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BANKING SYSTEM

American Banking System Worst In the World.

SO SAYS ANDREW CARNEGIE

"Bank Circulation Based Upon Gold Reserves and a Complete Extinction of All Government Credit Are at This Time Counsels of Perfection"

Americans have many advantages upon which we may plume ourselves as being in advance of other nations, but we have at least one humiliation to lessen self-glorification. Our banking system is the worst in the civilized world.

The statesmen of 1860 did not have a clean slate to begin with. Government credit was then precarious and needed support, and the temptation to use banking for this purpose proved irresistible. Sound banking was sacrificed to sustain the National credit when it was resolved that the currency should be placed upon Government bonds, which, in the opinion of Mr. Gage, ex-Secretary of the Treasury, resulted in giving a marketable value to these twenty per cent higher than they would have otherwise reached.

The result is that our banking capital is diverted to the extent of \$1,250,000,000 invested in Government bonds by the banks, because currency issued must be based upon an equal amount of these bonds deposited in the Treasury. A reserve of twenty-five per cent against deposits must be kept in cash and reserve of five per cent against circulation kept in Washington for note redemption. Mr. Fowler the able Chairman of the Finance Committee in the House, states that the loss caused by this reaches \$150,000,000 annually. Banking capital in France, Germany, England, Scotland, Canada, etc. escapes this loss, because their currency is based upon the assets of the banks. None of their capital is locked up in bonds as security for notes. Banks keep the reserves which experience proves to be necessary.

This, then, is clear—that banks in other countries start with a great advantage over ours, which are heavily handicapped.

There is another important advantage these banks possess over ours. Currency based upon the assets of banks rests chiefly upon trade bills. In the nature of things, the bank is called upon to issue or redeem notes just as business requires. Business brisk, more notes are needed, and they remain in circulation; business dull, less notes needed, and some are promptly returned to the banks for redemption. All is elastic and automatic.

The law in European nations does not restrict the issue of currency equal to the resources of the banks, except that when the Bank of England was reorganized in 1844 the Government owed it eleven million pounds and it was agreed that the Bank might issue uncovered notes to this amount, but any issued beyond this should be covered by gold. The practice in emergencies is for the Government to allow the Bank to disregard this and to issue additional currency uncovered, but the Bank must at all times redeem notes in gold upon presentation. In ordinary times the amount of notes issued by the banks does not exceed much, if any, one-half the amount issuable. Canada's average is fifty-four per cent, Scotland's is less.

We hear the reply, "All this would be a great improvement upon our system, except that our bank notes have the bonds of the Government behind them, the best of all securities. Our people would never agree to accept bank notes without this. Other nations have not this undoubted security."

Let us look into this. Take Canada as an example, which has a proper manner of banking modeled after the Scotch system. Canadian banks issue notes based upon assets. These are secured in the following manner:

First. They are a first lien upon all the resources of the bank.

Second. Every stockholder is liable to an amount equal to the par value of his stock to meet the debts of the bank—upon this the notes have also a first lien.

Third. The Government taxed the banks five per cent of their average circulation until a fund was obtained,

the proceeds of which are ample to pay any reasonable loss upon notes, and this fund the Government now holds. If it should ever be found insufficient, the tax is promptly to be increased. This special fund, however, has never yet been called upon for a dollar. The interest upon it is now returned to the banks as superfluous security.

No banks in Canada or in any of the other countries possessed of proper banking has ever failed to be paid upon demand.

Compare this with the security we have for our currency from Government bonds which have been sold in gold for a shade over one-third their face value (greenbacks fell to thirty-six cents,) and they may sell so again should we be drawn into a serious war. They are at a fictitious price to-day equal to twenty per cent. It is not true, therefore, that these are the best security.

The Government secures the legal tender notes by keeping in Washington a reserve of nearly fifty per cent in gold (150 as against 346 millions), but the only redemption fund against our currency is five per cent in legal tender paper money, which the banks are required to maintain in Washington against their circulation.

There is only one substance in the world which cannot fall in value, because it is in itself the world's standard of value, and that is gold, which the banks of civilized nations have as their reserve.

