COMMERCIAL BANK PROFITABILITY IN THE EARLY NINETEENTH CENTURY

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Commercial banks played an important role in the development of the United States in the early nineteenth century. Banks channeled savings from individuals to investors and thereby enhanced real capital formation. Their bank note issue supplemented the nation's scarce specie supply and facilitated the exchange of goods and services. Yet, sometimes commercial bank credit expansion aggravated inflationary tendencies, and at other times their credit contractions reinforced recessions. Because of its role in economic development, early American banking has been the subject of considerable research ranging from the classic works on the First and Second Banks of the United States to a multitude of state and individual bank histories.[1] Some of the more recent research has attempted to document the development and the role played by banks in American economic growth.[2] It is the purpose of this study to continue the latter line of research by presenting and analyzing data on the profitability of American commercial banks between 1807 and 1830.

Empirical data on commercial bank profits before 1830 are scarce. Fragmentary information exists in histories of individual banks, and historians often draw conclusions from the individual examples. Thus economic history books often contain examples of the dividends of banks such as Bank of North America, or the Massachusetts Bank and draw generalizations from them, or they contain statements like this:

"How profitable banking actually was during this period (1789-1865) is not known, but it seems clear that bank stock stood high among investment outlets."[3] The rapid growth in the number and capital stock of commercial banks in the early nineteenth century indicates that investors, indeed, expected high returns. Authorized capital stock of state banks grew from $3.1 million in 1790 to $168.5 million in 1830. But what returns did the investor actually realize?

This study attempts to answer that question. The dividends of incorporated banks in six states (from four geographic regions) are presented. The average annual dividend rates are examined by state and compared with other states. The trend of bank dividends throughout the period is examined, and the possibel use of bank dividends as an historical indicator of business activity is explored.

The Data

Before the analysis is presented, the nature of the primary source material should be explained. The dividend data were gathered through a search of libraries, newspapers and state archives. The latter proved most fruitful.

During the period between 1807 and 1830 private or unincorporated commercial banks seldom, if ever, sent reports of condition to state governments. However, private banks rapidly decreased in importance and most disappeared by 1820.[4] The absence of their statistics is not detrimental to the study. A few states required chartered banks to submit annual statements of condition. However, many states did not make these records public and in any case, net profit, dividends, and retained earnings were often not reported. As a result, the author found dividend records for only six states. But the bank records collected in these six states accounted for approximately 17 percent of all state chartered commercial banks in 1810, 32 percent in 1815 and 25 percent in 1830.[5]

The number of banks that reported dividend payments varied from year to year. This study includes all the incorporated banks in Virginia, Mississippi, North Carolina, and most of those in Massachusetts and Pennsylvania. Only one of the South Carolina banks is included (two to four banks operated during the period).

The form of dividend information varied from state to state. The actual dividends paid by banks in Pennsylvania, Virginia, Mississippi, and North Carolina are used. Dividend rates for Massachusetts banks were available for only six months of each year. Banks in all states paid dividends semi-annually. Therefore, the six-month figure for Massachusetts was doubled to get the average annual dividend rate. This estimate should result in few errors, however, for the tendency at that time was to declare the same rate of dividends for each six months in any one year. The South Carolina bank reported net earnings rather than dividends, and they are used in the study.

Ideally, this study should focus on the return to capital (net earnings as a percent of capital). However, since only dividend data are available, they serve as a proxy for net earnings, and the two are used interchangeably in this study. The direction of net earnings whould not differ materially from the direction of dividends, and there is little evidence to conclude that banks generally retained much profit each year.

Commercial Bank Profitability, 1807-1830

Bank earnings then as now are a function of managerial talent, management, philosophy, the degree of state regulation, the local demand for loans, the investment opportunities, and the amount and stability of deposits, among other things. Different combinations of these factors were quite evident in early banks, for net earnings varied from bank to bank and state to state.

The dividends of some banks swung widely while other banks paid the same rate for several years in a row. For example, dividends of the bank of the state of Mississippi ranged from 6 to 17 percent per year, from 1820-1829, while the State Bank of North Carolina paid 8 percent per year during the same period.[6]

The dividend rates of individual banks are fascinating to examine however, the aggregation of dividends by state provides a truer reflection of the industry. Table 1 presents the average annual dividend rates of reporting commercial banks in six states. The average dividends shown in the Table 1 were developed by the division of the total dividends by the total paid in capital stock.

