War II period, however, capital markets would burgeon and become globally integrated. At the same time, the financial field would grow crowded with commercial banks, investment banks, insurance companies, brokerage houses, foreign banks, government lending programs, multilateral organizations, and myriad other lenders. Gradually Wall Street bankers would lose their unique place in world finance. Never again would a private bank such as J. P. Morgan be the most powerful financial agency on earth. Far from standing guard over scarce resources, bankers would evolve into glad-handing salesmen, almost pushing the bountiful stuff on customers.

The new Bretton Woods bodies were shaped by the interwar lending disaster. The memories of the 1920s were fresh, with over a third of foreign government securities still in default. The World Bank's decision to finance only meticulously conceived projects was a reaction to this loose sovereign lending. Even so scrupulous a lender as Morgans smarted from a flood of outstanding defaulted bonds—$197 million in Japanese debt, $20 million from Austria, $151 million from Germany. No banker was foolish enough to assert that countries never went bust or that government loans were less risky than commerical loans. Since the World Bank had to tap U.S. capital markets—only the United States had spare cash—it needed to please Wall Street and erase the stigma of foreign lending.

The World Bank's second president, John J. McCloy, had to safeguard the new institution's credit and consulted Leffingwell about Morgan's interwar experience. With his usual style of passionate urgency, Leffingwell told McCloy about the bank's sense of betrayal over foreign loans that had enjoyed phantom government guarantees—most notably the German loans. McCloy concurred in Leffingwell's critique of 1920s lending—that politics had gotten confused with finance, encouraging debtors to regard loans as disguised foreign aid. This destroyed discipline and invited excessive borrowing, followed by default.

Considering the defaults on Latin American loans, McCloy asked whether the bank should lend to the region. Leffingwell shot back, "Except for the Argentine, I do not think of any Central or South American country that hasn't got a contemptible, discreditable record of default to American investors."[4] (Argentina was always a special case: when Juan Perón came to power in 1946, the country boasted a large supply of gold amassed from food exports to wartime Europe; Peron even favored paying off foreign debt to

avert bondage to foreign bankers.) If the World Bank made Latin American loans, Leffingwell warned McCloy, it might tarnish the World Bank's own bonds with American investors. McCloy had greater sympathy for the Latin Americans than Leffingwell did, arguing that bankers had tempted the region into over-borrowing. "The competition that went on in Europe and in Latin America for loans was something to see," he told Leffingwell. "I know because I was a part of it."[5] Although the World Bank made Latin American loans, it insisted that Peru and other nations first settle outstanding debt with private bondholders. This shored up creditors and prevented Latin American debt from contaminating the bank's own credit.

Leffingwell thought private lending to Europe couldn't resume until political turmoil in the area ended. In 1946, Churchill sounded the alarm with his "Iron Curtain" speech in Fulton, Missouri. His fears of European disintegration were spookily analogous to those following World War I, especially with food shortages and poor crops in early 1947. As Under Secretary of State Robert Lovett had warned Lamont, "At no time in my recollection have I seen a world situation which was so rapidly moving toward real trouble."[6] Leffingwell feared a stingy, punitive approach to rebuilding Europe, reminiscent of Versailles. He, in turn, warned Lovett, his friend and Locust Valley neighbor: "Western Europe is drifting toward catastrophe. Penny-wise and pound-foolish, we dribble out little loans and grants, too little and too late, meeting a crisis here or there . . . while we neglect to deal constructively on a great scale with the problem of the reconstruction of western Europe"[7] He stressed aid to Britain and France, without strings: "The British and French are not infants nor aborigines to be dictated to by the nouveaux riches Americans."[8]

With U.S. investors still skittish about foreign bonds, the World Bank couldn't cope with the Western European crisis. In December 1947, Truman presented Congress with plans for the multibillion-dollar Marshall Plan to raise Europe from wartime rubble behind a NATO defense shield. "What took place after World War I was the forerunner of the Marshall Plan," noted McCloy, who had worked on the Dawes loan in the 1920s. "But back then the rehabilitation of Europe was done in a private capacity."[9] The scope of the Marshall Plan—$5 billion for the first year alone—far exceeded Wall Street's meager resources, still depleted by the Depression, war, and Glass-Steagall.

The internationalism that had always ostracized the House of Morgan in the hinterlands was now irrevocably established in Washington. The war, television, and foreign travel all acted to reduce American parochialism. As the Republicans shed their traditional isolationism, the bank had a party in which it could place implicit faith. No longer would Morgans rise as an alien institution, conspiratorially aligned with foreign powers. If this increased the

bank's political comfort, it also reduced its influence. Foreign governments with better entree in Washington had less need of a Wall Street agent to conduct their diplomacy.

During the early summer of 1947, the Truman administration was in a quandary over whether to include the Soviets in the Marshall Plan. George F. Kennan wanted to invite the Soviets to participate because he assumed they would spurn the offer and get blamed for partitioning Europe. Lovett wasn't convinced and received permission from Truman to sound out Leffingwell at 23 Wall. According to his son-in-law, after pondering whether to invite the Soviets, Leffingwell told Lovett, "Bob, the answer is very simple. If you don't ask Soviet Russia, there will be hell to pay. If you do ask them, they'll tell *you* to go to hell."[10] Leffingwell managed to convince Lovett where Kennan had failed. As Kennan and Leffingwell predicted, the Soviets later rebuffed the overture.

In the late 1940s, it looked as if Morgan political influence would be limited to such sophisticated advisory roles. As an investment bank before Glass-Steagall, it had floated many government bond issues. As a commercial bank lending its own money, it strained just to eke out postwar loans to England and France. When J. P. Morgan and Company and Chase co-managed two French loans totalling $225 million in 1950, they nearly exhausted Morgan resources. Leffingwell wanted to aid France despite his rather harsh view of de Gaulle: "There is no place in modern France for the general on horseback. De Gaulle can be and is I think a disturbing influence. . . . He has never shown statesmanship, judgment or common sense. In a way it was the very lack of these qualities which made him a great war leader of the resistance."[11]

The capital-short House of Morgan had to neglect many former foreign clients and was powerless to help devastated Japan. Clinging to a dated view of England and America as coequal partners, Leffingwell couldn't fathom Britain's demotion to a second-class power. In 1947, he wrote his friend T. J. Carlyle Gifford of the British Treasury, "However bungling we may think the governments of the West, it is plain that there can be no hope for democracy and a world of free men except that England be restored and aided to take her place again in the world."[12] To his friend Lady Layton he said, "Nothing matters as much as the British empire and the United States of America and their collaboration."[13] Britain's diminished place in world affairs would lessen the value of Morgan ties to the British Treasury and the Bank of England. Unlike the 1920s, after World War II the United States no longer deferred to Britain's financial leadership. When John Maynard Keynes proposed that the World Bank and the International Monetary Fund be based in London or New York, the United States, in a symbolic act, placed its

Bretton Woods wards a short walk from the White House.

For Leffingwell, the touchstone of any policy was how it would affect both America and Britain. Like others at Morgans, he was violently anti-Zionist, imagining that agitation for a Jewish homeland would stir up the Moslem world against the British Empire. J. P. Morgan and Company was still a Wasp, homogeneous bank, drawing a large fraction of its people from Ivy League schools and prominent families. Leffingwell championed minority rights but was impatient with minorities who asserted those rights too aggressively. In 1946, his close friend Morris Ernst, a Jewish lawyer active in civil liberties causes, chided Morgans for having no Jewish directors. Leffingwell fairly breathed fire in defense: "Why not be just citizens and Americans and drop all this talk about the rights of Jews. . . . So long as some Jews regard themselves as a racial and religious minority in other people's countries, and agitate for their rights, I fear they will be disliked."[14] After delivering this churlish judgment, Leffingwell ended with a tribute to Ernst's own brilliance. Ernst, in turn, urged Truman to consult Leffingwell as an adviser, assuring the president he wasn't a publicity monger like Tom Lamont.[15]

If there was a bilious quality to Leffingwell's thoughts in later years, it probably came from too many political disappointments. Known around Wall Street as the resident Morgan liberal, he was less of a dreamer than a hard, practical man. And he loved the cut and thrust of debate. He thought the League of Nations was a sad mistake, a cover for taking territory from Germany and Austria. He once told Lamont, "The truth of the matter is that this is a predatory world in which some if not all nations go out to take what they want sooner or later by force."[16] In the early 1950s, he believed the Soviets were hellbent on world domination and cited Berlin, the Balkans, Iran, Yugoslavia, and Korea as examples.[17] He had little use for disarmament and talked unapologetically about the United States serving as the world's policeman. He had seen too many dictators.

While deploring McCarthyism, Leffingwell wanted to root out subversives and argued that schools and governments should have a free hand to fire such persons. Later appointed by Truman to an internal security commission headed by Admiral Chester W. Nimitz, he thought civil liberties should yield priority to national security: "I think employee tenure and civil rights generally have to be subordinated to the rights of the nation to defend itself against Russia, which is the enemy of all civil rights and all the freedoms."[18]

At the start of the Korean War, during the summer of 1950, George Whitney wrote to Truman pledging the bank's support. While the two had had a testy exchange during the Wheeler railroad hearings years before, Truman now recognized the need for national harmony. The president told Whitney rather shamelessly that his letter had "brought back pleasant memories of our

meeting so many years ago."[19]

Despite their support for the Korean War, the Morgan officials grew alarmed in the fall of 1950 when South Korean troops reached the Chinese border and General Douglas MacArthur seemed to yearn for a showdown with the Chinese Communists. This brought out an old Morgan bias against China as well as a fear that the United States would save Asia at the expense of Western Europe. Leffingwell warned Truman that the country shouldn't go to war "with those miserable 400 million Chinamen. They have been the victims of their own war lords, and of their own misgovernment, and of their Japanese conquerors, and now of their Communist conquerors. We have no mission to kill Chinamen; and to get involved with them will leave us defenseless at home and in Europe."[20] Truman agreed. In April 1951, he relieved MacArthur of his duties after the latter urged the United States to emphasize Asia instead of Europe and take the war to the Chinese mainland.

The House of Morgan shared Truman's cold war liberalism yet differed with him on economics, where the president reverted to his earlier cynicism about Wall Street. This became clear when Leffingwell met with Truman at the White House in early 1951 to make a plea for market-based interest rates. Since early in the Second World War, the Federal Reserve had pegged long-term rates at 2.5 percent, a policy prolonged after the war with Truman's blessing. In the early 1920s, Truman had been dumbfounded when his government bond dropped in price after Ben Strong raised interest rates. He didn't see this as bad luck but as a sinister betrayal of the bondholder, and it made him disposed to fix interest rates. The Fed was now spending billions of dollars to keep prices high and yields low on Treasury bonds. Along with Allen Sproul of the New York Fed, Leffingwell thought this a waste of money and wanted to return to free market interest rates.

Treasury Secretary John Snyder spied in Sproul and Wall Street a cabal intent on returning to the good old days, when the New York Fed and Morgans dictated monetary policy. Truman was eager to stifle inflation jitters during the Korean War and was irritated by what he saw as the bankers' patent selfishness. He gave Leffingwell a tongue-lashing reminiscent of the earlier New Deal diatribes:

I appreciate your interest in this matter but it seems to me that an emergency is a very poor time for bankers to try to upset the financial apple cart of the nation. The stability and confidence of the nation are entirely wrapped up in the two hundred and fifty-seven billion dollar debt that is now outstanding. . . . For my part I can't understand why the bankers would want to upset the credit of the nation in the midst of a terrible emergency. It seems to be what they want to do and if I can prevent it they are not going to do it.[21]

There was something strained in Truman's cordiality toward the House of Morgan, and at moments his real but usually carefully guarded feelings would flare up again.

WHEN George Whitney became Morgan chairman in 1950—leaving Russell Leffingwell to hover as a wise man during the decade, firing off position papers—J. P. Morgan and Company was a hothouse bank surpassed in size by ten other New York banks alone. It was compactly squeezed into 23 Wall, with Whitney seated at a rolltop desk at the end of the glass-enclosed room along Broad Street, his white hair well-brushed, his elegance unbending, and his tailoring faultless. As publicity man fames Brugger recalled, he was "patrician, reserved, terse in speech and blunt in comment, [his] countenance cool but capable of crinkling with a mischievous grin."[22] The elegance was sometimes belied by a booming voice and a gruff manner.

Whitney was always haunted by his brother's embezzlement scandal and vowed to pay back every penny, even though doing so markedly thinned his own fortune and that of his heirs. "It was emotionally debilitating to him," said his grandson George Whitney Rowe. "The reputational disaster was even harder than the money. It cost him a tremendous amount of money near the end of his earning power, but he made every penny good."[23] He was forced to sign away easy, pretax money of the 1920s. Worried about his grandchildren, he asked John M. Meyer, Jr., a later chairman, to watch out for their interests. In the Morgan tradition of nepotism, several Whitney heirs ended up working at the bank. The Whitneys tried not to treat Richard like a pariah, but the subject was so touchy and explosive that family members came to blows over it. Barred from finance, Richard performed odd jobs—he imported Florida oranges at one point—but was mostly supported by his heiress wife, Gertrude.

Perhaps as a result of his brother's crimes, George Whitney made a fetish of honesty. In 1955, J. P. Morgan and Company and Morgan Stanley teamed up on a General Motors "rights issue"—new shares offered at a discount to existing shareholders. The company wanted to raise $325 million for retooling in order to produce cars with power steering, power brakes, and V-8 engines. Morgan Stanley handled the financial end and J. P. Morgan the clerical end—the typical arrangement of the day. In a massive team effort, Whitney pitched in to deal with crowds. A *New Yorker* reporter recorded a telling vignette of J. P. Morgan's Boston Brahmin as recounted by a broker:

While [Whitney] was on duty, a lady stockholder came in to exercise her rights for two shares and handed him a stack of bills that supposedly totalled a hundred and fifty dollars. Whitney, it seems, was too polite to count them in her presence, so he just took them, smiled, shook her hand, and gave her a

receipt. Well, after she had left, he counted the money and was flabbergasted to find that it came to a hundred and *seventy* dollars. Everybody was in a terrible tizzy until it was discovered that the papers hadn't yet disappeared into the files, so they knew who the stockholder was and could send the overpayment back to her, along with her stock.[24]

The 1950s would expose the extreme damage done to the House of Morgan by Glass-Steagall in a way not clear during the Depression, when nobody needed loans anyway. As an investment bank, J. P. Morgan and Company had towered over its rivals, while as a commercial bank it couldn't match the more plebeian banks that courted retail deposits. Nationally it fluctuated in size somewhere between twentieth and thirtieth. It was hard to believe that this small, genteel, somewhat stuffy bank had been the glowering red-eyed dragon of American finance.

Even in its reduced state, the House of Morgan still fancied itself Wall Street nobility. Employing seven hundred people, it retained the gentlemanly mood of an old Wall Street partnership. It was so tiny that to celebrate staff members who were returning from the service in 1947, the entire staff was able to fit into a dinner dance at the Waldorf-Astoria. George Whitney did the hiring himself, mostly bringing in men with prep-school and Ivy League backgrounds; everybody started in the mail room and rotated upward. Once a year, Whitney would stroll over to Davis, Polk, ask for the year's legal bill, go back to his desk, and write out a check. Morgan style was simple, British and informal. The bank of the fifties would have still been recognizable to partners of the twenties. At 10:30 A.M., the top twenty officers met around a large table to comment on world affairs and swap news, an exchange that continued over free lunches.

The paternalistic Morgans pampered its people. Employees lived in a warm cocoon and received better pay and longer vacations than anyone else on Wall Street. The bank had a plantation atmosphere. Its dining room was staffed by white-gloved black waiters who ladled out soup from beautiful metal tureens. One newcomer nearly protested when a waiter seemed to drop dirty ice cubes into his iced tea. Then he realized that the cubes were *made* from tea, so that they wouldn't dilute the drink. It was that kind of place.

The bank lovingly tended its image, the glamorous *23* on its door. Its phone number was Hanover 5-2323, the license plate on its black company Cadillac G-2323. As banker to old money and high society, it obeyed strict etiquette. When calling, young bankers wore hats, and in the office risked irreparable career damage if they removed their jackets *en route* to the men's room. In this prudish place, the ladies' room of the Trust Department was left unmarked because red-faced bankers couldn't agree on the sign's proper wording. The preferred style was low profile. Clients were never mentioned to outsiders, annual reports contained no pictures, and advertising was strictly

forbidden. When one new arrival asked the publicist his job, he was told, “I’m the guy paid to keep the bank out of the press.”[25] With client relations still close and raiding the business of competitors taboo, there was no particular need for self-promotion.

Even as the Morgan bank exploited its mystique, a lot of bluffing was going on. “The reputation of doing business only with the biggest of the big, the image of aloofness, could be off-putting to a new generation of entrepreneurs and corporate executives,” remarked Jim Brugger, the bank’s publicist. “Without enunciating it in so many words, the bank in this period worked to shed some elements of the mythology that clung to it.”[26] The Gentleman Banker’s Code dictated that clients come to bankers. Yet Morgans could no longer afford such imperial passivity, and Whitney dispatched young “bird dogs” across the country to scout up business. He wanted greater geographic breadth in the client base. Without putting too fine a point on it, the mighty Morgans was begging for new clients, which offended some old-timers. As Longstreet Hinton of the Trust Department later wrote, “A few people within the organization believed that potential customers should take the initiative to do business with the bank and some even had the strange notion that no existing clients would ever even dream of taking their business elsewhere.”[27]

An enduring Morgan myth was that the bank required a $1-million balance for personal checking accounts. These rare Morgan checks were cashed on sight anywhere in the world and were good for cultivating executives. At a Bond Club spoof in the 1950s, a vaudeville team satirized the Morgan approach, singing “Our tellers have a million-dollar smile. They only smile at people with a million dollars.”[28] This exclusivity could be self-defeating. At one annual meeting, George Whitney created a sensation by denying the $l-million minimum. “WHITNEY EXPLODES ‘MORGAN MYTH’” ran the the incredulous *New York Times* headline; “LESS THAN MILLION DEPOSIT TAKEN.”[29] But further down in the article, Whitney seemed to waver, saying the bank wasn’t “geared physically” to small accounts. He finally left the impression that perhaps there was a $l-million minimum for personal deposits after all.

THIS posturing hid problems at the House of Morgan that would intensify through the decade. They stemmed from the way Wall Street banks financed their operations—especially a practice called compensating balances. In exchange for a loan, companies would leave up to 20 percent of the money behind in interest-free deposits. By paying such tribute, the borrowers preserved the banking relationship and received free services, such as the

right to consult the bank economist or have a merger arranged. Compensating balances also guaranteed credit during times of scarcity, an assurance that reflected historic corporate anxiety about maintaining a constant flow of capital. This setup bound Wall Street banks to their customers in an intimate relationship and gave banks free cash to lend at high spreads. It was a wonderful racket. In these fading days of relationship banking, profits seemed almost guaranteed, producing a pleasant but stolid generation of bankers.

In retrospect, it may seem peculiar that companies should have left so much idle money with their banks. But while inflation and interest rates were low, they really sacrificed little. Leffingwell was in the forefront of those arguing for free-market interest rates. The bank knew that the easy days of compensating balances were numbered. Nevertheless, it got a jolt in September 1949, when it found itself the unexpected victim of a sensational crime—a tabloid story that didn't make the financial pages but had a profound impact at the bank.

A French-Canadian jeweler known as J. Albert Guay had an illicit passion for a nineteen-year-old waitress named Marie-Ange. Determined to get rid of his interfering wife, Guay tucked a bomb into her suitcase just before she boarded a Quebec Airways flight. He wanted not only to indulge his illicit ardor but to collect his wife's $10,000 in life insurance as well. Fifty miles northeast of Quebec, the plane exploded, incinerating Quay's wife and twenty-two other passengers. The scheming jeweler collected neither cash nor mistress, but ended up condemned to death by hanging.

Such melodrama seemed worlds away from the sedate J. P. Morgan and Company. Yet the plane victims included E. Tappan Stannard, head of Kennecott Copper. Stannard belonged to Kennecott back when Dwight Morrow helped the Guggenheims to organize it during World War I. In 1942, soon after Morgan's incorporation, he became the first "outside" director on the bank's board. Now Stannard's mystified successor asked his chief financial officer about a $60-million deposit the copper company kept at Morgans. The flustered CFO said the company always kept big balances there. Not schooled in such absurdities, the new president asked, why not leave $10 million and invest the other $50 million? This bright idea shocked 23 Wall: Kennecott was withdrawing 10 percent of the bank, despite the fact that George Whitney was a Kennecott director. (According to other versions of the story, Morgans actually encouraged Kennecott to spread its deposits among several banks for reasons of safety.) The move foreshadowed a central feature of the Casino Age—the death of relationship banking, which had been characterized by exclusive ties that bound major companies to the House of Morgan and other Wall Street banks.

Morgans needed these big cash balances to survive. Under legal lending limits, it couldn't commit more than 10 percent of its working capital to a

single customer. (Bank capital was actually smaller than deposits—essentially, what would remain after the bank had paid off all its debts.) This meant it could provide only a piddling $5 million or $6 million to a General Motors, a U.S. Steel, or a General Electric. With directors on these companies' boards, Morgan still had an inside edge, but its shortage of capital threatened to rob it of major business. As Leonard McCollom of Continental Oil (afterward Conoco) told George S. Moore of National City, "J.P. Morgan's not big enough to be an oil bank, but you are, and you should gear up for it."[30] Continental, it may be noted, was formed by a Morgan-arranged merger back in the 1920s, and McCollom was even a J. P. Morgan director. If they had to, companies would bolt traditional bankers and no longer feared antagonizing Wall Street. Their options in the Casino Age were far more diversified than they had been in the old days of captivity.

The House of Morgan wrestled with the unpleasant fact that it was too small to survive as a major financial institution and that only a merger could restore its former power. In 1953, John J. McCloy, the former World Bank president who was now chairman of the Chase Bank, made a merger overture to Whitney. Chase was now a colossus beside Morgans; its vast assets put it third in size nationwide. Yet the House of Morgan believed unquestioningly in its special destiny. When Whitney explored the possible merger with McCloy, he bargained as if J. P. Morgan were the bigger bank. Whitney inquired who would control the merged bank and extracted a surprise concession from McCloy: "I am quite prepared to step aside if, as a result of. . . analysis, it would seem that others should conduct the affairs of this bank."[31] When Whitney pursued this extraordinarily generous offer with his colleagues, he found no jubilation. Rather, he faced intransigent opposition from two sons of famous partners—Henry P. Davison and Tommy S. Lamont—who refused to merge with anyone, let alone Chase. They didn't want to adulterate the purebred Morgan culture. By decade's end, this clan-nishness would belatedly force the Morgan bank into a lifesaving merger. McCloy, meanwhile, resumed talks with the Bank of the Manhattan and consummated a merger that turned Chase from a wholesale bank into the leading retail bank, Chase Manhattan.

DURING the Truman years, the Morgan bank was still subject to political attacks that echoed the New Deal. It was now accused of the old political crimes without having actually enjoyed committing them. Yet reformers couldn't believe the House of Morgan had been emasculated. In 1950, Representative Emmanuel Celler of New York showed that J. P. Morgan directors sat on the boards of companies whose assets totaled over $25 billion, which he called a "breath-taking figure." Similarly, during a brief brouhaha

about Morgan power, U.S. Steel chairman Irving S. Olds reassured an annual meeting with these words: "It happens that a member of J.P. Morgan &. Co. is on this board. I say that J. P. Morgan & Co. or no other financial interest or group controls U.S. Steel."[32] The imagery suggested here, borrowed from Money Trust days, now seemed anachronistic. The giant American corporations, multinational in scope, were no longer beholden to a single Wall Street bank.

By the early 1950s, the anti-Wall Street vendetta that had raged for twenty years was petering out, and Morgan executives could again function as political allies. Yet the political involvement was of a different nature. George Whitney and others felt the bank had gotten burned by fooling around in politics. Gun-shy, they shrank from the power-broker role that Tom Lamont had played in the Republican party. Although a lifelong Republican, Whitney had no stomach for public fights and associated politics with public exposure, scandal, and demeaning interrogation. His influence would be more personal than institutional in nature and so discreet as to be invisible to the general public.

Whitney had a close relationship with Dwight D. Eisenhower, which came about almost by chance. Whitney's son Robert had served on Eisenhower's staff during the war and worked in his presidential campaign; he introduced his father to Ike, who lunched with the Whitneys in Old Westbury when he was president of Columbia. In 1951, George Whitney helped bankroll the volunteer group Citizens for Eisenhower, which encouraged Ike Clubs to sprout across America.

When Eisenhower went to Paris in 1951 as the military commander of SHAPE (Supreme Headquarters Allied Powers Europe), he invited Whitney to draft weekly or monthly letters outlining his views on topical issues at home. Whitney obliged with long, opinionated letters that were acerbic in their judgments of most politicians, labor leaders, and businessmen but deferential and affectionate toward Eisenhower. Ike felt at sea on economic and financial issues and welcomed these lectures. "Your letters are one of the brightest things in my office life," he told Whitney.[33]

Whitney's letters reflect a frustration with the contemporary economy that says much about the fallen state of bankers in the new age. By his own admission, his favorite bugbear was organized labor, yet he was no less reluctant to chastise management for caving in to labor's demands. Although he had sat on the General Motors board for twenty-seven years, he took more pot shots at GM president Charles E. Wilson than anybody else. He was especially irate that Wilson had negotiated a cost-of-living allowance with the United Auto Workers, which he thought would foster inflation, even if it might benefit the company. At one point, Whitney mockingly sent Ike a

Wilson speech about stopping inflation, pointing out the incongruity between author and subject. The days when the House of Morgan dictated to its industrial clients were over.

Whitney loathed the Truman administration, which he saw as perpetuating the worst New Deal tendencies—a welfare-state mentality that encouraged people to expect support from government, imposition of federal controls over business, and a bias toward fighting unemployment rather than inflation. He thought Truman scapegoated the rich and exploited class divisions. Yet he was no less fearful of the Republican candidacy of Senator Robert Taft of Ohio, whom Lamont had rejected in favor of Wendell Willkie a decade earlier. In late 1951, Ike was still evading any commitment to run for president, citing the nonpartisan requirements of his position at SHAPE. But when Whitney heard that Taft had announced his candidacy in October 1951, he went beyond gentle prodding and made a strong plea for Eisenhower to get into the race: "It is quite clear that the work you are now carrying on would be put in jeopardy if Taft's candidacy succeeded because his strongest backers represent the strongest isolationist movement in this country. . . . I see little comfort in a Republican Administration headed by Taft."[34] Ike's election confirmed the ascendancy of the internationalists in the postwar Republican party.

Only a month after Eisenhower's election, Whitney's pleasure in the victory was cut short. His thirty-six-year-old son, Robert, an assistant VP at the bank in charge of Southwest business and a ruggedly handsome, athletic man, was hit by a car one evening in late December 1952 and was killed instantly. Robert Whitney left behind a wife and four children.

For a man whose early life had suggested easy prosperity, George had led a life full of trouble. Dwight and Mamie Eisenhower sent a handwritten note of condolence: "We can find no words to express the shock and grief we suffer from the news we have just received of Bobby's tragic accident."[35]

In Eisenhower, the Morgan bank had a nearly perfect ally—conservative on economic issues yet opposed to economic nationalism and political isolationism. Not since Hoover had the bank enjoyed such a neat fit. Calling Whitney his Wall Street "listening post," Eisenhower invited him to his White House "stag dinners" for business friends—occasions that produced charges of Ike's being corrupted by rich friends. The president clearly heeded Whitney's advice. In the early 1950s, there was a movement to unfix the price of gold. Some wanted higher, other lower, gold prices. Whitney and Leffingwell convinced Eisenhower to keep the gold price at $35 an ounce, where it had stood since 1934. Ike thought Leffingwell's memo on the gold question the best he had read.

The early Eisenhower years certified that the long-standing Morgan

preference for international economic cooperation was firmly entrenched in Washington. The historic split that had so bedeviled Morgans—between rural isolationists, who favored inflation, and eastern-seaboard bankers, who favored hard money and had financial ties to Europe—had become a thing of the past, a topic for history students. American companies were going abroad, farmers were cultivating export markets, and Washington was operating military bases around the world. America no longer seemed so distant from the rest of the world and was explicitly tied to Europe through the Atlantic alliance. The House of Morgan had ceased to be an alien presence in America's political culture.

CHAPTER TWENTY-SIX
MAVERICKS

IF the Wall Street of the 1950s was a closed, privileged club, the trend-setting firm and social arbiter was Morgan Stanley. It was a remarkably small place, with fewer than twenty partners, a hundred staffers, and a paltry $3 million in capital. Nonetheless, it was the paragon of investment banking and exerted enormous influence. Its one office at 2 Wall Street, with green carpets and white walls, overlooked Trinity Church. In an elevated area called the platform—analogous to the partners' room at Morgan Grenfell—stood a double row of mahogany rolltop desks, exact replicas of those at 23 Wall. Like a twin separated at birth, it showed common ancestry with J. P. Morgan and Company down the block.

Morgan Stanley boasted a matchless list of Fortune 500 clients and had tight handcuffs on many old House of Morgan stalwarts, including General Motors, U.S. Steel, Du Pont, General Electric, and Standard Oil of New Jersey. In the late 1940s, it added Mobil, Shell Oil, Standard Oil of Indiana, Bendix, H. J. Heinz, and numerous others. It represented six of the seven-sister oil companies and pumped out more bonds than any other firm. As confidants of the mighty, Morgan Stanley partners dealt mostly with chief executives and were privy to their secret long-range plans. They monopolized the stock and bond issues of client companies. Nobody tried to steal Morgan Stanley clients, which was considered bad form and fruitless to boot.

A palpable warmth still existed among the Morgan firms, many senior people having worked together at J. P. Morgan and Company or Guaranty Trust in the 1920s and 1930s. They might be divided by the Glass-Steagall wall, but they sent a thick trail of vines snaking over the top. J. P. Morgan and Morgan Stanley encouraged their employees to fraternize and referred business to each other. Each year, they hosted an honorary dinner, assigning ten promising young people in each firm to attend; like doting parents, they pushed the children together. Morgan Stanley shared a cafeteria with J. P. Morgan and Company at 120 Wall Street. Morgan Stanley partners had personal accounts at 23 Wall and were among the few mortals to possess J. P. Morgan home mortgages.

Wherever possible, the two Morgan firms cooperated on business. J. P. Morgan managed Morgan Stanley's pension fund and profit-sharing plan, while Morgan Stanley sponsored J. P. Morgan securities issues. If Morgan

Stanley floated a bond, J.P. Morgan paid out the dividends. They were wedded by a special bookkeeping arrangement that dated from the Depression, when Morgan Stanley feared cyclical fluctuations in securities work and wanted to keep overhead low. Morgan Stanley had no clerical or back-office staff, and the "closing" on bond issues—the physical exchange of checks and securities—still took place at 23 Wall. At this point, however, the fraternal Morgan relationship was highly unequal. Morgan Stanley was now the uncontested leader in investment banking, while J. P. Morgan was a shabby genteel aristocrat in commercial banking, backed by a great deal of tradition, but without comparable contemporary power. As partners in their firm, Morgan Stanley people made far more money than their 23 Wall counterparts. During these community-of-interest days, Morgan Grenfell people also apprenticed at both J. P. Morgan and Morgan Stanley. Despite Glass-Steagall, it was still a happy Morgan family.

Far more than J. P. Morgan and Company, Morgan Stanley shrank from political involvement and never displayed an equivalent sense of either public service or *noblesse oblige*. Harold Stanley was all business, and Harry Morgan shared his father's distaste for politicians. As mostly an issuer of blue-chip bonds, Morgan Stanley seldom dealt with the SEC and had little need to lobby Washington on industry issues. At one point in the 1950s, Eugene Rotberg (later World Bank treasurer) and Fred Moss of the SEC visited Morgan Stanley to study "hot issues"—new stock offerings that soared and gyrated wildly after issue. The SEC visit was unprecedented, even an occasion for mirth at 2 Wall Street. The two SEC men were greeted by a man in livery—a red jacket with white bands across the chest—who escorted them to the platform. At a desk in the middle stood Perry Hall, the funny, fiery managing partner, who introduced himself by saying "My name is Perry Hall—partner, Morgan Stanley, Princeton." Fred Moss retorted, "My name is Fred Moss—SEC, Brooklyn College. Before my name was Moss it was Moscowitz. And before that it was Morgan, but I changed it in 1933."[1] Following an old House of Morgan custom, Morgan Stanley didn't sell, trade, or distribute securities but allocated them to other firms, its partners worked far from the vulgar din of the Stock Exchange and wouldn't stoop to sponsor new companies. It turned out that Morgan Stanley partners didn't know what "hot issues" were.

In the Truman years, there was still a lingering New Deal suspicion of Wall Street which culminated in one last cannonade against the Morgan interests. In October 1947, the Justice Department filed suit against seventeen investment banks and their trade group, the Investment Bankers Association, charging them with conspiracy to monopolize underwriting in violation of antitrust laws. The suit, *U.S. v. Henry S. Morgan et ah*, designated Morgan Stanley the leader of the plot and Harold Stanley its devious mastermind.

Now in his sixties, the very proper Stanley—nobody's idea of a conspirator—gruffly dismissed the case as "utter nonsense." He thought the instigator of the suit was Cleveland financier Cyrus Eaton, the head of Otis and Company, who had tried to make a financial comeback after the collapse of his investment trust in the 1929 crash. In a thinly veiled reference to Eaton, Stanley said that "someone, for whatever reasons, has misled the Department of Justice."[2]

Dubbed the Club of Seventeen, these swank gangsters handled 70 percent of Wall Street underwritings. The rich procession of suspects included Kuhn, Loeb; Goldman, Sachs; Lehman Brothers; First Boston; Smith, Barney; Kidder Peabody; Dillon, Read; and Drexel and Company. Such firms as Lazard Frères, Merrill Lynch, and Salomon Brothers (which sympathized with the government's case), weren't yet influential enough to be suspected of gross criminality. Some, however, were secretly heartsick at being excluded from this band of class martyrs. As defense lawyer Arthur Dean of Sullivan and Cromwell said of those snubbed by the government, "It made them feel like second-class citizens."[3]

The suit extended charges raised in the late 1930s by the Temporary National Economic Committee. The chief instigators were vocal Morgan critics who had then advocated competitive bidding for railroads and public utility issues—Cyrus Eaton; maverick railroad man Robert Young, chairman of the Alleghany and C&O railroads, who had ambushed Harold Stanley by demanding competitive bids at a C&O board meeting in 1938; and Harold Stuart of Halsey, Stuart and Company, formerly banker to utility mogul Samuel Insull. Although larger than some Club of Seventeen firms, Halsey, Stuart and Eaton's Otis and Company were excluded from the suit, confirming suspicions that those firms had provoked it. Toward the end of World War II, Stuart and Eaton held dozens of briefings with the Justice Department. Their efforts got a fillip when Truman became president: Truman, a disciple of Brandeis, favored compulsory bidding for securities to drive a wedge between companies and their customary bankers.

When the Justice Department first lodged its suit, in 1947, some pundits saw an attempt by Truman to resurrect FDR's crusade against the "money changers." If so, Truman quickly lost interest, for there was no longer a public clamor to slay the bankers, who now looked more like dwarfs in giants' robes. The suit came at a time of meager earnings, and the Money Trust had never looked less forbidding. The New Deal had chased the real financial giants—the old House of Morgan, National City, and Chase—out of the securities business. Ten members of the Club of Seventeen couldn't even muster $5 million in capital. If one added up the combined capital of Morgan Stanley and the next seven investment banks, together they were only a third the size

of the Chase and National City securities affiliates of 1929. Investment banks were populated by genteel, graying men in their fifties and sixties; younger men still shied away from a stodgy Wall Street that had never fully recuperated from the damage of 1929.

The case was assigned to Judge Harold Medina, who would monopolize it like a stand-up comic working a nightclub audience. With clipped mustache and glasses, bow tie and furrowed brow, the cigar-smoking Medina sat through the interminable trial like a frazzled Groucho Marx, murdering the self-confidence of the prosecution. Appointed to the bench by Truman in 1947, Medina had sacrificed a lucrative law practice. He specialized in real "stinkers," as he called them—long, tough, complex cases. After presiding over a stormy trial of eleven Communist party officials charged with conspiracy to overthrow the government, he won the nickname of the Patient Judge. But his patience flagged during the juryless trial against the Club of Seventeen. As the case dragged on for more than six years, producing a thirty-two-thousand-page transcript, Medina turned it into a comic purgatory, from which he delivered occasional howls of pain.

The trial itself began on November 28, 1950. The government's case was fine sociology but inept prosecution. It mistook a club for a conspiracy and a highly ritualized form of competition for oligopoly. Prosecutors got the externals of investment banking right, showing a white-glove world governed by gentleman's agreements, back scratching, and tacit understandings—the Gentleman Banker's Code. These practices were unquestionably clubby and unfair and worked to exclude outsiders. They just weren't illegal.

The case hinged on something called the triple concept. This said that blue-chip companies possessed "traditional bankers," who retained exclusive rights to manage their issues. When these bankers formed syndicates to float a company's securities, the rules of the game required that they assign the same "historical position" to participating firms—that is, the same allotment as on previous issues. Finally, by the rule of "reciprocity," investment banks would swap places in each other's syndicates. The triple concept captured the collusive form but missed the cutthroat spirit of Wall Street. The rules didn't civilize the sharks but kept them from devouring each other in vicious feeding frenzies. Any firm would happily steal away another's client—*if they could*—but most of the territory was pretty well carved up. Even Morgan Stanley never chased department-store business, which was locked up by Jewish houses.

At first, the government traced the conspiracy to Morgan's $500-million Anglo-French loan of 1915. While this added a little wartime drama, it also introduced a problem: how did the conspiracy survive Glass-Steagall and the breakup of so many banks? To solve this, the government devised the notion of "successor" firms—that is, J. P. Morgan had metamorphosed into Morgan

Stanley, Guaranty Trust into Smith, Barney, and so on. Although Harold Stanley dismissed this as “farfetched” and “silly,” it had a rough plausibility. Old-timers still called First Boston “First of Boston,” which was an echo of its derivation from the First National Bank of Boston. To keep the trial’s length manageable, Medina cut off the successor issue. So the government revised the conspiracy to date from Jack Morgan’s 1933 statement before Ferdinand Pecora. Why Jack would have broadcast the new conspiracy to a nationwide audience before a hostile investigating committee wasn’t clear.

Swamped with thousands of documents, Medina ordered an intricate, custom-made cabinet to manage the flow of paper. To learn more about underwriting, he followed a syndicate put together for a Con Edison issue at Halsey, Stuart’s Wall Street office. Yet the trial nearly brought him to a nervous collapse, a strain relieved only by doomsday humor. Bemoaning the suit’s slowness, he said, “I guess I was never supposed to have been a judge.”[4] At one point, he counted six children born to lawyers during the trial. When a government attorney suggested a recess, his face brightened. “It’s wonderful to see that little glimpse of paradise,” he said.[5] Coming back from one summer recess, he said bluntly that he “hated to get back to the trial.”[6] At another point, the tension became so great that he leaned across the bench and whispered to the opposing lawyers, “How about a ball game?”[7] They recessed to attend a Dodgers-Giants baseball game. When it came to gallows humor, Medina vied with Morgan Stanley’s lawyer, Ralph M. Carson of Davis, Polk, who described the proceedings as an “endless sandy waste” and “a Sahara of words.”[8]

As a legal duel, the trial was highly uneven—three or four government prosecutors lined up against thirty-five of the highest-priced attorneys in New York. The courtroom crackled with sophisticated repartee. Terrified of losing, Morgan Stanley thought the suit was too important to be left only to lawyers. Young associates dredged up soot-blackened syndicate records from 23 Wall’s basement, and Perry Hall proofread the trial transcript daily. The partners only reluctantly opened their files to competitors and spent a lot of time studying other firms’ documents. As letters and memos were made public, clients were also examining them in what turned into a great game of rampant voyeurism. Some at Morgan Stanley thought that Con Edison was never again as close to the firm after certain documents were made public.

As managing partner until 1951, Harold Stanley was most directly involved. Unlike the feisty, red-blooded Perry Hall, Stanley was austere and remote and, to young associates, seemed older than God. He was so aloof from everyday affairs that at one syndicate meeting at 2 Wall, he was asked for his name by a young Morgan clerk. When he said, “Harold Stanley,” the young man replied, “And the name of your firm?”[9] He was prepped for the

trial by two young assistants, Alexander Tomlinson and Sheppard Poor. One day, Poor was waiting for a cab when Stanley appeared on the same corner, and the assistant graciously yielded to the older man. As Poor held the door open for him, Stanley said, “Thank you, Tomlinson.”[10] Clerks were indistinguishable. But Stanley’s depositions proved a major factor in the trial.

At first, Medina was impressed by the plethora of government documents. Yet in scanning charts of the Club of Seventeen’s performance, he noticed that while Morgan Stanley always stood at or near the top, telltale shifts occurred down below. First Boston zoomed up from number-ten underwriter during World War II to second place behind Morgan Stanley by the time of the trial. If the defendants were united by a deep, dark pact, why these striking shifts? Medina was also struck by the fact that no Morgan Stanley letter or memo even vaguely referred to the conspiracy. What sort of conspiracy lasted for decades but left no fingerprints? Without a documented agreement, Medina refused to apply the antitrust provisions of the Sherman Act.

By the time Medina published his landmark 212-page opinion in February 1954, he believed he was chasing a phantom conspiracy constructed from flimsy circumstantial evidence. Where the government saw collusion, Medina saw “a constantly changing panorama of competition among the seventeen defendant firms.”[11] He noted that when companies switched bankers, the winning firm gladly accepted the new client—a violation according to the rules of a conspiracy. Firms didn’t hustle Morgan Stanley’s august clients, he said, because “there was no point in running around, wasting one’s time, in a patently futile attempt to get business, where a competitor was on good terms with an issuer and doing a good job.”[12]

Medina’s opinion was a paean to Morgan Stanley and probably the best advertising the firm ever got. He was amused by its policy of appearing alone atop syndicate mastheads or not at all, which reminded him of Hollywood starlets fussing over their marquee billing. He was enormously impressed with Harold Stanley. He praised Stanley’s “absolute integrity” and said Morgan Stanley’s entire history would have been different without him. Then he added, “The fact that Stanley denied the existence of any such conspiracy as charged . . . is one of the significant facts of the case.”[13] This was a very peculiar statement: Medina was saying that a defendant’s mere assertion of his own innocence was somehow proof of that innocence.

The Medina trial would soon seem an almost nostalgic glance at a rapidly fading Wall Street. “Banker domination” wouldn’t be the problem of the Casino Age, and even dedicated trustbusters at the Justice Department thought the suit about fifteen years too late. The cozy banker-company ties would finally end, not through judicial ruling or executive fiat but by structural changes in the marketplace. Over the next generation, the entire

system that the Justice Department exposed would be rudely torn apart, and the firm most directly threatened would be the one with the most loyal clients to lose—Morgan Stanley.

IN the last stages of a trial conducted by depositions, Judge Medina yearned to question a live witness—someone he could "look in the eye," as he said eagerly. The government obliged with Robert Young, chairman of the Chesapeake and Ohio Railroad and certifiably America's most rabid Morgan-hater. He was the man who smarted after being rebuked by Tom Lamont for his testimony at the Wheeler railroad hearings in the late 1930s. Touted by the press as the Justice Department's "anti-Morgan machine gun," he so ardently supported the suit that Davis, Polk's Ralph Carson suggested it be renamed *Young v. Morgan.*[14] Sounding his favorite theme of Morgan and Kuhn, Loeb domination of the railroads, Young fired broadsides from the witness stand until Medina glared at him. "This is a courtroom and there will be no appealing here to the public over the head of the judge," Medina snapped.[15] He criticized Young's "hell raising propensities" and mocked the notion that any banker could control Robert Young.[16] When Young stepped down from the stand, he extended his hand to Medina, who just gave it a withering look.

A dapper, pint-sized Texan, Young could seem boyish, with his bulbous nose, pink cheeks, and dimples. Then his face would tighten, his blue eyes would blaze, and he would stare with icy fury. His lifelong Morgan obsession bespoke secret envy. He told Medina that as a young man, he felt "in banking all roads led to Rome and to me the Corner was Rome."[17] He rose through the Morgan universe, first as a worker at a Du Pont plant during World War I, then as a General Motors assistant treasurer in the 1920s. Before the 1929 crash, he advised Pierre du Pont to switch from stocks to bonds and won a following as an investment adviser among rich executives. And in 1937, Young and his sidekick, Allen P. Kirby, had bought control of the bankrupt Alleghany empire, still heavily indebted to J. P. Morgan and Guaranty Trust. The House of Morgan always suspected that he espoused competitive bidding to camouflage the fact that, by controlling six railroads, he was a monopolist himself.

Robert Young was a prototypical man of the new age, a publicity monger adept at courting public opinion. In the early 1950s, he seemed to grin from every magazine cover, deriding the sleeping cars he called rolling tenements and blaming "Wall Street banker control" for decaying railroads. In one celebrated ad, he showed a happy hog riding in style in a cross-country cattle car, the caption read, "A HOG CAN CROSS THE U.S. WITHOUT CHANGING TRAINS—BUT YOU CANT.'[18] He even had a magazine moniker dreamed up by his

publicists—the Daring Young Man of Wall Street. This exponent of people's capitalism lived like a mogul, buying a forty-room Tudor mansion in Newport from a Drexel family member. He had a cream-colored Spanish villa in Palm Beach and a sumptuous apartment at Manhattan's Waldorf Towers.

For a man of such ambition, the giant C&.0—a dusty, coal-carrying railroad—lacked suitable cachet. Instead, he craved the glamorous New York Central, America's second-biggest railroad, which ran sleek passenger trains, such as the Twentieth Century Limited from Chicago. For a century, it was known as the Vanderbilt road or the Morgan road. It still boasted two authentic Vanderbilts on its board, plus George Whitney and five other Wall Street bankers. For a Texas insurgent like Young, the New York Central epitomized the eastern financial establishment. It was the final inner sanctum that he longed to enter. By 1947, Young, with four hundred thousand shares of the railroad, was its largest stockholder. But feeling threatened, the board refused to grant him more than two seats, and even these were then withheld by the Interstate Commerce Commission on antitrust grounds.

By late 1953, Young and his troops amassed one million shares of New York Central stock, or nearly 20 percent of the total. Ordinarily this would translate into control, but the railroad wouldn't submit gracefully to its fate. In February 1954, its blue-ribbon board met at the University Club and adamantly refused to put Young on the board or make him chairman, as he demanded. It was a pompous, hidebound reaction of people who were clinging to outdated prerogatives. Perhaps to forestall charges of Vanderbilt-Morgan control, one Vanderbilt and George Whitney skipped the critical meeting. A humiliated, vengeful Young launched a proxy battle that would turn into the decade's most bellicose corporate skirmish, prefiguring takeover wars of a generation later. To avoid antitrust problems, he resigned from the C&O board and sold its New York Central stake to a friend, Cleveland financier Cyrus Eaton. Now he could storm the Central.

Though Young mouthed old Money Trust cliches, the financial landscape had changed markedly. Family ownership was a disappearing force in the American economy. Where William Vanderbilt had once inherited 87 percent of the New York Central from Commodore Vanderbilt and hired Pierpont Morgan to disperse the shares, his descendant, Harold Vanderbilt, now owned less than 1 percent of outstanding shares. The "banker-dominated" board held less than 2 percent of all shares. After Glass-Steagall, Morgans, Chase, National City, and the rest couldn't hold large equity stakes in companies, further eroding their influence. So the glue that compressed companies, banks, and rich families into a coherent financial class was coming unstuck. Meanwhile, New York Central stock was dispersed among forty thousand small shareholders, whom Young called Aunt Janes and assiduously courted. However much he railed against the "interests," Young knew that financial

power was becoming more pluralistic in the new age. The real threat to the House of Morgan would come, not from Washington, but from new financial powers beyond the control of the old eastern elite. The short Texas raider was a portent of later raiders and mavericks, many from the old populist strongholds of the South and West, who would take pleasure in taunting the Wall Street establishment.