There never was a time, and there never can be a time, as far as we can see, when a million dollars' worth of gold will not redeem a million dollars' worth of debt. Hence the currency of European nations is absolutely secure, being based on gold, while the currency of our country is not. A serious war would affect it, because our bonds would fall in value. Other nations go through wars, their bank notes never affected, because the reserves held in their own vaults are in gold. Their business world goes on much as usual. Ours would be in constant danger of collapse.

Men have railed against gold as if it had received some adventitious advantage over other articles. Not so; gold has made itself the standard of value for the same reason that the North Star is made the North Star—it is the nearest star to the true north, around which the solar system revolves. It wanders less from, and remains nearer to, the center than any other object. It changes its position less. To object to gold as the standard of value, therefore, is as if we were to refuse to call the star nearest of all stars to the true north, the North Star. Man found that gold possessed many advantages as a metal and was the one that fluctuated least in value; therefore its merits have made it the standard of value. That is all. If another metal appears that keeps truer to uniform value, it will displace gold and make itself the standard, as the star Lyra, under present conditions, will finally displace the present North Star.

Some men high in authority these days seem to be haunted and affrighted by the dread specter of war, and clamor for four battle-ships this year when last year the President announced to the world that no increase of our navy was required, but only one battle-ship per year to keep the present navy effective. Those thus afflicted ponder upon the consequences that would befall our whole financial fabric if, under the strain of war, its basis crumbled even in a small degree compared with that which occurred during the Civil War. France, when overcome, the enemy besieging her capital, moved on in all peaceful business departments in perfect serenity. Gold commanded one per cent premium for a few days, owing to the disorder reigning in Paris, which rendered it difficult for people to attend to business needs. With this exception all went on as before from start to finish. As a war measure, the President should not delay asking Congress before it adjourns to lay the foundation—the only possible foundation—for a safe and perfect banking system, by separating the banks from the Government and requiring them to keep reserves in gold coin as European banks do. A beginning might be made by enacting

that after a certain date banks should keep increasing amounts of their reserves against deposits and circulating notes in coin; as this increased, the bonds now held for security being released. This is practically the Indianapolis plan, which has won wide acceptance. Gold coin can easily be obtained. There is twelve hundred millions of dollars of it in the country to-day, with power to increase this, since our exports exceed our imports. Details should be left to the future, whether the European plan of one central bank or the Canadian plan of establishing a point of redemption in each district be adopted, or an organization of all National banks be made to co-ordinate the system and have authority in emergency to authorize an extension of notes issue as central European banks have under Government authority, all our banks to be responsible pro rata for such additional issues. All these and other secondary questions are not now in order. To-day's duty is simply to make a beginning toward basing our banking system upon gold, instead of Government bonds liable to fluctuation under exceptional conditions.

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To reach proper banking we need no revolution. We should make haste slowly. All our progress should be tentative, avoiding anything like shock to our present system so fraught with danger and rapidly assuming proportions that threaten recurrent disasters. We only need to turn our faces and keep them in the right direction by beginning to inject more gold directly into our present system little by little, until, in the fullness of time, we can establish a banking system complete in itself, such as that which the leading nations and even Canada now so happily possess.

When we at last become fully prepared for the substitution of asset for bond secured currency, this can easily be accomplished without causing even a ripple of disturbance, thus relieving the Government from all part in our banking, as other Governments are relieved under their systems which work so admirably.

Our present plan is primarily an instrument designed to strengthen public credit, and scarcely deserves to rank as a banking system at all. Public credit no longer needs this support. Let us therefore, gradually,

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not hastily, but slowly, very slowly, frightening neither the most ignorant nor the most timid, transform it into the instrument which the country so imperatively needs, if it is to be secure, as other countries are, against financial cataclysms, either in peace or in war.

Men in public life who keep before them this important task will live long in the grateful memories of their future countrymen, for our present plan is one of the greatest of mistakes pardonable only because made under the pressing conditions surrounding the Republic after the Civil War.

We that read in the Senate recently Senator Lodge, one of its leading members, declared that "banks circulation based upon gold reserves and a complete extinction of all government credit are at this moment counsels of perfection." This is true indeed. Senator Lodge has all the leading authorities upon banking affairs known to the writer in agreement with him. The statesmen of today, when dealing with the subject, will have no excuse to offer if they fail to turn the country in the direction of this perfection. There is but one right path.