In general, dividends were lowest in the New England banks and increased in the Middle Atlantic, the Southeast, and were highest in the Southwest. Massachusetts had the lowest average dividend rate (6.22 percent) while Mississippi had the highest rate (10.38 percent). The degree of fluctuations in annual average dividend rates from year to year, moved in the same direction; Massachusetts had the lowest (7.96-4.98 percent) and Mississippi had the largest (17.00-6.00 percent).

Table 1

AVERAGE ANNUAL DIVIDEND RATES OF
REPORTING COMMERCIAL BANKS IN SIX STATES: 1807-1830

State	Average Annual Dividend Rate (Percent)	Range High-Low (Percent)	Years
Massachusetts	6.22	7.96 - 4.98	1808-1830
Pennsylvania	6.44	9.24 - 4.44	1815-1830
North Carolina	7.50	12.00 - 3.10	1809-1830
Virginia	8.84	12.00 - 6.50	1807-1816
South Carolina	10.14*	16.45 - 5.89	1815-1830
Mississippi	10.38	17.00 - 6.00	1811-1830

*Average net earnings.

Source: Table 4 in Appendix.

The low dividend rate in Massachusetts may well reflect the maturity of the business community, the tight control over banks by the state and the Suffolk System, and the relatively large amount of commerce and industry in the state.

In the remaining states, the higher yields and greater rate variation may reflect higher lending rates, a greater shortage of loanable funds, and a less conservative specie reserve philosophy. Of these, the most important difference in earnings was probably the relationship of specie to notes and deposits which the banks held. Table 2 presents the ratio of bank notes and deposits to specie in commercial banks in five states. In each state, except Virginia, the dividend rate tended to increase as the amount of bank notes and deposit liabilities increased per dollar of specie. In fact, this difference could account for a large part of the earnings variations among the states, without appreciable interest rate differentials.

Table 2

RATIO OF BANK NOTES AND DEPOSITS TO SPECIE IN COMMERCIAL BANKS IN SEVERAL STATES: 1807-1830

State	Average Annual Ratio	Range High-Low	Years
Massachusetts	5.35	9.63 - 1.57	1807-1830
Pennsylvania	6.13	19.20 - 3.78	1815-1830
North Carolina	7.60	12.53 - 4.31	1819-1830
Virginia	7.12	18.73 - 2.84	1807-1816
South Carolina	9.94	18.46 - 3.61	1815-1830

Source: Table 5 in Appendix.

Two other factors must be noted in this interpretation. First, the averaging of a large number of banks in Massachusetts and Pennsylvania tended to hide the high and low earnings of individual banks, thus the dividend rates appear more stable in these two states than in others. With only one bank in South Carolina and Mississippi, highs and lows were not dampened through averaging. Second, the South Carolina rate is the actual return on capital rather than a dividend rate and must be used with care. It may reflect some retained earnings which were not included in the dividend rates of the other states.

Retained Earnings

As mentioned earlier, net earnings were not often reported, and therefore, little information on retained earnings is available. Several factors, however, indicate that they were small for many banks. The originators of many banks did so to create a source of loans.[7] In such cases the dividend policy would probably emphasize payout, rather than retention. In some states the legislatures discouraged the retention of earnings. In Pennsylvania, for example, in order to collect a tax on dividends, the state required chartered banks to pay dividends. If a bank refused to do so for a specified length of time, the state revoked its charter.[8] This law probably reduced the level of any planned retained earnings of banks, and could have weakened many of them.

Finally, information on the State Bank of Mississippi shows that through the period 1811-1830 all but about .5 percent of the earnings were paid out in dividends.[9] There was, however, some discrepancy between the time the earnings occurred and the dividend payout.

Comparability of Commercial Bank Dividends in Different States

In the early 1880s the nominal yields on bank stock in different states were not strictly comparable from an investor's point of view, for the dividends were probably paid in each bank's own notes. The value of a bank's notes fluctuated with the distance from the place where they could be redeemed and with the bank's reputation. Even the notes of the Second Bank of the United States passed at a discount when some distance from the branch issuing them. In order to strictly compare the bank dividends by states, the dividends of each state must be adjusted to the value of its banks' notes at the home of the stockholder. For example, if a person in Philadelphia owned stock of banks in all six states, the dividends received would have to be adjusted to their purchasing power in terms of Philadelphia bank money. The average annual dividend rates at Philadelphia, for the years 1814 to 1830, are presented in Table 3.