A proxy fight, an attempt to elect a dissident slate of directors, was the favorite takeover device of the 1950s. It stacked the cards in favor of management, which could usually marshal more resources and out-gun the opposition. As a rich outsider, however, Young waged a campaign in the style of a national election, producing a flurry of press releases, newspaper ads, and even direct-mail pleas. The new age would witness many such loud, brassy, vituperative campaigns. Pierpont Morgan and Tom Lamont had waged their corporate struggles behind closed doors, dealing with like-minded bankers. In the New York Central battle, Young forced the sedate clubmen of Wall Street to fight in the open—where they felt naked and profoundly uncomfortable. Both sides spent over $ 1 million and grew so paranoid that they swept their respective headquarters in search of hidden microphones.

Robert Young did everything that gentlemen bankers thought undignified. He appeared on *Meet the Press* and promised to triple the railroad's profits, evoking a vision of high-speed, futuristic train service. He hired a small army of three hundred vacuum-cleaner salesmen to telephone shareholders and even sued directors on the New York Central board, including George Whitney. Despite his own tremendous wealth and railroad empire, he managed to portray himself as a doughty little David combating the Goliath of the New York Central's board.

Although it seemed tangential, Young spent much of the campaign assailing the House of Morgan. He urged companies to renounce their exclusive relations with Morgan Stanley and solicit competitive bids from other bankers. He blurred the identities of J. P. Morgan and Company and Morgan Stanley and lumped them together as the "Morgan crowd." "He assumed that fighting one meant fighting both, plus Guaranty Trust and other banks," said Clifford H. Ramsdell, then an Allegh-any vice-president.[19] Young revived ancient myths that a single Morgan director on a board could bully the rest, claiming the "real issue" was whether the railroad would "continue to submit to a Morgan non-ownership board with countless conflicting interests."[20] The Brandeisian rhetoric is less notable than its application by a millionaire corporate raider in the middle of a takeover battle. The New Deal had only wanted to curb Morgan power; Robert Young wished to appropriate it.

There was an element of bear baiting in Young's attacks on the Morgan

interests. He must have known these proper gentlemen wouldn't emerge from their clubs, roll up their sleeves, and resort to fisticuffs, they had no tactical repertoire for street fights, which they considered ill-bred and highly offensive. Morgan Stanley lacked any publicity apparatus and so found itself contending in a strange, alien world. "Young was beneath our respect," said Perry Hall. "Why get into a public fight with a person like that?"[21] In an unprecedented move, Morgan Stanley ran a large advertisement attacking Young and denouncing government-stipulated competitive bidding. However strong this seemed to Morgan Stanley partners, it was tame stuff compared with Young's merciless guerrilla warfare.

J. P. Morgan and Company was no less baffled in countering Young. Like Saint Sebastian, it stood still taking the arrows. The bank dispatched an emissary to Allen Kirby and asked whether Young could please stop making such nasty statements in public. "Publicity is the only effective weapon we have and we are going to use it," Kirby replied.[22] In April 1954, the Morgan bank published an open letter from president Henry Clay Alexander denying Morgan control of the New York Central. Alexander noted that the bank couldn't own stock and competed with several other banks on the railroad's board. "You are wrong and I have a deep suspicion you know it," Alexander lectured Young. "You think, no doubt, it is good propaganda in seeking stockholders' votes . . . we welcome the opportunity to demonstrate once again that the theory of Morgan banker domination is a fantasy and a myth."[23] He called Young a Little Caesar setting up straw men. This was the closest 23 Wall ever came to invective.

Two months later, Young startled Wall Street when he won the proxy battle by more than a million votes. The speculators backed Young, as did the big retail houses, such as Merrill Lynch and Bache, whose margin accounts went for Young. Lifting his hands like a boxing champ—he didn't mind rubbing it in—Young strode into the New York Central headquarters at 230 Park Avenue and sat down beneath a portrait of Commodore Vanderbilt. When the board met in June, no Morgan banker or Vanderbilt sat on it for the first time since the nineteenth century. The Visigoths had sacked the Holy City. Young's board included Lila Acheson Wallace of the *Reader's Digest* and Indianapolis publisher Eugene C. Pulliam—businesspeople from beyond the Wall Street pale. Ever since the 1930s, economists had commented on the separation of management from ownership in the modern corporation. Now a corporate raider had acted on that momentous shift.

On Wall Street, crestfallen financiers wondered why the Morgan houses hadn't mounted a more spirited defense or formed an informal syndicate to keep the road in friendly hands. *Fortune* asked, almost plaintively, "Why did Morgan not use its prestige?"[24] The answer was partly that the Morgan

houses were still smarting from the New Deal controversies. As president Henry Alexander said, “We don’t try to run other people’s business and there have been so many charges in the past that we want to avoid the appearance of doing so.”[25] While Young played on old associations, J. P. Morgan power stood at its modern nadir. Young’s success had proved, paradoxically, that bankers didn’t control the railroads. The lack of a more tenacious banker defense also reflected the decaying fortunes of the roads. Morgan Stanley hadn’t handled a major public offering for the New York Central since 1936. There just wasn’t that much business at stake.

The Morgan houses had one last sour laugh on Robert Young. Like many hostile raiders, he was ignorant of the true state of his target. And the New York Central was bankrupt. All those slick passenger trains that had dazzled Young were losing money, and freight traffic was being siphoned off by trucks and planes. Young appointed Alfred E. Perlman as the railroad’s president, the first Jew to hold that position. When they first examined the Central’s books, Young said, “Al, aren’t you afraid?” Perlman replied, “No, but we’d better get to work.”[26]

During the 1957 recession, the New York Central, battered by heavy losses, opened merger talks with its historic rival, the Pennsylvania Railroad. In January 1958, the Central skipped its dividend payment, which plunged Young into a terrible state of depression. For a long time, he had struggled with deep psychological problems, veering between brisk optimism and deep melancholia. A close friend, Edward Stettinius, Jr., son of the late Morgan partner, had once found him sitting alone in his Newport library, staring absently into space while a gun lay on his desk. Perhaps after so much brave talk, his failure with the New York Central was too shameful for him to face. On January 25, 1958, he went into the billiard room of his Palm Beach mansion, the Towers, picked up a shotgun, and shot himself to death.

THE chummy world of Wall Street bankers and corporate executives that so enraged Robert Young reached its peak in the 1950s and began to slip. In this high noon of industrial power, before the European economies rebounded or the Pacific rim threatened, the United States dominated automobiles, steel, oil, aluminum, and other heavy industries. As investment banker to big smokestack firms, Morgan Stanley was in an enviable position. Like a caretaker of a cache of crown jewels, it didn’t need to scout out new wealth. The sole objective was to stand guard over the franchise—the superb client list inherited from the old House of Morgan. As the firm’s William Black later said, “All you needed to do in the 1950s was to execute superbly on client business.”[27]

In pleasing clients, a smooth golf swing or a convivial party style was the

standard weapon in the investment banker's arsenal. By modern standards, it was a very sociable, leisurely world, with two-hour lunches at the Bond Club still in fashion. The master at entertaining clients was Perry Hall, the managing partner from 1951 to 1961. Where Harold Stanley was gray and austere, Hall was pleasantly brash and garrulous, blessed with a salesman's patter. Freckled and chunky, he had a broad face and penetrating eyes. He terrified subordinates, charmed women, and lorded it over corporate chieftains. He could sell refrigerators to Eskimos. Like Andre Meyer of Lazard Frères or Sid Weinberg of Goldman, Sachs, he was on a first-name basis with every American CEO. "He would shout at presidents and thump the table and tell them what he thought," said one person who observed him in those years. "His relationship with all those tycoons was unique."

Hall had emerged from an F. Scott Fitzgerald world where Princeton eating clubs and Yale secret societies were the passports to Wall Street success. A 1917 Princeton graduate, he had sat next to Fitzgerald in many classes, due to the alphabetical proximity of their names. (Hall was unimpressed by Fitzgerald's prose and insisted that several forgotten classmates were superior stylists.) For Hall, Ivy League sports provided his all-purpose pantheon of heroes. Whatever his partner's business accomplishments, for example, Harold Stanley remained for him captain of the Yale baseball and hockey teams. Hall hired his own successor, Bob Baldwin, two weeks after watching him play baseball for Princeton. A varsity letter was perhaps the most eloquent letter of introduction at Morgan Stanley.

As the last managing partner from the old House of Morgan, Hall never modified his conviction that FDR was the "worst enemy the U.S. ever had."[28] Hall had worked at the Guaranty Company, survived the 1920 bomb blast, and become a bond manager at J. P. Morgan and Company in 1925. After the 1929 crash, Jack Morgan separately summoned Hall and Charles Dickey. He asked Dickey to become a J. P. Morgan partner and Hall to become a Drexel partner in Philadelphia. Jack, it seems, had bungled his instructions to offer both young men Drexel partnerships. The error deeply wounded Hall and led to a Morgan Stanley tradition of having two people present at important announcements. In 1935, Hall moved over to the new Morgan Stanley, which he liked to regard as his personal creation. He was boastful, but invested his vanity with considerable charm. "We were the *crème de la cième,"* Hall remarked. "Everybody was jealous of us."[29]

Hall was perfectly suited to the relationship banking of the 1950s. He would entertain clients while shooting wild turkeys in South Carolina or fishing near his house in Woods Hole, Massachusetts. (At age seventy-three, he was still powerful enough to harpoon a 552-pound sword-fish.) An amateur golf and tennis champ, he attracted corporate executives who wanted

to test their game. Hall would perform elite missions for clients and behaved like a member of their family. When a General Motors chairman was upset by his daughter's plans to marry a Pakistani, Uncle Perry went to reason with the young woman. He asked whether her children would get into the right schools, have the right friends, and so on. She was persuaded. Such services made General Motors an untouchable Morgan Stanley client in the 1950s.

Hall admired Tom Lamont and his prankish spirit. Once, at an all-night party on Gramercy Park, Hall got separated from his wife. Wandering about, he came upon Marlene Dietrich and Salvador Dali in a doorway. Hall told the actress that he had idolized her ever since *The Blue Angel*. His wife, Alice, then appeared, and Hall pretended not to know her. "Hey, blondie," he called to her. "Wanna try this bed?" Alice sat down, pretended to test the bed. "This feels pretty good," she replied. Later Dietrich cornered Hall. "Did you know that woman?" "I never saw her before in my life," Hall replied. "You're the freshest man I ever met," said Dietrich and stormed off. Hall treasured this anecdote more than he did the biggest General Motors or U.S. Steel underwriting.

Morgan Stanley people were extremely bright—like the old House of Morgan, the firm rewarded intelligence—but investment banking didn't require an enormous amount of financial ingenuity. Inflation was low, currencies were stable, and the securities business was relatively straightforward—if you had the right clients. Underwriting spreads were fat in industrial issues. Right off the bat, Hall told his young recruits from Princeton and the other Ivy League schools to coddle their clients and study their needs. "I'm interested in the man who can bring the business in," he said. "Leave the rest to the business school students. Once you do the deal, put on your hat and go home."[30] With securities issues pretty standardized, companies had little incentive to shop around among investment banks; the astrophysicists had not yet arrived on Wall Street. That Morgan Stanley offered an extra, indefinable mystique was all the inducement most clients needed to remain loyal.

After the New Deal, it was vital to prepare a good securities prospectus and comply with the new legislation. Investment bankers had to exercise "due diligence" and testify to the accuracy of offering documents. Wall Street feared the legal liability that came with the securities laws. Here the firm's secret weapon was the profane, irreverent Allen Northey Jones, who had headed the J. P. Morgan bond department. A Trinity College alumnus, Jones enjoyed tweaking his partners and would grouse within earshot of Hall about "those goddamn stupid Princeton bastards."[31] Son of an impoverished Episcopal minister, bald, and moon-faced with bulging eyes, Jones would chug around the office in red suspenders, smoking a pipe.

He enjoyed shocking people. Once, when the partners were interviewing a

new recruit, he bellowed at the nervous young man, "Are you spoiled?" When the interviewee said he had been lucky in life and was indeed spoiled, Jones jumped up, barked "Hire him and send him to me," and walked out.[32] In new recruits, he inculcated a meticulous attention to detail. He would dump a thick prospectus in a rookie's lap and tell him there was a single error and the young man had until the next morning to find it. He wanted Morgan Stanley to produce the best prospectuses, and corporations counted on the firm to shield them from legal problems. This led to such manic perfectionism at Morgan Stanley that Harvard MBAs proofread every SEC submission. If the old Wall Street was a restricted club, it had the luxury of exercising extreme care in the kind of business it did.

Northey Jones trained a generation of Morgan Stanley partners. If a trainee wished to learn railroad finance, Jones would sit with him late at night, poring over maps of a railroad's tracks and unlocking the company's secret business strategies. His dedication was total, almost monastic. A perennial bachelor, he glanced at his watch one Saturday and sprang to his feet. "I've got an appointment in half an hour," he said. The appointment was for his wedding. Jones did as much as anyone to ensure Morgan Stanley's reputation for excellence.

The influence of Harry S. Morgan, Jack's younger son, was more elusive. He probably stayed at Morgan Stanley out of a sense of family duty and actually spent more time yachting than issuing securities. He worked beneath a framed certificate of U.S. Steel shares from Pierpont's 1901 issue. Harry had a classic Morgan resume—commodore of the New York Yacht Club, trustee of the Metropolitan Museum of Art, General Electric director, Harvard overseer. His North Shore estate at Eaton's Neck, near Huntington, included a manor house, cottages for butler, chauffeur, and gardener, a swimming pool, and an eight-car garage. Sometimes crusty, he was also kindly and gentlemanly and fairly popular at the firm—with reservations.

Like his father, Harry was wary of the public and obsessively private. In the 1960s, Princeton made a pitch to house the Morgan papers and sent several distinguished scholars to lobby him over lunch. When they had finished their presentation, Harry startled them by saying, "I'm sorry to tell you gentlemen, there *are* no Morgan papers." Faces dropped. Arthur Link, a noted Woodrow Wilson scholar, stammered, "But there *must* be Morgan papers." Harry said his father had warned him to scatter or destroy any papers, lest the government get hold of them and again harass the Morgan family as Pujo and Pecora had. In fact, there were papers, a rich collection, which Harry eventually left with the Pierpont Morgan Library.

Perry Hall was somewhat disdainful of Harry Morgan, whom he felt occasionally got in the way. "The other partners were jealous and annoyed at the continued presence of an older man who contributed nothing in their view

but yet held the reins in his hand," said someone close to the firm. "This got more and more true as time went on." In 1956, there was a bruising fight over whether Harry's son Charles F. Morgan would be made a partner. Harry had retained legal title to the Morgan name, which he threatened to withdraw unless his son were brought into the firm. To other partners, it seemed that Charlie was a pleasant fellow with little interest in, or special aptitude for, banking. After some testy exchanges, Harry traded his rights to the Morgan name for Charlie's partnership.

Charlie Morgan would be the only partner in Wall Street history to serve primarily as office manager—he often sat behind heaps of construction blueprints. Years later, when a new partner arrived for his first day, he was told that the man down on his knees fixing his doorknob with a screwdriver was his new partner Charlie Morgan. "If ever two people, father and son, were miscast in life, it was Harry and Charlie Morgan," sighed an ex-partner. When Morgan Stanley moved uptown to the Exxon Building, Charlie supervised the installation of the new telephone system.

After the Charlie Morgan feud, so much residual anger remained that when Harry's younger son, John, was proposed as a partner, an antinepotism rule was invoked. (The rule was passed after one partner, the son-in-law of a prominent partner, proved to be an alcoholic.) Morgan Stanley now rebelled against the Morgans. Thus John Adams Morgan, who even bore his great-grandfather's bulbous nose, was blackballed. "Harry Morgan was told, 'You've got Charlie, that's enough," said an ex-partner. The irony was that John A. Morgan proved the son most interested in finance and later headed the corporate finance departments at both Dominick and Dominick and Smith, Barney.

In his time, Harry Morgan tried to set the tone and uphold standards at Morgan Stanley. Following family tradition, he gave everyone in the firm a bonus on his twenty-fifth anniversary there, in 1960. "Harry stood for the gentlemanly, principled way of doing business that we felt in those days Morgan Stanley and J. P. Morgan epitomized," said a former Morgan Stanley partner, Sheppard Poor. At the annual partners' dinner at the Union Club, he would say, "Gentlemen, the hardest ship to sail is a partnership."[33] In an often greedy business, he presented himself as "brakeman on the Morgan Stanley express train." Harry prevented the place from degenerating into a haven of the Social Register and perpetuated the Morgan tradition of taking smart, ambitious people from modest backgrounds and turning them into aristocrats. He would say, "We recruit and hire in accord with Morgan tradition—which is to hire people who are brighter than the partners." Each year, he visited the Harvard Business School and spoke with finance professors about their most promising pupils; he would often conduct initial job interviews himself. Because Harry Morgan also lent money to young people to become partners,

he had more than his nominal $2 million in the firm, giving him veto power.

Though the world's prestige investment bank, Morgan Stanley seldom appeared in the press. It didn't promote itself and conscientiously avoided publicity. "It was like a doctor not advertising," said Perry Hall. To advertise would be "kind of cheap."[34] Investment bankers subordinated themselves to clients and tried to keep their profiles low. There was a huge internal row about whether to put the partners' pictures into a promotional booklet—an agony resolved in the affirmative after GM chairman Fred Donner said they were all so ugly they would probably scare clients off anyhow. This aversion to publicity was related to the restrained style of competition: if you couldn't raid other firms' clients, why bother to advertise? Morgan Stanley's goal was to freeze the status quo.

Morgan Stanley did have one form of advertising, however—the tombstone ads listing the members of underwriting syndicates. All Morgan-sponsored issues were printed in Ronaldson Slope typeface. Sometimes, when traveling, Morgan people stuffed Ronaldson Slope type into their pockets, in case local printers lacked the numerical fractions. Prospectuses were always done in royal-blue type. The great Morgan Stanley hobbyhorse was that its name stand alone atop tomb stone ads and that the firm single-handedly manage issues. This enabled it to price issues and allocate shares among participating firms; it also didn't have to split lucrative management fees with a co-manager. On the rare occasions when Morgan Stanley deigned to join somebody else's syndicate, it asked that its name be omitted. By managing the huge industrial syndicates, Morgan Stanley shaped the Wall Street pyramid and decreed the relative standing of firms. This produced a self-assurance that partners would describe as pride but competitors would see as arrogance.

As the Justice Department noted in the Medina suit, syndicate rankings seldom changed for a particular company. If Morgan Stanley expelled a firm from a syndicate, the firm might not regain admittance for a long time. Risks were widely distributed in the 1950s, so firms didn't need much capital. On big industrial issues, Morgan Stanley might enlist three hundred underwriters and eight hundred dealers, endowing itself with godlike powers. The firm had virtually nothing to do with selling securities and was strictly a wholesale outfit. It had a clerk on hand to sell unsold syndicate shares around the Street, usually at a loss. This was as close as it ventured into the world of trading.

Nobody could afford to alienate Morgan Stanley, which presided over most of the decade's record issues, such as the General Motors $300-million debt issue of 1953 and its $328-million stock issue of 1957, the $231-million IBM stock offering of 1957, and the $300-million U.S. Steel debt issue of 1958. These securities didn't finance speculation or line the pockets of a self-serving management. They went for new V-8 auto engines or a steel plant on

the Delaware River or IBM’s expansion into the computer business. At this point, investment banking still functioned according to a textbook model in which capital was tapped for investment, not financial manipulation. Investment bankers were still intermediaries between providers and users of capital, and they considered it unprofessional to function as the “principal” in a transaction. The age of financial engineering hadn’t yet dawned.

Morgan Stanley’s monopoly of so much of America’s industry made the firm far less adventurous than J. P. Morgan and Company in exploring foreign markets. In the early postwar years, its few foreign financings had a distinctly Anglo-Saxon or European bias. It sponsored large issues for Australia and Canada, smaller ones for France and Italy. During the 1950s, Morgan Stanley made only one exception to its sole-manager policy, and that was for the World Bank, where it co-managed issues with First Boston. The names of the two firms alternated in the top-left corner of the prospectuses. Through the World Bank, Morgan Stanley partners believed that they made their contribution to European reconstruction and the Atlantic alliance.

In the early days, the World Bank was a highly conservative institution. The International Monetary Fund, however—and contrary to its later image—was then feared as a hotbed of left-wing activism. Russell Leffngwell derided it as a “dream child” that would prop up overvalued currencies, and the American Bankers Association lobbied vigorously against its creation. But the World Bank seemed a pillar of sound finance and was congenial to Morgan Stanley. Because the bank depended on U.S. capital markets for money, early World Bank presidents were chosen from Wall Street. In 1949, Eugene Black, formerly a senior vice-president at Chase, replaced John J. McCloy as president. After a brief experiment with competitive bidding, Black (whose son Bill was later a Morgan Stanley executive) chose Morgan Stanley and First Boston as a permanent team to market the Bank’s triple-A-rated issues in 1952. Black later explained his choice: “Morgan Stanley has a close connection with Morgan Grenfell in London, and with the old firm of Morgan in Paris. They had a very fine reputation in Europe.”[35]

In selling the World Bank to investors, Morgan Stanley and First Boston faced a formidable job. Its very name—the International Bank for Reconstruction and Development—was a mouthful. There were fears—noted earlier—that it might repeat the foreign lending disasters of the 1920s. To promote the bank, Morgan Stanley and First Boston organized huge syndicates of up to 175 underwriters, put on road shows, published booklets, and even seconded people for brief stints at the bank. Morgan Stanley got a critical guarantee that World Bank bonds were backed by America’s capital contribution and were therefore as good as obligations of the U.S. Treasury itself. Morgan Stanley partners always took immense pride in the World Bank account, which marked the summit of the firm’s success: they were banker to

the world's bank, a big enough honor to satisfy even the most swollen Morgan ego.

IN the 1950s, the City of London hadn't yet awakened from its Depression slumber. It was stuffy, inbred, and unimaginative, feeding off past glory. England had lost a quarter of its national wealth in defeating Germany and couldn't function as a world banker. It had lost Italy to the Marshall Plan and China and Eastern Europe to the Communists. Its old foreign clients were fair game to be picked off by Wall Street firms: in 1946, Dudley Schoales of Morgan Stanley snared the first postwar loan to Australia—already a J. P. Morgan client in the 1920s—and the firm sponsored Qantas Airlines two years later.

The City was hobbled by exchange controls and a weak pound. Under the postwar Anglo-American Loan Agreement, the United States lent Britain $3.75 billion to cover its payments deficit. In exchange, Britain was supposed to make sterling convertible to other currencies by July 15, 1947. The attempt failed abysmally as investors rushed to dump pounds for dollars. Speaking at the Lord Mayor's Dinner in October 1947, Lord Catto, governor of the Bank of England, ruefully reviewed this blow to British pride: "Confidence was returning; sterling balances were being more and more freely held in London as in the days before the war. . . . At any rate, we were obliged to try."[36] The sterling market was largely shut to foreigners until Margaret Thatcher dismantled exchange controls in 1979. In its century-long contest with the City, Wall Street had won hands down.

Like most places of obsolete splendor, the City was full of charming eccentricities. At one merchant bank, incoming mail was laid on a table each morning so partners could scan each other's correspondence. At N. M. Rothschild's townhouse, partners shook little bells marked "butler" when they sought refreshment. At the manorial Hambros, senior people were called Mr. Olaf or Mr. Charles. Self-respecting merchant bankers still wore bowler hats and carried furled umbrellas; their reading glasses were always crescent-shaped. Junior men wore stiff collars and were considered dangerously uppity if they let them soften. In this conformist world, when a Lloyds Bank chairman appeared in black suede shoes, people buzzed for days about the frightful lapse in taste.

With slightly over one hundred employees, Morgan Grenfell emerged from the war in relatively strong shape. In U.S. banking terminology, it was a cross between a commercial and an investment bank, underwriting bond issues but also managing pension funds and making loans. Like Morgan Stanley, it seemed to have a monopoly on major industrial accounts. In 1945, it sponsored the first postwar share issue and floated debt for virtually every

British electric company, including Associated Electrical Industries and British General Electric. It also handled denationalization of steel companies—the legacy of Teddy Grenfell's work with Monty Norman to rationalize the industry in the 1930s—and participated in World Bank issues. But the firm was softened by prewar success. The partners (technically directors) had a lazy, custodial attitude toward accounts and wouldn't dig up new business or stir from their chairs. When they disappeared to Boodle's or Brooks's for lunch, they might return—or they might call it a day. Rod Lindsay, a later Morgan Guaranty president who apprenticed at Morgan Grenfell, recalled the somnolent mood: "By Thursday afternoon at four, one of the senior partners would come across to the juniors and say, 'Why are we all still here? It's almost the weekend.' "[37]

J. P. Morgan and Company still held a passive, one-third share in Morgan Grenfell. It was the only foreign bank with a sizable stake in a merchant bank on the elite Accepting Houses Committee. Lacking a London office, J. P. Morgan and Company used the firm as its U.K. branch equivalent, and the two houses traded apprentices and clients. When Esso mapped out big postwar expansion plans for refineries in Western Europe, 23 Wall Street steered the company to Morgan Grenfell. Ditto for Procter and Gamble, Monsanto, Inco, Alcan, and General Foods. After stepping down as Bank of England governor in 1949, Tom Catto took a desk back at Morgan Grenfell (though he didn't resume his partnership) and extended the special access of both J. P. Morgan and Morgan Grenfell to the Bank of England.

Morgan Grenfell was so heavy with peers that it was derided as the House of Lords (in sometimes sniggering tones) by its J. P. Morgan counterparts. In a caste system common in the City, partners were drawn largely from family members, with only Sir George Erskine, a brilliant, driving Scots banker, rising from the managerial ranks to become a partner. (By no coincidence, he was the best banker.) The aging Lord Bicester—Vivian Hugh Smith—reigned, somewhat terrifyingly, as senior partner, and his authority was unquestioned until his death, in 1956. He treated other partners like errand boys as they rushed in and out to get his approval. Everybody called him the Old Man. He was a sphinx who kept his own counsel and never tipped his hand. During eighteen years in the House of Lords, he never delivered a speech. Once, on a deadlocked charity board, he was asked whether he favored a proposed measure. "No," he said, then added, "Or have I said too much?"[38] To be interviewed for a job by Bicester was to endure an array of skeptical snorts, grunts, and harrumphs.

Even when he was in his late seventies, Vivian Smith wouldn't pass the reins to his son, Rufus, who had patrolled on the roof of 23 Great Winchester Street during the wartime buzz-bomb raids. Rufie was relegated to a sad

Prince of Wales role. A portly man with a jolly well-fed look, round-faced and mustachioed, he acted the grandee: he was the sort of large, stately man who would rap on doors with the knob of his cane. He loved steeplechase horses and hunting and tossed off whiskey by the tumblerful. Like his father, he had connections everywhere. He served as a director of Shell, Vickers, and AEI and also sat on the Court of the Bank of England. His wife, Lady Helen, was a daughter of the earl of Rosebery.

Rufie was cowed by the thunderous presence of the Old Man and patiently suffered a marathon apprenticeship lasting well into late middle age. In the late 1940s, Sir Edward Peacock, the senior partner of Barings, told Russell Leffngwell how the Old Man was pleased that Rufie had taken the lead in a Shell financing and proven himself as a good, sound fellow.[39] Yet Rufie had already been through two world wars! In 1949, Lord Bicester relented and let his son take part in a major steel business. "Oh well, the boy's got to learn sometime," he sighed.[40] The boy was then fifty-one and had been a partner for almost twenty years.

In the City of the 1950s, with most business revolving around relationships, Morgan Grenfell was hard to match. It was the City's major portfolio manager for the Vatican, thanks partly to the flamboyant, multilingual Francis Rodd (the second Baron Rennell), son of a former ambassador to Italy. A portly, snuff-taking man who blew his nose into a big red handkerchief, Rodd was a protege of Monty Norman's and a former British manager of the Bank for International Settlements in Basel. As a close friend of T. E. Lawrence (Lawrence of Arabia), he was once asked by Monty Norman to recruit Lawrence as secretary of the Bank of England. (Lawrence declined.) Rodd himself was spirited away to Morgan Grenfell by his father-in-law, Vivian Smith, in 1933.

Assigned to Harold Macmillan's wartime staff in 1943, Rodd was made chief civilian aide to Sir Harold Alexander, who administered occupied territory in Italy. Left-wing commentators criticized the choice, noting that Morgan loans had propped up Italian fascism and warning that Rodd might help to give former fascist finance officials a voice in postwar Italy. Nevertheless, Rodd acted ably to alleviate hunger and sickness in liberated Naples. Macmillan thought Rodd a *prima donna* and an intriguer but also praised him as "quick, intelligent and persistent."[41] So long as Rodd was around, the Vatican business stayed in Morgan Grenfell's hands.

The chief partner for portfolio management was Wilfred William Hill Hill-Wood, who provided Morgan Grenfell with entree to Buckingham Palace. A shrewd, entertaining fellow and a brilliant cricketer, Hill-Wood had served as intermediary between Morgan Grenfell and 23 Wall. Like Jack Morgan, he was a close friend of George VI. "Uncle Willy became friends with George

VI at Trinity College, Cambridge, and the king asked him to look after some of his personal finances," said his nephew Sir David Basil Hill-Wood.[42] Hill-Wood reported regularly to the king on his finances, keeping details of the account to himself. His friendship with George VI guaranteed that when Elizabeth became queen in the early 1950s, Morgan Grenfell would manage a significant portion of her wealth as well. The queen was amused by Willy and apparently on easy terms with him. When she knighted him at Buckingham Palace, she took the sword from behind the curtain, tapped him, and then whispered slyly, "You can get up now, Willie."[43]

Rich in memorabilia, Morgan Grenfell's atmosphere in the 1950s was antiquated. Partners sipped sherry by coal fires while young clerks on tall stools copied accounts into large bound books. These victims of the "fagging system" didn't emerge into adulthood until about age forty, by which point many were thought brain dead. Sexual segregation at Morgan Grenfell was strict. To mask their sexuality "tea ladies" were required to wear linen dusters around the office and leave their jobs when they married. Nomenclature was highly revealing: the firm called itself a countinghouse and directors were partners; it was listed under "merchants" in the London telephone directory.

The thunderclap that roused the City from this profound torpor was Siegmund Warburg's first hostile raid in the famous aluminium war of 1958-59. To understand the furor, it is necessary to note the City's cultural homogeneity. It was a hermetic world of men who had passed through Eton and Oxford, Cambridge, or the Guards and met at Lord's or Wimbledon on weekends. Shot through with class barriers, the City made upward mobility all but impossible for foreigners. From an eminent Hamburg banking family, Siegmund Warburg had fled Hitler in the 1930s and started a merchant bank in 1946. As a Sephardic Jew with a German name and a German accent, bored by shooting and yachting, he seemed to grate on City bankers. One merchant banker admitted, "Siegmund's Jewishness was a problem. He was a little *too* Jewish, as they say in the City."

Warburg was an unlikely revolutionary who followed all the old merchant-banking folkways. He posted no nameplate, opened no branch offices, and valued personal contacts. But he was always an activist, an innovator, and he would quote Dwight Morrow, whom he had met as a young man in the 1920s. "The world is divided into people who do things and people who get the credit. Try if you can to belong to the first class, there is far less competition."[44] In his Belgravia apartment were books in six languages, and he said he would rather hire someone steeped in George Eliot than someone steeped in banking. His use of handwriting analysis for recruiting employees added to his eccentric image.

While Morgan Grenfell floated through long, pleasant lunches, Warburg

ran a firm disciplined in Prussian punctuality. Some Warburg people sat through two lunches—one at 12:30, one at 1:30—to maximize the business they conducted. Young recruits arrived early, stayed late, and worked weekends, while young Morgan Grenfell men were out shooting blizzards of birds from the sky. Warburgs, significantly, was the first firm to scrap the bowler-hat-and-umbrella costume in favor of modern dress.

With a cool outsider's perspicacity, Siegmund Warburg saw that the City disliked unpleasantness and would tolerate mediocrity just to avoid a row. This wasn't surprising, with so many family-run banks and such extensive intermarriage in the City. Warburg also saw that merchant banks no longer had the capital to finance industry or government on a large scale. In the advisory area, by contrast, small capital was no handicap. "In the sense that bankers provide money for industry, they're becoming less important," he said; "but in the sense of being consultants—what I call 'financial engineers'—they're becoming much more important."[45] This was the critical insight of the Casino Age, the idea that would push merchant bankers from the staid world of securities issues into the piratical world of takeovers. The merchant bankers would no longer hand out free merger advice to preserve underwriting relationships. Before Siegmund Warburg was through, the "stuffy" City would be rife with marauders.

In 1958, Warburg mounted the first major hostile takeover in postwar Britain. Takeovers had existed there for decades—they had formed Imperial Chemical Industries, Unilever, Shell, and the big deposit banks. As early as 1925, Morgan Grenfell had negotiated General Motors' investment in Vauxhall Motors. But these were genteel affairs, consummated over sherry. By mid-1958, Warburg had persuaded Reynolds Metal of Virginia to launch a hostile bid for British Aluminium. To give the move a British veneer, Reynolds allied itself with Tube Investments, a Midlands engineering group. Moving stealthily, Warburgs had bought more than 10 percent of British Aluminium by October 1958. Siegmund Warburg would shift the City battleground from contacts to capital and introduce an unsettling new form of democracy.

When British Aluminium learned of Warburg's scheme, management summoned Olaf Hambro and Lord Kindersley of Lazard Brothers. (Lazards was close to Morgan Grenfell in the 1950s, with the two firms even sharing a box at Covent Garden.) In comparison with the upstart raiders, British Aluminium had a true-blue patriotic image. The managing director, Geoffrey Cunliffe, was a son of the World War I Bank of England governor. Its chairman was the bemedaled Lord Portal of Hun-gerford, a wartime hero as chief of air staff and a president of the Marylebone Cricket Club. Although the firm was already negotiating a partnership deal with the American colossus Alcoa, the Hambro-Lazard defense rested on a bogus threat to

national sovereignty. “One day, a party consisting of Olaf Hambro and other senior figures paid a state visit to the partners’ room at Morgan Grenfell,” recalled Tim Collins, a later Morgan Grenfell chairman. “They said, ’This is a patriotic duty and the City is going to collapse otherwise.’ The Morgan Grenfell partners joined in without a fight.”[46]

In November, Sir Ivan Stedeford, the self-made chairman of Tube Investments, presented a proposal to Lord Portal by which Tube and Reynolds would buy a majority stake in British Aluminium for a generous 78 shillings per share. Lord Portal curtly refused, made veiled references to talks in progress, and brazenly withheld Stedeford’s plans from shareholders. Later he issued the following mystifying statement: “Those familiar with negotiations between great companies will realize that such a course would have been impracticable.”[47] Although its defense was predicated on scare talk about a Yankee invasion—Tube was dismissed as Reynolds’s “window dressing”—British Aluminium continued talks with its “white knight,” Alcoa. Within a week, it negotiated a deal that allowed Alcoa to buy one-third of the company at a miserly 60 shillings a share. The institutional investors—the new powers of the age—were inflamed by this wanton disregard for shareholders. And they became a key constituency in Warburg’s camp.

In the popular mind, it was still axiomatic that nobody could prevail against the unified power of the merchant banks. Schroders and Helbert Wagg sided with Warburgs. Otherwise, the City closed ranks behind British Aluminium in a seemingly invincible phalanx, including Hambros, Lazards, Morgan Grenfell, Flemings, Samuel Montagu, and Brown Shipley. From an *aide-mémoire* prepared by Hambros and Lazards, it’s clear that Warburg’s ungentlemanly method upset the group far more than the noisily trumpeted demerits of the Reynolds-Tube proposal. This internal document conceded the offer’s soundness, only inveighing against its irresponsible manner. It was clear that Warburg himself, not some alleged American invasion, was the real issue. The City establishment thought he had failed to play by accepted rules. Members of the establishment either had to join forces to defeat him, or he would wreck British industry.[48]

The next day, these City men, who ordinarily negotiated unseen in their clubs, published the first defensive advertisement that had ever been used in a hostile takeover. The game was no longer being played in their preferred cloakroom style. In late December 1958, fourteen City institutions created a war chest of £7 million, with Morgan Grenfell chipping in £500,000. Where Lord Portal had been prepared to sell his company for 60 shillings a share, the City consortium now made a partial bid for British Aluminium at 82 shillings a share. This not only topped the Tube-Reynolds offer by 4 shillings but indirectly exposed the cheapness of the earlier deal.

Awed by this strength, the London *Times* referred to "an array of City institutions on a scale never before seen in a take-over battle."[49] The *Daily Express* likewise trembled before the heroic show of firepower: "Lined up on the City side supporting British Aluminium are such famed financiers as Lords Bicester, Harcourt, Rennell, Astor, Glenconner, Kindersley, Cowdray, Poole, and Brand. . . . But as history has seen in the past when the big battalions of the City unite, they can almost be sure of victory."[50] One paper toted up twenty-seven titles on the British Aluminium-Alcoa side, including a marquess, sixteen lords, ten knights, and—as if tossed in for good measure—the queen's uncle.

By New Year's Eve, the British Aluminium side had two million shares and felt confident of victory. Lord Cobbold, governor of the Bank of England, and D. Heathcoat Amory, chancellor of the Exchequer, asked Warburg to desist, noting that Prime Minister Harold Macmillan concurred. But Warburg had coldly analyzed the situation and later said, "It was not a deed of genius at all; I had just mobilized big amounts of money for the cash purchases of my clients."[51] Defying government pressure, Warburgs lifted its bid to 85 shillings a share and began huge share sweeps on the Stock Exchange, sometimes buying hundreds of thousands of shares per day. By January 9, 1959, Tube-Reynolds obtained over 50 percent of British Aluminium and declared victory.

The City was stunned. It was an apocalyptic moment. At first, the merchant bankers refused to alter their style or acknowledge that things had changed. Lord Kindersley of Lazard said flatly, "I will not talk to that fellow" and would cross the street to avoid Warburg. The dazed elite couldn't comprehend why the press and investors had lionized the outcast Warburg. Like Robert Young in his battle for the New York Central, Warburg realized the need to court public opinion as share ownership became dispersed. Henceforth, the City would shift from its opaque, secretive style to greater visibility. As one banker commented prophetically, "No company [head] whose shares are publicly quoted could sleep well from now on, because he must always wake up in the middle of the night and wonder who will make a raid on the company."[52]

After a period of estrangement, Olaf Hambro went around to see Siegmund Warburg. Embracing him, Hambro cried out, "Siegmund, haven't we been awful fools?"[53] The bitterness persisted much longer at Morgan Grenfell, which had thought Warburg's behavior monstrous and unforgivable. After all, if capital and cunning counted for more than contacts, what would happen to Morgan Grenfell? For an astonishing fifteen years, the firm refused to deal with Warburgs, even as the latter became London's most innovative firm in the Euromarkets. Warburg made peace overtures and even asked Morgan

Grenfell to share in a deal for Associated Electrical Industries. Morgan Grenfell refused and, far from appreciating the gesture, haughtily said it wanted to do the deal alone.

It’s tempting to say Morgan Grenfell’s fate was decided by the aluminium war. For beneath the indignation flowed new subterranean currents. A group of Young Turks, notably Stephen Catto (son of Tom) and Tim Collins, son-in-law of Rufus Smith, felt the firm was stuck in suicidal snobbery. In many ways, they wanted to ape Warburg, not condemn him. “The aluminium war showed that Morgan Grenfell wasn’t aggressive enough,” said Stephen Catto. “It came as quite a shock here. We were outmaneuvered and demoralized. It was almost the first time and it had a marked effect.”[54]

Within a decade, Morgan Grenfell would not only undertake but specialize in flamboyant takeovers and flaunt its transformation. It would learn to beat Warburg at his game and come to symbolize the new, aggressive way of doing business. Like Morgan Stanley in New York, Morgan Grenfell would show in bold relief the death of the sleepy old world of high finance and the dangerous birth of the new. As the firms that had profited most from old-fashioned relationship banking, the Morgan houses had the most to lose and would react to the threat in an unaccustomed, bare-knuckle style.

CHAPTER TWENTY-SEVEN
JONAH

IN the late 1950s, it seemed the parade had passed J. P. Morgan and Company by and that the name would take on a venerable but slightly antiquated ring, as Rothschild and Baring had. It seemed to be a banking dynasty in terminal decline. While Morgan bankers stuck to their wholesale formula, the competition took banking to the masses. Such large commercial rivals as National City and Chase were raking in consumer deposits, invading shopping centers, and appealing to the new suburban middle class of the Eisenhower era. Bankers Trust, which had insisted on a $5,000 minimum account, dropped the rule and went retail, too.

Henry Clay Alexander, who succeeded George Whitney as chairman in 1955, saved Morgans from genteel oblivion. Despite a shared sense of the essence of banking, the two men were very different. Whitney was the East Coast patrician, while Alexander "was graced with an easy Southern affability, relaxed in conversation, intense and enthusiastic at business—Hollywood handsome with an unruly forelock," recalled Jim Brugger, then the bank's publicist.[1] Both Whitney and Alexander were so handsome that when they appeared in public, women chased them down the block.

Henry Alexander was probably Wall Street's most popular banker in the fifties. He appeared on the cover of *Time*, and his winning personality took some starch from the Morgan image. As a young Davis, Polk lawyer, he had been assigned to lack Morgan during the Nye "merchants-of-death" hearings. "I like that young man," Jack had said. Those five words secured Alexander's fortune. On Christmas Eve 1938, Jack invited him to become the first new partner since the Pecora hearings. "Think about it," Jack said. "We will have a talk a month hence."[2]Alexander agonized over whether to be a Morgan or a Davis, Polk partner. "You have been dealt two straight flushes," a law partner said, "and you've got to pick between them."[3] He chose Morgans and performed legal work for the bank's incorporation. He was a protege of Lamont, who thought him precociously wise, and of Whitney, who said, "Henry's so remarkably able."[4]

Like Lamont, Alexander was a self-invented figure whose elegance appeared hereditary. Tall and slim with wavy hair and a weak chin, his dapper look was sometimes accentuated by a pocket handkerchief and homburg. Yet

he was from Murfreesboro, Tennessee, the son of a grain-and-feed merchant. He attended public high school, Vanderbilt University, and Yale Law; he first learned law hanging about a sleepy southern courthouse. He had a politician's versatility. Once on a visit to Tennessee, he chatted with a mule farmer who said afterward, "He is the nicest mule trader I ever met."[5]

Alexander projected contradictory images. He was a Jacksonian Democrat by birthright, he said, yet a registered Republican. He favored sound, orthodox financial policy—as well as tax cuts to spur growth. As a Methodist with an Episcopalian wife (who was a former Powers model), he would say, "I'm a Methodist in town and an Episcopalian in the country."[6] This kept everyone thoroughly confused about his identity. Tutored in secrecy, Alexander wouldn't name clients and once told a reporter, with excruciating circumlocution, that the number of Morgan clients was "more than half-way up to 10,000."[7]

Alexander relaxed the bank's pontifical image. He sailed a ten-foot dinghy, drove a Chevrolet station wagon, and bought suits off the rack. As American business power shifted toward the South and the West, the home base of many oil companies and defense contractors, it helped to have a chairman with a southern accent who could drum up business in Texas, California, and other places so long *terra incognita* for the bank. Alexander played the smart hick superbly. His occasional corn-pone patter—his sly, down-home aw-shucks manner—belied real sophistication. "When and if you decide you would like to borrow a little money," he would tell corporate executives, "I hope you will not forget your country cousin at 23 Wall Street."[8] It was a shrewd way to disguise the fact that the bank badly needed new business.

During Eisenhower's second term, the Morgan bank had excellent access to the White House. In early March 1956, Ike had wrestled with the decision of whether to keep Richard Nixon as his vice-president. A flurry of rumors reported that he would dump Nixon, who prepared to announce his retirement. Eisenhower made it the subject of a "stag dinner" and invited George Whitney to attend. Whitney recommended that Ike choose the older and more experienced Christian Herter as his running mate. Nixon, he said in a subsequent letter, could be better groomed as a future Republican leader in a high-appointed post—a tactful way of shoving him aside. In a reply marked "personal and confidential," the president agreed, but added resignedly, "The attitude [among politicians] seems to be 'do the thing that seems most popular at this moment.' "[9]

Henry Alexander was so popular at the White House that the press dubbed him "Ike's banker." Although Alexander was the most domestically oriented chairman in Morgan history—he came in after the foreign loans of the twenties and never lived abroad—he fully internalized the Morgan

identification with Britain. This was patent during the Suez affair. On July 26, 1956, Egypt's prime minister Gamal Abdel Nasser nationalized the Suez Canal. The next day, the British prime minister, Sir Anthony Eden, informed Eisenhower that Britain was drawing up military contingency plans to reclaim the canal. By early November, Britain, France, and Israel invaded Egypt, to the great dismay of Eisenhower and his secretary of state, John Foster Dulles.

The Suez affair produced a deep rift in the Atlantic alliance—always painful for the House of Morgan—and the bank tried to win back U.S. support for Britain. Speaking at the Executive's Club of Chicago on December 7, Henry Alexander, in a rare bit of verbal pyrotechnics, conjured up a Nasser who "stirs the Arab world and breathes fire and damnation." He argued that the Soviet Union planned to join with Nasser in strangling NATO through their joint control of Middle East oil. Alexander proposed an American doctrine for the Middle East like that which the United States had extended to protect Greece, Turkey, and Formosa. In his peroration, he urged that the United States get back on "speaking terms" with Great Britain and France. He said, "We must save our alliances. They are mainstays of our defense, the floodgates holding back the Communist tide."[10]

George Whitney, meanwhile, had always refrained from exploiting his friendship with Eisenhower; this modesty had enhanced his credibility. But on December 26, 1956, in an unusual step, he sent Ike a grave letter bluntly advocating a tougher approach toward Nasser:

At some point somebody has got to tell [Nasser] where he gets off in no uncertain terms, taking the calculated risk of what this may blow up. Probably you have already done so; if not, I am afraid you might. Every day that goes by without some forward motion carries with it more serious risks. It is not only the financial plight of Western Europe, it is the injury to the prestige of the Western powers that to me is the most unfortunate repercussion. I am ready to assume the United States' position has been improved with a good many people in Asia and Africa, but I am afraid that this may have been attained at an unprecedented cost to the Western world.[11]

Eisenhower showed the letter to Dulles, who knew Whitney well. The secretary of state reminded Eisenhower that the Morgan bank was the fiscal agent for the British government and submitted that Whitney's sources were "somewhat biased."[12] Ike sidestepped Whitney's letter. By the time he replied, he reported that he had just heard of Anthony Eden's resignation as a result of England and France's lack of success in the Suez affair. Then he abruptly turned to personal pleasantries.

Unlike the situation of the 1920s, the Morgan influence at the White House

was vastly disproportionate to the bank's slender resources. During the fifties, the bank seemed to shrink, if only because its rivals grew so rapidly. It had to cobble together syndicates to serve large clients, such as France. Nevertheless, Alexander stayed aloof from branch banking and the spree of banking mergers. The old Wall Street vanished as musty, dignified old banks were snapped up by hungry retail giants. The First National Bank of New York—the bank of Pierpont's pal George F. Baker—was illustrative of the situation. Refusing to hustle for business and demanding client introductions, it was dying with dignity, like a fussy old dowager, and was acquired by National City. Spurned by Morgans, Chase took over the Bank of the Manhattan Company; Chemical acquired New York Trust; and Manufacturers Trust later merged with Hanover Bank. Over a third of New York's banks vanished. They had to merge if they were to grow to a size commensurate with their multinational clients.

