AN ANALYSIS OF THE BANKING AND CURRENCY SYSTEM OF THE UNITED STATES

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Trieste

An Analysis of the Banking and Currency System of the United States

INDICATING THE CAUSE OF PERIODIC PANICS AND SUGGESTING A REMEDY

BY CHAS. W. DISBROW

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of Baltimore, Maryland

ANNOUNCEMENT

Believing that one of the most important subjects before the American people today is the reform of our Banking and Currency System, we take pleasure in presenting herewith some thoughts on the subject prepared by Mr. Chas. W. Disbrow, of St. Louis, Mo., manager of the Missouri Department of this company. Mr. Disbrow has been connected with this company for many years, and while manager of its Mountain Department, with headquarters at Denver, Colo., was empowered by it to underwrite bank depository bonds, guaranteeing the solvency of banks. This brought him in the closest possible touch with the individual banks of the West, and made him familiar with the entire banking situation. We believe his views will be received with interest. ∴ ∴ ∴ ∴

THE UNITED STATES FIDELITY AND GUARANTY COMPANY

JOHN R. BLAND, President

Baltimore, Md., December 20, 1909.

....INTRODUCTION....

This pamphlet is designed to show that the periodic financial panics in the United States result from certain fixed and specific causes, and that an analysis of these causes indicates that the approach of such panics may be clearly noted and effectually prevented.

It is designed to show that of the existing currency in the nation, only a portion finds its way into the banks. That with a given quantity of currency in the banks only a definite amount of credit can be extended by the banks. That periodically, owing to the growth of business and the expansion of bank loans, the entire banks of the nation reach the extreme limit of their loaning capacity and can grant no more credit, with the result that a "capital famine" ensues, immediately affecting all branches of industry and precipitating a financial panic.

It is also designed to show that all of our currency is based upon and supported by the gold in circulation; that a given quantity of gold will only support a given quantity of paper, and that we shall invite commercial disaster and national dishonor by injecting too much paper into our circulation; so that there is a definite limit to the quantity of currency.

The amount of our currency can not be indefinitely increased, and it is therefore necessary to get the greatest possible use out of the currency that we have, and to so regulate our affairs that we shall get along on the credit that can safely be granted with such amount of currency.

It is the opinion of the writer that the trouble with our existing system is two-fold:

First. That there is no machinery for the regulation and control of bank loans and credits, and no method by which a gradual check can be placed upon the expansion of bank credits when the reserves of currency run low.

Second. That there is no adequate organization among the banks for mutual support, and, therefore, each individual bank must keep on hand in a dead reserve fund too large an amount of currency, with the result that the amount of bank credit that can be granted is unduly limited.

The remedy suggested is the creation of a Central Bank with strictly limited powers which shall hold the surplus reserves of all of the banks, and also the moneys of the National Government, and which shall use such moneys solely for the purpose of rediscounting short-term bank paper. This will enable the individual banks to safely operate on small cash reserves, as they will be in position to obtain more currency instantly from the Central Bank while there is any surplus currency available in the nation; while the Central Bank, by manipulating the rate of discount, can regulate and control the entire bank loans of the nation. The said bank should have no power to issue paper money except temporary emergency paper strictly limited in amount.

The first portion of this pamphlet is devoted to the study of the uses of currency, and the quantity needed to properly carry on the business of this nation; the second part to a discussion of what that currency shall be composed and the third part to the proposed remedy.

In dealing with these questions the report of the Comptroller of the Currency of the United States for 1908 is used, and the figures showing the condition of the banks as of November 12, 1906, is made the basis of computation. A copy of the material parts of this report is attached to this pamphlet for greater clearness.

The term currency is used to include all kinds of money, whether specie or paper.

In the opinion of the writer, there is nothing vitally wrong with the currency system of the United States, and the only changes in the existing laws necessary to establish an ideal banking and currency system are to repeal the provisions of the National Bank Act relating to reserves, to abolish the Independent Treasury System, and to create a Central Bank with strictly limited powers, as above indicated.

Quantity

There are two main questions involved in the currency discussion, first how much currency is needed to properly carry on the business of the nation; and, second, of what that currency shall be composed.