The discount on bank notes tended to rise with the increase in dividends. Massachusetts banks had the least erosion in dividend payments due to bank note discounts while Mississippi had the largest. The discount adjustment reduced the value of average dividends in Philadelphia of the banks of Massachusetts, .01 percent; Pennsylvania, .03 percent; North Carolina, .05 percent; Virginia, .05 percent; South Carolina, .06 percent; and Mississippi, .07 percent. Although the higher earning states lost a greater share of their dividends as a result of the bank note discount, the rank of earnings was not significantly changed. The Southeastern and Southwestern banks still had the highest returns.

If Charleston, South Carolina, Boston, Massachusetts or any other city had been chosen as the par base, the bank note discounts and comparable earnings would have been different.

Table 3

AVERAGE ANNUAL DIVIDENDS OF COMMERCIAL BANKS OF SEVERAL STATES ADJUSTED TO THEIR BANK NOTE DISCOUNT AT PHILADELPHIA: 1814-1830

State	Average Annual Dividends Nominal (percent)	Average Annual Dividends Adjusted (percent)	Years
Massachusetts	5.88	5.80	1817-1830
Pennsylvania (outside Philadelphia)	6.44	6.28	1815-1830
North Carolina	7.16	6.80	1814-1830
Virginia	10.07	9.56	1814-1816
South Carolina	10.14	9.51	1815-1830
Mississippi	11.67	10.89	1825-1830

Source: Tables 4 and 6 in Appendix

*Average net earnings.

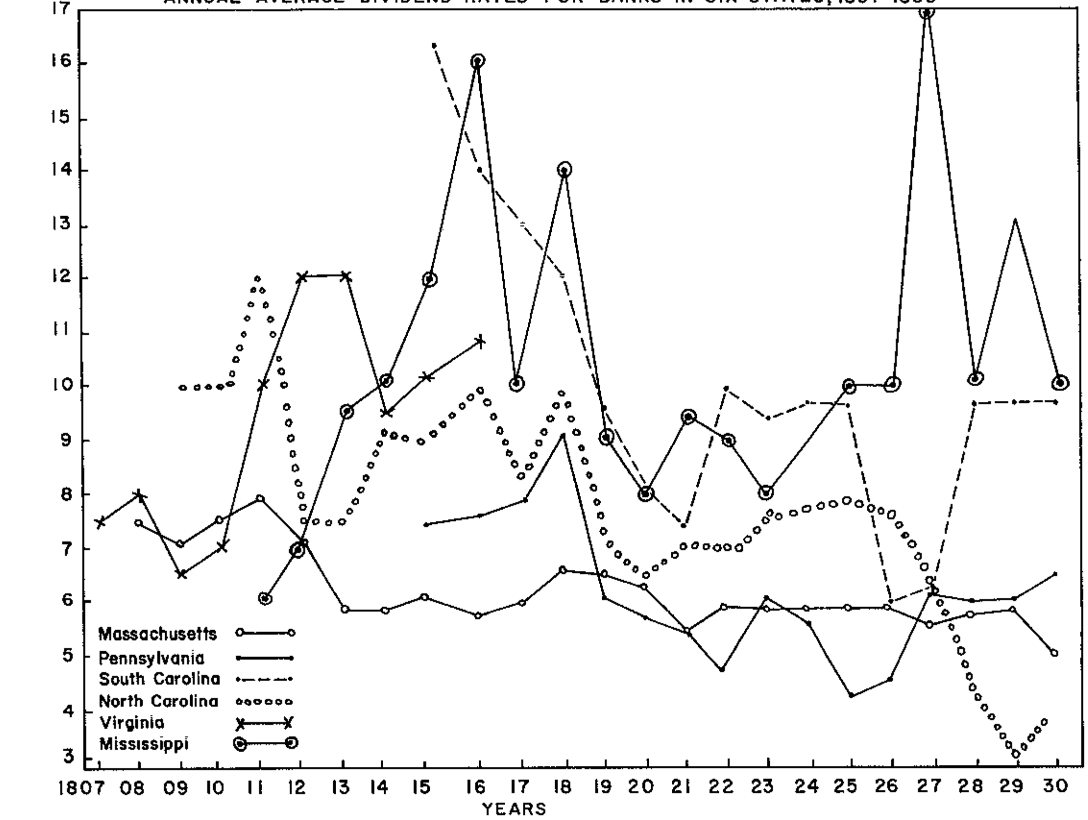
Trends in Commercial Bank Dividends: 1807-1830

The average annual dividend rates for 1807 to 1830 indicated a general level of commercial bank profitability for the period, and their adjustment to some par base revealed one of the problems that the individual investor faced. However, the annual dividend rate fluctuations can also be useful, for they reflect the impact of changes in economic and political factors on commercial bank earnings. It would be very useful to have a rate series which reflects the profitability of commercial banks throughout the nation each year during the period. But such a rate devised from the statistics presented in this study would be meaningless. Not only are a number of states not included; but the larger number of banks in Massachusetts and Pennsylvania, would unduly influence the final figure. It is, therefore, more meaningful to speak of ranges and relative levels of earnings.