It was a brand-new age of banking, one with a less austere image. The stereotypical banker had been a grumpy Scrooge who closely scrutinized loan applications and was congenitally biased toward rejecting them. That befit a historic situation of scarce capital rationed by bankers. But the situation was reversed in the Casino Age, which was characterized by new financial intermediaries and superabundant capital. The banker now evolved into an amiable salesman who belonged to the Rotary Club, played golf, and smiled in television ads. Where banks once resembled forbidding fortresses or courthouses flanked by Corinthian columns, they switched now to inviting exteriors. In 1954, Manufacturers Trust opened a Fifth Avenue branch that wooed pedestrians. Its thirty-ton safe sat behind the bank's plate-glass window so that strollers could peer through its open door. Inside the new banks, marble corridors and tellers' cages gave way to soothing pastel shades, open counters, and soft furniture. Chase launched its advertising campaign with the slogan "You Have a Friend at Chase Manhattan." For elitist Morgan bankers, this was too much. "You can't provide custom tailoring to a mass market," sniffed Henry Alexander.

Showing their new subordination to corporate clients, many Wall Street banks moved their headquarters to midtown. Now past were the days when supercilious bankers expected company chairmen to troop to them. Between 1950 and 1965, hardly any new construction occurred on Wall Street. Chase, a large downtown landlord, feared property values might fall. To protect the bank's interests and restore faith in Wall Street, John J. McCloy and David Rockefeller worked out a deal with real estate mogul William Zeckendorf to create Chase Manhattan Plaza, one block from Wall Street.

As part of this package, Chase had to find a buyer for its thirty-eight-story tower at 15 Broad Street. The natural buyer was the adjoining House of Morgan. When Zeckendorf broached the subject with Alexander in 1954, they

had a highly revealing conversation:

> “We’re not real-estate people,” Alexander said. “We already have this beautiful little corner here. We play a special role in finance; we are not big, but we are powerful and influential, we have relationships. Furthermore, we don’t want to be big and don’t need the space.”
>
> “Henry,” said Zeckendorf, “you’re going to get married.”
>
> “What?”
>
> “Someday you are going to merge with another bank, a big one. When you do, this property will be in the nature of a dowry coming with a bride; you will be able to make a better deal with your partner.”
>
> “Morgan will never merge.”
>
> “Well, that’s just my prediction.”[13]

Zeckendorf would later remind Alexander of this talk.

Bankers who had survived the Depression shied away from property speculation, and Alexander bargained fiercely for 15 Broad. He got it for $21.25 million with a 3’/2-percent mortgage—terms so unfavorable for Chase that it later bought out the mortgage. Fifteen Broad was then joined internally to 23 Wall, which became the larger building’s triumphal entryway. The flamboyant Zeckendorf used the deal to conquer Morgan’s aversion to real estate lending and ended up getting loans from the bank. He later told of how a journalist he met while flying back to New York from a trip had coaxed him into stopping *en route* to attend a wedding at a nudist camp. By the time he arrived at a 23 Wall meeting, press photos had appeared of him with the wedding revelers. He thought this publicity might end his relationship with the decorous Morgans. Instead, every high officer, including Henry Alexander and George Whitney, turned out to hear the juicy details.

Many Morgan people opposed a merger because they liked working in a small, paternalistic bank with terrific perks; they thought a merger would cheapen the genuine article. There was a deeper dilemma: if the bank merged with a bigger bank to increase capital—the only sensible reason for doing so —it would become the junior partner, and J. P. Morgan and Company would effectively cease to exist. Finally, though, a decision would have to be reached. But even in late 1958, Alexander was still bluffing about the bank’s self-sufficiency: “Some mergers are a good thing. But while I wouldn’t say it can’t happen here, we have no desire to merge. We’ve been doing very well, thank you, sticking to our last.”[14] He told people, “We don’t have the urge to merge.”

Henry Alexander solved the problem with brilliance and extraordinary luck. Around the corner at 140 Broadway stood the fat, sleepy, dowdy Guaranty Trust. Long on capital and short on talent, it was the mirror image of Morgans. Its huge lending limit was larger than that of all the Chicago

Loop banks combined. A former Money Truster, it had been a Morgan ward after its disastrous sugar lending in the early 1920s. After merging in 1929 with the National Bank of Commerce—once known as Pierpont Morgan's bank—it became New York's second largest bank. In the 1930s, George Whitney chaired its trust committee and Tom Lamont its executive committee. It was a blue-chip bank with almost all of America's top-one-hundred companies as customers. "We used to think of Morgans as a nice small bank," remarked Guido Ver-beck, then a Guaranty officer. "Because of their lending limits, when they participated in large loans, they could only take a small share and they were very worried about it."[15]

Guaranty's chairman was J. Luther Cleveland. An old-school banker, he had rimless spectacles, neatly brushed hair, and a somber mien. Curt and humorless, he tried to run the whole bank, and his autocratic style prompted an exodus of talented people. He was the imperious Mr. Cleveland to subordinates, and grown men quailed in his presence. His own son would pop up like a jack-in-the-box when he entered the room. Cleveland would let visitors wait in his outer office, then grill them when they came inside. Despite shareholder discontent and sluggish business, he snorted at the idea of branch offices and small checking accounts.

J. Luther Cleveland was an expert practitioner of relationship banking. He sat in a gloomy office, a dark, sleep-inducing room, attending to a single document on his desk. "It was a list of ten names," recalled A. Bruce Brackenridge, then with Guaranty and later a group executive at Morgan Guaranty. "These were ten very important clients to the bank. He made sure that he called them periodically to let them know he was interested in their business."[16] A former Oklahoma oil banker, Cleveland had a powerful array of oil clients, including Cities Service and Aramco, the four-member consortium (today's Exxon, Mobil, Texaco, and Chevron) with exclusive rights to pump Saudi Arabian oil on very sweet terms. To stay on good terms with his board, he played poker with the directors. One oil director even packed a rare $10-thousand bill in his wallet, always ready for a quick game. The whole operation, ex-employees allege, was riddled with cronyism. "The only loan I ever saw Cleveland approve was a stock option loan to a crony of his," said a Guaranty banker. "It was later criticized by bank examiners." Adding to Guaranty's troubles was a paralyzing conservatism left over from the sugar debacle. "It was more important not to lose money than to make money," remarked Frank Rosenbach, then a Guaranty credit analyst.[17]

Eventually Cleveland's monstrous ego precipitated a board rebellion. When a director asked who could replace him, Cleveland thundered, "Nobody!" So the board opened merger talks with Henry Alexander in order to dump Cleveland. The last straw came when Ford Motor, dismayed by Guaranty's

handling of its pension fund, switched the fund to Morgans. The board told Cleveland he couldn't be doing a very good job if he couldn't keep his largest account. At first, Guaranty's board came to 23 Wall with a proposal for a new bank called Guaranty Morgan—an insufferable thought to Alexander. A year later, in December 1958, with mounting frustration over Cleveland, the board swallowed hard and consented to Morgan Guaranty. When the autocratic Cleveland assembled his vice-presidents to break the news, it was the only meeting of the bank's officers anyone could remember having ever taken place.

In taking over a bank four times the size of J. P. Morgan and Company, the press likened Morgans to Jonah swallowing the whale. Alexander had engineered the dream deal. Guaranty was strong in railroads and public utilities. While J. P. Morgan was the lead bank for U.S. Steel, Guaranty had Bethlehem Steel. While Morgan had Kennecott Copper, Guaranty had Anaconda. While Morgan was peerless in the northeastern United States and Western Europe, Guaranty was well-connected in the South, the oil patch, the Middle East, and Eastern Europe. It had historic branches in London, Paris, and Brussels, having been the U.S. Treasury's agent in Europe during World War I. Guaranty had provided financing for Thomas Watson's IBM in the 1920s, and several of its executives had grown rich investing in the company. It held more American Express deposits than any other bank. And it claimed the account of Huntington Hartford and the A&P. What a prize!

On Wall Street, people said that Guaranty had really merged with Henry Alexander. When Bill Zeckendorf came to congratulate him, Alexander said, "You know, I've often thought of that conversation we had and how right you were." "I wasn't right, Henry," Zeckendorf replied; "I was wrong." "How so?" asked Alexander. "You're not the bride," Zeckendorf answered.[18]

Alexander chaired the merged bank while Luther Cleveland played almost no part, retiring after a year. Tommy S. Lamont and Henry P. Davison, Jr., became vice-chairmen, with Dale Sharp as president—the sole Guaranty person to retain a top post. While 23 Wall and 15 Broad were refurbished for the merged bank, Alexander and the others temporarily moved into Guaranty's offices at 140 Broadway. Far from feeling defeated or humiliated, the Guaranty troops in the trenches felt liberated by the advancing Morgan army. The one grievous error Alexander made was not notifying Morgan Grenfell of the merger until an hour before it was publicly announced. It was a terrible blow to the London bank, especially since Guaranty had a large, competitive London office.

After the merger was consummated on April 24, 1959, Alexander summoned the combined staff and indoctrinated its members with Morgan groupthink: "I want all of you to know—as the relatively fewer Morgan people here know—that an important element of your career path will be how

well you train the people underneath you to replace you."[19] This close-knit corporate culture, which stressed the group over the individual, would distinguish Morgan Guaranty from other Wall Street banks, which functioned as collections of contending egos.

Even with swollen ranks, Alexander kept up the traditional meetings with department heads. Although Morgans had been stingy with titles, Alexander liberally handed out promotions in order to smooth relations with Guaranty officers. In merging the two banks, petty problems of style proved most intractable. There was prolonged squabbling about a typographical style for the stationery. Since both banks used mono-grammed silver in their dining room, weighty talks occurred over silverware and matchbook covers.

In April 1960, Junius S. Morgan celebrated the merger with a luncheon for eight hundred people at his North Shore mansion, catered by Louis Sherry's. Jack's elder son was even less suited for banking than his brother, Harry, and had remained in the business out of family loyalty. The colossal Morgan energies had petered out in this pleasant but somewhat ineffectual generation. Junius, a commodore of the New York Yacht Club, had yearned to be a marine architect, and his home was full of model ships in glass. Generous, charming, but lacking ambition, he'd become another Morgan male lashed to the wheel of the family dynasty. Though he put on pinstripes and fedora each morning, he never quite looked the part. "Junius was the nicest man you've ever known," a colleague remembered. "But he should have been in the Navy. He didn't know anything about banking and it was pitiful to watch him."

That luncheon would be Junius's farewell to the bank. Tall, and handsome in an old patched jacket, he greeted his guests in the doorway of his forty-room stone mansion, Salutation, a place of faded elegance and English furnishings. Seven massive glazed Ming pottery figures stood in the main hall's niches. Shaking hands, Junius stood by his wife, Louise, whose cardigan had a hole in it. Described by some family members as artistic and eccentric—by others as pushy and spoiled—Louise yearned to "touch up" John Singer Sargent's portrait of Jessie Morgan. She bred golden Labradors, and dozens of them ran about the tents and tables, the twenty acres of gardens, the tennis courts, and the swimming pool. Six months later, at age sixty-eight, Junius died from a sudden attack of ulcers while on a hunting trip in Ontario.

By merging with Guaranty, the House of Morgan regained its status as the world's largest wholesale bank. Suddenly flush, with over $4 billion in deposits, it now stood fourth in size behind First National City, Chase Manhattan, and Bank of America. But this didn't tell the whole story of its corporate strength. It had an unmatched number of corporate accounts, ten thousand including ninety-seven of the hundred biggest U.S. companies. By the mid-1960s, the newly merged bank would do more corporate lending

yearly than the next five competitors combined.

The new bank produced fears of a sort missing since the New Deal. But they were expressed by other banks, not by Washington. Twenty years before, a Morgan-Guaranty merger would have raised impassioned shouts of protest in the populist heartland. Now there were only mild peeps, notably from Texas Congressman Wright Patman, who wanted to stop the merger on antitrust grounds. Approving it, New York State banking authorities noted certain altered facts of the Casino Age: corporations could now bypass banks and turn to life-insurance companies for capital, raise money through bond issues, or finance expansion from retained earnings. As banks lost their special position as providers of capital, the old fears of excessive bank power disappeared as a major issue in American politics.

At first, the Kennedy years looked auspicious for Morgans. Although his father had been snubbed by Jack Morgan and the financial establishment, President John F. Kennedy wanted to court Wall Street to counteract his slim victory over Nixon. "He was also financially conservative," remarked C. Douglas Dillon. "A lot of people didn't realize that. I think it was the influence of his father."[20] He turned to Robert Lovett, then of Brown Brothers Harriman, for advice on cabinet selections. Lovett suggested John J. McCloy, Douglas Dillon, or Henry Alexander for Treasury secretary. Apparently Alexander had the appointment sewn up but then made a strategic blunder. After Kennedy spent an hour with him during the campaign, Alexander declared his support for Nixon. "I don't think there is any question that the head of the Morgan bank . . . would have received the job," said Robert Kennedy of Alexander's faux pas. "Jack felt that this was a personal insult."[21] Dillon won the job. Alexander probably wouldn't have fit into the Kennedy cabinet anyhow. Even as cabinet selections were being considered, he was telling bankers, apropos of Nixon's defeat, "Let's not, as businessmen, wall ourselves off or sulk in our tents."[22]

Alexander was drawn into one historic episode in the Kennedy White House, however—JFK's confrontation with U.S. Steel chairman Roger M. Blough over a steel-price increase in 1962. The administration had applied pressure to the steelworkers' union to accede to a moderate wage settlement in exchange for price restraint by management. So Kennedy felt double-crossed when Blough came to him on April 10, and informed him of a 3.5-percent price increase. This was the betrayal that prompted Kennedy's famous outburst: "My father always told me that all businessmen were sons of bitches, but I never believed it until now."[23]

While Kennedy started a campaign against the price increase and resorted to harsh invective against businessmen, the administration cast about for more discreet ways to influence U.S. Steel. Henry Alexander was on the company's

board, and John M. Meyer, Jr., of Morgans was on its executive committee. Robert V. Roosa, under secretary of the Treasury and former Brown Brothers Harriman partner, telephoned Alexander and asked him to appeal to Blough. The House of Morgan no longer had the mythical power to rescind a U.S. Steel increase, but Alexander might have gotten Blough to soften his anti-administration rhetoric at a news conference during the standoff. After Blough finally responded to Kennedy's pressure and rolled back the increase on April 16, Alexander accompanied Blough on a series of meetings to repair relations with the White House.

Still, the Kennedy years provided a politically friendly environment for bankers, who were no longer the bogeymen, as they had been in the 1930s. The Morgan bank even got giddy and overreached itself. In 1961, finally catching deposit fever, Alexander decided to drop Morgan's ancient aversion to retail business. By affiliating with six large upstate banks, he hoped to create America's biggest bank, a holding company monstrosity called Morgan New York State. "The basic idea was that the bank would have a Cadillac division and a Chevrolet division," explained Bruce Nichols, a partner with Davis, Polk, and Wardwell. The stately Morgans would suddenly have 144 offices in places like Oneida and Binghamton. It turned out there was some vestigial fear of bankers among the populace, and Morgans had awakened it. James J. Saxon, JFK's comptroller of the currency, torpedoed the move on antitrust grounds. Some believed the bank had bungled things by proposing an overly grandiose plan. Afterward, Alexander sighed to colleagues, "Well, we'll just have to stick to wholesale banking." Later the bank would feel that Saxon had saved it from a ghastly mistake.

When the Morgan Guaranty entourage swept back into the renovated Corner, the building's interior mirrored a new era of banking. Everything was open: the glass-and-marble enclosures had been torn down. The signature rolltops, with their secret cubbyholes, were traded for flat, leather-topped mahogany desks. An enormous Louis XV chandelier, of a sort found in old German and Austrian palaces, now shed a rich glow over the room; the old mosaic panels were covered with apple-green fabric. The grandeur remained, but the old mystery had vanished. The most important change was that this banking floor—once the entire bank—was now just a gorgeous anteroom for the 15 Broad Street skyscraper, although top officials kept their offices on the second floor of 23 Wall. As if showing off its disregard for mundane concerns of cost, the bank rejected proposals to expand its short landmark building. Standing in the perpetual shade of skyscrapers. 23 Wall probably remained the least cost-effective use of real estate in the world.

SHORTLY after the merger, American banking began to wriggle free from

its regulatory confines. Under Eisenhower, bankers had dreamed of deposits: in pursuit of billions in beautiful deposits, Henry Alexander had wooed Guaranty. But as interest rates floated up to a heady 4.5 percent by the late 1950s, corporate treasurers were loath to leave behind interest-free deposits ("compensating balances") in exchange for loans. In what some bankers thought heresy, Morgans helped clients move their deposits into higher-yielding money market instruments. As George Whitney told critics, "My customers are not stupid."[24]

The prospect was for a progressive erosion of the free balances. For the House of Morgan, without a cushion of consumer deposits, the specter of losing corporate deposits was especially ominous. Some inside the bank saw the dismal future of wholesale banking with remarkable clarity. Thomas S. Gates, Jr., who would succeed Alexander as chairman, used to say to him kiddingly, "You know, this isn't a very good business to be in."[25]

Emancipation was at hand. In 1961, George Moore and Walter Wriston of First National City figured out how to circumvent the regulatory cap on interest rates. By law, banks couldn't pay interest on deposits held under thirty days. But by selling "negotiable certificates of deposits" that matured in more than thirty days, banks *could* pay interest. These CDs could also be traded (hence, the "negotiable" in their name). Their use sparked a revolution in the way commercial banks operated, freeing them from reliance on deposits. Bankers no longer had to wait for deposits and were liberated from both companies and consumers. Now they could roam the world and raise money by selling CDs in overseas wholesale markets. The new system was known as managed liabilities. (In banking parlance, loans are assets and deposits, liabilities.) So relationship banking was crumbling on two sides—that of the restless corporate treasurers, who demanded yields from their deposits, and that of the freewheeling bankers, who could dispense with deposits and turn to money markets.

The Morgan innovator was the tall, florid Ralph Leach. A University of Chicago graduate and a disciple of Milton Friedman, he started out as a Federal Reserve Board staffer and tennis partner of Fed chairman William McChesney Martin: the two would dash from morning meetings of the Federal Open Market Committee to grab the Fed's court by noon. When Leach left for Guaranty Trust in the early 1950s, Martin, who'd been the first salaried president of the New York Stock Exchange, told him, "Don't forget, Ralph, your associates in the next year or two will be people we could have put in jail fifteen or twenty years ago."[26] As Morgan Guaranty's treasurer, Leach still advised the Fed and coached its board of governors and staff on money market operations. In the new era, Morgans' intimacy with the Fed would come not through lending, as in the Twenties, but through its Treasury

operation. It would act as the Fed's eyes and ears in the marketplace and sometimes receive central-bank intelligence in return. It would now have better connections at the Washington Fed than it did during the New Deal. In the 1950s, Morgans had hired Arthur Burns as a consulting economist, and he would follow Martin at the Fed.

At Guaranty Trust, Leach had peppered Cleveland with memos showing how the bank could manage its capital more aggressively. The patronizing Cleveland would reply, "Young man, go upstairs and run the portfolio and we'll run the bank."[27] After the merger, Leach got to pursue his experiments and pioneered in the Federal funds market. Fed funds were reserves that commercial banks deposited with the Fed. Some banks would temporarily have "surplus" Fed funds—that is, reserves beyond their legal requirements. Morgans began to take the temporary, unused reserves from small interior banks and either use them or lend them to other banks on an overnight basis. The size of these short-term loans rose spectacularly, to $1 billion or $2 billion a day. Some banks believed the new market shouldn't be used for trading profits. Leach, however, a born trader, viewed the Fed funds market as a source of profit.

For commercial bankers, the world of negotiable CDs and Fed funds signified a dramatic change. As banking switched from a deposit to a money-purchase business, the center of gravity shifted from the banking floor to the trading room. The business acquired a new speculative cast as banks built up huge, diversified investment portfolios. Banking became not only riskier but more impersonal. The old-fashioned banker lunched with corporate treasurers to make sure they kept deposits at the bank. But traders were a lean, hyperthyroid breed who spent days on the telephone, riveted to the changing prices; they didn't need to be particularly polite or cultured. The leisurely pace of deposit banking was replaced by the traders' snap judgments.

The Fed saw perils in this volatile new form of banking. Would savings and speculation become jumbled, as they had in the 1920s? Hadn't Glass-Steagall shielded banks from such fast-moving markets? Morgans handled its trading operation with great panache, and its trading desk would be a postwar strength. But how would the new system work in clumsier hands? Would it turn into a dangerous instrument? "The Fed would say to us, 'It's all right for Morgan to do it, but what if Bank of America or City did it?" recalled Leach. "Their feeling, in many cases, was, 'It's good for you guys, but bad for the country.' When they asked how other banks would fare, I would duck it by saying that I wasn't arrogant enough to answer."[28]

Gradually the House of Morgan drifted back into capital and money markets. Banned from corporate securities by Glass-Steagall, it became the most active dealer in Treasury and municipal securities in the 1960s. Unlike

the straitlaced bankers of old, Leach would place large bets on the direction of interest rates. Now a commonplace banking practice, this was a frighteningly novel departure for conservative souls at 23 Wall. In 1960, Leach saw an excellent chance to speculate on one-year Treasury notes being auctioned by the Fed. When he calmly proposed a huge bet to the Morgan board, Henry P. Davison, the vice-chairman, asked, “Ralph, what kind of numbers are we talking about?” Leach said airily, “Oh, $800 million to $1 billion.” Swallowing hard, Davison replied, “This is going to take us time to digest, Ralph. That was the size of our entire bank a year ago.”[29]

This new banking would wake up the drowsy Wall Street of the 1950s. Soon the tenth floor of Morgan’s building at 15 Broad Street had scores of frenetic young traders taking positions in T-bills, negotiable CDs, foreign exchange, and Fed funds. Before long, Leach oversaw $ 1 billion of market transactions daily. In 1966, *Fortune* claimed that Leach “very likely handles more money in the course of a year than any other man in private industry.”[30]

At one point, Leach became too assertive, and the government stepped in. In August 1962, the Treasury auctioned $1.3 billion in bills maturing in three months. Leach placed a shockingly large bid—$650 million, then the largest bid ever submitted for T-bills. Wall Street saw an attempt to corner the market. Although Leach blandly denied any sinister intent, Treasury Secretary C. Douglas Dillon promulgated a new policy, courtesy of the Morgan bank. Henceforth, no single bidder would be awarded more than a quarter of the bills offered at any weekly auction. The Morgan allotment was halved to $325 million.

It would take the general public many years to catch on to these changes. The rise of bought money, negotiable CDs, and daring trading would have an enduring effect on banking. Bankers formerly had been preoccupied with the “asset” side of the business—that is, making loans. Now the liability side—the money on which loans were based—took on equal importance. Profits could be expanded in two ways—by securing higher interest rates on loans or by buying money more cheaply in the marketplace. In this new environment, that bastion of conservatism, the House of Morgan, elevated the trader to unaccustomed eminence.

Unfortunately for the banks, this new world of wholesale money markets also worked to the advantage of their corporate customers. Just as the Morgan bank could sell its CDs around the world, so a General Motors or a U.S. Steel could circumvent the bank and sell promissory notes called commercial paper at interest, rates lower than those they would pay for a bank loan. In the wholesale corporate world in which Morgans operated, the banker was shedding his unique place as an intermediary between the providers and the users of capital. In the Casino Age, large corporations would increasingly

serve as their own bankers, creating a crisis in the wholesale lending business, which had seemed so safe to the J. P. Morgan partners back in 1935.

THE rise of the Euromarkets accelerated the banking revolution of the early 1960s. With scarcely a whisper of public protest, these unregulated overseas markets subverted the spirit of Glass-Steagall. In the 1950s, so long as America was rich and other countries poor, bright young Morgan bankers avoided international banking. Henry Alexander's career was emblematic: he lacked the ties to foreign ministers that were symbolic of the careers of Tom Lamont and Russell Leffingwell. Yet he foresaw foreign trade and investment as the next phase of American economic life. American companies were expanding overseas at a rapid clip. Soon after the Morgan-Guaranty merger, Alexander and Walter Page went abroad to set up Morgan offices in Frankfurt, Rome, and Tokyo, resurrecting the old international network. Morgans used the 1919 Edge Act, which allowed American banks to take equity stakes in foreign banks if a country didn't allow U.S. bank branches. By 1962, the House of Morgan had interests in eleven financial houses from Australia to Peru to Morocco. Once again, in the Casino Age, American banks were trailing after their multinational customers, not leading them.

To round out the foreign side, Henry Alexander recruited Thomas Sovereign Gates, Jr., Eisenhower's last defense secretary. They had complementary contacts: Alexander knew the corporate heads and central bankers, Gates the prime ministers and foreign secretaries. It was also hoped Gates would use his administrative talents to organize the larger, more bureaucratic bank produced by the merger.

Gates seemed a rare lateral entrant into the Morgan hierarchy but really had true-blue Morgan roots. His father was a Drexel and Company partner and president of the University of Pennsylvania. As a Drexel bond salesman in the 1930s, Tom, Jr., had apprenticed at J. P. Morgan and Company. Drawn to intrigue, he served with Naval Air Intelligence in World War II. Starting his Washington career in 1953, he served as under secretary and secretary of the navy and finally succeeded Neil McElroy as defense secretary.

Rich and affable, a cowboy in well-tailored suits, Gates gave off an easy air of authority, an engaging conviviality. A macho hero to subordinates, he loved wine, women, and warplanes. "Gates liked living and liquor better than anybody I knew," recalled an admiring associate. At the Pentagon, he was a blunt, no-nonsense manager. After receiving a bulky study arguing for the retention of a troublesome traffic light that caused congestion near a Virginia navy arsenal, Gates scrawled across the top, "Turn off the damn light."[31] He took flak as navy secretary by closing useless bases. When he closed one in Texas before consulting Lyndon B. Johnson, the future president never

forgave him and later harassed him with an FBI investigation.

As defense secretary, Gates loved covert activity. Through the National Security Council, he contributed to a four-point plan to topple Fidel Castro, an early blueprint for the Bay of Pigs disaster. He revered Secretary of State John Foster Dulles, a frequent dinner guest at the Gates household. Gates was closely involved with the U-2 spy plane and authorized its final flight, even though Ike told the CIA to stop such activity. "It was just an unbelievable thing, that U-2," he said nostalgically while Morgan chairman. "I often dream about the U-2."[32] When the plane was shot down, just before Ike's summit in Paris with Nikita Khrushchev, Gates advised the president to take responsibility. He also added to the controversy by putting U.S. forces on alert during the tense summit. "The timing of the exercise was just a shade worse than sending off the U-2 on its perilous mission two weeks before the Summit," noted Walter Lippmann.[33]

The day before his inauguration, John Kennedy was briefed by Gates, who painted an alarming picture of the imminent fall of Laos to the Communists and advocated limited American military involvement. He said it would take a couple of weeks to get American troops into Laos. An early plan had Gates being reappointed as defense secretary, with Bobby Kennedy his under secretary, and a year later Bobby would succeed him. This scheme ran into trouble when JFK's advisers pointed out an embarrassing discrepancy between Kennedy's campaign rhetoric about a U.S. Soviet "missile gap" and a Gates reappointment. When Robert S. McNamara, president of Ford Motor, got the job instead, Henry Ford II proposed a "swap"—Gates as president of Ford and McNamara as defense secretary. Gates was also asked to head General Electric. Nonetheless, he chose Morgans. "He said he was always a banker and didn't want to learn how to make toasters," said his son-in-law Joe Ponce.[34]

Gates brought an easygoing style to the bank. One subordinate remembered a meeting between Gates and Jimmy Ling, head of Ling-Temco-Vought, the acquisitive aerospace and electronics conglomerate. Gates was bubbling over in his enthusiasm for a favorite warplane, while Ling kept asking whether Morgan would finance his acquisition of Wilson Sporting Goods. "No problem, Jimmy," Gates said, then returned to his beloved warplane. When Gates at last dispatched a subordinate to Stuart Cragin, head of the Credit Policy Committee, the latter flatly turned down Ling's request and overrode the casual Gates. Morgans thus became the first Wall Street bank to stop Ling's acquisitions binge.

Gates never fully recovered from Potomac fever. He was a good friend not only of Eisenhower, who volunteered to back him for a Senate seat, but of two later Republican presidents, as well, Richard Nixon and Gerald Ford.

(His subordinates speculated as to whether the second phone on Gates's desk was a hot line to the White House.) His connections extended everywhere. He belonged to an exclusive group formed by Stephen Bechtel, Sr., of the secretive San Francisco-based construction firm and an active Morgan director after 1954. At the Carlyle Hotel, Bechtel regularly convened a study group that included Pan Am founder Juan Trippe, Texaco chairman Augustus Long, General Lucius Clay, and Gates. These brandy-and-cigar discussions might feature Bechtel on Saudi Arabia, Long on oil-price trends, and Gates on NATO and the Russian threat.[35] Gates would exploit his numerous contacts to spread Morgan influence around the globe.

WHEN Kennedy first took office, nobody could have foreseen the international thrust of banking in the 1960s. What was apparent was that the president had to staunch a massive outflow of American capital. In early 1962, Eisenhower convened a meeting of his old cabinet and Republican leaders. Tom Gates was impressed by a talk by Arthur Burns, who warned that a continuing drain of U.S. dollars and gold abroad would so badly damage the country's balance of payments that JFK would have to resort to extreme measures. Burns "believes the only thing left will be some direct controls," Gates warned Alexander. "The Administration does not wish such controls, but is drifting into a situation where they will probably be the only answer."[36] The House of Morgan braced for a new era in which American multinationals would get their financing abroad. As Alexander said, "As business goes, so goes banking."

In late 1962, Alexander, presiding over a turbulent meeting, asked a question that had not been heard for thirty years: should the House of Morgan return to underwriting, this time in Paris? In a decision that produced mild wonder at 23 Wall—wonder that the bankers kept to themselves—the Fed had passed a tentative ruling that Glass-Steagall would pose no obstacle outside the United States. But would it withstand a legal challenge? People were wary. "There was reluctance on the part of the other senior people to do something that could be seen as skating close to the edge of legality," recalled Evan Galbraith, then with the bank and later ambassador to France. "But Henry was quite visionary about it." Alexander went around the room listening to antagonistic opinions. At last, overriding objections, he said, " 'Well, I think this will be what you call a business decision.' "[37] The plan called for a new Parisian underwriting subsidiary, Morgan et Compagnie, Societe Anonyme, with Morgan Grenfell and Mees and Hope of Holland as passive, minority shareholders. (The name Morgan et Compagnie had been dormant since the Guaranty merger.) Content with its American business, Morgan Stanley spurned this first invitation to enter Europe.

On July 18, 1963, Kennedy proposed an Interest Equalization Tax to throttle the dollar outflow. By penalizing the sale of some foreign securities to American investors, it provided incentives for banks to flock abroad. Hearing the news, Alexander divined a watershed. Assembling Morgan officers that afternoon, he made a quick, prescient judgment: “This is a day that you will all remember forever. It will change the face of American banking and force all the business off to London. It will take years to get rid of this legislation.”[38] Two years later, Lyndon B. Johnson imposed voluntary restraints on lending to foreign borrowers and personally stressed their importance in White House meetings with Gates.[39] Suddenly overseas banking became the preferred career path for the ambitious.

Luckily, dollars abounded outside the United States—in part from the payments deficit itself—forming a pool of stateless money. The first Eurodollars had come into being after World War II, when the Soviet Union, wary of reprisals by American authorities, deposited its dollars at the Banque Commerciale pour l’Europe du Nord in Paris and in London’s Moscow Narodny Bank. In time, *Euro* came to signify any currency held outside its country of origin. In other words, Eurodollars are dollars held outside the United States, Euroyen are yen held outside Japan, and so on. By the mid-1980s, this free-floating unregulated market—a free marketeer’s pipe dream—would swell to $2.5 trillion in deposits.

A wholesale world catering to big business, governments, and institutions, the Euromarkets were immediately congenial to the House of Morgan. Here banks didn’t pay deposit-insurance premiums on dollar deposits or set aside mandatory reserves against deposits; they could lend dollars as freely as they pleased. Conditioned by New Deal legislation, American bankers were initially edgy about this freedom but soon adapted. Along with the new trend of buying money instead of gathering deposits, the creation of the Euromarkets lifted restrictions on growth. If the Fed tightened credit in the United States, banks could sell large CDs in London and use Eurodollars to finance their domestic lending.

The New York banks doggedly fought to retain these privileges. At one point early in the Johnson administration, Washington tried to stop American banks from keeping Eurodollar accounts in branches abroad. An assistant Treasury secretary named Paul Volcker invited Morgan’s head of international banking, Walter Page, and others to Washington for comment. The bankers delivered a stern warning. “We said it was the end of the American banking system,” recalled Page. “You will throw us out of Europe and Singapore and Japan. And, my God, Paul that evening rewrote the whole basis with me. He got it all done before you could say Jack Robinson.”[40] The regulation was dropped. In Volcker, Morgans had its paladin for the next twenty-five years.

While Morgan Grenfell dozed, that perennial London iconoclast, Siegmund Warburg, sponsored the first Eurobond issue for the Italian *Autostrade* in 1963. Morgan's new Paris subsidiary was an early star in this market. Since the Guaranty merger provided duplicate Paris offices and an embarrassing surplus of mansions, Morgan kept its place Vendome branch, while the new Morgan et Compagnie, S.A., moved into the chandeliered Guaranty branch at 4 place de la Concorde near Maxim's. Once called the Hotel de Coislin, the building was a national monument. In it, Benjamin Franklin signed the treaty with France recognizing U.S. independence, and Chateaubriand wrote his romances. During World War II, it was occupied by the Gestapo. From its glittering interior, the House of Morgan would launch its assault on global securities markets.

Besides opening up the Paris operation, the new Euromarkets provided a chance for the Morgan banks to expand their relationship with the Vatican. During the 1950s, almost all Vatican funds in New York were managed by the J. P. Morgan Trust Department, just as almost all Vatican funds in London were under Morgan Grenfell's supervision. In the late 1950s, after the retirement of Bernardino Nogara—the mysterious, powerful creator of the Special Administration of the Holy See—the House of Morgan lost its foremost papal ally. To fortify the relationship, Morgan Guaranty, Morgan Grenfell, and Morgan Stanley joined with the Vatican in 1963 to form a Rome investment bank called Euramerica. The Vatican was financially rich and innovative in the 1960s—it controlled Immobiliare Roma, which built the Watergate Hotel in Washington—and Euramerica was supposed to be the first American-style investment bank in Italy.

The new operation was managed by Dr. Nicola Caiola, whose father headed a prewar Vatican trade department and who himself grew up in Vatican City. After working as a junior stock analyst under Nogara in the late 1940s, he got a Banca d'Italia fellowship and apprenticed at J. P. Morgan and Company and Morgan Stanley in the early 1950s. While Caiola was visiting Rome in the early 1960s, the Vatican expressed interest in sharing an investment bank with the Morgans; Caiola returned to the United States to prepare a blueprint. Morgan Guaranty and Morgan Grenfell leapt at the chance, but Morgan Stanley, which then had a curiously provincial and complacent attitude toward the outer world, joined in only reluctantly. On the eve of Caiola's departure for Rome, Harry Morgan summoned him and said, "Remember, it took us a long time to establish our name. Our name is now in your hands."[41]

The Vatican took a one-third interest, and the Morgan houses another third, while the remainder was divided among Italian companies. Despite its weighty Vatican patronage, Euramerica was a swinging operation, a Euromarket pioneer. Although based in Rome, it did dollar financing and

challenged the investment banking monopoly of Italy's omnipotent Mediobanca. It was profitable every year until 1971, when the Morgans bowed out because they faced a conflict of interest with their thriving Paris operation.

Meanwhile, in Paris, Morgan et Compagnie, S.A., made what looked like an extremely auspicious debut. In February 1963, it launched a Euroequity (stock) issue for Germany's largest mail-order house, Neckermann, which owned twenty-three department stores. In taking his company public, founder Josef Neckermann planned to retain a majority interest. Friedrich Flick, possibly Germany's richest man, the scion of a steel family and a convicted war criminal, wished to sell his Neckermann stake. Neckermann feared that these shares would fall into the hands of German banks, which are permitted to hold industrial stakes. He was particularly eager to bypass Deutsche Bank, Germany's largest, which controlled a veritable industrial empire. Neckermann favored global syndication, with only a small portion of the shares allotted to Germany.

For the new Paris operation, the Neckermann issue seemed a smashing success. Morgans bought the $30-million issue, then turned around and resold it to Belgian, Swiss, and Dutch banks. In London, where Morgan Grenfell led a large purchasing group, the issue shot up to a premium. Said Evan Galbraith, then a leading Morgan man in Paris: "It was the first internationally marketed issue. People saw you could distribute something on an international basis."[42] There was one telltale hint of trouble, however. When Morgans sent out the offering by telex, German banks didn't answer. When Deutsche Bank then complained about the issue's being sold outside Germany, Galbraith said Morgans was simply heeding the client's wishes. He didn't quite fathom the depth of anger he had aroused or how deeply he had offended tradition. Deutsche Bank would bide its time and get even in extremely dramatic fashion.

Though extraterritorial in nature, the early Euromarkets were riled by fierce nationalistic clashes. Except in the Eurodollar market, banks expected to lead issues denominated in their own currencies. (The U.S. Treasury even briefly insisted that American firms lead Eurodollar issues.) The now-swaggering Morgans came up against this parochialism when it tried to invade the most sacred banking monopoly of all—that of Switzerland. Crédit Suisse, Swiss Bank Corporation, and Union Bank of Switzerland formed a cartel that dominated Swiss franc issues, and outside banks defied them at their own peril. The Morgan Paris operation did just that in September 1963, when the city of Copenhagen wished to raise money and its treasurer consulted friends at Morgan Grenfell. As Tim Collins of Morgan Grenfell, recalled, "Somebody had the bright idea that since interest rates were low in Switzerland, why not

denominate the issue in Swiss francs?”[43]

This time, Galbraith warned 23 Wall Street to expect an angry response, though nobody quite expected the furor that erupted. “The Swiss banks went bananas,” said Galbraith. “They called up Henry Alexander and said, ’You can’t do this. Swiss francs are *not* an international currency. They should be controlled by the Swiss. . . . Henry was swamped with phone calls, threatening all sorts of things.”[44] The Swiss government told Washington that if further flotations occurred, they would convert dollars into gold and sink the dollar. They refused to let their money function as an international currency. They also pressured the Bank of England. “There was a *froideur* between the Bank of England and the Swiss central bank for some time,” recalled Collins.[45] The ill-fated Copenhagen issue was both the first and the last Swiss-franc Euroissue for a generation.

Meanwhile, the Germans still smarted from the Neckermann issue and awaited a chance to retaliate. When Morgan et Compagnie, S.A., announced an issue for another German mail-order house, Friedrich Schwab and Company, Deutsche Bank saw its golden opportunity for revenge. Instead of obtaining written contracts from underwriters, Morgans proceeded with far more tenuous “indications of interest.” This would prove a fatal mistake. The firm also enlisted a small German trade-union bank that would prove too weak to stop the coming onslaught. Once the issue was announced, Deutsche Bank sprang its power play, putting intense pressure on banks around the world not to participate. It was a full-scale disaster for Morgans, which had to swallow $9 million worth of the $13-million stock issue, a huge amount for those days. The New York office was stunned.

The passive partner, Morgan Grenfell, was very upset by the brash “American” way in which the Morgan Guaranty people had conducted themselves. Under U.S. law, 23 Wall couldn’t pump in more capital, and Morgan Grenfell had to organize a temporary rescue among London’s merchant banks—an act for which it felt itself insufficiently appreciated by its American cousins. The Paris operation was later bailed out when Singer Company chairman Donald Kircher, who sat on Morgan Guaranty’s board, bought Schwab for $16 million.

In the meantime, another complication arose, deepening the sense of disaster in Paris. The SEC ruled that Morgans couldn’t both act as a trustee for companies in New York and underwrite for them in Paris. This was the last straw: Morgan Guaranty withdrew from running the Paris operation. “John Meyer, head of international operations, was very downhearted as a result of the Schwab deal,” recalled Galbraith.[46] Shattered by the Schwab affair, Morgan Guaranty wouldn’t return to Euromarket issues for more than a decade. For a bank so surefooted in foreign markets in the 1920s, it was a

crushing defeat and left a legacy of self-doubt in securities work.

Enter Morgan Stanley, then a bit belatedly discovering the Euromarkets. While Henry Alexander had busily set up operations around the world, Morgan Stanley still lacked a single European office. It began to shed its insularity in 1966, when Bill Sword and Frank A. Petito made a secret trip to Rome and met with Guido Carli, head of the Banca d'Italia. Petito, born in Trenton, New Jersey, was the first Italian-American partner at Morgan Stanley and had always been a potential secret weapon in Italy. But he didn't speak Italian, and the aging, aristocratic Giovanni Fummi, who still advised the Morgan houses in the 1950s, scoffed at him as a peasant.

The imaginative Petito had an inspiration. From Italian exports and overseas remittances, Carli had stored up $4 billion in excess dollars. Petito suggested that Morgan Stanley's big clients in Italy—Exxon, General Motors, and Du Pont—could borrow in liras and convert them into dollars the same day, relieving Carli of his excess. Carli was delighted and swore Morgan Stanley to silence about this exclusive deal. In two whirlwind months, Morgan Stanley did $600 million worth of the secret lira loans, whetting the firm's appetite for European work and building its reputation for finding pockets of money buried around the world.

In January 1967, Morgan Guaranty brought in Morgan Stanley to run the ailing Paris operation, selling it two-thirds of the business; it retained a one-third share with Morgan Grenfell, the Dutch firm of Mees and Hope, and the Wallenberg family's Enskilda Bank of Stockholm. The one-third stake was patterned after Morgan Guaranty's one-third stake in Morgan Grenfell. Petito was willing to give Morgan Guaranty half the Paris operation, but the bank's confidence was shattered after the Schwab debacle, and it preferred a minority share.

For this new Morgan et Compagnie International, the old crew was pushed out and a more seasoned Morgan Stanley group under Sheppard Poor came in to run it. Their advent coincided with a Eurobond boom. Once Morgan Stanley shook off its insularity and discovered the outside world, it made a spectacular success in Paris, financing Standard Oil of New Jersey, U.S. Steel, Eastman Kodak, Texaco, American Tobacco, Procter & Gamble, Amoco, and so on. As the lugubrious atmosphere waned, the Paris venture surpassed all rivals. By 1975, it would issue $5 billion in yearly offerings.

With Morgan et Compagnie International, the Morgan community of interest evolved into a more direct fusion of overseas securities work. Without fanfare, the House of Morgan was being welded back together. It was a loose partnership. Morgan Guaranty's involvement in Paris was passive, one of many minority stakes it held, and John Meyer, Jr., saw it mostly as a way to avoid having to refer clients to Chase or First National City for Eurobusiness. Yet whatever its limitations, Morgan et Compagnie International represented

partial repeal of Glass-Steagall.

At 23 Wall, it hurt Morgan Guaranty to hand over the Paris reins to Morgan Stanley. The Morgan Stanley people felt Morgan Guaranty never delivered the promised clients, while Morgan Guaranty always sensed inadequate gratitude for having launched Morgan Stanley abroad. (The Morgan houses were always amazingly thin-skinned with each other.) It was a turning point for Morgan Stanley, which gained a critical foothold in Europe. It sent "revolvers" to Paris, who got international seasoning. Morgan Stanley proudly applied its new Morgan et Compagnie label to all overseas issues except those of Australia. In those days, it never dawned on Morgan Guaranty that it was breeding a competitor or that it would emerge as a rival investment bank of Morgan Stanley in the 1980s.

Morgan Guaranty kept one piece of European business all to itself. In 1968, it started Euro-clear in Brussels, the largest clearing system for Eurosecurities and the first to automate the market. Initially it aroused powerful, paranoid resistance from European banks, which thought their inner secrets would be divulged to the House of Morgan. The genius of Euro-clear, in fact, lay elsewhere. It became enormously lucrative because traders left in the system money that could be lent to other participants, who used their Eurobonds as collateral. Morgan Stanley was never invited to share in the Brussels operation. The community of interest among the Morgan banks was always a community of convenience. Whenever one bank dug up buried treasure, it hoarded it and tried to keep it from its Morgan brethren. Hence, this era of collaboration among the Morgan banks, far from bringing them closer together, would eventually drive them apart, breeding mutual suspicions and accusations of double-dealing. Their relations would end up having the special rancor of a family feud.

JAPAN was the country that produced the most persistent friction between Morgan Guaranty and Morgan Stanley. Outside Europe and North America, finance ministers frequently assumed Morgan houses were closely affiliated and constituted a *de facto* House of Morgan. This confusion was most pronounced in Japan, which had its own conglomerates, or *zaibatsu*, organized around core banks. "Every time they wrote about us in the Japanese newspapers," recalled Jack Loughran of Morgan Guaranty, "they would refer to the Morgan *zaibatsu* that controls General Motors and U.S. Steel."[47]

For a long time after the war, the problem seemed academic as Japan emerged slowly from its defeat. When Tokyo's stock exchange reopened in 1949, it was a small, provincial affair. During the occupation, General Douglas MacArthur reformed Japanese finance along American lines and even authorized a Glass-Steagall equivalent, Article 65, separating banking

and securities work. MacArthur wanted to splinter and neutralize the *zaibatsu* that had dominated interwar Japan and cooperated with the military in their East Asian conquests. Briefly, Japanese banks took on neutral occupation names. When the Americans left, Mitsubishi, Sumitomo, and the others reverted to their traditional names. During the occupation, four American banks—National City, Bank of America, Chase, and Manufacturers—set up branches to serve military personnel. After admitting American Express for traveler's checks, the Ministry of Finance halted further foreign penetration, and the "bamboo curtain" descended.

As their economy rebounded in the early 1950s, the Japanese wanted to reinstate their spotless credit reputation and make good on old Morgan-sponsored debt—the 1923 earthquake loan and the 1930 gold-standard loan—on which they had stopped payment after Pearl Harbor. Boasting that they hadn't defaulted in two thousand years, they made a great ceremony of resuming payment and refurbishing their Morgan ties. After Japan signed the peace treaty with the United States in 1951, a Ministry of Finance official came to 23 Wall saying, "I have come to honor my signature."[48] With help from Smith, Barney and Guaranty Trust, Japan serviced its bonds in full, and two Smith, Barney officials were decorated by the emperor.

J. P. Morgan and Company had always been proud of its preeminence in Japan. The bank would cite decorations bestowed by Emperor Hirohito upon Jack Morgan, Tom Lamont, and Russell Leffingwell. But in the 1950s, its scant resources were exhausted by England and France, and it couldn't re-create its special relationship with Japan. This began to change after the merger with Guaranty, which had been a major trustee for Japanese government and electric-utility bonds. It was also a Wall Street training ground for many Japanese bankers, who went home and copied its forms for their own banks.