In order to ascertain the quantity of currency needed it is necessary to note clearly for what purposes currency is used and the exact work it does.

From the report of the U. S. Comptroller of the Currency it appears that the total currency of all kinds in the United States on November 12, 1906, was a little over three billion dollars. This currency was divided into three portions and served three separate and distinct purposes.

USES OF CURRENCY

The first portion consisted of $325,000,000 lying in the vaults of the United States Treasury and its branches. This portion enabled the government to carry on an independent banking system of its own for its own purposes. Currency in payment of taxes and customs is collected by the government agents and deposited in the Treasury; and payments by the government are made by drafts on the Treasury. The government frequently deposits with national banks a portion of this currency, but the report of the U. S. Comptroller shows that at no time since 1900 has there been less than $284,000,000 in currency in the Treasury vaults, nor has it amounted to above $349,000,000. The government may or may not really need this vast amount of currency; perhaps it would be very much better if it was in general circulation; but the fact remains that it has it, and has had it for many years. The amount of currency in the Treasury is likely to be greatest during times of the greatest national prosperity, because at such times the government revenues from imports and internal taxes are the greatest.

The second portion consisted of $1,733,000,000 in the hands of the people, in general circulation outside of the banks, being $20.48 per head of population. This portion served the purpose of a medium of exchange for small transactions.

While the great bulk of commercial payments are made with bank checks, yet there are a vast mass of petty transactions that call for the direct use of currency, and for that reason every one carries more or less currency on his person, and every merchant carries more or less currency in his petty cash drawer for making change, etc. There is also a vast quantity of currency paid out daily for wages, and, while this currency quickly finds its way back to the banks, there is always a large quantity of it afloat outside of the banks.

The more prosperous the times the more currency the people will carry on their persons and the more currency will be afloat outside of the banks for petty cash transactions. The men standing in the bread lines during hard times are not likely to have any currency in their pockets—the same men working for good wages during prosperous times are very sure to have some currency with them. The amount of currency that 80,000,000 people keep at all times outside of the banks is enormous. During the prosperous times of 1893 it amounted to $16.14 per head. During the hard times following 1893 it dropped to $13.65 per head, and then steadily increased as times became better, being $17.11 in 1900, $18.77 in 1904 and $20.48 per head, or $1,733,000,000 in 1906, as above shown.

Some of this $20.48 per capita may have been "hoarded," but there was no apparent reason for people to hoard money prior to November, 1906, for we were then in the midst of the most prosperous times the world had ever seen; stocks were at the highest point and there was not a cloud on the financial horizon—following that date when stocks began to drop in value there might have been reason for uneasiness, and people might have "hoarded" their money, but the reverse was the case, because the report of the comptroller for 1907 shows that by June 30, 1907, the amount of currency held by the people had dropped to $19.36 per head, or to $1,686,000,000—so that during the very period that is is claimed the people were "hoarding," they actually gave up to the banks nearly $100,000,000. If figures ever meant anything, these figures certainly disprove the charge that the money stringency of 1907 was caused by "hoarding" by the people.

But for whatever reason the people hold out and keep afloat outside of the banks this vast mass of currency—more than one-half the total supply, the fact remains that they do hold it, always have held it and have it now—and the more prosperous the times the more they will have.

The third portion consisted of $1,010,000,000 in the hands of the banks, this being the balance of currency left after the government had taken what it desired for its Independent Treasury system, and the people had taken what they desired for their individual purposes. The banks are but the custodians of the people's money and have only that currency which is voluntarily left with them after all other purposes have been served; hence the more prosperous the times the less currency the banks will have, because it is at such times that the demands of the government and the people are the greatest.

This currency in bank served the purpose of a reserve for the support of the deposit liabilities, and was in fact the only foundation for the vast credit system of the nation.

It is to be presumed that the government had taken all of the currency that it desired for its purposes because it had to its credit with many banks large sums and could have called upon such banks for payment of such credits in currency; and it is to be presumed that the people had taken all the currency they needed, for they could have taken it all had they so desired; **had the banks needed more currency, however, they could not have obtained same, as there was no more currency in existence.**