Discussion of
“Towards a More Perfect American Payments Union: The Civil War as a Political Economic Watershed” (James/Weiman)

Bruce Champ
Federal Reserve Bank of Cleveland

March 29, 2006
Authors claim that the National Banking System (NBS):

- Created a uniform national currency.
- Did not completely succeed in creating an integrated payments system.
- However, the NBS made significant inroads in this area.
- New York City banks played the major role in the payments system through their correspondent relationships.

Of course, the NBS had other problems:

- Seasonal fluctuations in interest rates
- Recurrent banking panics
- These were the primary focus of reform proposals
Recognition of a Need for a Uniform Currency

“It is, however, essential to every modification of the finances that the benefits of a uniform national currency should be restored to the community.” (James Madison, 1815)

“In referring to the causes which had the most decided influence in calling the United States Bank into existence, the inconveniences resulting to the community from the inequality in the rate of exchange between the different sections of the Union stand eminently prominent.” (Secretary of the Treasury William Crawford, 1817, p. 540)
Prior Attempts at Providing a Uniform Currency

- Suffolk System (1825–1858)
  - Net clearing of New England bank notes
  - Notes of participating banks traded at par
Prior Attempts at Providing a Uniform Currency

- **Second Bank of the United States (1816–1836)**
  - Nicholas Biddle claimed success: “The experiment was interesting and hazardous. It was to try how far the institution could succeed... in diffusing over so wide a surface of country a currency of large amount and of uniform value at all places and under all circumstances. [The bank has fulfilled] all the purposes for which it was created. At present these exchanges are generally either at par, or at the utmost one-half of one per cent.” (*Niles Register*, referred to in Catterall, pp. 132–33).
  - Andrew Jackson disagreed: “It must be admitted by all that [the bank] has failed in the great end of establishing a uniform and sound currency.” (State of the Nation Address, 1829)
Prior Attempts at Providing a Uniform Currency

- Second Bank of the United States (1816–1836)
  - Nicholas Biddle claimed success: “The experiment was interesting and hazardous. It was to try how far the institution could succeed... in diffusing over so wide a surface of country a currency of large amount and of uniform value at all places and under all circumstances. [The bank has fulfilled] all the purposes for which it was created. At present these exchanges are generally either at par, or at the utmost one-half of one per cent.” (*Niles Register*, referred to in Catterall, pp. 132–33).
  - Andrew Jackson disagreed: “It must be admitted by all that [the bank] has failed in the great end of establishing a uniform and sound currency.” (State of the Nation Address, 1829)
Increased Use of Drafts & Checks

- Prior to the Civil War, bank notes were the primary means of making long-distance transactions.
- During the NBS, drafts and checks eventually become the primary method of payment.
  - Use of these instruments required a network of correspondent relationships and large holdings of bankers’ balances.
### Increased Use of Drafts & Checks

<table>
<thead>
<tr>
<th>Location</th>
<th>Wholesale 1896</th>
<th>Wholesale 1909</th>
<th>Retail 1896</th>
<th>Retail 1909</th>
</tr>
</thead>
<tbody>
<tr>
<td>Country</td>
<td>88.7</td>
<td>94.6</td>
<td>63.1</td>
<td>68.8</td>
</tr>
<tr>
<td>Other Reserve</td>
<td>93.2</td>
<td>96.7</td>
<td>74.1</td>
<td>75.7</td>
</tr>
<tr>
<td>New York</td>
<td>98.2</td>
<td>98.6</td>
<td>79.4</td>
<td>86.5</td>
</tr>
</tbody>
</table>

Source: James and Weiman (2006)
New York City Due To/Individual Deposits
New York City & Chicago Due To/Individual Deposits

![Graph showing the trend of New York City (NYC) and Chicago deposits from 1880 to 1915. The graph indicates an upward trend in both cities with fluctuations over the years.](image_url)
Domestic Exchange Rates: Does the Trend Continue?

- Authors note changes in the pattern of domestic exchange rates before (1850s) and after the Civil War (1860s and early 1870s).
  - Premiums and discounts reduced
  - Volatility in premiums and discounts diminishes
- Do further reductions occur later in the period?
Authors note changes in the pattern of domestic exchange rates before (1850s) and after the Civil War (1860s and early 1870s).

- Premiums and discounts reduced
- Volatility in premiums and discounts diminishes

Do further reductions occur later in the period?
Yes. The standard deviations are reduced another 50% by the beginning of the 1900s.

Table 3. Standard Deviation of Domestic Exchange Rates (bp)

<table>
<thead>
<tr>
<th>City</th>
<th>1850s</th>
<th>1860s</th>
<th>1899–1908</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chicago</td>
<td>51</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>New Orleans</td>
<td>52</td>
<td>11</td>
<td>4</td>
</tr>
<tr>
<td>San Francisco</td>
<td>NA</td>
<td>NA</td>
<td>7</td>
</tr>
</tbody>
</table>

Ranges of exchange rates are also cut roughly in half.

Table 4. Ranges of Domestic Exchange Rates
(1899–1908, percent)

<table>
<thead>
<tr>
<th>City</th>
<th>Range (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chicago</td>
<td>-0.085 to 0.050</td>
</tr>
<tr>
<td>New Orleans</td>
<td>-0.178 to 0.075</td>
</tr>
<tr>
<td>San Francisco</td>
<td>-0.130 to 0.500</td>
</tr>
</tbody>
</table>

Source: Kemmerer (1910).
Chicago Domestic Exchange Rate (1899–1909, percent)

Source: Kemmerer (1910)
Why weren’t state banks that converted to national bank status able to attract new correspondent deposits, whereas newly-formed national banks were able to do so?

How large a role did other reserve cities play in the payments system?