The two banks had another advantage in pursuing Japanese business—a virtual monopoly in American depositary receipts or ADRs, which were invented by Guaranty Trust back in 1927. ADRs permitted American investors to buy foreign stocks in the United States with a minimum of difficulty. They would actually buy receipts against shares held in a foreign bank vault. The coopera-ting American bank would convert dividends into dollars and spare the investor foreign-exchange problems. In the spring of 1960, Regis Moxley of Morgan Guaranty, an evangelist for ADRs, visited Japan to preach their virtues. Afraid ADRs would breach the nation's capital controls, the Ministry of Finance warily consented to an ADR for Sony, the first ever for a Japanese stock. Setsuya Tabuchi, chairman of Nomura Securities, later said, "If there was a single milestone in the internationalization of the Japanese financial market, it came in 1961 when

Sony issued American depositary receipts in the U.S."[49]

As with Schwab, Morgan Guaranty, long absent from foreign markets, inadvertently stirred up local ire. With ADRs, Morgans had to assign a foreign bank to hold the actual shares while it issued tradable receipts in New York. Naively hoping to spread business democratically among Japanese banks, Moxley tapped the Bank of Tokyo as custodian for Sony's ADR. He didn't realize that as Sony's principal banker, Mitsui would resent encroachment on its territory. An incensed Mitsui delegation appeared at Morgan's doorstep to protest this serious violation of protocol. "They almost chopped my head off," declared Bob Wynn of Morgan Guaranty. When the bank issued ADRs for Toshiba, Hitachi, and Fuji Iron and Steel, it didn't repeat the error.

In the 1960s, Morgan Guaranty decided to pierce the bamboo curtain and upgrade its representative office into a Japanese branch—extremely difficult at the time. It faced a terrible handicap because of Morgan Stanley's attitude toward the country. Morgan Stanley had mostly confined its foreign dealings to tried-and-true Western clients—Canada, Australia, France, and Italy. Spoiled by its rich American clientele, it was more ambivalent about foreign markets than was Morgan Guaranty. The problem was compounded by the fact that several partners were war veterans and openly antagonistic toward Japan. This attitude didn't matter in the 1950s, when Japan was still poor and borrowed heavily from the World Bank. Later in the decade, however, World Bank president Eugene Black told two Ministry of Finance representatives that a rejuvenated Japan had outgrown the World Bank and should tap Wall Street on its own. When they asked Black whom they should see, he handed them—just by coincidence—a World Bank prospectus with First Boston and Morgan Stanley on the top.

Preparing for a large metropolis of Tokyo issue, the Japanese went first to First Boston and were so impressed that they accepted them as co-managers. Expecting equally considerate treatment at Morgan Stanley—wasn't the House of Morgan Japan's honored friend?—they were coldly and uncivilly rebuffed. "The old-timers in the Ministry of Finance were really horrified," said Morgan Guaranty's Loughran, who had to deal with the unpleasant consequences for 23 Wall.[50]

Why did Morgan Stanley spurn Japan? The decision contained elements of both business calculation and xenophobia. Morgan Stanley still held to an unswerving policy of managing securities issues alone or not at all, a lucrative form of snobbery that allowed the firm to pocket all management fees. Barging in blindly, the Japanese didn't realize that their casual decision to accept First Boston first made it impossible for Morgan Stanley to participate without violating its cardinal rule. The sole exception it had made was for the

World Bank itself, which doubtless misled the Japanese.

Why didn't it make another exception? "The prestige of being banker to the World Bank was regarded as greater than being banker to a defeated country," explained former Morgan Stanley partner Alexander Tomlinson. "The Japanese didn't realize what a sensitive subject it was for us. The partners involved in the war weren't enthusiastic about doing business in Japan anyway. And the older partners had deeply resented the attack on Pearl Harbor. They had a personal relationship with Japan that they felt had been offended."[51] Also, in Western eyes, Japan seemed less of a full-fledged industrial power than a superior version of a developing country. In the early 1960s, it was still the second most heavily indebted country in the world, after India.

Whatever the business rationale, the Morgan Stanley decision was laced with a subtle racism, for similar objections never stopped the firm from doing business with Italy or Germany. "The Germans somehow converted themselves into nice guys," an ex-partner said cynically. "All the Nazis seemed to have been purged." At the time, a single Morgan Stanley partner could blackball a major decision. One partner who was a former fighter pilot made rabble-rousing patriotic speeches invoking Hirohito, Pearl Harbor, the sale of war bonds, and so on. To this day, Perry Hall is unrepentant about the decision: "I wouldn't do business with the Japanese even now."[52] Although younger partners thought the older ones a bunch of stubborn fools, the latter wouldn't budge.

This intransigence was a big problem for J. P. Morgan and Company, which was then trying to wrest big balances from Japan's Ministry of Finance. Fearing fallout from Morgan Stanley's insult, international chief John Meyer had long, angry talks with his close friend John Young, who was Morgan Stanley's senior partner for foreign business. The problem acquired new urgency for Morgan Guaranty after a September 1964 meeting in Tokyo. Morgan Guaranty director, Steve Bechtel, Sr., and his friend General Lucius Clay, former military governor of Germany, prevailed on Meyer to try to open a Japanese branch. Bechtel said Tokyo was becoming a world information capital. More to the point, his own firm planned to open an office there—always strong inducement for Morgans to follow. A decision was made to open a Japanese branch as part of Morgan's strategic blueprint to establish branches in major world markets and end its Eurocentric bias.

Japan was then far more closed than it is today, and no bureaucrat cared to accept the political stigma of admitting Morgans. The government felt there were enough foreign banks; approving more was extremely sensitive business. In 1965, Tom Gates, who had fought at Iwo Jima and Okinawa, made an initial presentation for a branch license to Michio Mizuta, Japan's

foreign minister. Even with the Japanese, Gates had a straightforward style; skipping ceremony, he bluntly asked for a branch. Far from settling anything, this meeting was the opening round of a long, dreary battle. For all the bowing and deference to the Morgan name, the Japanese made the bank grovel for twenty-nine months. The Finance Ministry laid down two rules: Morgans couldn't discuss the negotiations with the U.S. embassy (honored) or with a lawyer (flouted). The talks sometimes seemed to be endurance contests, conducted by the Japanese in an elaborate language of shrugs, sighs, and veiled allusions to nameless difficulties.

The bank deployed many emissaries and sent international head John Meyer, Jr., for early talks. Meyer, who would follow Gates as Morgan Guaranty chairman in 1969, was the most austere and humorless of the postwar bank chairmen. Tall and granite-hard, he had a bald domed head and huge bushy eyebrows, which the Japanese interpreted as the sign of a great samurai spirit. He seldom smiled as he puffed watchfully, enigmatically, on his pipe. With his elephantine memory and vast experience, he always seemed several steps ahead of everybody else, and his thoroughness at the House of Morgan was legendary. Having started at the Guaranty Company in 1927, he could remember obscure details of railroad bonds from forty years before.

Unlike the charming Henry Alexander and Tom Gates, Meyer made subordinates feel uneasy. Borrowing an old trick from FDR, he would assign more than one person to the same task, although he often knew the answer in advance. He would pretend to defer to the judgment of some young banker on a giant loan, then watch the young person squirm. He had an incomparable mastery of detail that some colleagues found counterproductive. "He would read every last word of a credit report on a tiny $9-million loan to Ireland," said a former colleague.

Meyer carried Morgan secrecy and discretion to new lengths. Despite a vast awareness of political developments, he had the lowest public profile of any Morgan chairman. Constantly absorbing financial intelligence from around the world, he was thick as thieves with Arthur Burns, Fed chairman after William McChesney Martin, and they had long phone talks each Sunday. "Meyer should have been in the CIA," remarked an admiring former associate; "he was a real inside man, with a style of quiet influence." With Meyer, the Morgan bank would no longer exercise the visible Wall Street leadership that had come so naturally to his predecessors.

A man of legendary strength, Meyer's idea of a happy weekend in Tokyo was climbing Fujisan. He was capable of outlasting even the Japanese. Each time that Meyer in New York would ask Loughran in Tokyo what he needed, Loughran would cable back, "Patience, patience, patience."[53] The patience would be rewarded: Morgan Guaranty became the first American bank since 1952 to win branch approval and penetrate the bamboo curtain.

In breaking through Japan's *cordon sanitate*, Morgan negotiators profited unexpectedly from history. Some Finance Ministry old-timers remembered Tom Lamont. Of even greater help was the memory of a beautiful, fated *geisha*. In 1904, Pierpont Morgan's nephew George Morgan, living in Yokohama and collecting Japanese art, married Yuki Kato. Although George's friends told reporters, "I understand that the young lady he has married comes of an excellent family," George had actually bought out the contract of a young *geisha*.[54] During their honeymoon in Newport and on Long Island, Yuki Morgan was ostracized by George's family, and the couple ended up living in Paris. When George died, in Spain in 1915, his wife inherited his wealth.

Yuki's trust fund was administered by J. P. Morgan and Company, which was unable to send her payments during World War II. Afterward, Henry Alexander went to Cologne as vice chairman of the U.S. Strategic Bombing Survey Committee. He tracked her down and gave her not only the accumulated interest but interest on the interest as well. When Yuki later moved back to Kyoto, she told her neighbor, "You always must trust the Morgans."[55]

On March 24, 1969, the day the Morgan branch finally opened in Tokyo, one of Yuki's Kyoto neighbors traveled in to deposit her life savings of Y 8 million (by this point, Yuki was dead); the neighbor was gently told that Morgans wasn't that kind of bank. Adding to Yuki's fame was a musical based on her life, which depicted her pining for a young student as she was signed over to George Morgan. When Morgan negotiators made the rounds in Tokyo, staid bureaucrats would stop to ask about Yuki Morgan. "The Japanese are very sentimental," explained Morgan's Loughran, "and everybody over forty knows the story."[56]

Another arrow in the Morgan quiver was Aisuke Kabayama. As the prewar Count Kabayama, he had squired Tom and Florence Lamont around Tokyo and in the 1930s had helped Lamont set up an information bureau. After the occupation, he had to renounce his title; now he would be an elite Morgan adviser. Employed by the new Morgan branch, he could perform no prosaic mortal labors but only advise. Even without his title, his noble identity was well-known, and he could get an appointment with anybody from Emperor Hirohito on down.

In its quest for a branch, the House of Morgan had had one last weapon, a man of indeterminate nationality known as both Satoshi Sugiyama and David Phillips. In the 1950s, John Phillips, an American professor working with the U.S. Air Force in Japan, befriended a Mr. Sugiyama of the Asahi newspapers, who wanted an American education for his son Satoshi. (An American education then inspired veneration in Japan.) Phillips adopted the boy;

rechristened David Phillips, he lived for thirteen years with the Phillips family in Long Beach, California. He studied Japanese daily. After graduating from Berkeley, he worked in New York for Morgan Guaranty's stock-transfer unit. Then the Immigration and Naturalization Service challenged his adoption and threatened to deport him; Davis, Polk lawyers contested in vain. So in 1964, David Phillips, *né* Sugiyama, was posted to Morgan's representative office in Tokyo.

The deportation had unexpected consequences within the Morgan empire. While Phillips started as office manager, he was soon caught up in the secret lobbying for the Morgan branch. As he said, "Because of my Japanese face, the Japanese press would never question why I was going into the Ministry of Finance all the time."[57] With no real bank training, he was good at scouting out new business and didn't mind going out nightly on the Ginza, Tokyo's main commercial district. He was a perfect Morgan hybrid—a fully bilingual, bicultural man who wore expensively tailored suits and cuff links and smoked Dunhills.

44. Jack Morgan dandling circus midget Lya Graf during the 1933 Pecora hearings. The stunt humanized Jack's image but deeply scarred him.

45. Russell C. Leffingwell hunting on the Devonshire moors with his wife and daughter, 1927. Leffingwell was the lone Morgan partner to foresee a financial crisis in 1929.

46. The 1929 crash at Broad and Wall streets. This photo reveals several flappers and a surprising number of young people.

From the Grenfell family album

47. The dapper Edward C. (“Teddy”) Grenfell with Jessie Morgan and her two daughters, Jane and Frances

48. Jack Morgan and Captain Porter aboard the *Corsair* off Nassau in the Bahamas

49. Jack and Jessie Morgan (at Jack’s right) and Teddy Grenfell aboard the *Corsair* with a Mr. Gardiner and a Miss Williams. The House of Morgan was known as a white-shoe bank.

The central bankers

50. The bearded Montagu Norman of the Bank of England greeting Dr. Hjalmar Schacht of the Reichsbank at Liverpool Street Station, December 1938. Hitler fired Schacht a month later.

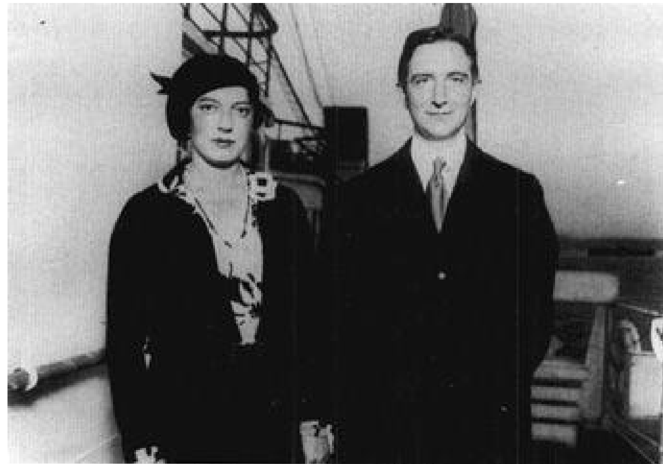
51. Junnosuke Inouye, governor of the Bank of Japan and finance minister. Inouye was murdered by a nationalist fanatic in February 1932.

52. Teddy Grenfell, who became a Bank of England director a year after he became a Morgan partner The Depression hearings

The Depression hearings

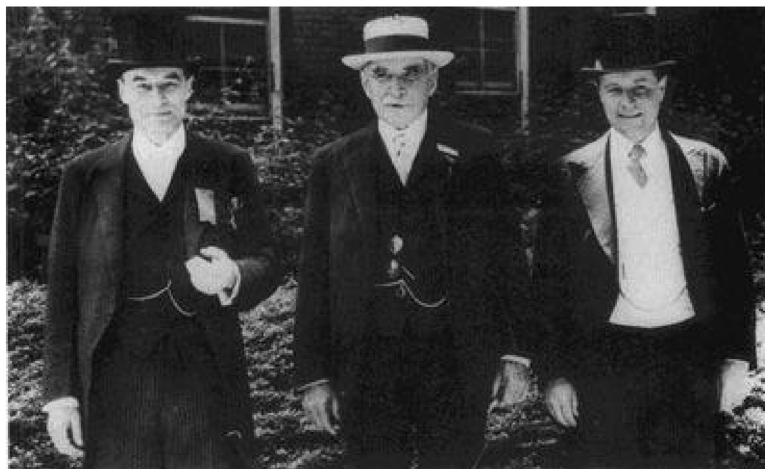
53. Counsel Ferdinand p’ecora (left) eyeing his quarry, Jack Morgan. Senator Carter Glass, in hat, scoots between them.

54. Tom Lamont, George Whitney (center), and Jack Morgan huddling during the Nye “merchant-of-death” hearings on morgan involvement in world war I, January 1936



55. S. Parker Gilbert returning from Berlin in 1930 after retiring as agent general for Germany, with his wife, Louise, who later married Harold Stanley. Their son, S. Parker, Jr., chaired Morgan Stanley in the 1980s.

56. Lady Nancy Astor, right, and her son William Waldorf entertain the Henry Fords at Cliveden. Several Morgan partners sympathized with the Appeasement sentiments of the Cliveden set.



57. Jack Morgan at the 1939 Harvard commencement exercises with his sons. Junius (left) remained with J. P. Morgan and Company; Harry was a founder of Morgan Stanley.

58. Harold Stanley (left), George Whitney, and Russell Leffingwell (right) at congressional monopoly hearings in 1939. Whitney's hair has turned white since his brother's scandal.

The Richard Whitney

59. Richard's wife, Gertrude, at the Whitneys' New Jersey estate during a hunt of the Essex Fox Hounds.

60. George Whitney, who survived his brother’s embezzlement to become chairman of the Morgan bank in 1950

61. Richard Whitney entering Sing-Sing to serve a five- to ten-year sentence for grand larceny. Note Whitney’s pocket handkerchief.

World War II

62. King George VI and Jack Morgan sip tea at the embassy garden party in Washington, June 1939.

63. Jack Morgan greets “war babies” at a Manhattan pier in July 1940. Beside him are eleven-year-old Lord Primrose and six-year-old George Vivian Smith, grandson of Morgan Grenfell’s Lord Bicester. The two boys spent the early war years at Jack’s estate.

The 1950s

64. Judge Harold Medina, who supervised the antitrust trial against seventeen leading investment banks. The judge’s humor enlivened a dreary ordeal.

65. Perry Hall, the towering figure at Morgan Stanley in the 1950s

66. Texan Robert Young lifting his arms in victory after his successful 1954 fight for the New York Central. He is seen here with Lila Acheson Wallace of the *Reader’s Digest*, whom he made a director of the railroad.

67. A 1955 dinner in New York. Vice-President Richard M. Nixon chats with Fed chairman William M. Martin (second from right) and Viscount William Harcourt (far right), a Morgan Grenfell partner then serving as British economics minister in Washington. At far left is Rudolph Smutny of the Investment Bankers Association.

68. Morgan Guaraniv chairman Henry Clay Alexander (left) as he tried to mediate the 1962 dispute between President Kennedy and U.S. Steel chairman Roger M. Blough (center) after the latter raised steel prices

69. Frustrated by his slow rise at Morgan Stanley, Robert Baldwin (right) served as navy under secretary from 1965 to 1967. He is sworn in by Rear Admiral Wilfred A. Hearn and Navy Secretary Paul H. Nitze (center).

70. Bob Greenhill of Morgan Stanley, the first takeover star of the new Wall Street, wearing his trademark suspenders.

71. Antonio Gebauer, head of Morgan Guaranty’s Latin American lending in the early 1980s and later at the center of an embarrassing scandal

Morgan Grenfcll

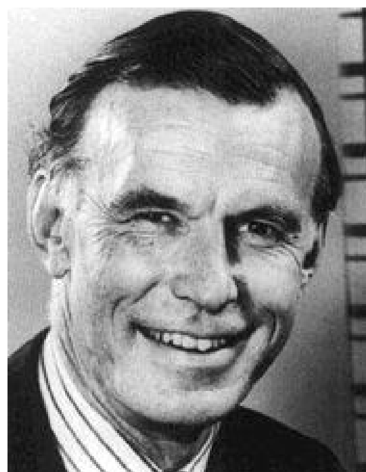
72. The partners’ room of Morgan Grenfell. In this pre-Guinness photograph, Lord Stephen Catto, chairman of the holding company, sits between joint chairmen Christopher R. Reeves (right) and Charles F. M. Rawlinson.

73. 23 Great Winchester Street, home of Morgan Grenfell since the 1920s

The Guinness affair

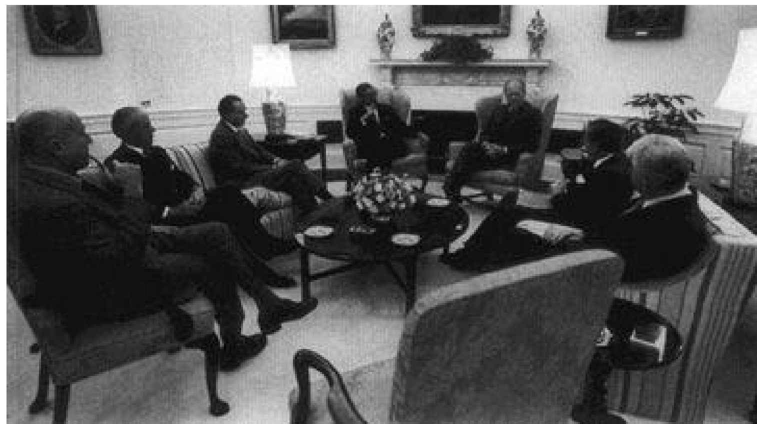
74. As chief adviser to Guinness, Roger Seelig led Morgan Grenfell into the worst scandal in the firm's history.

75. Chairman Bill Mackworth-Young, whose untimely death, in 1984, set Morgan Grenfell up for the scandal



76, *77.* Margaret Thatcher demanded the heads of Christopher Reeves (left), chief executive, and Graham Walsh, corporate finance chief.

The modern House of Morgan



78. White House meeting on the New York City fiscal crisis in 1975. From left to right: L. William Seidman, President Ford’s economic assistant; Ellmore C. Patterson, Morgan chairman; Walter Wriston, Citicorp chairman; Treasury Secretary William Simon; President Gerald R. Ford; Chase chairman David Rockefeller; and Fed chairman Arthur Burns

79. Dennis Weatherstone, the London transport-worker’s son who rose to the top of the House of Morgan

80. Lewis T. Preston, the tough, witty ex-marine who steered the Morgan bank back toward investment banking

81. 60 Wall Street, the new Morgan bank headquarters; more space and computers, but less poetry and mystery

The advent of Phillips helped Morgan Guaranty solve its Morgan Stanley problem. To overcome any lingering Japanese doubts about the Morgan banks, John Meyer kept urging John Young of Morgan Stanley to open a Tokyo office. With the imposition of U.S. capital controls, Morgan Stanley needed to find money around the world for its clients, and Japan was becoming too big to ignore. So in 1970, Morgan Stanley agreed to set up a Tokyo representative office on two conditions—that it get space adjoining a new World Bank liaison office in Tokyo and that David Phillips head the office. Morgan Guaranty obliged on both counts.

So remarkable was Phillips's work for Morgan Stanley that in 1977 he became its first nonwhite managing director. He always surprised new clients. "I've been with David a few times when we are meeting clients," said Morgan Stanley's Bob Greenhill, "and you can just see their jaws drop."[58] Phillips signed up Hitachi, Mitsubishi, Industrial Bank of Japan, and Nippon Steel. He won a large private placement from Sony despite competition so feverish that Goldman, Sachs reportedly asked Henry Kissinger to talk with Sony chairman Akio Morita. Yet as much as Morgan Guaranty people admired Phillips, they

watched with dismay as he exploited the old confusion about the Morgan *zaibatsu.* Morgan Guaranty, for instance, had floated a convertible Eurobond issue for Takeda, a Japanese pharmaceutical company. Yet after the senior Takeda died, his son took a bond issue to Morgan Stanley, thinking he was rewarding an old friend. David Phillips, thought the Morgan Guaranty people, didn't always clear up such misconceptions.

Business for the new Morgan Guaranty branch was extremely profitable, with huge profit margins on loans. The bank made yen loans to American multinationals in Japan and dollar loans to Japanese companies, including Hitachi, Toshiba, Nippon Steel, Honda, and Nippon Tel and Tel. Both Morgan houses targeted the Mitsubishi group, which stressed shipping and heavy industry and meshed with Morgan's smokestack orientation. As a purveyor of clothing and other army provisions, the Morgan bank's prewar favorite *zaibatsu*, Mitsui, hadn't fared as well after the armistice.

What made Japanese business irresistible was that dollar loans to companies were guaranteed by their Japanese bankers. In 1976, Ataka and Company, Japan's third largest trading house, failed after taking losses on a Newfoundland refinery; Morgans had a loan outstanding to Ataka. The morning he received the news, Bob Wynn called Lew Preston, head of international banking, and said, "Lew, it looks like you've got your first loss in Japan." Before the day was over, however, the Bank of Japan stepped in and ordered Ataka's principal banker, Sumitomo Bank, to bail the company out. That afternoon, an astonished Wynn called Preston back to say their unsecured loan would be honored after all. "Why the hell are they doing that?" asked a bewildered Preston. "They've got their marching orders from the government," Wynn replied.[59] In this banker's paradise, Morgan Guaranty would steadily expand its country lending limit. Nobody ever regretted the marathon ordeal of acquiring the Tokyo branch.

CHAPTER TWENTY-EIGHT
TABLOID

ALTHOUGH Glass-Steagall had supposedly banished banks from the securities markets, the House of Morgan and other Wall Street banking firms exerted a major impact on the stock market through their trust departments. Despite their unequal size, J. P. Morgan and Company and Guaranty Trust brought $3 billion apiece in trust assets to their merger, forming America's biggest trust operation. Morgan's money was mostly in pension funds and Guaranty's in personal trusts. The merged bank also provided "corporate trust" services that formed the infrastructure for much stock trading on Wall Street. As transfer agent for nearly six hundred companies, it received over twenty-five thousand certificates daily and sometimes handled a quarter of all shares traded on the New York and American stock exchanges. It mailed out twelve million dividend checks a year and maintained updated shareholder lists for many companies.

The old House of Morgan had commanded a sizable portfolio for its own account, but it was a less-than-scientific operation. Allied with the Guggenheims and the Oppenheimers, it gambled 30 percent of its entire portfolio on copper stocks in the early 1930s. Before 1940, the bank offered investment advice informally to wealthy individuals and old families. Partners managed money for their pet institutions, such as Dwight Morrow for Amherst College, Tom Lamont for Phillips Exeter Academy, and Russell Leffngwell for the Carnegie Corporation. The House of Morgan was always a magnet for ecclesiastical institutions, which shared its discretion and somber dignity. In 1917, Jack Morgan contributed start-up money for the Episcopal church's pension fund, and the bank always handled part of that money. Under Henry Alexander, the Presbyterians also switched their money to the Morgan Trust Department.

Eligible for trust work after the 1940 incorporation, the bank converted Jack Morgan's mirrored, marble-walled barber shop into a waiting room for patrons. The first objective was to snare estates of the rich and recently dead. This required patience, waiting until a sufficient number of clients had died. After a dinner spent wearily sifting through names of potential chieftains, George Whitney turned to a young associate, Longstreet Hinton, and said apologetically, "Street, I guess you're it."[1] It was then considered quite daring and unorthodox for a nonlawyer to run a trust department, which was always

entangled in legal estate questions.

Street Hinton was from Vicksburg, Mississippi, and reminded everybody of a Southern cavalry general. He was tall and spare, ramrod straight, somewhat curmudgeonly, with a long face and prominent ears. His father had ended up as minister of Saint John's of Lattingtown in Locust Valley, the "millionaire's church" so dear to Jack Morgan. Hin-ton's formative experience was in settling Jack Morgan's estate. He drew upon the art expertise of Belle da Costa Greene. "She told me that Fifty-seventh Street was the crookedest place in the world and not to trust anyone," recalled Hinton of his first foray into the world of art dealers.[2] A tough customer, he quickly took control after the merger, telling the people who had run the Guaranty Trust Department: "What makes you think you know how to run a trust department?" He reminded them that they had lost their largest account, Ford Motor, to J. P. Morgan. Hinton ran the combined show.[3]

Trust departments had been regarded as loss leaders. Hinton thought they should make money. Most trust managers were sober men with iron-gray hair who put money into government bonds and they weren't notable for their imagination. When the Morgan Trust Department made its first common-stock purchase, in 1949, it was thought so audacious that Hinton had to telephone Russell Leffing-well, on vacation in Lake George, New York, to clear the purchase. After 1950, changes in tax laws and collective bargaining prompted an explosion in pension funds, and much of this money gravitated to commercial banks. After General Motors designated Morgans as one of its pension-fund managers and allowed investment of up to 50 percent in stocks, the business boomed. "What made us was the General Motors fund," said Hinton. "When we led the parade there, then everybody else wanted us."[4]

In the early 1960s, the Morgan Trust Department operated from a wood-paneled room with antique furniture, facing the New York Stock Exchange. Forty impeccably dressed managers in dark suits and black shoes sat in leather armchairs before glossy rolltop desks. Invoking Pierpont Morgan's philosophy, Hinton initiated the gospel of buy and hold. When a corporate director asked for a policy statement, he replied, "It's easy. We don't have one. We never sell stocks."[5]

Hinton had more flexibility than he conceded and was a cagey manager. At meetings with portfolio managers, he would call on Peter Ver-milye, the resident bull, if he wished to buy stocks; if he wished to sell, he favored Homer Cochran, a durable bear. During the Kennedy bull market, the Morgan Trust Department became a trendy place. Young Ivy League portfolio managers loaded up with the glamorous growth stocks of the day—the so-called nifty fifty that so mesmerized money managers. Hinton's young highfliers bought Schlumberger before people could pronounce the name and

were early buyers of Xerox, which multiplied a hundredfold. Symbolic of the new style was Carl Hathaway, who drove a fire-engine-red sports car and issued solemn dicta, such as “Never invest in companies run by fat men.” “Lazy people bore me,” he said. “The most successful of my friends remind me of a 727 at takeoff: full throttle and straight up.”[6]

By the mid-1960s, Morgan was managing an incomparable $15 billion in assets, yet trouble lurked ahead. Control of such gigantic sums invited new public scrutiny, especially from Representative Wright Pat-man, the bullnecked populist chairman of the House Banking Committee. Like Louis Brandeis, Patman saw bankers’ possible abuse of “other people’s money” and feared that banks would use trust assets to exercise influence over business. In 1966, he issued a report that accused big commercial banks of dangerously “snowballing economic power” over large chunks of U.S. industry.[7]

The Patman report disclosed how banks had hijacked the new pools of investment capital. Of more than $1 trillion in assets held by U.S. institutional investors, 60 percent resided in commercial banks’ trust departments. Because of the Wall Street merger wave, most of these assets were now concentrated in the hands of Morgans and four other banks. There were eye-popping figures on Morgan holdings. It held gargantuan stakes in two old Guggenheim standbys: 17.5 percent of Kennecott Copper and 15.5 percent of American Smelting and Refining,-and it could have bossed around the entire airline industry, with a 7.4-percent stake in Trans World Airlines, 7.5 percent in American Airlines, and 8.2 percent in United. The danger was more latent than actual, for the conservative Morgan bank usually sided with management in disputes and didn’t try to substitute its own judgment. But since a 5-percent holding could now control most companies in an age of dispersed share ownership, the numbers were disturbing.

There were also new fears about insider trading of a sort that took the banks by surprise. In the twenties, fortunes had been made through whispered tips and sly winks. The public tolerated this because only a tiny percentage of them owned stock. As personal investing grew in the 1950s and early 1960s, the public didn’t wish to take part in a rigged game. It took time for the banks to perceive the danger, or at least the new public apprehension. In the 1960s, trust departments weren’t yet segregated from other departments. At Morgans, senior bank officers—many of them directors of five or ten companies—sat on the Trust Committee, which also had as members outside directors of the bank, including, at various times, people such as Alfred P. Sloan of General Motors and Henry Wingate of International Nickel. These men were expected to bring their specialized knowledge to bear in picking stocks. At that point, banks didn’t worry that they might misuse confidential information from the lending side in making investment decisions; there

weren’t yet legal barriers, or “Chinese walls,” between the commercial and the trust departments.

It was amid new concerns that the SEC in April 1965 charged thirteen people associated with Texas Gulf Sulphur of profiting from inside information about an Ontario ore bonanza. One illustrious name leapt from the headlines—Tommy S. Lamont, son of the famous partner and only recently retired as Morgan Guaranty’s vice-chairman. Lamont was accused of relaying information to Longstreet Hinton, who had bought Texas Gulf for Morgan trust accounts. It was a shocking charge, for since the 1930s the bank had been obsessed with its integrity and was undoubtedly one of the world’s most reputable banks. Street Hinton worshiped George Whitney and had watched his anguish over his brother’s scandal. Tommy Lamont had gone through the Pecora hearings, in which he was charged with making “wash sales” to his wife—an experience he didn’t care to repeat—and he had cherished a reputation as a highly principled banker.

Thomas Stillwell Lamont resembled his father. Perhaps the face was rounder, the neck a shade fuller, but he had the same strong voice that emerged surprisingly from a slight build. Like many at Morgans, he patterned himself after a sainted father, adopting his interests. He became president of the Phillips Exeter board and a member of both the Harvard Corporation and the Council on Foreign Relations. Adopting his father’s literary bent, he mailed birthday verses and sentimental greetings to friends and proudly chronicled the Lamont family history. Yet despite certain outward similarities, Tommy Lamont was more proper, more remote, and certainly more private than his famously gregarious father.

Tommy Lamont had been the House of Morgan’s ambassador to the mining world, joining the Texas Gulf board in 1927. He had helped install Claude Stephens as company president and rated him so highly that he recommended the stock to Street Hinton for the Trust Department in the early 1960s. When the company cut its dividend, an already skeptical Hinton soured on the stock, and there matters stood for a while.

In November 1963, Texas Gulf drilled a secret hole at Timmins, Ontario, that flabbergasted its chief mining engineer: it was richer than anything he had seen, richer than anything ever reported in the technical literature. This mother lode of copper, zinc, silver, and lead was later valued at up to $2 billion, it was rich enough to supply 10 percent of Canada’s need for copper, 25 percent of its zinc. It was a vein so fabled that the ore sat right on the surface and could be “scooped up like gobs of caviar,” as one miner said.[8] As Texas Gulf ran tests that winter, its stock doubled, based on rumors of feverish miners mortgaging their houses to buy more shares in the company. Texas Gulf withheld an official announcement of the strike, fearing it would drive up the cost of surrounding property.

How to hush up reports of El Dorado? On April 10, 1964, Claude Stephens telephoned Tommy Lamont and asked whether he had heard the rumor. Lamont said he had. “Is there any truth in it?” Lamont inquired. “We don’t know,” Stephens replied. “We need a little time to evaluate our program in this particular area.”[9] Lamont advised him to delay any statement, suggesting that he wait for the April 23 annual meeting in New York to make a formal press announcement.

The next morning, the *New York Herald Tribune* reported the biggest strike since Yukon days, a legendary bed of copper six hundred feet thick. On April 12, prodded by the SEC, Texas Gulf issued a statement of such cool understatement that the government later condemned it as false and misleading. Even though it knew it had at least ten million tons of copper and zinc, the company blandly described Timmins as a “prospect” that required more drilling for “proper evaluation.”[10] Texas Gulf scheduled a board meeting and press conference at the Pan Am Building in New York for April 16. Street Hinton had taken notice of the wildly gyrating stock and asked Lamont to report to him after the meeting.

April 16, 1964 would be a day nightmarishly imprinted on the memories of both Hinton and Lamont. The Texas Gulf meeting began at nine sharp, with a full complement of fifteen directors. At about ten o’clock, twenty reporters were herded in for a press conference. It was “a New York corporate version of the old days when the old prospector rushed into the saloon to announce he had struck it rich,” said Jerry E. Bishop, who was there for the *Wall Street Journal*.[11] The company wanted to keep all reporters in the room until the press conference was over. But once Claude Stephens finished his announcement, Norma Walter, covering her first spot news story for Merrill Lynch’s monthly magazine, managed to slip out a side door. She got the news on the firm’s in-house network at 10:29 A.M. A reporter for a Canadian wire service got out another door. Meanwhile, the other reporters stayed put, forced to watch color slides of the ore deposit. At the first moment of freedom, they dashed to the telephones to report the sensational news. Jerry Bishop’s dispatch appeared on the Dow Jones “broad tape” of market news at 10:55 A.M.

After the meeting, Lamont mingled with reporters, viewing core samples and color slides of Timmins. About 10:40 A.M., he phoned Hinton from the Texas Gulf offices. “Take a look at the ticker,” Lamont said. “There is an interesting announcement coming over about Texas Gulf.” “Is it good?” Hinton asked. “Yes, it’s good,” Lamont said.[12] Later Hinton would testify to a curious sense of having seen the news flash over the broad tape. In fact, he failed to verify that it had appeared. Hinton then was treasurer of the Nassau Hospital Association and personally ran its portfolio. He at once telephoned

the trading desk and bought three thousand Texas Gulf shares for the hospital. Then he advised Peter Vermilye to add the stock to a Morgan Guaranty profit-sharing plan and a mixed fund that invested for two hundred pension plans; Vermilye bought one thousand and six thousand shares respectively. All the while, the story hadn't shown up on the Dow Jones broad tape, even though it had been flashed to 159 Merrill Lynch branches.

Unaware of having committed any crime, Lamont returned to his office at 15 Broad Street and at 12:33 P.M. bought three thousand Texas Gulf shares for himself and his family. Now the news had been on the Dow Jones wire for over an hour and a half. The stock market had reacted deliriously. Driven by a 7-point rise in Texas Gulf stock, by day's end the New York Stock Exchange smashed all previous volume records. Far from feeling guilty, Hinton was disappointed the next day to learn how modestly Vermilye had bought. Only twelve days later did Lamont learn of the Trust Department purchases triggered by his call. He hadn't advised Hinton to buy. He later claimed he was discharging a duty and not phoning in a hot tip.

A year later, Texas Gulf directors were planning a reunion to savor their Timmins triumph. Though still a Morgan director, Tommy Lamont had now taken his mandatory retirement at age sixty-five. On the eve of the Texas Gulf meeting, a reporter reached him at home to say that the SEC had just charged him with "tipping off other bank officials" about the Timmins strike. Lamont was stunned. "I did not tip off other bank officials," he shot back.[13] The publicity value of his golden name was such that it dominated a front-page headline in the *Times* the next morning. He was tossed in with Texas Gulf executives and geologists who had blatantly traded on the inside information —a bit of editorializing that deeply embittered him. The *Times* sent a reporter to eighty-three-year-old fudge Ferdinand Pecora, now an elderly New York Supreme Court justice. Leaning back in his large red-leather chair on East Seventieth Street, Pecora marveled at the "extraordinary coincidence" that Thomas W. Lamont's son was involved in the insider trading scandal: "It's history repeating itself. It's symptomatic of the temptations of Wall Street."[14]

That Lamont was a member of the Morgan Trust Committee allowed the SEC to spotlight a broader problem of institutional investing. It branded the entire department an inside trader. Although not directly charged, Hinton was crushed, thunderstruck. Inside the bank, he had a reputation for sometimes ferocious independence and for telling the rich and powerful where to go. Peter Vermilye, now head of Baring America Asset Management, recalled:

At one point, AT&T came to Hinton and said, "We want to make you a major pension fund manager for AT&T, but we'll only pay you quite a low fee." Hinton said he couldn't charge them less than any other client and refused to do business with them. Exxon said to Hinton, "We want to do business with

you, but we want to direct the brokerage fee.” Hinton thought the Exxon treasurer wanted to make a big figure with his brokerage friends out in the Hamptons and said, “No way.” Another time, Meshulam Riklis bought control of a company that was a Morgan client and wanted to use its pension funds for his own machinations. Hinton threw him out of the office.[15]

What made the affair so devastating for Hinton was that Lamont blamed him for making the purchases. (Perhaps the most convincing proof of Lamont’s innocence.) “He never forgave me,” recalled Hinton emotionally. “All the other Morgan officers tried to tell him he was wrong, but he never forgave me.”[16] Lamont was haunted by the case and treated it as a personal crusade. Insisting upon his innocence, he ran up enormous legal bills with Davis, Polk and fought in both the legal and the political arenas. Stung by the *Times* coverage, he typed up a twelve-page critique and handed it to executive editor Turner Catledge over lunch. It said the paper had “over and over again given special emphasis to me in its stories dealing with the Texas Gulf case. . . . I am bothered by this record of inaccurate reporting and careless editing.”[17] Ducking the issue, Catledge said that headlines by their very nature were cryptic.

Some people charged by the SEC were clearly guilty of insider trading. One geophysicist had bought shares the day before the news conference; another company official, the previous night. Ordinarily, insider prohibitions disappeared once news was publicly disclosed. Now the SEC promulgated a new standard, arguing that news had to be released *and* digested by the public before insiders could trade—a hazy definition that would prohibit buying for minutes or days afterwards. At first, the SEC identified 10:55 as the moment the legal embargo ended, when the Timmins news moved on the Dow Jones tape. A year later, it arbitrarily stretched the period to encompass Tommy Lamont’s purchase at the office at 12:33 P.M.—an outrageously long time after the news conference was disbanded. As Hinton said hotly, “If the SEC intends to make a new rule on that point, well and good . . . but it is not fair to write a rule retroactively.”[18]

Lamont’s defense team dwelled upon a supposed twenty-minute delay before Jerry Bishop’s report ran on the Dow Jones broad tape. Lamont was alleged to be the victim of a technical glitch. But Bishop and his editors didn’t think there was any delay at all. A year or two after the trial, Bishop figured out why there appeared to be a delay. Lamont’s lawyers had assumed that Norma Walter had filed her Merrill Lynch report after the news conference; in fact, she had filed her story twenty minutes before the other reporters. Whether or not Bishop is correct doesn’t affect the guilt or innocence of Tommy Lamont, who instructed Hinton to watch the tape. But if he is correct, Lamont must have gone to the phone almost immediately.

In December 1966, District Judge Dudley J. Bonsai exonerated eleven of the thirteen defendants, including Lamont. He said the facts were public information once relayed to reporters on August 16, 1964, and that Lamont and Hinton had acted entirely properly. While the SEC appealed, Lamont's health took a turn for the worse. He had a heart condition and suffered from fibrillations exacerbated by tension and depression. In April 1967, he checked into Columbia-Presbyterian Medical Center; he never regained consciousness after undergoing open-heart surgery. As soon as the SEC heard the news, they called S. Hazard Gillespie, Lamont's lawyer at Davis, Polk, and said they were dropping their appeal. Perhaps in atonement, the *Times* ran a fulsome, three-column obituary of Lamont that was disproportionate in length to his historical importance. It was a recurrence of an old Morgan condition—public exposure and political harassment leading to death.

However misguided in its pursuit of Lamont, the SEC in the Texas Gulf case drew attention to the growing dangers of financial conglomeration in the Casino Age. As both commercial and investment banks developed huge, diversified operations, it would be increasingly difficult for them to segregate diverse and often legally incompatible operations. A few years later, the Morgan bank was accused of selling stock in the failing Penn Central based on information passed to the Trust Department by a lending officer—charges the bank always denied and that were never conclusively settled. Its Trust Department was finally moved to Fifty-seventh Street so that it would be physically separate from the rest of the bank. Years later, the problem posed by conglomeration would reappear for Morgans as it entered merger work, and it would generally shadow the burgeoning Wall Street banks and brokerage houses throughout the postwar years.

IN London, meanwhile, the City had sloughed off its sleepy atmosphere. By the mid-1960s, there were now two Cities. One was a clubby, bowler-hatted core that dealt in sterling and was protected from foreigners by the Bank of England. Here whispered references to Grandma meant the governor of the Bank of England. This world required attendance at good schools and the right contacts for success and was ruled by patrician families.

The second City was a rich colony of foreigners trading in the new Euromarkets, and it would eventually surpass the domestic City in size. As if deploying an army for battle, Morgan Guaranty sent its crack young executives to London. So many Americans flocked to the City that the British press muttered about "Yank banks" and dubbed Moorgate the Avenue of the Americas. Starting with a Bankers Trust issue for Austria in 1967, these foreign bankers put together large syndicated loans, for many countries, paving the way for massive Latin American lending in the 1970s. In this more

egalitarian City, capital, not contacts, determined success.

With the Guaranty merger, Morgans inherited a full-fledged London branch on Lombard Street, a short walk from Morgan Grenfell. This sharpened an old dilemma: were Morgan Grenfell and Morgan Guaranty partners or competitors? Protestations of fraternal warmth were often clouded by mutual suspicion. Morgan Guaranty's London staff thought Morgan Grenfell "didn't help them any more than any other merchant bank and, in fact, were inclined to be a little more suspicious of them," declared Rod Lindsay, later a Morgan Guaranty president.[19] When Lew Preston managed the London branch in the late 1960s, he found Morgan Grenfell opportunistic, quick to share bad deals but tending to hoard the good business. "Lew perceived the one-way-street nature of things," remarked an associate. "The benefits were flowing in one direction." Preston found it hard to convince his troops that Morgan Grenfell wasn't a competitor.

There was cultural friction, too. Junior Morgan Guaranty people were excluded from the partners' room at 23 Great Winchester Street when seniors went inside. Especially infuriating was Morgan Grenfell's condescending treatment of a young British foreign-exchange trader, Dennis Weatherstone, son of a London transport worker. In 1946, Weather-stone, at the age of sixteen, had started as a bookkeeper at Guaranty's London branch while attending night school. With his quick mind for figures, he excelled in the lightning-fast trading that was now transforming banking. In the mid-1960s, he was spotted by Lew Preston, who noticed that people kept stopping by his desk to ask questions; Preston promoted him to deputy general manager in London. The short, wiry Weatherstone was a local hero for working-class recruits to the City. Some of Morgan Grenfell's aristocrats found no romance in this proletarian success story and snubbed Weatherstone, who later ended up president of the House of Morgan: he would decide that his career opportunities in New York were wider than those in the class-bound City.

Morgan Grenfell was an inbred, marginally profitable firm that was being strangled by its own pomposity, as the acrimonious aluminium war had shown. Its stagnation spawned gloomy humor. One City journalist, Christopher Fildes, recalled his editor keeping a headline in standing type: "FIRST WIN FOR MORGAN GRENFELL"; the editor joked he might need it some day.[20] Morgan Grenfell directors stuck to their old, informal style of doing business. They wouldn't advertise, seldom held formal meetings, and made decisions informally in their partners' room.

Entering the 1960s, the firm was owned by a tight-knit cluster of families—Grenfells, Smiths, Harcourts, and Cattos—and by Morgan Guaranty, which held a one-third share. To create incentives for its young executives, the bank issued new shares, which would gradually dilute the power of the old

families. Morgan Grenfell also created new “assistant directors”—a seemingly petty organizational detail that for the first time allowed commoners to ascend into the formerly closed caste of directors: the senior partner, Viscount Harcourt, wanted to end the rigor mortis. In 1967, right before the second Lord Bicester—the jolly Rufie—died in a road accident, Harcourt recruited the virile Sir John Stevens, executive director of the Bank of England, to open up overseas outposts.

Among its young professionals, Morgan Grenfell’s stodgy reputation bred an exaggerated thirst for freedom. In 1967, Stephen Catto, the former partner’s son, invited film producer Dimitri de Grunwald for lunch at 23 Great Winchester. De Grunwald had a brainstorm: if distributors could finance film production through a global consortium, they could shatter America’s monopoly in filmmaking; he denied that only Americans could make westerns. Eager to show it could move with the times, Morgan Grenfell decided to back the venture.

To prove his point, de Grunwald signed up Sean Connery and Brigitte Bardot for *Shalako*, a film about an aristocratic safari of Europeans deep in Apache territory; it was an instant success. The idea of a staid old merchant bank financing Brigitte Bardot was symptomatic of Morgan Grenfell’s inner ferment, its itch for experimentation. Elated, de Grunwald talked of his dreams for developing film talent. “He believes the secret of success is not to play safe,” noted the London *Times*. These famous last words set him up for the catastrophic *Murphy’s War* (Murphy’s Law might have been more apt), on which Morgan Grenfell took such a bath that the Bank of England intervened; Grandma placed a man at 23 Great Winchester to straighten the mess out. “At least it kept us out of the shipping and property disasters of the early 1970s,” said Lord Catto philosophically.[21]

But the firm was shedding its past caution too quickly. The man who accelerated the process was Lord William Harcourt, a great-grandson of Junius Morgan’s. With trim mustache and narrow face, round spectacles, and a bow tie, Bill Harcourt was a funny, snobbish man who wouldn’t deign to shake hands with a junior member of the firm. Behind the imperious air, he hid a wicked wit, an acute sense of the ridiculous. He had served as British economics minister in Washington and U.K. executive director at the IMF-World Bank and was known as Morgan Grenfell’s political fixer.

The son of a colonial secretary and grandson of a chancellor of the Exchequer, Harcourt graduated from Eton and Oxford and married the only daughter of Baron Ebury. Harcourt and his wife lived in splendor at Stanton Harcourt, a family estate with several acres of gardens behind high walls. A visitor, Danny Davison of Morgan Guaranty, recalls gaping at its magnificence. “Gee, this is a magnificent place you have here,” he boyishly told Harcourt. “When did you get it?” “Ten-eighty,” was Harcourt’s crisp

retort.

The contradictory Harcourt piloted the firm into the treacherous waters of controversial takeovers. They were common in the City by the mid-1960s, driven by a new management creed that only multinational corporations could survive in the new age. By 1968, seventy of Britain's one hundred largest companies had been involved in takeovers in just two years. Where Morgan Grenfell had indignantly protested Siegmund Warburg's tactics in the aluminium war, it was now determined that the firm would surpass him in verve and even ruthlessness.

The takeover that revealed this shift was the battle for Gallaher, the manufacturer of Benson and Hedges cigarettes. In May of 1968, Morgan Grenfell and Cazenove, the blue-blooded stock broker, helped Imperial Tobacco sell off a 36.5-percent stake in Gallaher; Imperial had to divest it on antitrust grounds. The underwriting was a fiasco that left the underwriters with a third of the slumping shares and made Gallaher feel vulnerable to unwanted suitors. Indeed, by June, Philip Morris, backed by that Morgan Grenfell nemesis, Warburgs, began to close in on its prey.

Following these events in New York, Barney Walker of American Tobacco told Bill Sword and Jack Evans of Morgan Stanley that he wanted to expand his Gallaher stake and rescue the company from Philip Morris. Sword called Ken Barrington of Morgan Grenfell, who had just returned to his flat after a summer lawn party with the queen at Buckingham Palace. Barrington and his colleague George Law promptly flew to New York. In American Tobacco's boardroom, Barney Walker—a red-faced Irishman with no college degree—gave Sword and Barrington their marching orders. “Look, I wanna win,” he said. “I want an absolute guarantee that we will win. What will it take?” “I suppose it depends on the size of your purse,” said Barrington. “What'd he say?” grumbled Walker. “It depends how much money we're prepared to pay,” an aide translated. Walker barked that money was no object. At this pivotal moment, it was industry, not the bankers, who demanded a new red-blooded, cutthroat style of business. Both Morgan Grenfell and Morgan Stanley would later plead, with some justice, that they were provoked into aggressive takeovers by their clients and that their metamorphosis into merger artists didn't occur in a financial vacuum. In the 1960s, the bankers were still more the instruments than the engines of takeovers.

The Morgan Stanley-Morgan Grenfell team flew off to the City to mount the most vigorous operation in London Stock Exchange history, fortified by a $150-million credit led by Morgan Guaranty. Stymied by LBJ's capital controls, American Tobacco could afford only a partial bid, and this enforced economy led to the controversy. All over the City, insurance companies, pension funds, and other underwriters sat with unwanted, depressed Gallaher shares, gnashing their teeth at Morgan Grenfell. At a Sunday night meeting,

the takeover team plotted its strategy with Sir Antony Hornby, senior partner of Cazenove and Company, who was assigned to handle the Stock Exchange operation. They decided to go into the Exchange the next morning and buy the shares from the May underwriters. This controversial tactic—which would redeem Morgan Grenfell in the eyes of the underwriters—also guaranteed that the takeover would enrich a handful of institutions while small shareholders wouldn't learn about it until afterward.

Lately there had been many questions raised about the City. As takeovers grew bloody and unscrupulous, the Labour government threatened to impose strict regulations. To avert that, the Bank of England had created a committee, chaired by Morgan Grenfell's Ken Barrington, to strengthen the Takeover Code. To enforce it, Sir Leslie O'Brien, the Bank of England governor, had set up a Takeover Panel with offices in the bank itself. Lacking statutory powers, the panel was criticized as unhealthily close to the people it oversaw. Yet despite Barrington's role in devising the new code, Morgan Grenfell posed the first and stiffest challenge. Article 7 of the Takeover Code said no shareholder in a target company should receive an offer "more favorable than a general offer to be made thereafter to the other shareholders."[22] This principle was challenged by the American Tobacco takeover, which was a so-called "street sweep"—a huge share purchase without a tender offer.

On Monday morning, Hornby began whirlwind buying such as London had never seen. He went to the May underwriters and paid 35 shillings for Gallaher shares that had slumped to 18 shillings; he was instructed to purchase about five million shares that day. Instead, he was engulfed by a tidal wave of twelve million shares by morning's end. Most small shareholders didn't hear about the sudden windfall until lunchtime, by which point it was too late. They could get 35 shillings for only *half* of their holdings and were outraged by the apparent collusion between big institutions and merchant banks.

Morgan Grenfell had always cooperated with the Bank of England instinctively and sided with the financial authorities. Now it was acting more like a cheeky, defiant outsider, bent on stirring things up and testing the rules of the new Takeover Panel. Suddenly it resembled the assertive, iconoclastic Warburgs that had so offended its sense of propriety a decade before. In an amazing transformation, it had turned into its own worst enemy.

The Takeover Panel censured both Morgan Grenfell and Cazenoves. To the astonishment of the press, Harcourt and Hornby, those City demigods, didn't beat their breast in atonement. Within an hour of the panel's ruling, they simply rejected it out of hand! Here were Sir Antony Hornby, on the board of the Savoy Hotel and Claridge's, and Lord William Harcourt, with his huge estate, thumbing their noses at authority and rebuffing a panel clothed with the prestige of the Bank of England. Hornby sounded like a ruffian: "There's

a certain cut and thrust in the market that is the essence of City dealing. If you're going to wait for the amateurs then business will stop."[23]

Bill Harcourt's hauteur was memorable. He came up with a classic retort that expressed both his mischievous humor and magnificent contempt: "Can't a man go in on Monday morning and buy a few shares?" He finished by telling a startled news conference that he would entertain no questions. "I am totally confident that the purchases are in fully conformity with the City code."[24] Bill Sword later claimed that the American Tobacco team had secured approval of the Takeover Panel for its action but that Harcourt courageously withheld this information, lest the panel's authority be weakened. But his initial manner seemed far more defiant than respectful toward the panel and was so reported in the press.

The public was in an uproar. Not only did the press back the panel, but the increasingly powerful institutional investors displayed almost unanimous support for censure. Three-quarters even favored further action. These institutions were the new countervailing powers; merchant banks no longer held all the cards. As would happen on Wall Street, the providers of capital—the mutual funds, pension funds, insurance companies and so on—were growing powerful at the expense of capital-short merchant banks in London and investment banks in New York.

In a carefully staged reconciliation, Lord Harcourt, a humble, hair-shirted suppliant, told the panel, "I should like to assure the committee that it was never my firm's intention to show any lack of respect for the authority of the panel."[25] The Takeover Panel allowed that perhaps he and Hornsby had misunderstood the rules. Although Morgan Grenfell emerged unscathed and banked a gigantic $1-million fee, the damage to its reputation was severe. As London's *Sunday Telegraph* said, "The days when Morgans spoke only to Cazenoves and Cazenoves spoke only to God were clearly at an end."[26]

For Morgan Grenfell, the American Tobacco takeover showed that merchant banks with modest capital and large client lists could make a fortune in the new takeover game—precisely what Siegmund Warburg had seen. Here they could capitalize on old-school ties while both lending and securities work became commodity businesses, dominated by the biggest and strongest. At first, the old financial aristocracy was squeamish about performing hostile takeovers, giving Warburg his head start. But now, only ten years later, the old guard had already lost its compunctions, proving that it could behave with a ferocity ordinarily not associated with the country-house set.

SEVERAL months after the American Tobacco takeover of Gallaher, Morgan Grenfell entered a publishing battle that confirmed its new zest for

controversy. In this case, it assisted Rupert Murdoch in his purchase of the *News of the World*, a London tabloid. The paper was a trashy mix of sports, pinups, Tory editorials, and royal gossip. Its major coup was the 1964 purchase of Christine Keeler's memoirs recounting her dalliance with Secretary of State for War John Profumo and a Russian military attache. The paper sold six million copies every Sunday, topping all English-language newspapers. Half the British adult population loyally enjoyed its salacious pages.

Breaking into British newspapers was then exceedingly difficult: Fleet Street was the preserve of family fiefdoms, and major papers seldom came up for sale. "They were almost looked down upon as toy things by the proprietors," said Lord Stephen Catto, who was to advise Murdoch.[27] Since the nineteenth century, the *News of the World* had been controlled by the Carr family, with Sir William Carr alone holding a 30-percent share. He was oblivious to the paper's declining performance, said one observer, "because he was invariably drunk by half-past ten every morning, a habit which had earned him the popular alias 'Pissing Billy.' "[28]

When Murdoch, Australia's third-largest publisher, began scouting British newspapers in 1967, the objective was less to buy at rock-bottom prices than to crash the Fleet Street gates. He had already befriended Lord Catto, who was married to an Australian and, as a director of the Hongkong and Shanghai Banking Corporation, would stop by to see Murdoch on his Asian tours. Easygoing and convivial, Stephen Catto was less starchy and rigidly upright than his father, the former Bank of England governor. But his breezy manner and quick smile hid a shrewd detachment. Educated at Eton and Cambridge, Catto had trained at Morgan Stanley and J. P. Morgan and was good with "colonials."

Catto was emblematic of his era, just as his father had symbolized the City's solemn prewar rectitude. Catto *fils* didn't shrink from publicity and liked the fact that Murdoch was on call, day or night, in pursuit of a hot deal. In 1967, Murdoch visited Catto, saying he wanted to expand beyond Australia. "Much to my surprise, he sat down and said, 'I want to buy the *Daily Mirror,'* " recalled Catto, who patiently explained that Murdoch would have to pry it loose from the formidable International Publishing Corp. "Then let's start buying IPC," said Murdoch.[29] Catto liked Murdoch's confident, forthright style and had a premonition of bigger things ahead.

Accumulating a small stake in London's *Daily Mirror*, Catto and Murdoch spotted a more promising opportunity when Derek Johnson, a cousin of Sir William Carr, decided to sell his 26-percent stake in *News of the World.* Residing in France and Switzerland, Johnson had variously been a pilot, a steeplechase rider, and an Oxford spectroscopy professor. He wanted to spare

his sixth wife onerous inheritance taxes by selling off the stake. Yet he had enough reservations about the Carr family that he didn't automatically sell them the shares.

Carr knew that by controlling the shares, he would possess a solid majority holding in the tabloid and so offered 28 shillings per share for the stake. This was a foolishly stingy offer that fell a shilling short of the stock's current price on the London Stock Exchange. Not bothering to reply, Johnson's London banker, Jacob Rothschild, peddled the block at 37 shillings a share to Robert Maxwell, the publisher of Pergamon Press, the largest scientific and technical publisher in the country. Labeling the move "cheeky," Carr had *his* banker, Hambros, begin buying shares in *News of the World.*

Maxwell wasn't yet the world-devouring mogul of the *Daily Mirror.* Like Murdoch, he saw the Carr tabloid, for all its peephole proclivities, as his entree into the upper echelon of publishing. Born into a Czecho-slovakian peasant family as Jan Ludwig Hoch, Maxwell emigrated to Britain in 1940, changed his name, served in the British army, and took over Pergamon Press after the war. Massive, brawny, and smart, he had a prickly style that scared the daylights out of respectable folk. He was a self-made man who had been elected to Parliament as an avowed socialist. Recalling the episode, Catto stressed Maxwell's somewhat murky business reputation at the time: "Pergamon Press had the hard sell with their encyclopedias. They were virtually forcing them on poor people. There were also doubts about the way he managed his financing. He mixed his own private company with publicly quoted companies in a way that made one uneasy."[30] Nevertheless, Maxwell made a tender offer of over 37 shillings per share for *News of the World*, making Carr's bid look cheap and unsporting in comparison.

To the Carrs, Maxwell was a foreigner unfit to run their Tory paper. This set them up for the blandishments of Rupert Murdoch. One morning in the fall of 1968, Catto's wife heard on the news that the *News of the World* stake was up for sale. "Why don't you get your friend Murdoch to buy it?" she asked Stephen. He soon cabled Murdoch that he had spoken with Sir William Carr's bankers, Hambros, which had expressed interest in his support against Maxwell. Murdoch needed no coaxing.

On Saturday, October 19, Catto summoned Murdoch to come to London at once, tracking him down at a sporting event in Melbourne. Murdoch jumped on a plane to Sydney, where his wife, Anna, handed him a suitcase and his passport. Then he jumped on a Lufthansa plane for Frankfurt, where he switched to a flight for London. Landing at Heathrow's Terminal 2, he evaded reporters thronging Terminal 3. London was by now rife with rumors about Murdoch's arrival, and the press hunted for him relentlessly. Murdoch thought his room at the Savoy might be bugged. So Catto put him up at his country place, where he paced up and down, jotting notes on backs of envelopes. The

looming battle gave Morgan Grenfell another chance to shuck its musty image. As the London *Observer* said, "Morgan Grenfell, having been for long regarded as a grouse-moor bank, with a record of unsuccessful defensive battles, is nowadays determined to show it can be as aggressive as the rest of 'em."[31]

Despite the strident denunciations of Maxwell by the Carr forces, Murdoch resembled his competitor in many ways. Both were loners who hated committees and enjoyed a scrapping good fight. Even their politics weren't so dissimilar. As an Oxford student, Murdoch had flirted with political radicalism, and his supposed anti-British sympathies were cited as reasons to oppose his ownership of the *News of the World.* Like Siegmund Warburg, Murdoch thought the British upper class weak and effete, and this emboldened him in his maneuvering. Murdoch's output was already mixed. Though he published the staid *Australian,* he also put out a racy weekly called *Truth.* Nonetheless, Sir William Carr would embrace Murdoch as an unblemished white knight.

During their country-house weekend, Catto outlined to Murdoch a three-pronged strategy that called for securing Carr's support, beating Maxwell, then taking full control of *News of the World.* (Events would unfold in that precise order.) Carr wanted to use Murdoch to destroy Maxwell but without ceding full power to him. As Murdoch later said, "I was expected not as a white knight, but as a Sancho Panza to Carr's Don Quixote."[32] Catto laid out a plan to turn the tables on Carr. After buying a small stake in the *News of the World*, they would take advantage of Carr's vulnerability to gain control of the tabloid. Catto's guile was a revelation to Murdoch, who had equated the City with gentility, said one biographer; "yet here was Lord Catto, a principal in one of the City's most celebrated banks, proposing a strategy that bordered on the Machiavellian in its slyness—perhaps even of the deceptive and fraudulent, as Sir William Carr, its victim, would later claim."[33]

Coached by Catto, Murdoch then had breakfast with Carr at his Cliveden Place residence on Tuesday morning, October 22. Murdoch brashly said that he would buy a majority stake in *News of the World* but that he wanted Carr to step aside as top executive. When Carr balked, Murdoch got up to leave. "I'm here to help you if you want it," said Murdoch. "But I don't like to waste time on dither." "Sit down, Mr. Murdoch," Carr replied.[34] In a complicated deal, they agreed that Murdoch would buy more *News of the World* shares and secure their combined majority. In exchange, Murdoch would get a 40-percent stake in the paper through newly issued shares. They would jointly manage the paper, but Carr would remain as chairman. Murdoch chafed at these terms, but Catto assured him it was the "foot in the door" he needed.[35]

The first phase of the tabloid battle resembled a straight bidding war.

Maxwell put together a 30-percent stake by buying the original Derek Johnson block plus additional purchases. The Murdoch forces adopted more controversial tactics. Carr's banker, Hambros, bought *News of the World* shares in apparent violation of the Takeover Code, which forbade companies to buy their own shares. And through a Morgan Gren fell account, Catto bought a 3.5-percent stake in the paper that would be set aside for Murdoch.

In the American Tobacco-Gallaher affair, Lord Harcourt had arrogantly dismissed the press at his peril. Now, in announcing his pact with Carr, Murdoch hired a publicist. Catto found this departure exciting—while his father would doubtless have found it abhorrent and beneath a banker's dignity. At a press conference on Wednesday, October 23, Murdoch, age thirty-seven, made his debut on the British stage. He was tagged the "quiet Australian" by the London press, which knew little about him. At first relaxed and grinning, he tried to answer questions frankly, but he was stunned by a barrage of hostile questions accusing him of violating the Takeover Code. Catto sat quietly by his side, a contemplative finger at his lips.

Robert Maxwell protested to the Takeover Panel what he saw as a side deal between management and Murdoch not in the best interests of shareholders. He also claimed that the Carrs were violating the code by buying their own shares through a surrogate, Hambros. Maxwell had boosted his bid to a hefty 50 shillings per share, but was thwarted by the pact negotiated at breakfast at Cliveden Place. The panel found enough merit in the charges and countercharges to suspend trading in *News of the World* stock for two months. At the time of the standstill, neither side had a 51-percent stake. The panel turned the battle into a proxy fight to be decided at a general shareholders' meeting on January 2, 1969. Catto rallied Murdoch's spirits, saying the decision enhanced their chances for victory. Shortly before the meeting, the panel said neither side could cast votes obtained before Maxwell's first tender offer.

Sir Leslie O'Brien, the Bank of England's governor, fretted that the angry contest would wreck the code. Voluntary self-regulation seemed a feeble way to restrain the mercenary tendencies of the Casino Age. At the Lord Mayor's banquet on November 11, Prime Minister Harold Wilson had reiterated his dislike of the new marauding style in the City, exhorting merchant bankers to police their own behavior. Once again, Morgan Grenfell, long part of the City establishment, openly sparred with City authorities.

When the Carr-Murdoch deal was voted on at the Extraordinary General Meeting held on January 2, the atmosphere was ugly and xenophobic. The Great Queen Street hall was packed with ringers. Murdoch later admitted that some pro-Carr shareholders who couldn't attend had temporarily signed over their shares to *News of the World* staffers. When Sir William Carr marched in like a benevolent patharch, he was lustily cheered. Dressed in a flashy blue

suit, Maxwell was hooted and booed by a chorus shouting “Shame!” “Withdraw!” and “Go home!”[36]

Although Maxwell’s standing offer of 50 shillings was the financially superior one, the discussion pivoted on his fitness to run the paper. While Murdoch pretended that he would retain Carr as chairman, Maxwell candidly said he would replace him, telling the paper’s publisher, “Every time I have a haircut at the Savoy late in the afternoon, around 4 P.M., I find you and your *News of the World* cronies still drinking Martinis and I don’t think that is suitable training for any chairman of mine.”[37] Maxwell’s combative style didn’t work nearly as well as Murdoch’s crafty, self-effacing manner. In the final vote, the Carr-Murdoch group got 4.5 million shares, and Maxwell, 3.2 million. Murdoch celebrated with a party at his Embankment flat that night. For Morgan Grenfell, it started a long relationship with the world’s most powerful publisher. As an influential board member of Murdoch’s News International board, Catto would negotiate his future U.K. newspaper purchases, including that of the London *Times*. Yet the relationship between Murdoch and Morgan Grenfell would have a curious ambivalence, for the banking side of the firm wouldn’t lend to Murdoch, believing his operations too dangerously leveraged.

By mid-1969, Sir William Carr saw that with Murdoch he had admitted a Trojan horse. The Australian continued to buy shares after the meeting, so he would safely control more than 50 percent of the paper. He fired Carr’s jingoistic editor, Stafford Somerfield. Then he demoted Carr to president and took the chairmanship himself. Murdoch was launched in Britain. That December, he bought the London *Sun*, which would prove his real profit maker. Loading it with pinups, he soon doubled its circulation, to two million, and established it as Britain’s biggest daily paper.

The American Tobacco-Gallaher affair and the Murdoch-Maxwell brawl prompted reform of the Takeover Panel, which got a full-time chairman in Lord Hartley William Shawcross, a Morgan Guaranty adviser and a director of Morgan et Compagnie International. The code was revised to forbid partial bids of the American Tobacco variety, and new sanctions were introduced. In a single tumultuous year, Morgan Grenfell’s character had changed almost beyond recognition. Mergers were suddenly pitching in a third of the firm’s profits. It was operating publicly and flouting authority in a way that would have been inconceivable a decade earlier. Though the firm still issued securities and managed money, it increasingly would take its tone from the piratical world of mergers. This change would also affect the firm’s sociology; now a premium would be placed on intellect and experience, Morgan Grenfell would attract a new breed of talented, well-trained lawyers and accountants who could master the intricacies of the complex deals. The

new City would be more ruthless but also more democratic, and it would look much more like the Warburgs of the 1950s than the Morgan Grenfell of the 1950s.

CHAPTER TWENTY-NINE
SAMURAI

LIKE Morgan Grenfell, Morgan Stanley entered the 1960s a model of civility, then turned itself inside out. In the early 1960s, it radiated a winner's confidence. Nearly two dozen partners in Brooks Brothers suits and monogrammed shirts sat behind rolltop desks at 2 Wall Street. Decorated with English hunting prints, this platform area was a sanctum of mystical power. As one partner said, "It's one of the few places where a single phone call can raise $100 million."[1] Morgan Stanley partners didn't raid, compete, or crudely solicit business and had exclusive relations with their clients. If they hired somebody from another firm, they politely asked that firm's permission.

As befit a firm of illustrious heritage, tradition was venerated. The old House of Morgan had encouraged attendance at partners' meetings by handing out gold coins. In a modern variant, Morgan Stanley gave out ten- or twenty-dollar bills to partners when they entered a meeting. They also got to divide the booty left by absentees. The only unanimous attendance occurred once, in a snowstorm, when everybody planned to make a killing.

As students protested the Vietnam War in the 1960s, it was hard to lure graduates to Wall Street. When Frank A. Petito went to the Harvard Business School to try to recruit students, he ended up sitting alone in a classroom until a professor took pity on him and stopped by to chat. Although they had mostly gone to Princeton, Yale, or Harvard, Morgan Stanley partners came from diverse backgrounds. Like the old Morgan bank, Morgan Stanley was receptive to talented poor boys, even though it was unfairly stereotyped as a Social Register firm. Dick Fisher, a future president, was discouraged from applying for a job by a Harvard Business School professor who said Morgan Stanley required "blood, brains, and money" and that Fisher failed on two counts.

Nevertheless, the hauteur of the senior partners *could* be oppressive. Once at the firm, Fisher drove up to Canada with one of the partners to work on the Churchill Falls hydroelectric project. At the border, an immigration official, peering at Fisher in the backseat, asked the partner, "Who's that in the back with you?" "I'm traveling by myself," the partner answered. When the officer gestured toward the person sitting in the backseat, the partner said gruffly, "It's no one. It's a statistician."[2]

By the 1960s, Wall Street's religious segregation was crumbling. Many

Jewish firms had Protestant partners, especially in syndication, where they had to truckle to Morgan Stanley and First Boston. In 1963, Morgan Stanley hired its first Jew, Lewis W. Bernard, who had roomed at Princeton with Frank Petito's son and frequently stayed at the Petito home. "When Bernard was interviewed, everybody was in favor of hiring him," recalled a former partner. "But it was very hard for some older partners to overcome their ancient prejudice." One Morgan Stanley partner even rushed over to Standard Oil of New Jersey to sound out an official: if Morgan Stanley ever sent over a Jewish employee, would the company be upset? "I think you ought to know, if you don't," the official bristled, "that our chief executive officer is Jewish."[3] The partner slunk away. In 1973, at age thirty-one, Bernard became the youngest partner in Morgan Stanley history (except for the special case of Charlie Morgan), and he would develop into an important strategic thinker.

Entering the 1960s, Morgan Stanley seemed secure, almost invulnerable, in its supremacy. The nonpareil of American investment banking, it counted as clients fifteen of the world's twenty-five largest industrial companies, as well as Australia, Canada, Egypt, Venezuela, and Austria. These were comprehensive, exclusive relationships, a relic of the days when clients needed to wrap themselves in the aura of powerful banks. Morgan Stanley served its clients diligently and was always dreaming up new ways to finance AT&T or General Motors. As the Casino Age progressed, however, and capital was no longer so rare a resource, the traditional ties would erode.

Morgan Stanley would go to any length to serve a faithful client. During the 1950s, it managed securities issues for J. I. Case, a farm-equipment manufacturer. In 1961, when Case faced bankruptcy and bankers threatened to pull their loans, Samuel B. Payne of Morgan Stanley became temporary chairman of the company. For six months, Payne spent three or four days a week at Case headquarters in Racine, Wisconsin, turning the company around. Later, a rehabilitated Case was sold to Tenneco. Similarly, Morgan Stanley undertook a record financing for the billion-dollar Churchill Falls hydroelectric project in Labrador, Newfoundland, twice the size of Grand Coulee Dam. Some Morgan Stanley partners worked on it daily for eight straight years. In 1969, when the chairman of the Churchill Falls Corporation was killed in a plane crash, partner William D. Mulholland stepped in and ran the company.

The Morgan Stanley partner who first saw the cracks in this immaculate world of loyal bankers and loyal clients was Robert H. B. Baldwin, a protege of Perry Hall, who had retired in 1961. Baldwin was a man who sharply polarized opinion and was later seen as either the savior or the ruination of the firm. For better or worse, he would sweep away the cobwebs and drag Morgan Stanley into the modern era. At a place of proper gentlemen, Baldwin had a high energy level, fanatic drive, and a tremendous desire to manage

people. Tall and athletic with cold piercing eyes and a brusque, humorless manner, he was the opposite of the archetypal Morgan man. His partners found him cold and awkward, a man who had trouble relaxing or making small talk, and he seemed misplaced in Wall Street's most elegant firm. Yet that was perhaps an advantage, for he wasn't shy about assuming power, as were the gentlemen.

Opinion divides on the question of Baldwin's intelligence. He had an outstanding academic record: a triple threat in sports at Princeton—football, baseball, and basketball—he also received a *summa cum laude* degree in economics. Yet his intelligence wasn't subtle or reflective but obsessive and suggestive of an implacable will. In his office, he had a needlepoint pillow on which was stitched, "The harder I work, the luckier I get."[4] At a notably discreet firm, Baldwin would abruptly inform people that they were overweight or smoking too much. Entertaining clients, he would suddenly launch into extended monologues on his own achievements.

Bob Baldwin would develop into a classic hell-on-wheels boss who would dominate Morgan Stanley for years, making life memorably miserable for his subordinates. "He could be a real bastard in the supercilious way that he would exercise his power with subordinates," said one ex-partner. "And he sometimes made a terrible fool of himself in the process of trying to be a big wheel." Said another: "He lacks humility, he's self-centered and insecure and quite humorless. You don't want to have a drink with Bob Baldwin." Yet he was also honest and forgiving. More to the point, he was extremely perceptive about the strategic direction of investment banking.

Baldwin was relentless in pushing an idea. He once harangued legislators during testimony in Washington, then harangued his companion in a cab; when his companion got off, he harangued the driver. His hero was no dreamy poet or thinker, but Admiral Chester Nimitz. When his son was at Phillips Exeter Academy in the early 1970s, Baldwin, an unabashed defense hawk, addressed the student body on "the other side of the military-industrial society that was in such disrepute."[5]

Much like the Young Turks at Morgan Grenfell, Baldwin was maddened by what he called the white-shoe thing—the notion that Morgan Stanley partners were inept stuffed shirts who succeeded because of blood ties and social contacts. "My grandfather was a conductor on the Pennsylvania Railroad," he pleaded. "My yacht is a 13-foot Sunfish."[6] Or: "I get wild when they talk about that white-shoe thing. Why are we number one? Because we are nice people? Because we play golf? I stand on our record."[7] As at Morgan Grenfell, this discomfort with a sedate past sparked revolt among younger partners and enabled Baldwin to push for sweeping changes in the firm's *modus operandi.*

Baldwin was also perceptive about Morgan Stanley's defects in the mid-1960s. It was poorly managed and becoming too big for the old consensual style. There were no budgets, no planning, and no modern management—just endless collegial discussions. Bookkeeping was still done by clerks on high stools, who copied entries into leather-bound ledgers on tilt-top tables. All the while, the firm was growing and bursting in its small headquarters. In 1967, it vacated its cramped offices at 2 Wall Street. It was still unthinkable that Morgan Stanley would lack a Wall Street address. Harry Morgan was afraid that if the firm had a Broadway address, London friends might think him a theatrical producer. He was only reconciled to a new office building at 140 Broadway because it was the former Guaranty Trust address.

During the 1960s, Baldwin made repeated efforts to run the firm but was rebuffed. Stymied by his slow advancement, he went down to Washington from 1965 to 1967 and served as under secretary of the navy. In these years, Baldwin was always promoting schemes to proselytize for the war on college campuses. Partners who found him pushy hoped he wouldn't return. When he did, they again spurned his demand to take charge of daily operations, and he again decided to leave.

He nearly escaped to the giant Hartford Insurance Company. Felix Rohatyn of Lazard Frères was playing matchmaker between ITT chairman Harold Geneen and the Hartford board. As Hartford's investment banker, Baldwin frostily rejected an overture from Rohatyn. The Hartford board decided to bring in Baldwin as a one-man "white knight" to ward off ITT's advances. In December 1968, Baldwin was set to become Hartford's chief executive when Geneen, enraged by reports of his move, launched a hostile tender and forced Baldwin to retreat back to Morgan Stanley. Now it was a no-exit situation: Baldwin and Morgan Stanley had to come to terms. With his enormous frustration and bottled-up energy, Baldwin resumed his campaign to shake up the firm and in 1969 got it to call a rare planning session. Outvoted, he later conceded it was a "god-damned disaster."[8] What saved him was partly a generational change. As older, Depression-era partners retired, they were slowly being replaced by a new group recruited in the early 1960s. In 1970, the firm's twenty-eight partners admitted six young men, including Dick Fisher and Bob Greenhill. They were known as the "irreverent group of six," and eventually they would tip the power balance toward Baldwin, giving him the votes to launch change. But at first, they wanted the nice, tight, rich Morgan Stanley of old.

Contrary to the views of more myopic partners, Bob Baldwin saw Morgan Stanley as fighting for its life. He queasily noted the rise of Salomon Brothers and Goldman, Sachs, which were using their trading skills to chip away at the four dominant firms—Morgan Stanley, First Boston, Kuhn, Loeb, and Dillon, Read. At this point, Morgan Stanley still exhibited vintage snobbery about

"traders" being socially inferior to "bankers"—a tradition dating back to Pierpont Morgan. This was also true at First Boston, which would call its underwriting wing the House of Lords and its trading room the House of Commons. Trading was still thought a coarse commodity business best left to Jewish firms such as Salomon and Goldman, Sachs. In the Salomon Brothers culture, in contrast, traders stigmatized corporate finance people as "light-bulb changers" or "order takers."[9]

John Gutfreund of Salomon Brothers was using the firm's trading prowess to win new business and secure a better spot in syndicates. "Salomon and the rest were besieging chief financial officers with suggestions and ideas that we couldn't match," said Sheppard Poor, a former Morgan Stanley partner. "There was a proliferation of different financing vehicles."[10] Morgan Stanley had always cultivated the big corporations, the users of capital. Salomon and Goldman, in contrast, had close relations with the suppliers of capital, the institutional investors who now accounted for three-quarters of the New York Stock Exchange trading. And power was now tilting toward these providers of capital.

In the volatile 1960s, with inflation induced by Vietnam spending, pension funds, insurance companies, and so on were managing their portfolios more actively. Instead of buying large blocks of bonds and holding them until maturity, they wanted to swap new blocks for old ones. This was impossible for an underwriter like Morgan Stanley, which had no trading operation. Large investors had other specialized needs. Trading big cumbersome blocks of stocks, they needed intermediaries to do "block positioning"—that is, temporarily taking the block off their hands and selling it whole or piecemeal. Salomon Brothers had the capital and trading strength to perform such intricate feats and used these services to expand its underwriting business. As an outsider, John Gutfreund had no scruples about raiding clients or doing other things anathema to the Wall Street club. He was the first to show that "the power to distribute securities would become the power to underwrite them."[11]

Gutfreund seemed to enjoy tweaking Morgan Stanley. When former defense secretary Robert McNamara became World Bank president in 1968—the bank's first non-Wall Street president—he wanted to stimulate competition among underwriters and brought in Salomon Brothers along with Morgan Stanley and First Boston. In a tough bargaining session with the three firms, McNamara demanded a better price. Larry Parker of Morgan Stanley got up and said, "Well, I've got to go and consult my partner." In a puckish mood—but also telegraphing that he would compete on price—Gutfreund rose to consult *his* partner. Then he suddenly sat back down. "Well," he said slyly, "she's always said yes to whatever I want to do." This put pressure on

Morgan Stanley and First Boston to follow his lead.[12]

To maintain syndicate leadership, Baldwin saw that Morgan Stanley would have to admit people long shunned as the rabble of the business—salesmen and traders. This move toward trading and distributing securities—and not simply allocating them to other firms to sell—would explode the small, posh Morgan Stanley, which then had about 250 people. The firm could no longer monitor securities markets from a lordly distance. At a 1971 planning session, Bob Baldwin finally got a decision to develop a sales and trading operation, and Morgan Stanley ceased to be the stately underwriting house created in 1935. It would develop relationships with institutional investors by trading and distributing stocks and bonds. "We made one decision," said Dick Fisher later, "and that simple decision led to all the subsequent growth of our firm."[13] The changes were implemented piecemeal, with Fisher put in charge of corporate bond trading. Later, Archie Cox, Jr., son of the Watergate special prosecutor, presided over equity trading.

Trading meant risk and required more than the $7.5 million in capital that Morgan Stanley had in 1970. The younger partners had long feared that the firm's precious capital might be depleted by the death of its aging partners. To preserve capital, Morgan Stanley switched in 1970 from a partnership to a partially incorporated firm. This also allowed dividends to flow in from Morgan et Compagnie International in Paris without punitive taxes.

As Morgan Stanley expanded into a full-service firm, the corporate culture changed. For almost forty years, Morgan Stanley men had traveled in a sedate, elite world, dealing only with chief executives. Traders inhabited a rougher world. "It was a different kind of culture," said one trader. "Instead of the low-key, white-shoe style, this group was the raucous, tough-minded, four-letter-word kind of crowd that you get in a high-pressure situation." Many older partners wrinkled their noses at the traders. "There were also young partners who looked down on us as if we had dirt under our fingernails and were an inferior breed," recalled a former trader. Tastes changed: Morgan Stanley suddenly had a Sky Box at Madison Square Garden. A former partner noted that "Morgan Stanley partners didn't go to basketball games up till then."

At first, it was difficult to recruit people: nobody believed the august Morgans was serious about trading. Traders lived in a world of split-second, high-pressure decisions. Where corporate finance people ambled in at 9:30 or 10:00, traders were at their desks by 8:00. When Fisher tried to ban employees from eating lunch at their desks, he couldn't enforce the rule. In the superhuman effort to recreate the firm, some people worked all night. "I can remember someone asking me early one morning whether I was coming or going," recalled Frederick H. Scholtz, who came in from General Foods to

oversee planning.[14] His secretary would surreptitiously change her dress to hide that she had stayed all night.

The trading operation was built from scratch. Morgan Stanley hadn't had its own floor trader at the New York Stock Exchange. Partners had feared, rather vainly, that if the Morgan trader sold General Motors or AT&T, it would precipitate an avalanche of selling. Now traders were installed without setting off any market crashes.

This helter-skelter expansion had healthy side effects—especially an end to the firm's homogeneity. Before long, the Wasp citadel had "partners" with strange ethnic names. In 1975, Luis Mendez, a Cuban refugee with a distinctly Spanish accent, who had once wrapped packages in B. Altman's basement, was made a partner from the bond-trading desk. His success reflected a new stress on performance. This trend was strikingly revealed when Robert McNamara visited the firm. At a luncheon with Morgan Stanley executives, McNamara ignored more senior figures to question Mendez, who sat in the rear and could clarify pricing mysteries about World Bank issues. The blunt, streetwise Mendez told McNamara that the World Bank was overpricing its issues and alienating customers. Afterward, McNamara said to his companion, Eugene Rotberg, "This firm isn't as stuffy as I thought it was."[15]

Morgan Stanley tossed many traditions out the window. It no longer had the luxury of growing its own people and inculcating them with Morgan style. In recruiting traders, it had to favor those with youth, nerve, and stamina; almost half the managing directors enlisted after 1970 were under thirty-five. To attract traders, the firm introduced production-oriented compensation, which eroded collegiality and generated new rivalries and tensions. Baldwin gloried in this rough world of sharp elbows. Where Morgan men had disdained competition, he said approvingly, "The only way to make investment banking more competitive would be to gouge eyes out."[16] As the firm increased tenfold in a decade, it suffered terrible growing pains and throbbed with new tensions.

To woo institutional investors, Morgan Stanley established a Stock Research Department. In April 1973, Frank Petito called in Barton Biggs, a Yale man and an ex-marine, who had managed a hedge fund in Greenwich, Connecticut. Biggs had been a go-go "gunslinger" portfolio manager of the late 1960s, but a respectable version of the breed. As *Institutional Investor* said, "Biggs was definitely the kind of gunslinger you could introduce to your daughter."[17] Petito offered Biggs a partnership, which he accepted on the spot. It was one of the rare times in Morgan Stanley history that anybody was brought in as a partner.

The stock-research decision was controversial. Perry Hall and other senior

people opposed it, claiming it might threaten their blue-chip franchise and open up conflicts of interest with clients. As partner Larry Parker said, when Morgan Stanley started equity research, “We took a very deep breath.” To establish his autonomy, Biggs fired salvos at IBM in a 1974 piece in *Barron’s*. Scrapping an old Wall Street taboo, Morgan Stanley raided other firms, hiring analysts with such abandon that Baldwin was besieged with angry calls. “I’ve had a number of good friends call up and be damned mad at me,” he said. “I’ve promised we’d take no more.”[18]

In rapid succession, major elements of the Gentleman Banker’s Code were breaking down. Like Morgan Grenfell, Morgan Stanley kept up its gentlemanly aura only so long as nobody poached on its territory; once threatened, it retaliated with a vengeance. Both on Wall Street and in the City, the graceful, leisurely world of securities syndicates was being replaced by the predatory world of mergers and the freewheeling, irreverent world of traders. Form was simply following function.

During this transition, Harry Morgan continued to represent standards in a firm that was easily tempted to forget them. Although he became a limited partner in 1970 and technically lacked a vote, he still made his influence felt. Shortly after Morgan Stanley was incorporated, American Express tried to acquire it. Opinion was divided, some older partners favoring the acquisition, many younger ones dead set against it. Harry Morgan, in an emotional speech, said he wouldn’t sell his birthright for a mess of porridge. “You can do what you want, but the name Morgan is not for sale.” American Express was sent packing.

Similarly in 1969, the firm entered into a new venture with Brooks, Harvey and Company to finance and invest in real estate. This real estate offshoot got off to a shaky start. At one point, the Teamsters came along with an irresistible proposal: they wanted Morgan Stanley to manage all their properties in the United States. Almost everyone favored the move except Harry Morgan, who sat silently through the discussion. “Young fellows,” he said at last, “as long as I’m alive, this firm is not going to do business with the Teamsters.”[19] The discussion ended.

By 1973, the burgeoning Morgan Stanley was surveying both uptown and downtown sites for new offices. Many partners refused to abandon Wall Street to follow corporate clients to midtown. Baldwin disagreed but couldn’t budge them. Then he lunched with Andre Meyer of Lazard Frères, which had moved up to Rockefeller Center. He told Meyer about the controversy. “Fine,” said Meyer, laughing, “I’ll be having lunch uptown with your clients while you’re having lunch downtown with your competitors.” Baldwin went back downtown all fired up. He prevailed upon his colleagues to look at three floors available in the Exxon Building on Sixth Avenue.

Baldwin took them uptown via the Sixth Avenue subway, changing at West Fourth Street, rather than by way of the Seventh Avenue line, whose nearest stop, at Fiftieth Street and Seventh Avenue, was a popular spot for streetwalkers. The manipulation worked. In August 1973, Morgan Stanley, the very symbol of Wall Street, moved to the Exxon Building in midtown. The move underscored that paramount reality of the Casino Age—that once-proud and all but omnipotent bankers were now subservient to their corporate clients.

BOB Baldwin's palace coup at Morgan Stanley coincided with a top-secret attempt to recreate the old House of Morgan abroad. As finance became more global, the Morgan houses were colliding in obscure places and casting confusion. The problem was typified by fapan's stubborn belief that Morgan Guaranty and Morgan Stanley—whatever their mischievous, self-serving denials—belonged to the same *zaibatsu.* The situation was endowed with comic-opera complexity on account of Morgan Grenfell's global expansion in the late 1960s.

In the dozy 1950s, Morgan Grenf ell was boxed into Britain by exchange controls and the fear of clashes abroad with Morgan Guaranty. In 1967, to jolt Morgan Grenfell from lethargy, Lord Harcourt had drafted his friend Sir John Stevens as the new chief executive. Like Harcourt, Stevens had been British economics minister in Washington and U.K. executive director of the IMF-World Bank. During his six-year tenure, Stevens would exert a pervasive influence on Morgan Grenfell. At a firm weak in broad strategic thinkers, his vision of a global future was exceptional. He also brought an air of adventure to the stodgy old bank. During World War II, he had parachuted into Italy as a member of the Special Operations Executive, Britain's secret dirty-tricks intelligence unit, to finance the underground Piedmont Liberation Committee. He infiltrated occupied territory in Greece and France and in 1945 accepted the surrender of German divisions in northern Italy, receiving the freedom of the city of Turin for his work with Italian partisans. Fluent in six or seven languages, he became a roving emissary for the Bank of England and, in 1957, executive director. The next year, chattering in Russian and dazzling Muscovites, he made the initial contact between the Bank of England and the Soviet State Bank, later giving Morgan Grenfell a financial edge with the Soviets. By the early 1960s, Stevens was on the short list to be governor of the Bank of England. When he lost out, he accepted Harcourt's offer to come to Morgan Grenfell.

As Stevens toured the world opening up new Morgan Grenfell offices with Foreign Office recruits, the firm happily exploited 23 Wall's fame. Morgan Grenfell's overseas clients tended to be American companies who banked

with Morgan Guaranty. As David Bendall, one of Stevens's Foreign Office recruits, said, "As Morgan Grenfell went abroad, nobody knew the firm. But they did know J. P. Morgan and Company, and we used the name."[20] "They were known worldwide as the number-one American bank," conceded Stephen Catto, "and so the Morgan Guaranty stake was very helpful in our establishing business abroad."[21] Of course, as Morgan Stanley and Morgan Grenfell traded on the name, Morgan Guaranty's difficulties increased geometrically.

Morgan Grenfell was growing restless with Morgan Guaranty, which prevented it from entering the vital, lucrative U.S. market. Under Glass-Steagall, Morgan Grenfell couldn't function as an investment bank in New York. "And I'm sure that from the viewpoint of the older, more senior Morgan Grenfell people, we were American upstarts anyway—second-class citizens and clearing-bank types," said Rod Lindsay.

Morgan Guaranty, meanwhile, was going like gangbusters in the Euromarkets and by the early 1970s had nearly six hundred people based in London—nearly the size of the entire bank in the 1950s. Companies that used Morgan Guaranty in home markets, such as Michelin and Siemens, flocked to it in London. When Danny Davison became Morgan Guaranty's London manager in the late 1960s, he found Morgan Grenfell such a dry, sleepy place that he preferred doing business with Lazards or even Warburgs—a sore point at Morgan Grenfell. As liaison with 23 Great Winchester Street, Davison imagined he was entitled to share trade secrets. Early in his tour, he attended a partners' meeting but found that confidential sections were neatly snipped from his briefing book. Insulted, he swore never to return. It was the same old confusion bred by the bizarre situation in which Morgan Guaranty held a giant stake in Morgan Grenfell, but was supposed to remain passive. If this appeased the Bank of England and the Federal Reserve, it went counter to logic and human nature.

Around the same time, Lew Preston sent Sir John Stevens a letter protesting Morgan Grenfell's mounting foreign-exchange dealings. As its New York banker, he was disturbed by excessively large open positions Morgan Guaranty had to cover. "From then on, there was a perceptible cooling off, although in the most friendly way," recalled one ex-Morgan Grenfell executive. And as banker to Morgan Stanley's new trading operation, Morgan Guaranty was also intermittently disturbed by *its* overdrafts.

As shown by American Tobacco's electrifying dash at Gallaher, Morgan Grenfell and Morgan Stanley had been drawn together by merger work. Sir John Stevens of Morgan Grenfell and Bill Sword of Morgan Stanley now contemplated a scheme for closer global cooperation. But they couldn't proceed without Morgan Guaranty, which owned a third of Morgan Grenfell

and shared in Morgan et Compagnie International, the Paris underwriting operation Morgan Stanley had inherited. (The latter now handled at least twice the Eurodollar financing of any other U.S. investment bank.) Morgan Guaranty was indeed intrigued by the notion of a foreign merger after a Morgan Grenfell delegation broached the idea at a confidential New York meeting in August, 1972. Disputes over the Morgan name, especially in Japan and the Middle East, had caused unending friction. Since some foreign customers would never fathom the whole Byzantine Morgan history, why not make an advantage of necessity? Paris had already shown the fantastic power latent in combined effort.

So on June 20, 1973, exactly forty years after Pecora's thunderous denunciations, members of the three Morgan houses journeyed to the Grotto Bay Hotel in Bermuda, a honeymoon hideaway, for a secret meeting. Its purpose—to resurrect the House of Morgan beyond U.S. regulatory reach. The precautions for secrecy were extraordinary. The operation had taken the code name Triangle and was so hush-hush that only the most senior people knew of the meeting. (Over sixteen years later, when Ralph Leach, then chairman of Morgan Guaranty's Executive Committee, was asked about the Bermuda meeting, he replied, "What Bermuda meeting?" When it was described to him, he said bitterly, "Gee, it must be nice to be a Morgan insider."[22]) For older Morgan people, the proposed reunion seemed to be a chance to relive glory days. The plan called for the three houses to pool their overseas securities business in something called Morgan International. Morgan Guaranty and Morgan Stanley would each have a 45 percent stake and Morgan Grenfell the remaining 10 percent. The new entity, in turn, would own half of Morgan Grenfell. In foreign outposts where they had sparred, the three houses would cooperate instead. It would be an elegant solution to the chronic identity problem.

Important to these discussions was a momentous development that had taken place at Morgan Guaranty. In 1969, the firm created a one-bank holding company called J. P. Morgan and Company, reviving a name dormant since the Guaranty merger in 1959. "There was controversy about dropping the Guaranty name for the holding company," explained Guido Verbeck. "But we just wanted to keep pushing that Morgan name. It was magical."[23] At first, Morgan Guaranty constituted virtually all of J. P. Morgan and Company, but it would gradually shrink as Morgans became a diversified, financial conglomerate. Such one-bank holding companies allowed banks to expand into leasing and other fields and issue commercial paper exempt from Federal Reserve interest-rate ceilings. Along with CDs, commercial paper, and Eurodollar deposits, they helped to liberate 23 Wall from the constraints of Glass-Steagall. This new freedom perhaps made the bank more skeptical of

any alliance.

For all its imaginative appeal and historic resonance, the Bermuda meeting was a fiasco. A major obstacle was political: if banks no longer operated under direct political supervision, as they had with the 1920s foreign loans, they still behaved in a manner broadly consonant with national interests. They instinctively sought government protection for foreign loans and couldn't casually defy the State Department or Foreign Office. As in the 1930s, geopolitical divergences in U.S. and British policy made cooperation difficult. "Morgan Grenfell was lending money to our friend Castro in Havana," said Walter Page, then Morgan Guaranty president. "They were also lending money to North Korea. We couldn't do that and Morgan Stanley couldn't either. That kind of thing made it almost impossible."[24] The Cuban and North Korean loans were, in fact, guaranteed by the British government. Thanks to Sir John Stevens, Morgan Grenfell was also strong in export credits to Iron Curtain countries.

For Morgan Grenfell, the meeting brought out an old ambivalence toward "big brother" in the proudly sensitive junior partner. As the smallest of the three Morgan houses, the British firm feared that it would be overpowered by the bigger Americans. This sentiment was especially prevalent in the Corporate Finance Department, which threatened a revolt if the deal went through. Great Britain was about to enter the Common Market. On that basis, David Bendall of Morgan Grenfell pleaded for a special British role, arguing that his firm had the best access to Commonwealth countries and should "lead" the new joint venture into Europe. "I guess I was the one who put his foot in the plate," said Bendall. "The Americans said it was the most chauvinistic thing they had ever heard. But we felt we were being fitted into somebody else's structure."[25] Lewis Preston and the Morgan Guaranty people felt they had been grossly misled as to the level of Morgan Grenfell enthusiasm. They had been prodded into the meeting in the belief of an imminent Morgan Grenfell-Morgan Stanley deal. The two American houses were also deeply offended by Bendall's insinuation that Americans were disliked in Europe. Preston was so incensed that he threatened to sell Morgan Guaranty's one-third stake, although he was soon calmed down by Morgan chairman Ellmore C. Patterson.

The Baldwin coup at Morgan Stanley added complications. It had installed a new generation whose brusque, thrusting energy and irreverent style offended Morgan Grenfell sensibilities. "The Morgan Stanley boys were the real go-ahead graspers," recalled a Morgan Grenfell official. "You could see a mile off they were just there for the grab. They were assuming they would be entitled to boss the thing and lead it." Many Morgan Stanley naysayers, in turn, thought Morgan Grenfell a morguelike merchant bank full of lazy,

pompous dukes and earls employing anachronistic methods. They were not about to play second fiddle to the Brits.

The Morgan Guaranty people had secret reservations about the new venture with Morgan Stanley. As a former official at 23 Wall noted, “There was always a feeling at the bank that Wall Street [i.e., Morgan Stanley] was full of get-rich people.” The salary differential had always been a sore point: a Morgan Stanley partner might earn $150,000 in a bad year, $500,000 in a good year, so that even a junior partner might earn more than Morgan Guaranty’s chairman. Anybody who stayed at Morgan Guaranty had to believe it represented something superior. Otherwise why not jump ship and go to the more lucrative Morgan Stanley?

Morgan Guaranty also jealously treasured the fruits of a spectacular decade of building up overseas branches and taking equity stakes in foreign banks. Of the three firms, it had experienced the most robust growth, traveling far beyond the little hothouse bank that stood in Morgan Stanley’s shadow in the 1950s. “By Bermuda, Morgan Guaranty was a real entity in this world and had more feet in a lot of places than any of the others,” Walter Page explained. “We would have been giving up a hell of a lot that we had accomplished already in Japan, Australia, Singapore, and Hong Kong.”[26] By 1972, a third of J. P. Morgan and Company’s profits were coming from abroad, a figure that would soar to over 50 percent within a few years. It had moved furthest and fastest toward globalization and didn’t want to share its booty with others.

The final set of reservations in this complicated game came from Morgan Stanley. Buoyed by its success in Paris, the firm felt understandably brash and confident and willing to go it alone abroad. “They thought they were big, independent, and successful and didn’t need nannies,” recalled an observer. Yet not everybody was opposed. Shep-pard Poor later said, “The internationalists thought it would be beneficial to expand our ties overseas. The domestic people thought we would be giving away more than we were getting.”[27] Worried about Morgan Stanley’s limited capital, Frank Petito felt strongly about his firm’s need for Morgan Guaranty’s deep pockets. (The visionaries at all three firms were always obsessed with capital.) But Baldwin, suspicious of foreign business, which he often saw as a waste of time and money, didn’t provide the necessary push, despite his sentimental attachment to the Morgan name and history.

At the Bermuda meeting, the House of Morgan—as a dream, a possibility, a will-o’-the-wisp—ceased to be. Afterward, the three firms largely went their own ways and evolved into separate and quite combative competitors. The age of interlocking partnerships, of spheres of interest and mysterious interplay among financial powers, was over. In 1974, Morgan Grenfell set up

a New York representative office, the first beachhead of a counterinvasion. Far more than the two other firms, it would suffer from Bermuda's failure, which might have given it a strong, early presence in global securities markets, albeit at the cost of its identity. A minority, led by Lord Catto, presciently believed that it was better to be a major player in global markets, even if in a junior role, than to be doomed to second-rate autonomy. In 1976, Morgan Stanley bought up the remaining one-third interest of the Paris operation, renamed it Morgan Stanley International, and packed it off to London under Archie Cox, Jr. In 1979, Morgan Guaranty, having at last recovered from the Schwab trauma, set up Morgan Guaranty Limited in London for Euromarket underwriting, facing off against the Cox venture. Both times Morgan Grenfell spurned invitations to participate, afraid of being swallowed up. Now the three Morgan houses would fight each other without quarter.

At Bermuda, the House of Morgan died a quiet death. In characteristic Morgan style, the funeral itself was unknown to the outside world. No obituaries appeared in the press; it died in secrecy.

WHILE Morgan Guaranty retained a tweedy, well-bred style of banking in the mid-1970s, Morgan Stanley experimented with a more muscular approach to business. It faced competitive threats that didn't permit the old mannerly Morgan style. For all its braggadocio and chest-thumping swagger, the firm was very vulnerable, as Bob Baldwin realized when he campaigned for a new trading operation in stocks and bonds. As his chief visual aid, Baldwin would hold up an old tombstone ad and point out the legions of competitors who had perished. Morgan Stanley now faced a host of brawny rivals, trading powers such as Salomon Brothers and Goldman, Sachs, and that retail behemoth, Merrill Lynch. The gentlemanly way of doing business was becoming a privilege the firm could no longer afford. Morgan Stanley betrayed no mood of crisis. With clients such as

General Motors, Exxon, General Electric, AT&T, and Texaco, it didn't exactly panic. As *Business Week* said in 1974, "It is still the most prestigious of the investment banking houses, and its name still opens doors everywhere."[28] Even in appearance, Morgan Stanley partners seemed immune to the relaxed look of the times. Of a photograph of two dozen somber partners that illustrated the 1974 *Business Week* article, one writer noted, "The picture looked as though it might have been posed for at a mortician's convention."[29]

Nevertheless, a crisis lurked below the surface. The investment banker's historic role as middleman and gatekeeper of capital markets was being devalued. Mature companies could now sell commercial paper or place debt

privately with institutions. Some companies had grown so rich—Ford; Sears, Roebuck; and General Electric—that they would serve as banks themselves. Lewis Bernard of Morgan Stanley accurately predicted: "Clients will try to do more for themselves. Our principal competition is our clients."[30]

The new trading and distribution wing shored up Morgan Stanley's underwriting business. At the same time, it highlighted the fact that underwriting was becoming a humdrum commodity business. Morgan Stanley needed another main event, not just new sideshows. It found the answer in the predatory world of mergers and acquisitions, setting up Wall Street's first M&A department in the early 1970s. As Morgan Grenfell had already discovered, it was an ideal business for posh but capital-poor firms.

Merger work was no novelty to the firm. In the 1950s, Northey Jones had consolidated several carpet companies into Mohasco Corporation. Alex Tomlinson had been a matchmaker for British Petroleum in its purchase of a large stake in Standard Oil of Ohio. (Morgan Stanley's role was hidden to avoid angering its seven-sister clients, who might not warm to a new oil giant in the U.S. market.) And Bill Sword aided Morgan Grenfell in the American Tobacco takeover of Gallaher. In the past, Morgan Stanley had collected a modest fee for such work or used it as a free loss leader to generate underwriting business. Merger work formed part of a total advisory relationship with clients. Some Morgan Stanley partners now objected to marketing it as a discrete service. This segmentation of the business, known as transactional banking, would gradually supplant the earlier system of comprehensive dealings with clients, or relationship banking.

For the most part, Morgan Stanley had sat out the conglomerate wave of the 1960s. This movement attempted to reduce diverse companies to a common calculus of profit and loss. Conglomerates threw together scores of unrelated businesses to bypass antitrust restrictions that might block intra-industry mergers. The craze remade the corporate landscape, creating eighteen of America's one hundred largest companies; twenty-five thousand businesses vanished in the 1960s. Many takeovers were financed by inflated share prices of the conglomerates themselves—financial hocus-pocus that made Morgan Stanley nervous. The firm wasn't really pressed to participate in the craze. Most conglomerates were acquisitive upstarts and not the staid, blue-chip firms on the Morgan Stanley client roster.

Corporate restructuring was still curbed by Wall Street etiquette, which frowned on unsolicited takeovers. Afraid of conflicts with clients, Morgan Stanley had a rule against hostile takeovers. In 1970, it nearly engaged in its first hostile bid when Warner-Lambert decided to take over part of Eversharp's shaving business; in that case, the mere threat of a hostile takeover made the target submit. So Morgan Stanley's taboo-breaking hostile raid was postponed until 1974, when International Nickel (Inco) pursued the

Philadelphia-based ESB, formerly called Electric Storage Battery.

By this point, an ambitious young partner named Bob Greenhill headed the four-man M&A Department. He had reluctantly entered the takeover area, regarding it as a slow track to the top. Then he saw there was money—lots of money—to be made. As Wall Street's first takeover star, Greenhill would rewrite the rules of the game. He wanted the work to be tough, professional, and extremely disciplined. Most of all, he wanted it to be profitable and not a lagniappe thrown to a favored client. While some older partners still wanted to offer merger service free, Greenhill, Yerger Johnstone, and Bill Sword devised a fee schedule that took a percentage of the money involved in a takeover. From now on, the firm would ask for retainers just to scout mergers, a process in which employees sat around fantasizing matchups.

When merger work was a free service designed to preserve an underwriting relationship with a client, the investment banker had no incentive to approve or reject a takeover, thus guaranteeing his objectivity. Now the incentive system was quite heavily loaded toward advocating takeovers. The bigger and more frequent the takeover, the more profit for Morgan Stanley. The new fee-for-service mentality directly related to the declining importance of underwriting. If blue-chip clients brought in less bond business, why pamper them with extras? "We charge for the services we provide," Lewis Bernard explained. "When a client asks us to take on an assignment, we expect to get paid for it."[31]

Son of a Swedish immigrant and Baltimore clothing-company owner, Bob Greenhill came to Morgan Stanley via Yale, Harvard Business School, and the U.S. Navy. He was one of the "irreverent six" who participated in Bob Baldwin's bloodless coup. In the navy, he was called Greenie, and he remained so called at Morgan Stanley, a firm with a preppy relish for nicknames. (Baldwin was Baldy.) Short and trim with curly hair, powerful shoulders, and a narrow waist, he had a boyish grin that masked an obsessive intensity.

Greenhill personified the rock-'em, sock-'em style that would characterize Wall Street in the 1980s. He came alive in combat, and his stamina in all-night bargaining sessions was mythical. He was tailor-made for financial warfare. A former partner declared: "Bob is smart and completely insensitive. He couldn't care less what you think and he has no need for peer acceptance or approval. He marches to his own drummer. He's very rational, very focused. On the wall of his office, he has an Al Capp cartoon showing Fearless Fosdick riddled with bullets. The caption is MERE FLESH WOUNDS.' That's how Bob sees himself." Once called the "ultimate samurai," Greenhill had qualities that made him a formidable negotiator but a trying person. Another former partner remarked, "Bob knows he's good and he talks down to clients. But CEOs can't afford not to use the best. So they just decide to

stomach him because he's so good."

Greenhill was that Morgan rarity—a partner who emerges as a distinct personality in the public mind. Publicity accompanied transactional banking as naturally as secrecy did relationship banking. Where Morgan style of dress had been aloof and understated, Greenhill wore suspenders monogrammed with dollar bills. (Surely Harold Stanley would have cringed!) He resembled a commando more than the martini-drinking Morgan banker of yesteryear. He was a resourceful, derring-do character. Once in Saudi Arabia, after missing a scheduled commercial flight, he hired a private plane just so that he and two other partners could make a dinner appointment in another Saudi city.

Instead of tennis or golf, Greenhill liked solitary sports that tested endurance. Early each morning, he jogged near his Greenwich, Connecticut, home. He was also a motorcycle enthusiast. Once on a vacation, a bush pilot dropped him and several fellow canoeists into an icy river within the Arctic Circle. A month and five hundred miles later, the pilot rendezvoused with these wilderness explorers in the Atlantic. Green-hill's takeovers resembled such holidays. As a friend told the writer David Halberstam, "Bob regards these battles as miniature Okinawas."[32] Greenhill savored a new rhetoric of corporate battle: "It's important to know about a chief executive, whether he has the stomach for a fight. You see people with the veneer stripped away, in their elemental form."[33] The world of investment banking, once attractive for its leisurely elegance, was now a cockpit for pin-striped combatants.

In 1974, Greenhill was field marshal for Morgan Stanley's first hostile takeover—International Nickel's raid on ESB, the world's largest maker of batteries. It wasn't the first unsolicited takeover in Wall Street history: what was the 1901 Northern Pacific corner if not a raid by Edward H. Harriman? But the auspices shocked Wall Street, for Inco was a conservative, blue-chip firm and Morgan Stanley was the official custodian of the Gentleman Banker's Code.

The old House of Morgan had long dominated mining, having financed Anglo-American; Kennecott; Anaconda; Newmont Mining; Phelps, Dodge; and Texas Gulf Sulphur. Inco's plight typified that of Morgan Stanley's mature mining clients. In the 1950s, the Canadian company had controlled an astonishing 85 percent of Western nickel output. By the 1970s, its monopoly was slipping. Buffeted by fluctuations in nickel and copper prices, management decided to diversify. After the 1973 Arab oil embargo, Inco was tantalized by Philadelphia-based ESB, and there was fanciful talk about electric cars powered by ESB car batteries, with Inco nickel powder in those batteries.

It is important to note that the impetus for this landmark takeover originated not with Morgan Stanley but with Inco. Inco's chief financial

officer, Chuck Baird, had worked under Bob Baldwin as assistant navy secretary. It was Baird who convinced his superiors to undertake the ESB attack—with or without Morgan Stanley. By conducting such a raid, a new Inco management team wanted to shed the company's stolid image. So the proposal came from a trusted client, putting Morgan Stanley on the spot.

The merger business had boomed during the bear market of 1973-74. Hundreds of brokerage firms left the business, limousines disappeared from the canyons, and downtown rents plummeted. The Coachman Restaurant, a favorite luncheon spot, sported a sign that said 'ALL THE SALAD YOU CAN EAT" and "FREE FLOWING WINE."[34] Old-timers said the Street hadn't been so cheerless since the 1930s. Yet for the investment banks, there were hopeful signs in the new *stagflation*—the combination of inflation and economic stagnation. Stagflation suddenly made it cheaper to buy companies on Wall Street than to invest in bricks and mortar. The age of "paper entrepreneurialism," to use Harvard economist Robert Reich's term, had arrived.

The nearly forty Morgan Stanley partners (technically directors after the 1970 partial incorporation) debated whether to spurn Inco or defy a code that had governed the world of high finance for almost 150 years. The firm still moved by consensus in major matters. Against more squeamish souls, Greenhill had lined up Baldwin and chairman Frank A. Petito. Petito's role was curious. Although nominally the firm's chairman, Petito, shy and introverted, shrank from administration, ceding the task to Baldwin. Yet on important policy matters, his vote carried tremendous weight. He was very much the statesman and the conscience of the firm, inheriting the Harry Morgan role. Petito recognized the need for a new pugnacity. A revealing term had slipped into the Morgan Stanley lexicon: when Greenhill's squad needed to prod a reluctant senior man into aggressive action, they said he needed to be *japped*—a reference to frank *A.* Petito.

Greenhill made a pitch for hostile takeovers as an irresistible trend that was fair to shareholders, if not always to management. The argument of inevitability was probably the decisive one. As one partner recalls, "The debate was, if we don't do what our clients want, somebody else will." The partners were more receptive to this argument after Morgan Stanley's work with Morgan Grenfell, and Yerger (ohnstone cited unsolicited raids in London as a precedent for America. Bob Baldwin agreed: "We did a lot of mental gymnastics about it. . . . When the water rises in London, it will soon flood New York."[35]

Frank Petito figured out how to twist the desecration of tradition into seeming veneration: in obliging Inco, the firm would simply be honoring an old Morgan tradition of serving faithful clients. But Petito had enough qualms

about what they were doing to cast the upcoming Inco raid as an exception. A compromise was forged: the bank, in future, would engineer hostile raids only for existing clients and would fully warn them of unpleasant consequences. This, of course, didn't rule out much business. Morgan Stanley's large clients were just the sort that would now want to conduct raids, and they would know all about the unpleasant consequences. The compromise mostly reassured the firm's clients that it wouldn't be coming after *them.*

At this juncture, Morgan Stanley made another unorthodox decision. Like Morgan Guaranty, the firm had long relied on the Wasp white-glove law firm of Davis, Polk, and Wardwell, which had looked on takeover work as vulgar and had avoided it. With Morgan Stanley partners terrified of lawsuits ensuing from takeover work, they now wanted a tough, seasoned specialist. Greenhill insisted on hiring the experienced Joe Flom of Skadden, Arps, Slate, Meagher, and Flom, whom he had met through Bill Sword. Flom was a short, friendly man in glasses who had attended Manhattan's tuition-free City College, then Harvard Law. He pioneered in hostile takeovers in the 1950s, when Skadden, Arps was still a humble, four-man operation. For twenty years, he thrived on the scraps from law firms that were too haughty or too dignified to conduct hostile raids.

When Flom was made a special counsel to Morgan Stanley, there were stormy scenes with Davis, Polk partners, who were deeply offended by the decision. Whatever its other consequences, the trend in hostile takeovers democratized the New York legal world and provided an opening in Wall Street for Jewish lawyers. Both Joe Flom and Marty Lipton of Wachtell, Lipton, Rosen, and Katz profited from the early refusal of old-line Wasp firms to sully their hands with takeovers. In time, Flom would earn $3 million to $5 million a year, and his law firm would end up as New York's largest, with nine hundred lawyers. Flom would be integral to Morgan Stanley's takeover machine. Greenhill later said, "we know each other's jobs so well that we're almost interchangeable."[36] In 1975, Morgan Stanley completed the incorporation process, not wanting to have unlimited liability with the risky Greenhill operation underway.

As for the Inco raid—on July 17, 1974, Bob Greenhill called Fred Port of ESB to say that he and Inco representatives wanted to visit him in Philadelphia the next day. Port was about to depart for a Kenyan safari. Stunned, he privately dismissed Greenhill as a whippersnapper but canceled his plans. Inco's outside directors didn't learn about the imminent move until the next morning, when Chuck Baird and Greenhill briefed them. Approval was nearly unanimous; the sole holdout was Ellmore Patterson of Morgan Guaranty, who cited his board seat at Union Carbide, an ESB rival, as his reason for abstaining.

The raiders then flew off to Philadelphia by helicopter. Their attack would

be vintage Flom-Greenhill—a *blitzkrieg* that gave them the advantage of surprise, a tactic that worked wonders in the early days when they faced inexperienced executives. ESB's Fred Port was shocked when told that Inco wanted to buy his company for $28 a share—a substantial premium over its $19 market price. When Baird added that they would proceed whether ESB liked it or not, Port flushed deeply.

Enlisting the aid of Steve Friedman of Goldman, Sachs, Port issued a letter denouncing such ungracious behavior. Friedman, suspecting shame was now obsolete on Wall Street, advised Port either to fight on antitrust grounds or find a "white knight." All at once, Morgan Stanley and Goldman, Sachs had settled into their respective slots in the takeover world. Representing the restless, mature giants who wished to diversify into other fields, Morgan Stanley took the offense. Associated with the more medium-sized and retail firms likely to be prey, Goldman, Sachs found its *métier* in defense. Billing itself the Robin Hood of Wall Street, Goldman, Sachs would refuse to represent aggressors, although it would sometimes offer them advice. Gradually Wall Street divided into two camps—the offensive (Morgan Stanley, First Boston, Drexel Burnham, Merrill Lynch, and Lazard Frères) and the defensive (Goldman, Sachs; Kidder, Peabody; Salomon Brothers; Dillon, Read; and Smith, Barney). And Joe Flom would consistently square off against defense specialist Marty Lipton.

ESB did bring in a white knight—Harry Gray of United Aircraft (later United Technologies), who leapt into a bidding war that sent the battery maker's price far above the initial bid. Spurred on by Greenhill, Inco delivered a knockout blow, boosting its final bid from $38 to a victorious $41 a share in a day. Inco was suddenly worth more than twice as much as before the frenetic bidding began.

Greenhill would remember Inco nostalgically, whereas Frank Petito would prove more sober and ambivalent about the hostile raids legitimated by Morgan Stanley. "Many did not work out," he later said. "But you've got to remember what the times were like. And it was always management that wanted to do them."[37] This was Morgan Stanley gospel in the 1970s—that the firm was a passive instrument of its clients, even a somewhat unwilling party. Greenhill insisted, "Wall Street had not created the merger trend. . . . We get the transactions done."[38] If this deterministic view spared the firm responsibility, it also betrayed some unspoken uneasiness. Greenhill could never quite mouth the words *hostile* or *unfriendly.* "We prefer not to call them unfriendly takeovers," he told *Business Week* in 1974. "Just because the management doesn't go along doesn't mean that the deal isn't in the best interest of the stockholders, and Morgan Stanley would never allow itself to get so involved in a deal that wasn't."[39]

Like Robert Young's New York Central raid, Inco-ESB would show the shot-in-the-dark quality of hostile takeovers. When Greenhill swooped down on Fred Port, the company had just registered record earnings of over $300 million for its fiscal year. For all its promises, Inco couldn't improve on that. ESB slipped in its rivalry with Dura-cell batteries and the Delco-Sears maintenance-free car battery. By 1980, it was losing money, and its new chairman, Chuck Baird, put ESB up for sale, professing discomfort with its retail-oriented business. That Bob Greenhill was later wistful about Inco-ESB says much about the way in which investment banking was becoming disconnected from the economic realities of jobs, factories, and people. By what logic could the takeover be construed as a victory? Investment bankers were beginning to take a shorter-term view of their clients' businesses.

Once Morgan Stanley sanctioned hostile takeovers, competitors jumped in. A year later, George Shinn of First Boston paired up Bruce Wasserstein and Joe Perella to launch a separate M&A operation. In 1974, $100 million was still considered a big deal. By 1978, over eighty deals exceeded that amount, with a $500- to $600-million range already commonplace. Unlike the conglomerate takeovers of the 1960s, which were financed with the shares of the acquiring company, the new takeovers were largely effected with cash. Because Morgan Stanley booked fees as a percentage of the total, its profits soared.

Like the trading operation, takeover work helped to diversify the firm. Three female professionals were assigned to the M&A Department. Yet Greenhill and his male colleagues erected a wall around the women and segregated them as "statisticians." Their wives also conspired to relegate the women to second-class status: when the unmarried Morgan Stanley women were about to travel to London and Cleveland on takeover business, two irate wives called, squawking about the arrangement. No Morgan Stanley woman would make managing director until the mid-1980s.

The Wall Street move into merger work accelerated into a stampede after May 1, 1975, when the SEC abolished fixed commissions on stock trades. This stripped away an easy, dependable flow of revenue and forced securities houses to forage for new business. Morgan Stanley, which now executed block trades for institutions, lobbied hard against the measure. Borrowing a term from his navy days, Bob Baldwin warned that "Mayday" might prompt the failure of 150 to 200 regional firms—an alarming forecast that proved on the low side. Morgan Stanley regarded these regional firms as possible buffers against retail giants like Merrill Lynch. As head of a wholesale firm long reliant on regional brokers, Baldwin was reluctant to see the demise of his cherished world of syndicates.

When "Mayday" arrived, in 1975, Morgan Stanley tried to buck the tide and cling to old rates. Unsubstantiated rumors spread through Wall Street that

the firm might blackball from its syndicates any firms that stooped to price cutting—a charge Baldwin labeled an “outrageous lie.” It was impossible, however, to hold back a sea of change, and commission rates plunged 40 percent for institutional investors. From these ashes arose the new, piratical Wall Street. Even conservative firms began adopting tactics once considered suitable only to disgruntled outsiders. In the Inco-ESB takeover, it was Morgan Stanley, the flagship of Wall Street, that first unfurled the Jolly Roger, and it would sail it through increasingly troubled seas.

CHAPTER THIRTY
SHEIKS

FOR Morgan Guaranty, too, the recession of 1973–74 disclosed a turbulent new world. The Arab oil embargo and consequent jump in world oil prices produced inflation and skidding financial markets. With an end to fixed exchange rates in the early 1970s, foreign-exchange trading became a wild poker game. In November 1973, Morgan president Walter Hines Page warned friends at Franklin National Bank against excessive foreign-exchange gambling and quietly alerted the New York Fed to the problem. In May 1974, Franklin's foreign-exchange losses led to the first major bank run since the Depression and the biggest bank failure in U.S. history. When Bankhaus Herstatt, West Germany's biggest private bank, mysteriously failed in June, it saddled Morgan Guaranty with a $13-million loss. That fall, *Fortune* warned, "The nation's financial system is facing its gravest crisis since the Bank Holiday of 1933. The crisis is one of confidence. The public has become increasingly worried about the solvency of even the most profitable banks."[1]

With this thick pall hanging over the banking world, the banks were suddenly tempted by Arab petrodollars. If the Arabs caused the financial crisis, they also presented an apparent cure. For Morgan Guaranty, which had struggled to retain balances, the shower of petrodollars had a surreal beauty, like a rainbow in a storm. "We were so worried about dollars," said Walter Page. "Then here came the Saudis with more dollars than we knew how to keep. You almost had to become Saudi Arabians—quickly."[2] The petrodollars flowed mostly into four U.S. banks—Morgan Guaranty, Chase, Citibank, and the Bank of America. Thoroughgoing snobs, the Arabs preferred conservative blue-ribbon banks and prized Morgan's old-money aura, its discreet style, and its resolutely Christian past (the bank had no high-ranking Jewish officer until the 1980s).

As bankers swarmed across the Middle East groveling before Saudi sheiks, Morgan Guaranty enjoyed access no carpetbagger could duplicate. The secretive Morgan-Saudi relationship dated back to Ibn Saud's forging of the Saudi kingdom in the early 1930s, when money-changing shops with mud floors served as makeshift banks. In April 1933, Standard Oil of California (Socal) negotiated the first oil concession with the Saudi finance minister, Abdullah Sulaiman. They agreed to an initial £30,000 gold loan, plus the first year's rent of £5,000 in gold. Making payment posed a riddle, for the

antediluvian Saudi monetary system employed only chunky metal coins; the kingdom wouldn't adopt paper money for another twenty years. So gold—massive heaps of it—was shipped in to make the payments.

The deal was nearly scuttled when FDR, heeding the advice of Walter Lippmann and Russell Leffingwell, embargoed U.S. gold exports. As an American company, Socal required U.S. Treasury permission to ship gold to Saudi Arabia. As it awaited the official go-ahead, its Saudi Arabian future seemed to ride on that one gold shipment. On July 26, 1933, Dean Acheson, then Treasury under secretary, turned down Socal's request. So the panicky oil company bought thirty-five thousand gold sovereigns from a Guaranty Trust branch in London, flouting the new regulations.

In early August 1933, this black-market gold sailed for the Persian Gulf aboard a P&O liner. When it arrived, a Socal representative counted out thirty-five thousand coins under Sulaiman's vigilant gaze. When the Saudis asked what they should do with the money, Socal recommended Guaranty Trust. For years, American oilmen shipped millions of British gold sovereigns to the Saudis by boat or plane. By the 1940s, Socal had taken Texaco, Standard Oil of New Jersey, and Mobil into its desert oil kingdom in a new operation christened the Arabian-American Oil Company, or Aramco. Aramco erected structures ranging from hospitals to camel troughs, exerting an influence in the kingdom rivaling that of the Saudi royal family itself. By importing a great deal of material, Aramco had a constant need for letters of credit and other old-fashioned banking services. And its stalwart banker was Guaranty Trust.

Guaranty's Harold Anderson was probably the only American banker who traveled regularly to Saudi Arabia after World War II, although the Dutch and French were well entrenched there. (The Netherlands Trading Society serviced Indonesian pilgrims to Mecca.) As long-time camel traders, the Arabs valued personal relationships, and the genial, easygoing Anderson brought them colorful gifts, like studded saddles, to win their friendship. Guaranty made loans to Saudi Arabia against oil revenues (possibly including small personal loans to King Saud) and also managed dollar accounts for leading Saudis. As Aramco's banker, Guaranty also managed Saudi oil revenues in dollars.

Although J. P. Morgan and Company had no dealings with Saudi Arabia in the 1950s, it was banker to that other ubiquitous giant in the Arabian Peninsula, Bechtel, the shadowy global construction giant that did the actual building for Aramco. Bechtel formed a close partnership with Saudi entrepreneur Suliman Olayan, a once penniless Aramco dispatcher who ended up with over $1 billion and a 50-percent stake in Saudi Arabian Bechtel Company. As a member of Morgan Guaranty's International Council, Olayan would form part of a dense, impenetrable web whose strands bound Morgan

Guaranty, Bechtel, the Saudi royal family, and American oil companies.

Like a storybook miser, Finance Minister Suliman was often said to hoard the nation's wealth—silver riyals and gold sovereigns—in a chest tucked under his bed. It was one of the world's few portable central banks. After 1950, as the Saudis split royalties with Aramco on the more equitable fifty-fifty basis, the coins came to fill a vault seventy feet long, seventy feet wide, and eight feet high. The old medieval finances would no longer suffice. Yet any attempt to modernize the monetary system ran up against the Islamic injunction against paying or receiving interest.

In 1952, when the Saudis created a central bank, they shrank from so labeling it, in order to avoid inflaming the faithful. Instead, they cunningly anointed it the Saudi Arabian Monetary Agency or SAMA, which started out with about $15 million. It issued Saudi gold coins and the kingdom's first paper money for use by pilgrims to Mecca. This gradually replaced the weighty coin of the realm. But many desert warriors and kingdom retainers preferred solid, precious metals, and King Faisal himself would keep bags of silver in the basement of the Netherlands Trading Society.

Morgan Guaranty helped reform Saudi finance through a remarkable man named Anwar Ali, a Pakistani who first went to Saudi Arabia on a two-week tour of duty as head of the IMF's Middle East department. In 1958, the Saudis drafted him to be SAMA's governor. His mission was to straighten out the kingdom's finances, then in critical disarray as a result of corruption, inflation, and extravagant spending. (The Saudi royal palace had the world's second largest air-conditioning system after that of the Pentagon.) Ali was gentle and scholarly, a devout Muslim in silver-rimmed glasses and urbane Western suits. He became personal financial adviser to King Faisal. As SAMA governor, he commanded more petrodollars than anyone on earth, more gold than Midas. As journalist Tad Szulc wrote in 1974, "Not many kings and presidents held such personal power."[3] With nice semantic juggling, he turned *interest* into *return on investment*, permitting SAMA to amass a modern securities portfolio without offending Allah. "One of the first things Anwar told me about the messy finances he faced was that he had discovered to his dismay that many Saudi accounts in New York were not drawing any interest," recalled William D. Toomey, then with the U.S. embassy in Saudi Arabia. "He found it touching that the banks were so sensitive to the Saudis' religious scruples against acceptance of interest."[4]

To map portfolio strategy, Ali recruited a tiny group of Western bankers, sometimes called the White Fathers or the Three Wise Men in this myth-shrouded operation. Among them was the tall, beetle-browed John M. Meyer, Jr., then head of Morgan's International Division and later chairman. Ali favored such conservative investments as Treasury securities, and Meyer was

just the old-school type to appeal to him. (Inside the bank, he was nicknamed Moody Meyer because he remembered in excruciating detail *Moody's* entry on every security, down to the smallest indenture.) Meyer was also secretive, inscrutable, and trusted for his plain truthfulness. He, in turn, admired Ali's incorruptibility in a land rife with corruption. (Harold Anderson's assistant, John Bochow, would tell colleagues sarcastically, "Never do business in a country where they don't wear overcoats part of the year.") Diverting SAMA deposits to Morgan Guaranty, Ali made it the major Saudi depository. The bank, in turn, hired Ali's son Pasha, a Yale graduate.

For several years, Morgan Guaranty provided SAMA with investment counseling. In the 1960s, however, the American bank became a casualty of its own success. As government adviser, it couldn't solicit Saudi business without encountering a conflict of interest. Morgans needed to open some breathing space between itself and the Saudis. "You couldn't have advisers in a government agency and deal with it at the same time," explained an ex-Morgan executive. So Morgans bowed out and brought in White, Weld of New York and Baring Brothers and Richard Fleming of London.

When the petrodollar gusher erupted, Morgan Guaranty was beautifully positioned. It could pose as protector of the defenseless Saudis against rapacious, self-serving bankers. Recognizing a need for new Saudi financial expertise, Ali toyed with the idea of an international merchant bank. In 1973, SAMA still operated out of a ramshackle building near the Riyadh airport and lacked telex machines. It was moving tens of billions of dollars in deposits around the world with a slim staff of only ten professionals.

At a 1973 IMF meeting in Nairobi, Meyer, Walter Page, and Lew Preston cornered Ali with a plan for a London-based Saudi merchant bank to be the kingdom's Euromarket outlet. Page recalled, "We told him, 'You have to have a window on the world of finance. You have to invest in the right way and keep current with what's going on in the world.' "[5] The Eurodollar market was then moving into high gear in London, and the timing seemed auspicious.

At first, the Saudis wanted to share this largesse in a consortium arrangement with their five principal bankers in Europe and Japan. Instead, Morgans deprecated the voguish consortium concept. "We told the Saudis that they had to tie someone with a bigger share to make it work," said Page.[6] And who, pray, would that responsible party be? When the Saudi International Bank was announced in 1975, SAMA owned 50 percent and Morgan Guaranty 20 percent, with 5-percent shares distributed to other banks. Edgar Felton of Morgans was dispatched to London to manage the new bank. This seemed an inimitable coup for Morgan Guaranty—a partnership with the Saudi central bank.

News of the SIB deal, secretly crafted by Morgan Guaranty, dealt the *coup*

de grace to the special relationship with Morgan Stanley. These were the waning days of the Paris partnership, and Morgan Stanley, learning the news only shortly before its public announcement, was stunned. A SAMA board member, Ali Alireza, told his nephew Hisham, then at Morgan Stanley, about the deal. The firm couldn't believe its total ignorance of the negotiations. According to a former Morgan Stanley partner, "It was a big disappointment to Morgan Stanley and Morgan Grenfell. The lure of the vast Saudi Arabian fortune and all the money to be made was too much for Morgan Guaranty. There wasn't an alliance any longer. Morgan Guaranty had clearly made its mind up to go its own way at the Bermuda meeting." A former Morgan Guaranty official concurs: "When the petrodollars came along, we no longer needed Morgan Stanley."

The Saudi International Bank was a fertile source of fantasies at 23 Wall. Some thought the Saudis might funnel all their export-import financing through the bank; others thought the SIB might have a big account at 23 Wall. The most specific expectation was that the SIB would train Saudi Arabia's future financial elite, allowing Morgans to seed loyal people throughout the Saudi power hierarchy. The country desperately needed a stratum of competent financiers, and the SIB promised to deliver them. The House of Morgan thus looked to be the one bank that would profit from a stress on Saudiizing Saudi finance.

In practice, the SIB never retained the rich young Saudis sent to train there. The explosion of oil prices in late 1973 and early 1974 put too much wealth at the disposal of young Saudis; business opportunities at home beckoned. These Bedouin Arabs were also too attached to culture and family to remain in London for an extended period. "There were never enough Saudis," said one Morgan person. "They all wanted to make their name in Saudi Arabia or peddle influence. Banking was too boring. We ended up dealing with the technocrats, not the royal family." Some Morgan people argue that the Saudi royal family never put its full weight and prestige behind the bank. It took small pieces of sovereign loans but never really blossomed. So its main utility to 23 Wall was simply in preserving the SAMA relationship.

Morgan Guaranty was protective of Saudi Arabia in U.S. politics. In early 1975, Senator Frank Church tried to extract figures on petrodollar deposits. He feared that by threatening to pull out their short-term deposits, the Arabs could blackmail the U.S. government. Morgans and other banks wouldn't divulge the information. Morgan chairman Ellmore Patterson declared: "Much of the information you request would involve a breach of our obligation to keep confidential the affairs of particular clients." Morgans was petrified that the Swiss banks would steal away the deposits. Fed chairman Arthur Burns brokered a deal with the banks, releasing aggregate deposit figures for Middle East states. Of $14.5 billion in deposits by the OPEC

states, 78 percent resided in six banks—Morgan Guaranty, Bank of America, Citibank, Chase, Manufacturers Hanover, and Chemical.

Senator Church proved correct in worrying that petrodollars would enlist the political allegiance of bankers in disturbing ways. The sheiks wanted to use letters of credit as a way of enforcing compliance with the Arab boycott of Israel. Under this arrangement, banks had to certify that goods being exported to the Middle East didn't originate in Israel or with blacklisted American companies, didn't bear the Star of David, and wouldn't travel aboard Israeli planes or ships. In 1976, the American Jewish Congress singled out Morgan Guaranty and Citibank for loyally executing this dirty work and cited their "pivotal role in the implementation of the Arab boycott."[7] Morgan Guaranty executed 824 letters of credit including the language of the boycott, although they protested and successfully expunged the offensive language in two dozen cases. While some banks welcomed tough anti-boycott legislation, Chemical Bank and Morgans testified against it; it was finally enacted in 1977.

As a general rule, the postwar Morgan bank had avoided the sort of political lobbying or proselytizing for foreign governments in which Tom Lamont had specialized. Yet in the case of the Saudis, the bank seemed to hark back to the old days. Along with Bechtel, GM, GE, Ford Motor, and the oil companies, Morgan Guaranty contributed to Georgetown University's Center for Contemporary Arab Studies. "Violent criticism of Israel and American support for Israel are the single most dominant themes of the center's extremely active program," explained one observer.[8] In 1980, the august Morgans also made an uncharacteristic foray into public television, after the broadcast of a British television movie, *Death of a Princess*. This controversial documentary told the story of a Saudi prince who ordered the execution of his own granddaughter after she balked at an arranged marriage. The woman was shot while the husband she had chosen instead watched; he was then beheaded. The Saudis were outraged, and the State Department tried to mollify them. So Morgans joined with Texas Instruments, the Harris Corporation, and Ford Motor to sponsor a glossy, benign three-part series on Saudi Arabia designed to counteract the movie.[9]

UNLIKE Morgan Guaranty, Morgan Stanley had no experience in the Middle East. In its clumsy, often farcical rush to woo Arabs, it ended up in bed with the shady Adnan Khashoggi, then commonly billed as the world's richest businessman. The son of a court physician to King Saud, Khashoggi brokered billions of dollars in arms deals with Saudi Arabia and skimmed off fees from over three-quarters of all defense contracts. He kept palatial homes in ten cities, had his own DC-8 and a yacht fitted with gold fixtures. In 1974,

the Saudi ambassador to the U.N. steered Khashoggi to Morgan Stanley. Allegedly worried about a two-tier Arab world in which Saudi sheiks drove Cadillacs while the masses starved, Khashoggi told the Saudi royal family that they couldn't live so luxuriously while the Sudan lay poverty stricken. The conservative oil states feared Sudan's flirtation with socialism. To correct this, Khashoggi wanted to introduce agribusiness into the region. With the blessings of Egyptian president Anwar Sadat, he planned to create a seventeen-thousand-acre dairy farm near the Suez Canal and a millionacre cattle ranch near the Blue Nile in Sudan. Needing the appropriate technology, Khashoggi eyed an American company called Arizona-Colorado Land and Cattle, which had huge property tracts and cattle herds out West. But the company wouldn't sell until Morgan Stanley came in and negotiated a $9-million stake for him.

In pursuing his vision, Khashoggi was often accompanied by Jan Stenbeck, a handsome blond bachelor from one of Sweden's richest families who was affiliated with Morgan Stanley. Stenbeck seemed to thrive on intrigue and entertained friends with stories about sitting on the tarmac at Khartoum with Sudan's president while the sand swirled around them. Khashoggi would spout a thousand inventive ideas about irrigation and agricultural development but then quickly lose interest and turn to other matters. Mostly he delighted in playing pranks on Stenbeck. Once arriving late at a Cairo hotel for a rendezvous with the Arab, an exhausted Stenbeck told the desk clerk not to disturb him with phone calls. After midnight, when Khashoggi arrived, he was told of Stenbeck's instructions, which suggested to him a practical joke. Mimicking an operator's voice, he dialed the sleeping Stenbeck's room and said his Morgan Stanley boss would soon come on the line from New York. As Stenbeck fought to stay awake, Khashoggi enjoyed his dinner. Periodically, he would pick up the phone to reiterate that Stenbeck's boss would soon be on the line and he must hold on. Stenbeck held on in desperation until he finally succumbed to sleep.

The clever, babbling Khashoggi tempted Morgan Stanley with another mesmerizing vision of riches. He said that his friend Crown Prince Fahd, having lost a reported $6 million while gambling in Monaco, was in hot water with King Faisal; to improve his image, the prince planned to set up a $1-billion foundation to perform good works, possibly with Morgan Stanley as its financial adviser. Would Morgan Stanley be interested in pursuing this with Prince Fahd at Deauville, in northwest France? Stenbeck, S. Parker Gilbert, and Bill Sword took a suite of rooms at a Deauville hotel. Khashoggi was a floor below, Fahd a floor above.

At 8:30 one evening, Khashoggi ushered the trio into his suite to meet the prince. There were over a dozen chairs set up in a circle, with a stool beside each. The prince entered ceremoniously, sat beside Sword, and expressed a

noble wish to do great things for humanity. At one point, when a gorgeous woman in an evening dress walked in, Khashoggi came over and whispered to Sword, “Do you mind if my secretary sits next to Prince Fahd?” Sword, a short, church-going Presbyterian, said no and slid over a seat, wondering at this beautiful secretary. Soon after, a somewhat older, but no less attractive, lady in her forties came in and sat down on Fahd’s other side. “We have here the wife of the editor of *Paris Match*,” Khashoggi whispered to Sword. “She’s doing a feature story on the prince.” Now every few minutes another beautiful young woman entered and sat down on a stool until there was one beside each man. When the room was full, Fahd announced that he had booked a Trouville restaurant for the evening. As the meeting ended, Sword went over and chatted earnestly with the *Paris Match* woman about Henry Luce, Axel Springer, and other publishers; he was surprised by how little she knew about publishing.

Back at the hotel, with the door shut, Gilbert and Stenbeck burst out laughing. They had caught on sooner than Sword to Khashoggi’s game: he had flown in “models” from Paris for a party. Stenbeck kidded Sword: “The Prince and all the girls were very impressed that you had picked out the lead woman, the ‘editor from *Paris Match*.’ She was the biggest hooker of them all.”[10] What Khashoggi’s biographer concluded of Stenbeck might be an epitaph for Morgan Stanley’s early efforts to drum up Saudi business: “He traveled with [Khashoggi] to see heads of state about projects to turn deserts into Gardens of Eden. But when the trips were over and the glitter gone, there was little to show for it.”[11]

FOR Morgan Grenfell, the petrodollar boom was providential, taking up slack as the late 1960s takeover boom wound down. Although it arranged the first Eurosterling issue, in 1972, it lacked the capital to be a top-flight Euromarket competitor and needed a new act in order to survive. It was a pretty dismal time. British exports flagged badly as a near-depression atmosphere overtook the nation’s industry. Amid rising interest rates, the City was rocked by a bust in the property market and a secondary banking crisis in 1973–74. When Lord Poole of Lazards was asked how he survived the debacle, he replied: “Quite simple: I only lent money to people who had been at Eton.”[12]

At Morgan Grenfell, the Arabs would temporarily answer the firm’s problems. With their penchant for secrecy and their appreciation of the confidential style of British merchant banks, the Arabs were naturally drawn to the mysterious maze of the City. They loved the cachet of old stately houses. Also, sympathy for the Arab cause was far more prevalent in the Foreign Office than in the State Department. “In the Mideast, Morgan

Grenfell could take advantage of the U.S. inability to act," declared Christopher Whittington, the firm's deputy chairman. "We could sell them Tornado fighter planes, while the U.S. couldn't because of Congress."[13] Morgan Grenfell had another edge: many London merchant banks were tainted by their Jewish ancestry. So 23 Great Winchester Street became the City firm most immersed in Middle East business. At its peak in the seventies, Arab business contributed up to 70 percent of the bank's revenues.

At first, the man leading the charge was Sir John Stevens, the inveterate traveler and former polyglot Bank of England executive who had advised Iran's central bank. By then he had planted the Morgan flag in old imperial outposts of Hong Kong, Singapore, Australia, and New Zealand and got a Morgan office going in Moscow. David Bendall, brought in from the Foreign Office, did the same in Latin America.

As at previous times in Morgan Grenfell history, stepped-up foreign business forged deeper links with Whitehall. Morgan Grenfell now specialized in arranging government-guaranteed export credits, which Britain was then using to win goodwill abroad. These credits led Morgan Grenfell to finance arms exports to Oman and Jordan as well as power plants, refineries, and other capital projects in the region. Through export credits, the bank also became more involved with Eastern Europe. In 1975, Morgan Grenfell became the first merchant bank to win the Queen's Award for Export Achievement, for managing over a quarter of the government-guaranteed credits. Through all the vagaries of merger work, the firm's rock-solid export credits and impressive portfolio management would lend strength to its balance sheet. In the last analysis, the dull, solid stuff would be its salvation.

Aside from Saudi Arabia, most Arab states before 1973 were too impoverished to be considered good credit risks. The sudden, almost overnight, revolution in their financial status was revealed in a controversial loan that Sir John Stevens secretly negotiated during the Yom Kippur War, in the fall of 1973. On October 6, Egypt, Syria, and Iraq attacked Israel. On October 20, during a fierce, bloody phase of fighting, news leaked out of a Morgan-led loan to Abu Dhabi. Israeli tanks had just advanced fifteen miles beyond the Suez Canal, knocking out Egypt's surface-to-air missile batteries. Disclosure of the loan sent up an uproar, especially among Jewish firms in the City. Official British policy was neutral. Then as now, Morgan Grenfell insisted on the loan's peaceful nature. According to Chris Whittington, "The Abu Dhabi loan was already in the works before the fighting began. We just didn't cancel it."[14]

It was the bank's most controversial loan of the postwar era, sparking heated debate. With each new report, this mystery loan seemed to expand. First announced as a £40-million loan ($100 million), it suspiciously

mushroomed to $200 million within three days. Even as Stevens talked of its use for hospitals or budgetary purposes, it sounded patently suspicious. Awash with oil money, the seventy thousand privileged residents of Abu Dhabi might have enjoyed the world's highest percapita income. In those years, $200 million was an enormous Eurodollar loan, representing nearly $3,000 for each Abu Dhabi resident—absurdly wasteful and unnecessary borrowing for a tiny oil sheikdom under ordinary circumstances.

Also heightening suspicion was the fact that on October 20, the London *Times* reported that the loan negotiations had just begun—suggesting that its origins hadn't antedated the war after all. Even the loan's dollar denomination raised eyebrows. All summer, the Soviets had sent weapons to Egypt and Syria and were now strapped for foreign exchange. It was known in diplomatic circles that in exchange for weaponry, they were demanding hard currency from the Arabs—in other words, dollars. Adding piquancy to the speculation was the fact that two of Morgan Grenfell's Middle East specialists were the sons of cabinet ministers—David Douglas-Home, son of Foreign Secretary Alexander Douglas-Home, and Rupert F. J. Carrington, son of Defense Secretary Peter A. R. Carrington.

With Abu Dhabi having just slapped an oil embargo on the United States, American banks reacted skittishly to a loan that, if problematic in the City, was plain anathema on Wall Street. Morgan Guaranty and First National City quietly bowed out of the syndicate—the more striking in Morgan's case in that it advised the small sheikdom on its $2.5-billion portfolio. The Japanese had no qualms about joining, however. In fact, Japan's government wanted to cultivate Abu Dhabi through direct oil purchases and thus bypass major oil companies. It saw a chance to buy friendship, and the Tokai Bank syndicated a $30- to $50-million piece of the loan among Japanese banks.

Admitting that money was fungible, even Sir John Stevens couldn't vouch categorically for the ultimate destination of the jumbo loan. Others involved no longer pretend about it. One claimed:

> It was certainly a war loan. Eurodollar loans at that level were very few and far between. The loan was prepaid in a matter of weeks. In fact, it did Morgan Grenfell no good whatsoever. As soon as oil prices quadrupled, Abu Dhabi's credit rating went from okay to extra special. So it was hard to explain to Abu Dhabi why the interest rate was so high. It seemed like pure usury to them. The reason the rates were high was because it was a war loan.

On October 27, 1973, after six years at Morgan Grenfell, Sir John Stevens died at the age of 59. He had already recruited his wife's cousin Bill Mackworth-Young, from the corporate stock-brokerage firm of Rowe and Pitman. Mackworth-Young was the leading new issue broker in the City, a man of acute intellect who would succeed Stevens as chief executive and

figure importantly in the firm's future. In retrospect, Stevens's death deprived the firm of a figure who might have propelled it into a global powerhouse, like the rival Warburgs. But he had already injected some dynamism into the firm and set it on an upward international course, restoring it to the front ranks of London merchant banking. Bolstered by lucrative Arab business, Morgan Grenfell would chalk up record profits in a recessionary environment.

With the chameleonlike adaptability of a merchant bank, Morgan Grenfell took on Arab colors with remarkable speed. To please the Middle Easterners, it adopted a policy of not hiring Jews, at least not on the international side. The firm would resort to euphemisms to describe this rule—saying it was "Arab-oriented" or "non-Israel-oriented"—but it boiled down to blackballing Jewish employees and Israeli business. The newly Arabized Morgan Grenfell advised Qatar and Dubai on investment strategy, entered into a joint venture with Jordan's Arab Bank, opened offices in Egypt and Iran, and formed a link with France's Compagnie Financiere de Suez, whose subsidiary, Banque de l'lndochine, had branches throughout the Middle East.

As its Middle East fame spread, Morgan Grenfell found at its doorstep people who required inside knowledge of Arab finance or introductions into Persian Gulf diplomatic circles. In 1975, it drew a suitor who demanded an ironclad guarantee of confidentiality—Henry Ford II. Emissaries from Ford Motor posed a maddening riddle: how could the company, blacklisted by the Arab boycott, operate in both Israel and Egypt? This seemed the political equivalent of squaring the circle.

Ford Motor was a pariah in the Middle East. From 1950 to 1966, it had operated an assembly plant in Alexandria, Egypt. Then an Israeli Ford dealer got permission to assemble Fords in Israel from imported parts. Despite the absence of direct Ford investment or personnel in Israel, the Arab League threatened a regional boycott of Ford cars if the Israeli deal weren't scuttled. For Henry Ford, the decision was sensitive because of embarrassment about his grandfather's anti-Semitism. So the grandson refused to renounce his principles or submit to Arab pressure, and the Israeli operation proceeded unhindered. "It was just a pragmatic business procedure," he later said. "I don't mind saying I was influenced by the fact that the company still suffers from a resentment against the anti-Semitism of the past. We want to overcome that. "[15] Some observers also credited Ford with a shrewd public relations maneuver.

When Ford Motor appeared on the Arab blacklist in 1966, its Alexandrian operation was shut down, starting Ford's exile from the Muslim world. Despite the loss of Arab business, Henry Ford never wavered in his decision. As he flatly told his close friend Max Fisher, a top American fund-raiser for Israel, "Nobody's gonna tell me what to do."[16] In 1972, Fisher accompanied

Ford on a tour of Israel, where they were received by Prime Minister Golda Meir, Moshe Dayan, and Shimon Peres. Ford seemed quite comfortable with his decision.

What Henry Ford never told Max Fisher was that he undertook secret efforts through Morgan Grenfell to reintroduce his company into the Arab world. He wanted to reopen the Alexandria plant as a joint venture with Egypt to manufacture diesel engines, tractors, and trucks. There was a high-level political agenda. Ford thought his company's presence in Egypt might erode Arab resistance, dissolving the sharp distinction between pro-Israeli and pro-Arab American companies. Egypt was more relaxed about the boycott than other Arab countries, although it still put up formidable obstacles. The Ford people had picked up encouraging hints in Washington and the Arab world that the company might soon come off the blacklist.

Ford came to Morgan Grenfell circuitously, after sounding out Morgan Guaranty and other banks as to who had the best Middle East connections. In the early postwar years, Ford Motor had viewed the House of Morgan warily because of its historic association with General Motors. Over the years, however, Morgan Grenfell had handled a remarkable variety of Ford business. It supervised the final sale of Ford U.K. to the Detroit parent company (which then held only a partial interest), introduced Ford stock on the London exchange with Lazards, and managed Ford U.K.'s pension fund. As added incentives to Henry Ford II, Morgan Grenfell had been commissioned by Egypt's central bank to study its nation's foreign-investment law and had even entered into a joint venture with the speaker of Egypt's Parliament.

In 1975, Morgan Grenfell outlined a precise sequence of steps to circumvent the Arab blacklist. The firm knew exactly which sheiks could fix things so that behind a facade of Arab militance, business could proceed unimpeded by religious or political zeal. Morgan Grenfell suggested selling equity stakes in the Alexandria operation to influential bankers, families, and institutions across the Arab world, not just in Egypt. This would build a powerful Arab constituency for getting Ford off the blacklist and would also help to line up cheap Middle East financing. This last was crucial, for Ford believed that only cheap financing could offset prohibitive operating costs in Egypt.

President Anwar Sadat took a personal interest in furthering the project. He was sympathetic to removing American companies from the blacklist if they made investments in the Arab world comparable to those they had in Israel. He insisted that Ford be removed from the Arab blacklist as a precondition for operating in Alexandria but also intimated that he might just go ahead and unilaterally strike Ford from the Egyptian blacklist. It was never entirely clear whether in the end he would courageously defy his Arab brethren or back off.

For two years, Morgan Grenfell and Ford Motor tried to seduce various

sheiks. They played on the willingness of royal Arab families to exploit their positions for personal gain. The Morgan Grenfell strategy accurately gauged the depth of Arab cynicism. Some shieks wanted exclusive Ford dealerships before participating. Some bankers wanted a personal share of Ford's Egyptian plant in exchange for loans. In Saudi Arabia, Morgan Grenfell had targeted Khalid Alireza, a shareholder in Morgan Grenfell and the Egyptian Finance Company. The Alirezas were a powerful, highly respected merchant family and importing agents for many American, British, and German companies. They had even held the Ford dealership before the Arab boycott. Nevertheless, as strict Muslims and uncompromising anti-Zionists, they finally refused to participate. In general, the Kuwaitis were more receptive than the more militant, hard-line Saudis.

This clandestine lobbying continued during the 1976 presidential campaign, when Henry Ford II was a leading business fund-raiser for Jimmy Carter. During the fall campaign, Morgan Grenfell shepherded Ford people around the Gulf states, a mission requiring airtight secrecy, given Ford's link with Carter and the potential for political embarrassment among Jewish voters. In February 1977, promoting his proposed Egyptian operation, Ford met privately with President Sadat for several hours. Sadat saw the Ford plant as a magnet that might draw other companies into an Alexandrian industrial zone. To Ford Motor, Coca-Cola, Xerox, and other American companies barred from the Arab world, he wanted to offer a deal—invest in Egypt, and he would work to delete them from the blacklist.

In May 1977, Morgan Grenfell nearly pulled off the supreme trick of Middle East politics: Egypt announced a joint venture with Ford to assemble trucks and diesel engines; Egypt's approval was contingent on Ford's securing the removal of its name from the pan-Arab blacklist. Egypt was to contribute 40 percent of the capital, and Ford Motor 30 percent, with the remaining 30 percent parceled out to the Arab friends Morgan Grenfell had rounded up. In October 1977, after Egypt removed Ford from its own blacklist, the agreement was signed.

In the end, the project was stillborn, apparently for a variety of reasons. There was thunderous Arab opposition: the lobbying effort hadn't silenced Arab militance or purchased the necessary high-level cooperation. Mohammed Mahgoub, Sudanese head of the Arab boycott, bitterly denounced Ford and threatened to boycott products made in the Alexandrian plant. And since the plant was to produce for export as well as domestic consumption, this would reduce its value to Ford. Perhaps the greatest sticking point was that the Egyptians, after endless haggling with Morgan Grenfell, refused to modify their Public Law 43, which set tough conditions on foreign investment. Without such changes, Ford felt that it couldn't operate at a profit.

The Egyptian initiative would disappear, despite public announcement of

the deal in 1977 and more meetings that year between Ford officials and Anwar Sadat. It was almost as if it had never happened, so completely was it buried and forgotten. When approached about it, Ford Motor wouldn't comment, saying the information was "legally privileged." And when Henry Ford's close friend Max Fisher was asked, he said, "Frankly, I have never heard of any of this before."[17] It was a Morgan operation in the classic style of Teddy Grenfell: it left no footprints behind.

THE exorbitant oil prices and interest rates that followed the Arab oil embargo produced many bankruptcies, and Morgan Guaranty spent much of 1975 desperately plugging fingers into dikes. It was lead banker to W. T. Grant, America's third largest variety-store chain, which foundered that year in history's largest retail failure. The House of Morgan took a $50-million write-off. "We don't make many mistakes," said Morgan's Rod Lindsay, "but when we do make one, it's a beaut."[18]

However grand its global operations, the House of Morgan remained a New York City bank. It had always regarded the city's credit as a proxy for America. To that end, it had saved New York in the 1907 panic, in August 1914, and in 1933. These earlier crises illustrated the strength of the Morgan bank. But by 1975, New York had a population the size of Sweden's and a budget as big as India's. During the city's fiscal crisis that year, the Morgan role would seem marginal compared with that of the three earlier rescues.

Starting with the administration of Mayor John V. Lindsay (brother of Morgan Guaranty's Rod) in the 1960s, New York City had borrowed heavily for expanded social welfare programs. By late 1974, city paper saturated the markets, driving up interest rates and causing steep losses for underwriters, including Morgans. (Commercial banks could underwrite municipal issues backed by taxing power.) That December, Mayor Abraham Beame held an emergency breakfast with bankers at Gracie Mansion. There an advisory group of three influential bank chairmen was formed—David Rockefeller of Chase, Walter Wriston of First National City, and Ellmore C. Patterson of Morgans. Patterson became the leader, because Wriston was ideologically hostile to government and Rockefeller's brother, Nelson, was then the nation's vice-president.

Ellmore ("Pat") Patterson was very midwestern, with a relaxed manner and a slow drawl. His description of the Morgan staff might apply as well to himself: "We're not known for geniuses charging around, but for good solid people with a strong feeling toward the bank."[19] Tall and straight, with a friendly grin, he wasn't a brainy executive, but he was popular and unpretentious. After Nixon devalued the dollar and imposed an import surcharge, Patterson lunched with the head of the Sumitomo bank, who

wanted to know how Patterson could let Nixon take steps harming Japan. “I don’t know the president,” Patterson said breezily. “I never met him.” His luncheon guest was shocked. “You—the head of Morgan Guaranty—don’t know the president of the United States?” Patterson, smiling, said no. If the story says something about Japan, it also says something about Patterson’s candor. He would express no fake altruism about the New York City rescue: “I just didn’t want to have that much debt going bust—just protecting my own hide, so to speak. I sure didn’t want to write off all those investments we had.”[20] His Financial Community Liaison Group held its (mostly unpublicized) meetings at 23 Wall.

In early 1975, when financial markets wouldn’t swallow more city paper, the Patterson group began to function as a *de facto* government. However Beame might bluster in public, he had to submit to the bankers’ coup. There was a transfer of power from the city’s highest elected official to a new, unelected mayor, Pat Patterson. The humiliated Beame would badger Patterson for news, sometimes telephoning him after midnight. When Patterson went golfing, he would see a golf cart speeding toward him and know it carried a message from the mayor. “He kept calling me and he’d say, ‘What’s going on?’ ” Patterson recalled. “As Beame lost more control, we gradually had to tell him what he could and couldn’t do.”[21]

Despite such seeming banker omnipotence, 1975 would actually demonstrate reduced banker influence. Unlike earlier Morgan-led rescues of the city, the bankers were as vulnerable as the city itself. They had granted multibillion-dollar credits to the city and held its paper; at one point, Morgan Guaranty alone had an estimated $300 million of city notes and bonds in its portfolio. By May, trading in New York City debt wound to an eerie halt. Along with a balanced budget and a commission to review city finances, the Patterson group wanted federal guarantees to pry open the closing market. From now on, their “rescue” would involve lobbying Washington and Albany. They were appealing to the government to rescue *them* and not just the city.

Patterson set up a White House appointment with President Ford, against whom he’d played college football. Accompanied by Rockefeller and Wriston, Patterson argued in the Oval Office that a New York City default would trigger general damage, depressing all municipal bonds. President Ford, thanking the group for coming, offered nothing in return. Long afterward, Beame would stand in Patterson’s office staring at a photograph taken during the Oval Office meeting. “If Ford had said yes that day,” sighed Beame, “he would have been president today.”[22]

The New York City crisis presented an ideological clash among conservative businessmen. Said Treasury Secretary William Simon: “It was one of the saddest days of my life when financial giants like Pat Patterson of

Morgan Guaranty and Walter Wriston . . . caved in and finally joined the others in asking Washington for federal aid."[23] Yet the House of Morgan had never adhered to extreme *laissez-faire* Republicanism. Much like Pierpont Morgan, it placed a premium on financial order. It was close to the Federal Reserve and favored government action to avoid financial disruption. It would never produce as ideological a hawk as Walter Wriston.

On May 26, 1975, Dick Shinn, head of Metropolitan Life, hosted a meeting at his home with Felix Rohatyn of Lazard Freres and other representatives of New York governor Hugh Carey. They worked out a plan for a Municipal Assistance Corporation ("Big MAC") to issue, under state auspices, bonds backed by city sales taxes. This permitted banks to exchange $1 billion in shaky city paper for new debt with an A rating. It was Carey's involvement, not the banks', that was the critical turning point. With the city again facing default in September, Carey created an Emergency Financial Control Board to assume budgetary powers from the city.

In mid-October 1975, world financial markets experienced one of those queer moments of falling pressure that sometimes presage storms. Amid fears of a New York City default, Patterson, Wriston, and Rockefeller pleaded for federal help before the Senate Banking Committee. Patterson warned that they were drifting into an unpredictable no-man's-land that could create an "economic downpull of general economic activity."[24] The three bankers asked for a direct federal loan or loan guarantee to prevent otherwise certain default.

In November, New York State announced a moratorium on $1.6 billion of short-term debt. Now fearing a generalized crisis, President Ford got spooked and had Congress approve a $2.3-billion line of credit to the city. Much as the state had put the city in its power, so the federal government put New York State under its control. Patterson felt vindicated: "There were a lot of people who would just as soon have seen New York go bankrupt. They thought it was a good thing to clean it out and get rid of the labor contracts. But our committee, fortunately, stuck with it."[25] Patterson was praised by labor leaders and government officials for his constructive, conciliatory approach.

In the end, the bankers exchanged their risky short-term paper for safe long-term MAC bonds. It had proven necessary to enlist state and federal help. The House of Morgan no longer presided over financial crises. As banks dwindled in power, they could cooperate with government-sponsored rescues instead of leading them. Even the largest could no more control the vast financial markets than they could bid the Red Sea part. The days when a Pierpont Morgan could sit down and extemporaneously write out a single sheet of paper to save the city were long gone.

CHAPTER THIRTY-ONE TOMBSTONES

TO the outside world, Morgan Stanley still presented a debonair facade in the late 1970s. An *Atlantic Monthly* reporter, visiting its six floors atop the Exxon Building, marveled at its aplomb, its artfully modulated decor in brown and ocher. “To stroll through the hallways of Morgan Stanley is to move through a landscape of rolltop desks and Brooks Brothers suits,” the reporter declared.[1] If it stumbled in the Middle East, it profited handily from the oil boom, arranging an astounding 40 percent of the money raised by the big oil companies. As investment banker to Standard Oil of Ohio, it did a record $1.75-billion private placement for the Trans Alaska Pipeline. In 1977, it supervised Wall Street’s end of a $1-billion offering of British Petroleum shares owned by the British government, the largest stock offering in history. Right through the mid-1970s, it ranked first in the stock and bond offerings it managed.

It didn’t seem a place in ferment, yet it was. Each year, it sprouted a new wing: portfolio management (1975), government bond trading and automated brokerage for institutions (1976), and retail brokerage for rich investors through its purchase of Shuman Agnew and Company in San Francisco (1977). The pride, even smugness, of the old Morgan Stanley stemmed from its extreme selectivity in hiring. Now, in a decade, the firm grew from about two hundred to seventeen hundred employees, with capital soaring from $7.5 million to $118 million. It was growing too fast to preserve a homogeneous culture.

As architect of this brave new world, Bob Baldwin often seemed disoriented by the range of new businesses. He had instinctively understood the need to trade and distribute securities yet never quite mastered these alien operations. He found it hard to adjust to a bizarre new world of fluctuating market signals and elevated risk. Risk, after all, had been foreign to the old Morgan Stanley, which only wanted sure things. When a $20-million bet on long Treasury bonds went the wrong way, Baldwin, in a sweat, summoned a meeting of all the senior partners. Another time, when bad news from Washington sent the market tumbling, Baldwin appeared on the floor insisting, “The market should go up. The market’s wrong!” This world couldn’t be controlled, even by somebody as strong and willful as Bob Baldwin.

Bob Baldwin probably saved the firm and destroyed its soul. This new Morgan Stanley was a monument to his force and clear vision, a brilliant adaptation to altered circumstances. Yet he badly politicized a firm long unified by a special *esprit de corps*. His management philosophy played people off against each other. If meant to improve performance, it produced a tense, unpleasant atmosphere. For the first time in the firm's history, senior partners defected for other firms. To some extent, turf fights were inevitable in a larger, richer firm. Baldwin, however, exacerbated the tensions. One example involved extremely close friends, Luis Mendez and Damon Mezzacappa, the two stars of the new trading operation. Yet Baldwin gave Mendez a $25,000 bonus, then went out of his way to tell Mezzacappa about it, saying Mendez was doing a better job. This was either obtuse or insensitive. As Baldwin became more abrasive and difficult, Bill Black, son of the former World Bank president, functioned as the great mediator, pleading for those who found it hard to deal directly with the difficult Baldwin. By softening Baldwin's rough edges, Black held the firm together and prevented an outright split between bankers and traders, such as would later shatter Lehman Brothers.

The major threat to Morgan Stanley's preeminence was its celebrated but increasingly tenuous policy of appearing as sole manager atop tombstone ads, those black-bordered boxes of underwriters' names that appear in newspapers. Tombstone positions were a life-and-death matter for Wall Street firms. Those in higher layers, or brackets, received larger share allotments, while the smaller firms tried to struggle their way upward. Within brackets, firms were listed alphabetically. During the Great Alphabet War of 1976, Halsey, Stuart adopted its parent's name, Bache, just to bootstrap up a few lines in tombstones. This was no joking matter. On May 13, 1964, Walston and Company had been demoted from a top bracket in a Comsat offering; the next day its managing director, Vernon Walston, shot himself, giving a macabre new aptness to the term describing the ad.

In the late 1960s and early 1970s, the top tier—called the bulge bracket—consisted of Morgan Stanley; First Boston; Kuhn, Loeb; and Dillon, Read. The first two originated most business, and Morgan Stanley was reluctant to relinquish the undivided profits of sole managership. A former managing director explained, "When I first went to Morgan Stanley, a senior person laughed and said to me, We only have to scare people into using us as sole manager 50 percent of the time and we're still better off." There was a touch of narcissism in wanting to appear alone in the top left corner of tombstones. There was also an unstated agenda: before the 1970s, Morgan Stanley lacked selling power and disguised this weakness by leading syndicates and having other firms do the selling. As Lewis Bernard later said, the firm "had to keep the Street from realizing the emperor had no clothes."[2] While other firms tried

to ape the sole-manager strategy, none succeeded nearly as often as Morgan Stanley.

In order to make the policy stick, Morgan Stanley had to sacrifice even powerful clients who demanded co-managers on issues. (The Japanese rebuff was an early and notorious example of this.) It skipped one underwriting after Houston Industries insisted on rotating lead managers. It skipped another when Singer wanted to reward Goldman, Sachs for some merger work by appointing it co-manager. But such was Morgan Stanley's evergreen mystique that many firms, from Du Pont to J. P. Morgan and Company itself, still submitted to its golden chains on all their underwritings.

Because up to two hundred firms participated in Morgan Stanley syndicates, they feared its displeasure. Before 1975, Morgan's syndicate manager was Fred Whittemore. Bright, sardonic, and voluble, an avid collector of Pierpont Morgan memorabilia, he was called the Godfather or Father Fred. He had a pervasive power on Wall Street. When William Simon wished to return to Salomon Brothers after serving as treasury secretary, it was Father Fred who interceded with John Gutfreund. In the early 1970s, many attributed E. F. Hutton's stunning rise to Father Fred's patronage, and he didn't hesitate to thwart competitors, such as Lehman Brothers. After each issue, Father Fred filled out large yellow cards listing each firm's performance. Sometimes participants lied or took losses just to look good.

There was always suspicion that Morgan Stanley exploited its sole-manager power to fend off competitive threats. "We could be talking to their clients about an investment banking relationship, and if Morgan saw this, instead of giving us half-a-million shares, they might hold back on us," one rival told the *New York Times* in 1975.[3] Morgan Stanley bristled at these anonymous snipes in the press, which appeared periodically. Father Fred created the modern Wall Street lineup. He kicked out the fading Kuhn, Loeb and Dillon, Read from the bulge bracket and brought in Merrill Lynch, Salomon Brothers, and Goldman, Sachs. After Kuhn, Loeb—historically the most redoubtable Morgan adversary—was absorbed by Lehman Brothers in 1977, senior partner John Schiff met Harry Morgan at a board meeting of the Metropolitan Museum of Art. When Morgan asked how this had happened, Schiff replied, "Henry, you chose your partners better than I did."[4] Schiff's remark pointed to a continuing strength of the Morgan houses—the sheer excellence of their people.

But by the late 1970s, Morgan Stanley's sole-manager policy was a gilded anachronism. How could you handcuff clients in global financial markets when corporate treasurers enjoyed so many options, so much room in which to maneuver? The firm, significantly, had never made the sole-manager policy stick at its Paris joint venture with Morgan Guaranty. A loyal home client like

General Motors Acceptance Corporation openly used other bankers abroad. In April 1977, in a final break with 23 Wall, Morgan Stanley closed up shop in Paris and set up Morgan Stanley International in London, linchpin of its Euromarket operations. The new operation had a rude shock when Australia, a faithful client since 1946, jumped to that old Morgan nemesis, Deutsche Bank. The event underscored not only the new power of global distribution, but the far more anonymous world of interlinked financial markets.

Even at home, there were new forces corroding the chains that bound companies to bankers. Since the days of Louis Brandeis, political reformers had advocated an arm's-length relationship between companies and investment bankers. It was the theme broadcast by Robert Young during his testimony before Judge Medina and in his fight for the New York Central. The system had survived, however, because companies craved the association with the august House of Morgan, a vestige of the days when capital was scarce. But how could bankers still lord it over companies when capital was no longer rationed—when it was available in many markets in many forms? What leverage did they have as new financial intermediaries sprang up? From the clients' standpoint, was there any longer a rationale for having an exclusive banker relationship? The answer was no.

So corporate America now did the work that was once solely the cause of reformers. One by one, corporate treasurers broke the links in the bankers' chains. In the 1970s, Texaco, Mobil, International Harvester, and other clients circumvented Morgan Stanley and placed their debt directly with institutional investors. Other companies used dividend-reinvestment plans or employee stock purchase plans to raise capital. Having to cope with inflation and unstable exchange rates, corporate treasurers were receptive to bright ideas thought up by competing banks to deal with the new volatility. Jack Bennett of Exxon delighted in making Morgan Stanley spar with other firms. "We decided that any time a banker came up with a good idea, we'd talk to him," said Bennett. When he set up "Dutch auctions" for issues, encouraging several competing syndicates, Morgan Stanley began to sense that its sole manager policy faced a mortal threat.

For Morgan Stanley, the doomsday trumpet sounded in 1979. That year, IBM asked the firm to accept Salomon Brothers as co-manager on a $1-billion debt issue needed for a new generation of computers. It was a telling sign of corporate autonomy in the Casino Age that IBM had a $6-billion pile of cash on hand. It had never needed a public debt offering. (Some Morgan people say the IBM relationship—nominally Bob Greenhill's account—was mishandled because nobody ever expected the company to require money.) In applying its sole-manager policy, Morgan Stanley had never before been obliged to turn down a client of such stature. Now here was one of the world's largest corporations, a twenty-year client with a triple-A rating, undertaking

the largest industrial borrowing in history.

Morgan Stanley directors had an emotional, protracted debate about whether to reject the IBM offer and miss a fee of approximately $1 million. The meeting was filled with high-flown rhetoric about upholding tradition. Bob Baldwin and Fred Whittemore were among the hawks who feared an IBM exception would embolden the other slaves to cast off their chains. After much resounding talk, nearly everybody voted to defy IBM and demand sole management. Morgan Stanley was shocked when word came back that IBM hadn't budged in its demand: Salomon Brothers would head the issue, as planned. It was a landmark in Wall Street history: the golden chains were smashed.

Before long, investment banks were raiding other Morgan Stanley clients with abandon, destroying the Gentleman Banker's Code. A competitor observed cheerily, "Once the client list starts unwinding, it's going to unwind all the way. It's just a matter of time."[5] Afterward, most of IBM's business went to Salomon. Swallowing its pride, Morgan Stanley agreed to share issues for General Electric Credit, Du Pont, and Tenneco. It even began to participate in syndicates below the level of manager—a sight as shocking to old-timers as that of a master suddenly donning the livery of his footman. The age of relationship banking was dead.

Snubbed by its blue-chip clients, Morgan Stanley displayed a new receptivity to emerging-growth companies. It had long been chary of lending its imprimatur to untested companies—the name Morgan was synonymous with *established*—and had refrained from initial public offerings of stock. This squeamishness dated back at least to the preferred-list disaster of 1929. In 1980, perhaps taking a swipe at IBM, Morgan Stanley introduced rival Apple Computer to the stock market. (It also bought Hitachi computers for the office, something it wouldn't have done before 1979.) For a long time, the firm had resisted high-tech start-ups. Now Morgan Stanley would lend its name to new ventures. Much like the indigent aristocrat who rents his castle to tourists, the firm would shamelessly trade on its class.

AS underwriting became a more mundane, impersonal business, Morgan Stanley relied more on its takeover department, which boomed under Bob Greenhill's tutelage. Already in the late 1970s, merger work was being hailed as the last gold mine by investment bankers who assumed that Glass-Steagall would someday collapse and lead to a securities business overrun by commercial banks.

Takeovers transformed Morgan Stanley's ethos. As a sponsor of securities, the old Morgan Stanley had fashioned a stately, incorruptible image. Emerging from the fury of Ferdinand Pecora, early partners took fright at the

first breath of scandal. This culture was now tested by the more lucrative takeover work. By the late 1970s, the four-man M&A Department had expanded to a crack squad of fifty. Just five years after the watershed Inco-ESB raid, the firm was handling deals worth $10 billion yearly, with a hundred potential deals in the hopper at any time. M&A was now the firm's major source of profits. At the same time, takeover work had become divorced from the old seamless relationship with faithful clients. It was a giant, disciplined machine separated from the rest of the firm.

Greenhill's brawny raids didn't fit easily into the old collegial firm, especially with his department contributing so disproportionately to profits. As one former partner recalls, "Greenhill was making a hell of a lot of money, and he was lording it over everybody." Opposition, predictably, emerged from the syndicate side. Thomas A. Saunders III, who replaced Father Fred as syndicate chief, issued truculent warnings: "Greenhill should remember that whatever success he has comes from the franchise."[6]

By now, Morgan Stanley had left the white-shoe stereotype far behind, as the brash style of corporate marauders replaced the sedate style of underwriters. The old leisurely syndicate pace gave way to the fast, staccato beat of takeovers, with their weeks of frenetic activity. People now wore beepers, worked ninety-hour weeks, and remained on call over weekends, restricting their outside cultural and political activities—hallmarks of partners in the old House of Morgan. As the corps of managing directors ballooned in size, decisions were no longer made by milling around, and the firm was run in a more autocratic, from-the-top-down style.

Expanding swiftly, Morgan Stanley found it harder to screen people or instill the old culture. As happened in the 1920s, a burgeoning financial industry rapidly attracted a new generation of young people. Untested college graduates were slipped into positions of great responsibility, with almost instant access to information worth millions. The demographic accent tilted to youth.

As questions of possible conflicts of interest in merger work surfaced, Bob Baldwin would quote Jack Morgan's dictum of doing first-class business in a first-class way: "Nobody's perfect, but we think we have the highest ethical standards in the industry."[7] In 1973, the *New York Times* ran an article on insider trading with this caption below Baldwin's photo: "ROBERT H. B. BALDWIN OF MORGAN STANLEY THINKS THE PRACTICE IS PASSÉ." "Maybe I'm naive," he said, "but I think the day of partners swapping that kind of information is long gone."[8] Baldwin wasn't cavalier about ethics, but he placed extraordinary faith in the power of so-called Chinese walls to insulate Greenhill's operation from the rest of the firm.

Morgan Stanley tried to throw the fear of God into merger specialists and

monitored their activities closely. Briefed on legal and ethical issues, young professionals had to sign statements that they understood house rules. To foster a healthy paranoia about using inside information for personal gain, scare memos listing grounds for dismissal were circulated periodically. Oil analyst Barry Good remarked, “I have visions of someone stalking into my office to rip the epaulettes off my shoulders, break my calculator over his knee and drum me right out of the corps.”[9] Every fortnight, security officers conducted electronic sweeps, and projects were camouflaged with the names of English kings or Greek philosophers. Staff members weren’t permitted to discuss them in halls or elevators and weren’t supposed to know each other’s deals. Stock-research people couldn’t even browse in the library’s corporate-finance section.

These safeguards grew more important as more major deals churned through the Greenhill mill. The deals—and the fees—were growing astronomically. In a 1977 milestone, Morgan Stanley got a $2.7-million fee for representing Babcock and Wilcox against a takeover by McDermott, advised by John A. Morgan (Harry Morgan’s bulbous-nosed, ruddy son, rejected by Morgan Stanley after the Charlie Morgan controversy) of Smith, Barney. Babcock demolished the myth that billion-dollar companies were immune to takeovers. Because its stock doubled during the bid—way above the usual 40-percent premium—it attracted a new breed of professional arbitrageurs. These speculators swept up the outstanding stock of takeover candidates, concentrating it in fewer hands, thus setting the stage for merger mania.

In the fall of 1977, Morgan Stanley became involved in an ethical tangle from which it never fully extricated itself. Like other big, Morgan-financed mining firms, Kennecott Copper wanted to diversify, and it turned to Greenhill as adviser. Among the prospects he scouted was a Louisiana forest-products concern, Olinkraft. While a friendly bid still seemed possible, Olinkraft provided Kennecott with confidential earnings estimates. Then Kennecott’s attention was distracted by a company named Carborundum, which it finally bought. Losing interest in Olinkraft, it returned the confidential data. Morgan Stanley apparently did not.

In early 1978, another Morgan-organized mining conglomerate, Johns-Manville, showed up for diversification advice and was assigned to Greenhill’s sidekick, Yerger Johnstone. When talk turned to Olinkraft, Morgan Stanley mentioned earlier talks with the company but didn’t divulge the valuable data. By late June, Johns-Manville had decided not to pursue Olinkraft. Two weeks later, Texas Eastern made a $51-a-share offer for Olinkraft, which the latter’s board approved. Now, having seen confidential projections that Olinkraft would earn over $8 a share by 1981, Morgan Stanley knew the company was selling out very cheap. So it shared the data

with Johns-Manville, which reversed its decision, stepped straight into a bidding war with Texas Eastern, and won with a top bid of $65 a share. As the dust settled, the question arose: had Morgan Stanley betrayed Olinkraft?

According to its later defense, Morgan Stanley consulted Davis, Polk, and Wardwell and Joe Flom's law firm of Skadden, Arps before making a move. Both approved disclosing data to Johns-Manville provided the confidential estimates appeared in an SEC filing connected with the bid. This was duly done. Yet when published in September 1978, the filing caused shock, since Morgan Stanley hadn't received Olinkraft's permission to share such internal information. It seemed that client-banker trust—the bedrock of merchant banking for a century—was being violated in an opportunistic way. When the *Wall Street Journal* broke the story on October 26, it saw the flap as betokening larger problems: "No one is accusing Morgan Stanley of any wrongdoing, but some close observers of the firm, including some clients, lately have grown uneasy about what they see as mounting aggressiveness at Morgan Stanley as it scrambles for sizable takeover-bid advisory fees."[10]

At first, Morgan Stanley couldn't produce a coherent defense. After its managing directors met for several hours, a spokesman said lamely, "I'm afraid we've decided we can't comment."[11] While some Morgan people reacted angrily toward the press, others, troubled by Greenhill's bravado, welcomed what they saw as a salutary rebuke. Petito and Baldwin published a nine-paragraph defense in the *Wall Street Journal*, which asserted that the firm had "acted with the highest standard of professional responsibility" in showing the Olinkraft data to Johns-Manville.[12] They pointed out that Morgan Stanley's action had benefited Olinkraft shareholders, who reaped a 25-percent premium over the Texas Eastern bid. True enough. But was such bidding fair to Texas Eastern? Greenhill argued that the withholding of vital information from Johns-Manville might have posed questions, too. "If someone tried to stir up trouble, he might come in and say, 'Hey, these guys are trying to buy a company with undisclosed, secret information.' "[13] This was a valid point—and a perfectly good argument for bowing out of the deal altogether.

Morgan Stanley's attempts at explanation only worsened matters. Speaking to *Institutional Investor*, Greenhill and Dick Fisher said the firm had neither a verbal nor a written agreement with Olinkraft that enforced confidentiality. For the House of Morgan—the historic custodian of the "my word is my bond" approach to business—this defense seemed a betrayal of the Morgan tradition. As *Institutional Investor* said, "Morgan Stanley appeared to be enunciating a new investment banking doctrine: that any information a corporation provides to an investment banker will not necessarily be kept in complete and lasting confidence unless that corporation obtains either a

written or oral promise from the investment banker to keep the information confidential."[14]

There was more bad news. About two years before, Morgan Stanley had set up a "risk arbitrage" department to speculate in takeover targets. As would become clear during the insider trading scandals of the 1980s, such operations were incompatible with M&A work. How could one side of a firm execute takeovers while another side was betting on them? Again Morgan Stanley extolled its Chinese wall, insisting its arbitrageurs existed in a sealed universe apart from Greenhill's group. Then, a second *Wall Street Journal* story disclosed that the Arbitrage Department had taken a 150,000-share position in Olinkraft in mid-July, soon after the original Olinkraft-Texas Eastern discussions were revealed. This $7-million stake was unusually large. Only two months later did Johns-Manville learn that one wing of Morgan Stanley had a huge vested interest in seeing it pay top dollar for Olinkraft.

Bob Baldwin refused to concede any lapse in the firm's vaunted integrity: "If you ask any 50 investment bankers on Wall Street which firm has the highest standards of ethics, I can assure you that Morgan Stanley will be the firm that is most often mentioned."[15] Elsewhere in Wall Street, the Olinkraft episode produced deep uneasiness. Morgan Stanley was the flagship of Wall Street and its troubles tarred everyone. "The Morgan Stanley situation is going to hurt all of us," said a rival. "For years we have all been cloaked in the integrity Morgan Stanley has shown in the corporate world."[16]

Olinkraft showed that as Wall Street firms grew and diversified, there were myriad opportunities for cheating and cutting corners. For some ex-partners who had grimly watched the firm evolve over the previous ten years, Olinkraft confirmed their fears. Some had thought it a matter of time before "accidents" occurred. One former partner said:

> Morgan Stanley took on jobs that visibly represented conflicts of interest and sooner or later they got into trouble. Before, the attitude was that if you saw a conflict of interest, you said "no" right away. There was no idea that you had to go for the last nickel. And you never looked at an individual buck outside of its effect on that basic business of preserving client relationships. That's what Morgan Stanley slipped away from for quite awhile. I always felt they lost their soul.

By now, the merger business had acquired an irresistible momentum. In 1979, Morgan Stanley earned a stratospheric $14.3-million fee for advising Belridge Oil on its sale to Shell Oil—then history's largest takeover. Among the losing auction bidders were two furious Morgan Stanley clients—Mobil and Texaco. The irate Mobil gradually shifted business to Merrill Lynch, while Greenhill pretended to be blase: "We'll always do our best for a client, and Belridge was the client."[17] Unlike syndicate work, takeover business

required antagonizing some clients to please others. It therefore eroded historic ties on Wall Street.

This was again revealed in August 1981, when Du Pont bought Conoco for $7.8 billion. Advised by Morgan Stanley, Conoco turned to Du Pont as a white knight to ward off Seagram's advances. Because Greenhill and Flom were already teamed up with Conoco, Du Pont—a House of Morgan mainstay from the World War I Export Department and the 1920 General Motors takeover—had to drop Morgan Stanley and turn to the surging First Boston team of Joe Perella and Bruce Wasserstein. The three-month battle netted Morgan Stanley $15 million. Afterward, Morgan Stanley found itself sharing Du Pont under-writings with First Boston. The new banker ties developed through takeovers translated into less loyalty in underwriting as well.

In 1981, Morgan Stanley was destined to suffer an embarrassment greater than that precipitated by the Olinkraft takeover. The case would darkly foreshadow later Wall Street scandals. It started with the hiring of Adrian Antoniu, a Romanian refugee whose family settled in New York in the 1960s. The Antonius had no money and spoke no English; Adrian's would be a classic success story: after his father died, he supported his mother, worked his way through NYU, and in 1972 graduated from the Harvard Business School. Hired as a Morgan Stanley associate that year, he worried about money. He fretted about his mother's failing fabric business in Queens and was concerned about making payments on his student loan.

Bright and sociable, Antoniu was mesmerized by the new wealth around him and took up a trendy lifestyle, complete with BMW and Park Avenue apartment. He belonged to a tony club called Doubles, frequented smart restaurants, and hung out at the Hamptons. The more perceptive wondered what lay below the aura of sophistication. "He just looked too good, too well-pressed and too well-groomed," said an acquaintance.[18] Starting in corporate finance, Antoniu was soon drawn into Greenhill's growing merger operation, where a newcomer could quickly lay his hands on valuable information.

In 1973, Antoniu hatched a deal with a former N.Y.U. classmate, James Newman, who worked in a brokerage house. Antoniu would feed names of takeover candidates to Newman, who put up the money to buy the stocks; profits were to be shared equally. He cut similar deals with two other graduates from his business-school class. At first, the bets were touchingly modest. In the first of eighteen deals, Antoniu told Newman that Morgan Stanley was defending CertainTeed in a tender offer by Compagnie de Saint-Gobain-Pont-a-Mousson. Their CertainTeed purchases netted $1,375. In a second deal—Newman had now moved to Miami and taken another brokerage job—Antoniu revealed that Ciba-Geigy, advised by Morgan Stanley, would soon launch a bid for Funk Seeds. Soon they were placing bigger bets. For instance, when Morgan Stanley helped North American

Philips in its bid for Magnavox, Antoniu and Newman bought 17,600 shares of Magnavox. Starting to show real flair, the young men took to using offshore Bahama bank accounts.

They grew strangely heedless of danger. Later on, they read a newspaper account of an insider trading case against three people at Sorg Printing who used inside information from tender-offer documents they were printing. “Look what happened to these people at Sorg,” said Antoniu, briefly dismayed. “Well, you see the worst that could happen in a case like this,” Newman replied. “They ask for your money back, and they give you a slap on the hand. People have to steal or kill to get this kind of money, but you don’t have to go to jail for it.”[19]

In early 1975, the conspiracy nearly ended when Antoniu was edged out of Morgan Stanley and hired for M&A work by Kuhn, Loeb, soon to merge with Lehman Brothers. Luckily, he found a new Morgan Stanley confederate in yet a fifth member of the Harvard Business School class of 1972. Unlike the free-and-easy Antoniu, the French-Canadian E. Jacques Courtois had an intense, tight-lipped expression. His father, a rich Montreal lawyer who headed a group that owned the Montreal Canadiens, sat on a bank board. Over chess at the Harvard Club, Antoniu drew Courtois into his scheme. Courtois promptly repaid his confidence with a tip—that Pan Ocean Oil, a Morgan Stanley client, was involved in merger talks with Marathon Oil. They made a quick killing of $119,000. Between 1973 and 1978, they would earn $800,000.

It took time before the authorities zeroed in on Antoniu. Meanwhile, he had fallen in love with Francesca Stanfill, daughter of Dennis Stanfill, the powerful chairman of Twentieth Century Fox. By the spring of 1978, when the government targeted him as a prime suspect, Antoniu was engaged to Francesca, who wrote about fashion for the Sunday magazine of the *New York Times*. He somehow neglected to tell Eric Gleacher, his boss at the M&A Department of Lehman Brothers Kuhn Loeb, that he was being investigated. Learning of this fact on the eve of Antoniu’s wedding, Gleacher saw double disaster: not only was Antoniu his employee but Twentieth Century Fox was a major Lehman client. He insisted to Antoniu, “If there is nothing to the charges and you want to have the Stanfills stand by you in defending against them, you really ought to tell them.”[20]

On June 28, 1978, Antoniu married Stanfill at a civil ceremony in Venice, neglecting to tell her family about the federal probe. Discovering this, Gleacher roared into the telephone from New York: “Unless you tell Mr. Stanfill before the church wedding, I will!”[21] On July 1, the church wedding took place at the Basilica di San Pietro di Castello in Venice, with Albino Cardinal Luciani, about to become Pope John Paul I, bestowing his blessing on the couple in a written message. Adrian delivered a poetic toast: “Here’s to

the longest run Twentieth Century Fox will ever have."[22] As guests waved good-bye, the newlyweds drifted off in a white gondola. Back in New York, Gleacher cleared out Antoniu's desk. Within a month, the wedding was annulled, presumably because the Stanfills learned of the investigation.

E. Jacques Courtois's voluntary departure from Morgan Stanley in 1979 caused great anguish. "Morgan Stanley was rocked at the time," said a colleague. "They had lost 3 people, including Jacques, in something like 3 weeks. They had a series of meetings to make sure they were hanging on to the rest of us."[23] Courtois said he might go into computer software or manage his investments. Marrying the niece of Colombia's president, he moved to Bogota. Courtois was fingered by government investigators because he alone in the M&LA Department *hadn't* worked on the takeovers in question. This raised questions about Morgan Stanley's claim that their people never discussed takeovers with others.

The criminal indictments handed down in February 1981 were the first such ever brought against investment bankers. Newman got a one-year prison sentence, while Antoniu's plea bargaining got him a suspended sentence. Antoniu said, "Anyone familiar with the securities markets knows these circumstances are not uncommon."[24] Courtois spent a year in prison and paid $150,000 in fines.

Morgan Stanley cooperated with the government and contacted clients to reaffirm its integrity. Lewis Bernard was chosen to inform the firm's managing directors. He recalled, "People in that room cried. They cried out of anger. We have the feeling of being violated."[25] Although the overwhelming majority of inside tips came from Morgan Stanley, Bob Baldwin complained that Lehman Brothers received less publicity: "What do the headlines say? Morgan. We make the headlines in these darned situations . . . we had people practically crying around here, they work so hard to do a first-class job in a first-class way."[26]

Public reaction to this insider trading ring distinctly echoed that to the 1933 preferred-list scandal and the Richard Whitney affair. People unconnected to Morgan Stanley felt as if a public trust had been violated. "I've always thought of Morgan Stanley as the *creme de la creme*," said Benedict T. Haber, dean of Fordham's Graduate School of Business. "It's like an icon has been knocked down."

CHAPTER THIRTY-TWO
SAMBA

BY the mid-1970s, J. P. Morgan and Company—the holding company of Morgan Guaranty—was drawing half its profits from more than twenty offices abroad. By a minor miracle, the bank's pell-mell global expansion didn't dilute staff cohesion. As Pat Patterson said, "Our operation is worldwide in a compact way."[1] The bank used various devices—from providing free lunches at its dining rooms to rotating executives—to preserve an inbred feeling. The refusal to open branch networks in foreign countries concentrated personnel, furthering intimacy. "It would be a little like a fish out of water for us to run a system of branches in Germany or England when we don't have it here," said the avuncular, balding Walter Page, who succeeded Patterson as chairman in 1978.[2]

When Morgans started underwriting in Paris in the early 1960s, it wasn't clear where the Euromarkets would settle; even Geneva and Zurich were in the running. During the oil boom of the 1970s, however, London emerged as the clear winner, recycling OPEC surpluses at a furious rate to debtor countries. The City of London suddenly had more American banks than Wall Street! They leapt into syndicated Eurodollar loans, which formed the genesis of the Latin American debt crisis. Latin American governments paid much higher interest rates on loans than corporations back home. And in the Casino Age, those corporations were bypassing banks to borrow in securities markets. Thus, the lemming rush into Latin American lending was symptomatic of the deterioration of the banks' commercial lending business. Foreign borrowing now expanded beyond the industrial countries that had received the bulk of cross-border lending in the 1950s and 1960s.

Previous cycles of Latin American lending and default dated back at least to the 1820s. During the Great Depression, every Latin American country save Argentina had defaulted on its foreign debt. The nations had been sternly lectured by the bankers that they would be forever barred from future lending. Yet this history was conveniently forgotten by the young bankers on the swank London party circuit, who booked huge loans to those same countries. As members of a venerable old bank, Morgan people should have had a better memory, and to some extent they did. "Lew Preston and I spent a lot of time talking about the parallels," recalled A. Bruce Brackenridge, the senior credit officer in the late 1970s. "We used to refer to the loans that the British made

here to our railroads. The money that J. P. Morgan and Peabody raised to build America—that was the sort of loans we made to the Itaipu Dam in Brazil. There's a very clear analogy there."[3] It was, alas, the wrong analogy, skipping over all the disastrous Latin American precedents. It also overlooked the fact that many American state and railroad loans in the nineteenth century had defaulted—a history that haunted George Peabody and subsequently made the Morgan imprimatur so sacred to European creditors.

In earlier generations, Rothschilds, Barings, and Morgans made Latin American loans through large bond issues that distributed risk among thousands of small investors. (An estimated half-million Americans were stuck with largely worthless foreign bonds during the 1930s.) Modern Latin American loans, in contrast, took the form of bank debt, concentrating the risk in the banking system. Large syndicate managers, such as Morgan Guaranty and Citibank, would unite up to two hundred banks for a loan. If this spread risk, it perhaps also created an illusory sense of safety in numbers.

Why didn't banks sell Latin American bonds? "Because you wouldn't have been able to sell the bonds," explained Brackenridge. This should have been a tip-off of high risk.[4] Since only a handful of developing countries were eligible to sell bonds, Morgan Stanley and other investment banks were mostly spared the Latin American debt crisis. (Both a commercial and an investment bank in American terms, Morgan Grenfell participated in some export credits and syndicated loans to Brazil and elsewhere.) So banks rushed in where investors feared to tread. This spared the "little people" the bloodshed of the earlier debt crisis but also introduced the potential for large disruptions in the global financial system.

Because the Latin American debt crisis originated with the recycling of Arab petrodollar deposits, the banks would later cite official approval of such lending. Indeed, Washington and the other Western governments cravenly ceded responsibility for the problem to the private banks. But as shown by the experience with German reparations and Allied war debt in the 1920s, even explicit official approval of loans didn't guarantee government support in case of trouble. There would always be popular cynicism about spendthrift foreign debtors—not to mention an assumption of banker greed—that would arise to hobble governments in solving the problem. Ironically, the petrodollar blackmail so feared by Senator Church wasn't the real problem. By *keeping* petrodollars and lending them out to Latin America, banks damaged themselves and the world economy.

Morgan Guaranty was a good bellwether of changing American attitudes toward Latin American lending. In the 1920s, the bank had proudly boasted of the number of South American governments it had turned down. In the 1940s, Tom Lamont was aghast when Franklin Roosevelt advocated postwar

lending to Brazil, and Russell Leffingwell urged World Bank president John J. McCloy not to lend to the region. In the 1950s, the Eurocentric Morgans largely limited foreign lending to England and France. But with its core lending business eroded in the Casino Age, it suddenly emerged in the 1970s and 1980s as an "MBA bank"—so-called after the first initials of the three largest Latin American debtors: it made $1.2 billion in loans to Mexico, $1.8 billion to Brazil, and $750 million to Argentina. For Wall Street's most conservative bank to have its largest foreign stake in Brazil showed its reliance on progressively riskier loans for profitability.

Several overriding illusions clouded judgment. One was that countries didn't go bankrupt—a canard associated with Citicorp's Walter Wriston. This almost inverted historic truth. Default on sovereign debt had been commonplace for 150 years. Even the discriminating old House of Morgan ended up with massive defaults on Austrian, German, and Japanese loans by World War II. There were more recent cases of debt repudiation as well, including China in 1949, Cuba in 1961, and North Korea in 1974. Banks could foreclose on companies but not on countries, making the latter more careless about repaying loans. And political risk was always piled atop economic risk.

Another factor of comfort to the bankers was the International Monetary Fund. By the 1970s, gunboat diplomacy was passe. For reasons of foreign policy, Washington was often more eager to appease Latin American governments than bully them about loans. Bankers didn't like meddling in foreign countries, especially now that they had branches abroad. In 1976, when Peru was nearly bankrupt, Citibank, Morgans, and other banks imposed an austerity plan in exchange for a $400-million loan. Requiring a steep rise in food and gas prices, it provoked riots in Lima and new charges of dollar diplomacy. The banks were appalled by the backlash. "It doesn't take much to whip up the peasantry with stories about the House of Morgan and U.S. imperialism to explain why there's no food," said a congressional staffer.[5] Stung by bad publicity, the banks turned to the IMF as a surrogate that could withstand political criticism in debtor countries. It seemed a useful shield behind which to effect painful economic reforms.

The IMF laid down strict conditions for loans. As banks made their loans contingent on agreement to the IMF austerity programs, the fund's power soared. The problem was that the fund was set up to handle temporary payment imbalances, not protracted debt problems. Nobody knew whether its orthodox prescriptions—cutting spending, ending subsidies, and deflating economies—revived economies or simply squeezed them to pay off bankers. There was the further problem that strong Third World countries, such as Brazil, bypassed the fund altogether and borrowed only from commercial banks. Yet whatever the fund's limitations, it encouraged bankers to believe

that they had some control over errant debtors, forcing them to undertake sound policies. And during the Latin debt crisis, the fund would indeed provide forms of control over debtor countries unknown to earlier generations of bankers.

The structure of syndicated loans invited banks to abdicate responsibility and coast along with the others. Some fifteen hundred banks worldwide piggybacked onto the expertise of a Morgans or a Citibank, especially in Brazil. Often new to foreign lending, small banks left the scrutiny of loans to the larger banks. In a world of telex-driven anonymity, banks would receive cursory "offering memorandums" of mostly boilerplate language. Tens of billions of dollars in loans were assembled through $10-million participations. By the late 1970s, a fierce price war cut profit margins on loans until they no longer reflected the gargantuan risks involved. Said one Morgan banker involved: "By the mid-1970s, it was very clear that things were getting out of control, with crazy lenders and crazy borrowers." It was a giant mechanism gone mad.

Somewhat more than most, Morgans tried to resist the wild grab bag. In 1979, its London syndicate operation was run by a young Smith graduate, Mary Gibbons, known for her toughness. "At 31, wielding all the power that Morgan Guaranty's position in the Eurocurrency market commands, Gibbons is unquestionably the most influential female decision maker in the City, if not in the entire world of international banking," said *Institutional Investor*.[6] She balked at credits even for Britain, Sweden, and Canada, fearing watered-down standards. In general, however, Morgans was swept up in the bankers' suicide dash. One ex-Morgan banker recalled, "There was a lot of unscrupulous lending and forcing loans down the throat of these countries. Anything to get a loan to a government."

The most convoluted, baffling Morgan relationship was with Brazil, a newcomer among its clients. Even as the House of Morgan advised the country, Brazil balked at granting it a branch, which rankled at 23 Wall. "They said that if Morgan got a branch, they would be dominant and then the government would have to let in forty other banks," said an ex-Morgan official. "It was a real sore point." The Morgan people were proud of their Brazil loans, which went to seemingly well-managed mining and electric enterprises. Recipients included the vast Itaipu hydroelectric project, with its World Bank patronage. The bank also boasted that Brazil had a good credit profile—that is, its loans matured at nicely spaced intervals. Sometimes Morgan people sounded as if history had cheated them, making their splendid Brazilian portfolio look miserable.

As a latecomer to Latin America, Morgan's position as chief adviser to Brazil was a startling achievement. It was accomplished through the virtuosity of an engaging young banker of mixed nationality named Antonio Gebauer.

Born in Colombia to a wealthy Venezuelan brewer of German birth, Gebauer had been educated at Columbia University's Graduate School of Business and was married to a Brazilian. He retained his Venezuelan citizenship while at Morgans. Short, with horn-rimmed glasses and sandy hair, he was fluent in Spanish, Portuguese, German, and other languages. He was both charming and impatient, bright but prone to a brusque arrogance. When he started at Morgans in the 1960s, domestic bankers were kings, and he seemed to have a slim chance for advancement. Then, as Latin American lending surged in the 1970s, the Anglophile Morgan bank, with its European bias, found Gebauer providential in catching up with Chase and Citibank in Latin America. His delighted bosses gave him a wide berth.

Tony Gebauer spectacularly developed new business and was trusted by Brazilian officials. He socialized in elite circles and was probably on a first-name basis with every Latin finance minister and central banker. In the heady world of petrodollar recycling in the 1970s, Gebauer was a jet-setting star, a frequent guest at Brazilian coffee plantations, his doings covered by Rio de Janeiro gossip columnists. He appeared on Brazilian television, landed on the cover of the country's top news magazine, *Veja*, and became president of the Brazilian-American Chamber of Commerce. It was highly unusual for the Morgan bank to tolerate such a high-profile approach to banking. Other bankers watched in wonder. At home, Gebauer threw flashy parties in his East Side apartment and at his East Hampton weekend home, which was called Samambaia, or "fern" in Portuguese. Carlos Langoni, Brazil's young central bank president, spent weekends there. All the while, Gebauer was booking Brazilian loans 2 percentage points above Morgan's own costs—spreads so profitable as to ease doubts about their soundness.

Occasionally there were fleeting concerns at high levels about this lending binge. At one point, Chairman Pat Patterson received an award from Brazil declaring him the country's best banker. He was slightly jarred and confided to President Walter Page that it was perhaps a dubious achievement. "Maybe we better not get another award and be busted," Patterson told Page.[7] But such doubts were momentary. By pushing back the exposure limits in each borrowing country by small increments, bankers averted their eyes from the developing danger. Brackenridge recalled, "We didn't say, 'How much of our capital should be in these loans?' We played with it, but we really didn't say, 'Hey, we really shouldn't have more than 50 percent of our capital in loans to Brazil just out of a spread of risk.' "[8]

Despite Gebauer's virtuosity, the Morgan bank had limited power to force Brazil to curb its prodigal, inflationary spending. In 1980, it vainly badgered the country to go to the IMF. When the bank went to the IMF instead to get its perspective on Brazil—an exercise meant to instill market confidence—

Delfim Netto, Brazil's short, squat, bespectacled planning minister, got very angry. He thought Morgans was going behind the country's back to check up on it. So the banks found it hard to police sovereign clients without antagonizing them. They began slipping into a situation in which they were hostages to their large debtors. The full extent of this bondage wouldn't become apparent until the fall of 1982. Then everyone would rediscover the old adage that if a debtor is big enough, he controls the bank.

THE April 1982 war over the Falkland Islands cast a black cloud over Latin American lending, projecting a view of the whole region as unstable. After Argentina invaded the islands, Britain retaliated by freezing its London-based assets. When hostilities ended, the House of Morgan undertook secret diplomacy to patch up relations between the two countries. The central banks of England and Argentina didn't know how to resume relations without losing face. Who would initiate talks? Tony Gebauer, now the senior vice-president for Latin America, acted as matchmaker. Representatives from the two central banks flew to New York and were closeted in a conference room at 23 Wall—the ice-breaking contact between them.

After the war, it grew harder for bankers to make nice distinctions among Latin American debtors. Regional banks were less disposed to share Morgan's view of Brazil as a textbook Third World country investing in sound infrastructure. Rather, they saw a nation grotesquely burdened with a $90-billion debt—the world's biggest—borrowing a stupendous $1.5 billion monthly to stay afloat. Morgans urged Carlos Langoni to come to New York to make reassuring speeches. In a rare coup, it even got Secretary of State George Shultz—as Bechtel president, a Morgan director in the 1970s—to accept an award from the Brazilian-American Chamber of Commerce along with Ernane Galveas, Brazil's finance minister; Shultz seldom consented to such mingling of private and public purpose.

When Mexico startled the world in August 1982 by announcing that it could no longer service its $87-billion foreign debt, it blackened the image of all Latin American debtors. They were being drowned in a common economic deluge of rising interest rates, global recession, and steeply falling commodity prices. On September 21, 1982, Langhorne Motley, the U.S. ambassador to Brazil, told the State Department that Mexico's troubles were sparking flight from Brazilian debt: "Japanese banks are out of the market, European banks are scared, regional U.S. banks don't want to hear about Brazil, and major U.S. banks are proceeding with extreme caution."[9]

In October 1982, under cover of a UN speech made by Brazil's president, Netto and Galveas visited 23 Wall for clandestine talks. Frightened by Mexico, banks had pulled up to $3 billion in short-term Brazilian loans. Netto

and Galveas didn't see how Brazil could escape default without an emergency loan of $2.5 to $3 billion, plus a rescheduling to reduce interest and stretch out payments of principal. In the protocol of such crises, the bank with the largest debt exposure ordinarily managed the rescheduling. But the Brazilians' faith in Tony Gebauer was such that they wanted Morgans to preside over this mammoth rescue, even though four other American banks had larger stakes. With $4.6 billion in loans to Brazil, Citibank was the natural leader. To avoid bruised feelings, Gebauer suggested that Citi co-chair the committee. "You have to go and do proper protocol," he told the Brazilians, to whom Citibank acquiesced. Gerard Finneran would be the Citibank representative.

The choice of Morgans and Citi had an intricate political backdrop. Some on Wall Street thought Morgans grabbed at the co-chairmanship in its frustrated quest for a Brazilian branch—a view that infuriated the bank. Perhaps more pertinent was the extremely intimate relationship between Fed chairman Paul Volcker and Lewis T. Preston, Walter Page's successor as Morgan chairman in 1980. This hidden relationship never surfaced in the press. Yet behind Preston's moves during financial crises, the cognoscenti sometimes discerned the fine hand of Paul Volcker. In 1980, Preston led a $1-billion rescue for the Hunt brothers when their attempt to corner the silver market collapsed, nearly dragging down Bache and other brokerage houses. The Hunts were hardly typical Morgan clients, yet the bank performed the rescue at the behest of Volcker.

With Brazil, Volcker apparently again used Preston as his proxy. Just as the House of Morgan in the 1920s provided a convenient back channel for government action, so Volcker could direct bailouts through Preston without advertising his presence. Morgan's smaller lending to Brazil was advantageous. A Preston confidant explained: "In the fall of 1982, Volcker told Lew that Morgan had to be in charge of the committee. He wanted Morgan to take on the Brazilian loan because we had far less exposure than other banks on Wall Street. We could, if necessary, take on more Brazilian debt without getting screwed up." (Other bankers, it should be said, pooh-pooh this story, stressing the Gebauer link.) More than any chairman since Henry Alexander, Preston was imbued with a Morgan sense of *noblesse oblige* and Wall Street statesmanship. "Lew has been thinking more and more of the system, even to the detriment of the bank," said the confidant. He tended to gripe at Citibank, which he often saw as acting selfishly and unilaterally without consulting the general good.

As in interwar days, the debt crisis produced bad blood between American and European bankers. More than half of Brazil's debt was held by non-American banks, yet Morgans and Citibank alone ran the show, as they had many of the earlier syndicated loans. Some in the City suspected that Brazil had groomed Morgans as its pet banker to secure lenient treatment. Guy

Huntrods of Lloyds International Bank feared Brazil's strategy was to cook up a sweetheart deal with New York bankers, then foist it on the Europeans. That October, he turned down Brazil's request for an emergency loan unless accompanied by an IMF loan and stiff emergency measures. So the all-American team of Morgans and Citi led the first phase of Brazil's rescue.

The debt rescues of the 1980s reflected global political realities as well as financial stakes. Again and again, steering-committee banks were predominantly American. Japan was second to the United States in Third World lending, yet in the early rescues it typically settled for a single, token representative from the Bank of Tokyo, which had the largest Latin exposure. Much as the rising financial power—the United States—had deferred to Monty Norman's intellectual leadership in the 1920s, so the Japanese, even while starting to overtake Wall Street, bowed to Paul Volcker's authority. Not until the late 1980s would Japan begin to demand a voice at the IMF and the World Bank fully commensurate with its new financial power.

Back in the 1920s, Tom Lamont had represented two hundred thousand Mexican bondholders worldwide. In the unwieldy modern debt crisis, Morgans and Citibank had to deal with a bureaucratic monstrosity—some seven hundred banks with large and small loans to Brazil. After secretly hatching a rescue plan with Brazil and the IMF, the two banks summoned Brazil's creditors to New York's Plaza Hotel on December 20, 1982. Carlos Langoni shocked them by stating that Brazil couldn't service debt coming due in 1983. Jacques de la Rosiere, the IMF's managing director, unveiled a complex, four-part Morgan-Citi plan for saving Brazil. Citibank would reschedule $4 billion in principal; Chase would maintain trade credits; and Bankers Trust would restore short-term "interbank" lines to Brazil. The linchpin was a Morgan-led effort to raise a new $4.4-billion loan for Brazil, the biggest in Morgan history.

The plan set a fateful precedent of "curing" the debt crisis by heaping on more debt. In this charade, bankers would lend more to Brazil with one hand, then take it back with the other. This preserved the fictitious book value of loans on bank balance sheets. Approaching the rescue as a grand new syndication, the bankers piled on high interest rates and rescheduling fees. It was hard to stop the greed so prevalent for so many years. The Europeans watched sourly from the sidelines. "It was very much an American party," said Guy Huntrods, a dogged, balding, talkative banker who became British point man on Latin American debt. "The Brazilians had taken no advice from anybody except Citi and Morgan Guaranty. We were told to go home and do what we were instructed. This created the most awful impression among us."[10]

Tensions rose between Wall Street banks, with their huge and irrevocable commitments to Brazil, and regional banks, which wanted to cut their smaller

losses and run. One German banker observed, “I come into these sessions and I find all these hillbillies. The big American banks have made the loans and sold part of them to the little ones. And these fellows, who don’t know the Baltic from the Barents Sea, were all crying, ‘I want my money back.’ ”[11] This split produced bitterness between the large and small banks and poisoned the atmosphere of the first rescue.

In early 1983, Morgan credit officers worked around the clock to raise the $4.4 billion. Although the megaloan was assembled in a remarkable two months, it left a residue of ill will toward Tony Gebauer, who embodied the big-stick approach of the Wall Street banks. The smaller banks felt they had been browbeaten into participating, and some, piqued by Gebauer’s high-handed manner, balked at providing new money.[12] But afraid of antagonizing the Fed and the Wall Street banks, they grudgingly abided by the plan.

On February, 24, 1983, Brazil hosted a dinner at the Waldorf-Astoria to thank their bankers for the rescue loans. Over dessert, the Brazilians let slip that they might not make timely payments on these new loans either. Nevertheless, the next day, several hundred bankers, bruised and battered, signed copies of the loan agreement that Morgans and Citi laid out for their signature at the Plaza Hotel. The IMF chipped in a $5-billion loan for Brazil in what appeared a successful finale.

This success was illusory. While the banks had committed $4.4 billion for the Morgan-led loan, they had also drained off a corresponding amount in short-term credit lines to Brazil. Thus some banks got their secret revenge. This financial legerdemain neutralized the loan’s effect. Gebauer was furious as he saw banks sabotaging the agreement. The whole sham got him hopping mad because among the banks he suspected of bad faith was Citibank—his co-chair in the rescue operation. By the spring of 1983, Brazil was missing its IMF economic-reform targets, and the fund and the banks halted their emergency payments. The Fed was alarmed by Brazil’s eroding short-term credit lines. On May 31, Volcker called in Preston and other chairmen to discuss the rescue. The Fed was disturbed by reports of Gebauer’s treatment of the regional banks, and Preston feared that he was alienating the British bankers. Gebauer was squabbling openly at meetings with Citibank’s Finneran, demoralizing the bankers further. A decision was made to replace Gebauer with William Rhodes of Citibank, who had headed the effort to rescue Mexico.

This came as a blow to Morgan pride, especially in view of the Morgan-Citi rivalry. “The Morgan bank was very high on Brazil and I think they were a little unhappy that the chairmanship had to be taken away,” remarked Anthony M. Solomon, then New York Fed chief.[13] Some Morgan people grumbled about a power-hungry Citibank bringing Brazil into its fold along

with Mexico and Argentina. Yet it was Preston who urged Citibank chairman Walter Wriston to relieve Morgan of the leadership burden. And there was secret relief at 23 Wall, which was uncomfortable with its unaccustomed high-profile role in the debt talks. Said one former Morgan official, “People had never identified Morgan that much with Latin America, and it suddenly became a liability.” Gebauer’s role drew attention to the bank’s embarrassingly huge Latin American exposure.

In a second Brazil rescue, Bill Rhodes didn’t want to work with Gebauer, whom he saw as tainted. To appease the bank, he brought in Leighton Coleman of Morgans as deputy chairman; to appease the British, he brought in Guy Huntrods of Lloyds as the other deputy chairman. The reschedulings became more global, creating tremendous creditor unity and averting the internecine feuds among nations that had so weakened the banks in the 1930s. Instead of the largely private bank solution of phase 1, Rhodes wanted to get creditor governments more involved and touched base with the IMF, the World Bank, the U.S. Treasury, the Fed, and the State Department. His actions confirmed the intrinsically political nature of sovereign lending—an old story.

The specter of Tony Gebauer wasn’t yet banished. As Brazil’s economy deteriorated during the summer of 1983, Rhodes opted for secret talks, hoping that blunt language would shock the Brazilians into strong action. On August 16, 1983, Rhodes, Huntrods, and Coleman flew to Brazil in a private plane. Rhodes and Huntrods were faintly nervous about having Coleman along, not on a personal level, but because they feared he might have shared information with Gebauer. In Brasilia, they believed their worst fears had been confirmed. Meeting with Netto, Langoni, and other powers at the home of Finance Minister Galveas, they delivered a stern warning. Rhodes began: “We can’t keep the banks on board much longer.” Coleman chimed in: “You’ve got to speak with one voice.” Huntrods delivered a dramatic peroration: “There is a smell of defeat around the streets of Brasilia that reminds me of France before Dunkirk.”[14] Because Netto had never heard of Dunkirk, a short lesson in history ensued.

Huntrods felt they had lost the critical element of surprise: he believed somebody had tipped off the Brazilians. “We had absolute certain proof that Gebauer, who was Coleman’s boss, had already telephoned the Brazilians what our game plan was,” said Huntrods adamantly. “*That* we knew beyond a shadow of a doubt.” He thought that Gebauer was either ingratiating himself with the Brazilians or, motivated by envy, was trying to sabotage phase 2. In the end, Gebauer never got back into the game and some say that his career at Morgans stalled afterward. Among bankers, the new Rhodes team would be credited with creating a more cooperative atmosphere and a spirit of shared sacrifice among the banks.

In the last analysis, phase 2 was simply a more workable way of muddling through the debt crisis and postponing the inevitable. The collective power of the commercial banks kept the lid on the pressure cooker in a way impossible in earlier times. These giant global banks had many more levers than the investment banks of the 1920s with which to keep debtors from outright repudiation. Among other things, they could cancel the trade credits of defaulting countries or reduce their overnight “interbank” credit lines. In consequence, as the 1980s progressed the banks were able to boost their loan-loss reserves and weather the crisis, while living standards tumbled in indebted Latin American countries. For most of the 1980s, the Baker Plan—the principle of lending new debt in exchange for economic reforms—was enshrined as the solution to the crisis, and it enjoyed the support of Lew Preston. But the promised economic growth never appeared. Instead, oppressed by interest payments and despite a prolonged boom in the industrial countries, Latin America suffered through a severe depression. How Latin American debtors could withstand the next global recession without widespread default was unclear as the 1980s came to an end.

In February 1987, Brazil, stifled by a $121-billion debt, which had grown monstrously through the reschedulings, declared a moratorium on repayment that lasted for a year and a half. The country seen as the model debtor in the 1970s had rudely disappointed the House of Morgan. In early 1988, Argentina stopped payment on its debt and fell billions of dollars into arrears. For all the power and ingenuity of the banks in dealing with the debt crisis of the 1980s, the upshot appeared frustratingly similar to that of earlier waves of default. In 1989, the new administration of President George Bush conceded that the only real solution was debt forgiveness. By that point, mobs were ransacking supermarkets in Argentina, as they had earlier in Brazil. In September, 1989, the Morgan bank acknowledged that its Latin debt was a hopeless fiasco by adding $2 billion to its loan loss reserves, fully covering its longer maturity loans. The Morgan fling with the Third World was temporarily over.

THERE was another coda to the Brazilian debt crisis that tattered the image of Morgan invincibility and belied any notion that it alone was immune to the corruptions of the Casino Age. Even as he chaired Brazil’s rescue, Tony Gebauer was leading a secret, illicit life as an embezzler—a term everyone later danced around in embarrassment, for it savored of small-time crooks and greasy hands in the till, not of the world’s toniest bank. Embezzlement was rare in the world of high-finance for obvious reasons: people made stupendous amounts of money, and if they wanted more, there were legal ways to get it.

At 23 Wall, there had been a curious negligence about Gebauer, a tendency

to look the other way. He enjoyed an entrepreneurial freedom that was rare at Morgans. Later people would recall the fruits of his suspiciously profligate spending—a $5-million Manhattan duplex coop, two homes in East Hampton worth a combined $2 million, an apartment in France, and a share in a Brazilian coffee farm. This didn't square with a $150,000-a-year salary. With mild shock, Walter Page learned of a yacht that Gebauer had bought from a wealthy friend on Long Island's Shelter Island. Only later did such details cohere into a telltale picture.

There were two reasons why no one examined Gebauer critically. Everybody had a vague, somewhat correct notion that he came from a wealthy Venezuelan family. More significantly, he had reaped tens of millions in profit for the bank, compensating for its late start and patrician discomfort in Latin America. From 1981 to 1984, as senior vice-president for Latin America, Gebauer controlled most of Morgan's Western Hemisphere lending outside North America. He was one of the few irreplaceable stars at a bank with a chronic glut of talented young executives.

Along with the big loans, Gebauer supervised the accounts of several hundred Latin American businessmen. Technically, they weren't personal accounts but belonged to executives with whom the bank had commercial dealings—an honored Morgan technique to please and befriend the influential. In 1976, Gebauer had started to divert money from some Brazilian accounts in order to furnish his duplex apartment. In the end, he would dip into four accounts, including those of a landowner and a construction mogul. The money mostly resided in six Panamanian holding companies from which he issued cashier's checks to himself. These illegal diversions lasted over nine years and amounted to $6 million—this at a bank that prided itself on tight internal controls. The thefts, remarkably, persisted right through the Brazilian debt rescue.

This was more than a straight embezzlement case, for Gebauer apparently drew on some form of "flight capital"—money smuggled from Latin America to evade taxes or exchange controls. Even as he withdrew the money, there was discussion of how such capital was jeopardizing the debt-rescue effort headed by him and the Morgan bank. As Brazil, Mexico, and Argentina raised billions of dollars in new loans, their disloyal, unethical nationals were stuffing suitcases with bills and flying north to open bank accounts. The big Wall Street banks making the Latin American loans wooed the flight capital and ended up taking as deposits money they had recently lent out.

Behind the title of international private banking, Morgans and other banks helped wealthy Latin Americans to invest in offshore trusts and investment companies. These devices could aid the unscrupulous in dodging taxes. In the 1970s, Morgan Guaranty and other banks also opened Miami subsidiaries to tap the personal wealth of visiting Latin Americans. In the wrong hands,

confidential Morgan accounts could serve as excellent cover for illegal activity. All the Wall Street banks had mysterious Latin American depositors who seldom appeared in person. “They particularly don’t want monthly statements or any other mail sent to their home countries,” noted *Fortune* in 1982. “Their accounts at places like Morgan are labeled ‘hold mail.’ They drop by in person from time to time to look at the statements.”[15]

By extreme estimates, commercial banks were booking more in deposits of flight capital than they extended in new Latin American loans, making them net borrowers from the region. Flight capital siphoned off an estimated one-half of Mexico’s borrowed money, one-third of Argentina’s. Among those bemoaning the problem was Morgan economist Rimmer de Vries. “Capital flight accelerates, enhances, and aggravates a problem that exists,” he stated.[16] Morgan chairman Lew Preston was no less disturbed, telling one annual meeting, “It’s a terrible problem for the banks. If the amount of Mexican investment abroad—if that interest—were brought back into Mexico, it would cover their debt service.”[17] Even though American banks could legally accept flight capital, Morgans had a stated policy of questioning depositors about the origin and purpose of any suspect accounts. Yet Gebauer was apparently plundering “hold mail” checking accounts. Otherwise, why did years elapse before depositors detected the theft? Why weren’t they monitoring their accounts more closely? One raided Brazilian depositor reportedly hadn’t shown up in five years.

Prohibited from maintaining dollar deposits in the United States, Brazilians customarily gave their Wall Street bankers wide latitude in managing their investments. It was later unclear whether Gebauer had permission to withdraw money from some clients’ accounts—something to which his lawyer would make cryptic allusion. Yet this couldn’t have been uniformly true, for Gebauer manufactured bogus statements on Morgan stationery, then mailed them to clients. To plug holes in the accounts, he secured Morgan loans of about $2.9 million. Why would he have resorted to these extraordinary measures if he were acting with the consent of his depositors?

In 1982, even as Brazil teetered on the edge, Gebauer took $1.5 million from the account of a Brazilian named Francisco Catao. This money represented a “commission” Catao received from an arms dealer in exchange for the dealer’s being introduced to Gebauer. This, in turn, led to a $35-million Morgan loan to the arms merchant. Might Gebauer have had a proprietary feeling toward that particular $1.5 million? In an equally bizarre twist, he diverted embezzled money into his own Latin American business, using it to make loans at low interest rates—as if he were entering the banking field as a minicompetitor to the Morgan bank itself.

Tony Gebauer lacked any of the standard motivations for committing a

crime. Unlike the routine cases, his crime coincided not with failure but with stunning success in the sphere of international banking. He had no reason whatever to resent the bank or wish to embarrass it. In fact, he had a deep, abiding love for Morgan traditions, lining his bookshelf with Morgan history and taking great pride in his association with the bank. At tremendous sacrifice to his personal wealth, he remained there when he could have parlayed his connections into a $1-million-a-year income at an investment bank. It's even conceivable that he resorted to crime so he could remain at the bank yet live in a style befitting his fantasies. He apparently let months pass without touching the Brazilian accounts and wasn't consumed by his crime. It was more tangential, gratifying some psychic need left unsatisfied even by his exceptional career.

Like many embezzlers, Gebauer planned to make restitution someday. Much like the Brazilians he rescued, he was defeated by the interest, not the principal, accumulating on his burdensome debt—$2 million of it. Late in the summer of 1985, after a twenty-four-year Morgan career, he left for Drexel Burnham Lambert, to work with Michael Milken on a special project to repackage Third World debt into junk bonds (the 1920s solution). Some at Morgans thought his career had been derailed by the controversial Brazilian debt rescheduling. Shortly after he left, the bank was alerted to his crime by a puzzled Brazilian client whose money supposedly on deposit in New York was wired from Venezuela. The timing seemed coincidental: neither Brazil nor the bank needed Tony Gebauer any longer. He was found out when nobody but he would suffer from exposure of the crime. The House of Morgan sent Price Waterhouse auditors and trusty Davis, Polk lawyers to Brazil to investigate. They netted an accomplice to Gebauer—Keith McDermott, a vice-president who allegedly received $200,000 in kickbacks for Morgan work on behalf of two clients. The bank's investigators passed on their information to the Fed and the U.S. district attorney's office. When confronted with the charges by Drexel Burnham officials, Gebauer resigned on the spot.

When the affair hit the news in 1986, it made headlines in Brazil as well as in New York. How had the world's best-run bank missed the scandal for nine years? Gebauer reportedly believed the millions were too trivial to warrant the attention of a bank grappling with billion-dollar debts. After the scandal broke, the bank was in a sticky situation, guilty of either incompetence or complicity. It portrayed Gebauer as a lone culprit and swore that no customer lost a penny in the end. "Our investigation convinces us that the responsibility for wrongdoing lies with one person. . . . We think it's unfair that other people be implicated," declared a spokesman.[18] Gebauer quickly became a taboo subject at 23 Wall. Morgan officials still find it hard to utter his name and often refer to him as "that fellow," as if they had never known him very well.

Gebauer didn't contest the charges. To avoid the stigma of embezzlement, he pleaded guilty to bank fraud, tax evasion, and doctoring statements. Because he had submitted some surreal tax returns—one year he banked over $1 million in taxable income but reported only $21,000—he owed the Internal Revenue several million dollars in back taxes and penalties. He also paid back $8 million in principal and interest to the bank. His clever lawyer, Stanley Arkin, referred obliquely to flight capital and hinted that Gebauer might have had authority to use some Brazilian money: "That authority was premised on the unusual and Byzantine relationships that often exist between bankers and flight capitalists."[19] Such loose talk made Morgans jittery and eager to strike a deal.

In February 1987, a contrite Tony Gebauer stood in a blue pin-striped suit before Judge Robert W. Sweet for sentencing. The judge saw a large dimension of fantasy in Gebauer's life, a venal excess characteristic of the age. "You are indeed a Lucifer, a fallen angel of the banking world," he told him. "Although your employment at the top of your profession provided you with a princely income, you spent like an emperor."[20] Gebauer received a three-and-a-half-year prison sentence but served only half that time.

The Gebauer affair left behind red faces and personal wreckage in the corporate suites at Morgans. Half a dozen executives were shifted about. In a sad conclusion, Tony Gebauer, so proud of his Morgan employment, ended up disgracing the bank.

CHAPTER THIRTY-THREE
TRADERS

IN the early 1980s, as the final vestiges of fraternity among the Morgan houses disappeared and Morgan Guaranty abandoned wholesale lending to enter global investment banking, it ran into Morgan Stanley. It was also on a convergence path with Morgan Grenfell. When Morgan Guaranty occupied a sleek building of brown granite and smoked glass near the Bank of England—snobbishly named the Morgan Bank, disregarding poor Morgan Grenfell some blocks away—the ancient Anglo-American link, too, was threatened. Starting in 1979, the London-based Morgan Guaranty Ltd. became a major underwriter in the Euromarkets. How could Morgan Guaranty retain a one-third stake in Morgan Grenfell as they clashed in foreign outposts and invaded each other's home turf? As Bill Mackworth-Young of Morgan Grenfell said, "It doesn't make sense to be 33$$$ owned by one of your competitors."[1]

Morgan Grenfell needed expansion capital but couldn't pry it loose from 23 Wall. The London bank's home success had bred hopes for bigger things abroad, especially in New York, where it had had a small office since 1974. To transcend that token presence was impossible so long as Morgan Guaranty owned a one-third stake. So in 1981, the Morgan chairman, Lew Preston, and president, Robert V. "Rod" Lindsay, flew to London to inform Lord Stephen Catto, over dinner, that 23 Wall had decided to sell its stake. The House of Morgan petered out, mourned by few. "It was a bit of a twinge for me and a few seniors at Morgan Grenfell and a few others around here," recalled Lindsay. "But it became clear to everybody that they needed more freedom to go their own way."[2] Lew Preston had grown uncomfortable with Morgan Grenfell as the old, aristocratic families faded from the scene, people who had all trained at 23 Wall. He explained, "The Bank of England expected us to share one-third of every loss, but there was a management evolution where we didn't know the people who were running the firm."[3] The new breed was typified by chief executive Christopher Reeves, a former assistant personnel manager at Hill Samuel, who had never passed through the Morgan Guaranty training program.

Thus ended a transatlantic axis more than a century old, the armature on which the House of Morgan had been built. Catto said, "I had seen it coming

with regret. We had one request: that they not sell it all at once, which would look like a loss of confidence in us. They agreed to sell it piecemeal."[4] Within a year, the bank took its stake below 4 percent, pocketing $40 million and leaving the Lloyd's insurance broker Willis Faber as chief shareholder, with 24 percent. In a declaration of freedom in 1981, Morgan Grenfell set up an investment banking subsidiary in New York, expanding its money management and international M&A businesses. By 1985, it belonged to the New York Stock Exchange. The pretense of brotherhood had given way to raw competition.

A creature of markets, J. P. Morgan and Company—the parent company of Morgan Guaranty—now operated by new principles. It raised billions of dollars daily in the money markets and was emancipated from dependence on loan spreads and deposits. Though the bank still had no retail branches, Morgan people joked that they *had* a retail bank—Merrill Lynch, whose money market fund bought Morgan CDs. The House of Morgan had all but given up on wholesale lending as an anachronistic business for a bank whose blue-chip clients could raise money more cheaply in the marketplace, as they increasingly did in the early 1980s. In 1983, international bond offerings, for the first time, passed global bank lending in scope. Lew Preston didn't want to join an extinct breed. "Basic lending is never going to return to the profitability that existed in the Fifties and Sixties," he predicted.[5] Foreign bank competition also thinned loan spreads.

The upshot was that the Morgan bank began making more money from investment banking fees and trading income. The future bank took shape in London, where Morgan Guaranty had become the top Eurobond underwriter among American commercial banks, with clients including Exxon, IBM, Du Pont, and even Citicorp. From number forty-six in 1980, it zoomed to second place in Eurobonds four years later. It also accelerated trading in gold bullion, foreign exchange, and financial futures.

The locomotive behind these changes was Lew Preston, who embodied the bank's old silken charm but imbued it with a new, sometimes fierce energy. A Harvard graduate from a rich Westchester family, he had started in the Morgan mailroom (as everybody did) in the early 1950s. He was first viewed by elders as a playboy, socialite, and jock. Tall and broad-shouldered, he played semipro ice hockey with the Long Island Ducks until he came home one night with six stitches in his head. "You damned fool," his wife said, "why don't you grow up."[6] His second wife, Patsy, was a granddaughter of newspaper publisher Joseph Pulitzer and mixed with Brooke Astor, Jane Engelhardt, and other socialites.

This Lew Preston seemed all tradition. Among the antique furnishings in his office were an oil portrait of Jack Morgan, a rolltop desk, and a

photograph of Pierpont and Jack striding manfully into the Pujo hearings. Wearing half-moon glasses and red suspenders and smoking Don Diego cigars, he could effect an extremely dignified presence. Once, after making a presentation to Noboru Takeshita, then Japan's finance minister and later prime minister, the dignitary breathed with admiration. "You were prime ministerial in your presentation," he said. "I am stunned."

The elegant manner and dryly mischievous wit covered early scars. When Lew was a boy, his father died of tuberculosis. He also struggled with dyslexia. ("It's very fashionable now," he remarked. "Everybody seems to have it."[7]) At seventeen, he enlisted in the Marine Corps and was sent to China. He ended up as a bodyguard to James Forrestal, later Truman's secretary of defense and a close family friend. Demobilized, Preston attended Harvard, from which he graduated in 1951. He would always be a cross between a Harvard socialite and a tough marine. Curt with fools, sometimes abrupt at meetings, he would show exemplary kindness to someone who was hospitalized, bereaved, or recently divorced. Some at 23 Wall revered Lew Preston, some were slightly afraid of him, and some both revered and feared him.

This dual personality mirrored the Morgan transition. Preston tried to perpetuate the old Morgan culture of teamwork and subordination of the individual to the group: "I want people who want to do something rather than be someone." With department heads, he held the traditional weekly meetings and encouraged senior people to lunch together in the executive dining rooms. This Preston conceded that "a little bit of conservatism in a bank is not a bad thing" and said rather loftily of Citicorp's Walter Wriston, "He's running a financial conglomerate and we're running a bank."[8] He tended the bank's image as if it were a stage set. "We spend an extraordinary amount of time just worrying about the environment," he said.[9]

At the same time, an avuncular style no longer worked completely in a bank with over fifteen thousand employees. Morgan elders had taken a fatherly interest in their staff, with talk of one's being "brought up" at 23 Wall. Now in a vastly speeded up bank, there wasn't time for prep-school camaraderie. Preston had to retrain masses of old-time commercial bankers and credit analysts, making them into risk-taking market whizzes. This meant encouraging aggressiveness and imagination, not just politeness and caution. Competing with investment banks, Preston had to pay huge bonuses and use other compensation methods that fostered divisiveness. By the 1987 crash, some Morgan traders earned more than Preston's own $1.3-million salary. As the eighties progressed, many people left the bank or were gently nudged out. Even among those who stayed, there was a bittersweet sense that the bank was less fun and caring than in the old days. It was also a far more diversified

firm. In 1984, for instance, Boris S. Berkovitch became vice-chairman of the bank—the first Jew ever to rise to the top of Morgan officialdom.

A major protagonist in this shifting drama was Preston's protégé, Dennis Weatherstone, the foreign-exchange wizard from London. A short, trim Englishman with crinkly hair and a quick smile, Weather-stone never lost his working-class accent. He had a natural grace and friendliness, not the cultivated polish of his Morgan colleagues. He joked about his early bookkeeping days as the time he had "no shoes." During a brief Royal Air Force stint, he had scanned radar screens in simulated air flights, computing fuel usage for planes—an experience, he said, that sharpened his mind for foreign-exchange trading. Weather-stone was the quintessential Casino Age banker—a man versed in new financial instruments, interest swaps, and currency swaps. Early on, he saw the impact of "securitization"—the packaging of loans as tradable securities—on the traditional lending business. In 1980, he became chairman of the bank's executive committee, right under the blue-blooded president, Rod Lindsay, and then succeeded Lindsay in 1987.

Preston and Weatherstone were complementary and inseparable. "They spoke in a patois," recalled a colleague. "They were like Siamese twins. One would start a sentence and the other would finish. They were very unlike, but they thought the same." Since much Morgan influence with central banks derived from its Treasury operation, Weatherstone fit handily into the special relationship with the Fed. "Both he and Preston probably have more credibility with Washington policy makers and regulators than any other bankers I can think of," said Anthony Solomon, former president of the New York Fed.[10] The Preston-Weatherstone team was therefore, predictably, at the center of the 1984 rescue of Continental Illinois Bank and Trust Company.

The Morgan role had some irony to it. The Chicago bank was a stiff competitor of Morgans and so similar in style and structure that it was called the Morgan of the Midwest. A prestigious, old-line wholesale bank, it had courted rich families and financed much American auto and steel business from its stately, pillared building on South LaSalle Street. In the early 1980s, it vied with Morgans for the title of premier corporate lender. Like Morgans, it had plunged into the roulette world of "liability management"—that is, it financed its operation from the money markets rather than by deposits. Rounding up $8 billion daily, it borrowed overnight Fed funds, sold CDs, or issued commercial paper. The House of Morgan had played this game with such panache since the days of Ralph Leach that its risks were often obscured. Continental's collapse would show the extraordinary perils inherent in the new banking.

Morgans had long suspected that Continental's success was a mirage. It undercut competitors too vigorously on real estate, agriculture, and energy

loans and rather cavalierly made loans to Chrysler, International Harvester, and other troubled firms. One Morgan official recalled, “All our younger bankers were saying, ‘How do these guys do it? They must be doing it with mirrors.’ They were making loans that any number of banks had shied away from.” Continental was also paying exorbitant interest rates for its $8 billion. It relied mostly on “hot money”—large, volatile deposits from foreign and domestic institutions. Such jumbo deposits ran anywhere from $5 million to $200 million and far exceeded the $100,000 lid covered by deposit insurance. Managers of such deposits were skittish and apt to pull funds at the first hint of trouble. Yet even so conservative a bank as Morgan Guaranty drew 75 percent of its deposits from “hot money.”

Continental began to unravel during the Fourth of July weekend of 1982 with the failure of the Penn Square Bank. This was the notorious Oklahoma shopping-center bank that had booked and resold to Continental $1 billion in bum energy loans. (One picturesquely modern aspect of Penn Square’s downfall was a run at its drive-in window.) To reassure institutions holding its paper, Continental began to pay higher rates on its CDs. When domestic money managers balked, the bank relied more on Japanese and European funds and sent its financial evangelists abroad to preach calm. “We had the Continental Illinois Reassurance Brigade and we fanned out all around the world,” said David Taylor, Continental’s chairman in 1984.[11]

The bank never fully recuperated from Penn Square, which led to the first global electronic bank run in May 1984. It began with a fugitive rumor floating around Tokyo that an American investment bank was shopping Continental to possible buyers. This triggered the sale of up to $1 billion in Continental CDs in the Far East, spilling over into panicky European selling the next day. The Continental run was like some modernistic fantasy: there were no throngs of hysterical depositors, just cool nightmare flashes on computer screens.

The bank’s new chairman, David Taylor, pencil-slim, aristocratic, and with a grave voice, struggled to contain the damage. To spike rumors, he sent what he thought was a reassuring telex to two hundred banks around the world. By spotlighting Continental’s troubles, however, it only intensified fears. The next day, Paul Volcker was on the phone with Lew Preston, who expressed skepticism about a private safety net. But in Washington, there was hope that a private credit raised by big banks could restore confidence in Continental. It was a political preference: Reagan administration ideologues were tantalized by a “market solution.” Bankers also thought they could more legitimately claim expanded securities powers if they didn’t always beg for federal protection. Even as the private credit was being organized that Friday, Continental borrowed $4 billion from the Chicago Fed. During the next week, the “private rescue” would have a slightly fictitious flavor, masking the

federal government's far deeper and more critical involvement.

Why did Continental choose Morgan to lead the rescue—a choice so reminiscent of 1907 and 1929? "Morgan Guaranty was the obvious choice," explained a former high Continental official. "It had the strongest financial situation and an unquestioned reputation." Morgans was also Continental's twin. "We felt Morgan was a similar institution that didn't have the problems we had, but was similarly funded," Taylor recalled.[12] Morgans also got the job by default. Citibank had earlier tried to invade Continental's Illinois turf, leaving behind acrimonious feelings.

Through a Mother's Day weekend, with telephone circuits jammed, Preston and Taylor assembled a $4.5-billion credit line from sixteen banks. These sophisticated bankers relied on primitive methods. Often, they simply called banks, got the security guards on duty, and had them track down their chairmen. Amazingly, the Federal Reserve Board didn't possess emergency home phone numbers of America's most powerful bankers. Security Pacific's chief credit officer was found windsurfing. While bankers haggled over their credit shares, they all knew the gravity of the crisis. As a Continental official said, "They knew that Continental's problems could spill over into a couple of other banks." There was a fear that Continental would focus unwelcome attention on Manufacturers Hanover's Third World debt or the Bank of America's bad real estate loans. "There were also fifty-odd Midwestern banks that had more than their entire bank capital on deposit at Continental," said Preston. "*That's* why it was worth saving."[13] By Sunday night, the $4.5-billion credit line was ready.

On Monday morning, global markets yawned at this show of strength by America's richest banks. A Pierpont Morgan might have commanded the gold market, but private resources now paled in global markets. The runs continued amid telephone calls between Volcker and Preston. "That Monday, Volcker didn't call anybody else but Preston, not even the administration," recalled Irvine Sprague of the Federal Deposit Insurance Corporation. "It became clear the bankers' rescue plan was not going to work. Obviously, the government would have to step in the next day."[14]

The stakes were tremendous: Continental was larger than all the banks that failed during the Depression *combined*. As a "hot money" bank, it was insured for only about 10 percent of its $40 billion in "deposits." Could the world really cope with $36 billion in losses? Nobody wanted to find out. At a meeting on Tuesday morning, May 15, Volcker, Comptroller of the Currency Todd Conover, and William Isaac and Irving Sprague of the FDIC agreed that a Continental failure would be cataclysmal and decided on an FDIC capital infusion.

They sold this idea to Treasury Secretary Donald T. Regan, who wanted to

keep alive the private rescue. The banks were to put up a portion of the money. After lunch, Volcker phoned Preston and asked him to set up a summit of seven bank chairmen in New York the next morning. They met in secrecy at Morgan Guaranty's offices at Fifth Avenue and Forty-fourth Street, an assemblage including the chairmen of Morgans, Chase, Citibank, Bank of America, Chemical, Bankers Trust, and Manufacturers Hanover and the top bank regulators, including Volcker. Chaired by Lew Preston, the meeting had both a sentimental and a combative mood. Some bankers made resounding speeches about past days of Wall Street glory, when the House of Morgan managed private rescues. John McGillicuddy of Manufacturers Hanover argued that the bankers should go it alone. Preston, low-key and conciliatory, let the more vehement bankers talk themselves out. "His style was quite cool," recalled Irvine Sprague. "He lay back and sort of nudged people. I thought he was very skillful."[15]

There was an element of make-believe in this "bankers' rescue," for they pretended to mount a rescue without the necessary resources. Some bank regulators saw the bankers trying to grab credit but pushing the real risk and responsibility onto the government. Citi vice-chair Thomas C. Theobald (later Continental's chairman) laid down especially stringent conditions for his bank's participation, asking for absolute government guarantees against risk. As Sprague later wrote, "They wanted it to look as if they were putting money in but, at the same time, wanted to be absolutely sure they were not risking anything. I said I would not vote for such a sham."[16]

That day and the next, restless regulators invited the bankers to provide $500 million of a $2 billion capital injection. At the last minute, Citi tried to insert language protecting the bankers from losses. Only a call from Volcker to Citi chairman Walter Wriston in California ended the impasse. It was largely sham heroics by the bankers: after agreeing to their $500 million, they sat around arguing about how to "lay off" the risk on other banks. William Isaac of the FDIC has said flatly: "The bankers lost no money, and in hindsight their participation was unnecessary."[17]

In the end, the FDIC effectively nationalized Continental, taking an 80-percent ownership stake. Setting a breathtaking precedent, it decreed that *all* depositors were insured; it had never before given such a blanket insurance for small bank failures. Washington was now saying that some banks were too big to fail. Yet even the full faith and credit of the U.S. government couldn't immediately stem the bank run. "Bankers around the world said, 'So what?' " recalled Preston. "They weren't impressed that the deposits were guaranteed by the U.S. government. *That* surprised me."[18] Continental Illinois's aftermath was ironic: although the affair exposed the unacceptable peril of large bank failures in modern financial markets, the government had created