The annual dividend rates for each state are presented in Chart I. Although there was wide variation in dividend rates among states, the general tendency was for rates to rise to their peak between 1810 and 1818 and then fall in 1819. The rates tended to stay lower through the remainder of the period, with Mississippi the noticeable exception.

CHART I

ANNUAL AVERAGE DIVIDEND RATES FOR BANKS IN SIX STATES, 1807-1830



Economic and political conditions accounted for some of the variations in dividend rates during the period (see Chart 1). For example, historians believe that many state banks fought against the recharter of the Bank of the United States, for its regulation of state bank notes affected their profits. Bankers believed that their profit would rise after its demise.[10] The First Bank of the United States ceased operations in March, 1811; and average dividends, in fact, did rise between 1810 and 1811 for banks in three states (see Chart 1).

The War of 1812 and the heavy bank financing undoubtedly helped to keep the earnings high in the Middle Atlantic and Southeastern States through 1814. On the other hand, the war was unpopular in New England, and the banks there made relatively few government loans; in addition, the war disrupted trade in the area. As a result, the earnings of Massachusetts banks fell.

The suspension of specie payments in September, 1814, removed another barrier to credit expansion. Note issues rose and earnings probably would have increased even more if not for the great rise in the number of banks and the growth in capital stock throughout the nation.

The establishment of the Second Bank of the United States in April, 1816, and the resumption of specie payments in February, 1817, apparently had little immediate effect on bank earnings for the Second Bank did not pressure state banks to redeem their notes. However, credit contraction of the Second Bank in October, 1818, and the Panic of 1819 did reduce bank earnings in all states. Dividends tended to remain lower for the rest of the period. Undoubtedly the control of the Second Bank was in a large measure responsible for this. The exception, Mississippi, can be explained in that it paid dividends in excess of current earnings in the peak years of 1827 and 1829 (see Chart 1).

The North Carolina banks are a special case. They refused to resume specie payment following the Panic of 1819 The Second Bank tried unsuccessfully to force note redemption until 1827. The North Carolina banks purchased their own notes to maintain their value. In that year, the Second Bank introduced branch draft notes and forced a reduction of North Carolina bank notes, thereby lowering their earnings from 1827 to 1830 (see Chart 1).

Summary and Conclusion

This study examined the dividends of commercial banks in six states between 1807 and 1830. These dates were chosen because it is the earliest period for which a significant amount of data are available. In general, the average annual dividend rates were between 6.22 and 10.38 percent. Massachusetts had the lowest and Mississippi had the highest. However, adjustments for bank note discounts were an important consideration for investors during the period.

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Bank stock was considered a prime investment in the early 1800s; however, the average earnings are not exceptional when compared to the return in numerous other industries which ranged between 10 and 20 percent per annum.

The data presented tended to substantiate several general assumptions widely held by historians. The demise of the First Bank of the United States did permit state banks to increase their earnings. The financing of the War of 1812 and the suspension of specie payments in 1814 did permit banks outside New England to increase and maintain higher earnings. The credit contraction of the Second Bank in October, 1818, and Panic of 1819 did reduce bank earnings. The control over state bank note issue by the Second Bank apparently worked, for state bank earnings remained lower from 1819 to 1830.

The banks represented in this paper are a small part of the total which existed between 1807-1830. However, their annual dividend rates give some indication of commercial bank profitability and also reflect many of the monetary and economic activities which took place during the period under study. This evidence suggests that the development of a time series of commercial bank earnings would be useful to the economic historian in interpreting American economic development. The data, although scarce for the period under consideration, are more readily available for later years and should be the focal point for further research.

NOTES

[1]Well-known books on early banking include: William G. Sumner, A History of Banking in the United States, (New York, 1896); A. Barton Hepburn, A History of Currency in the United States, (New York, 1915); Horace White, Money and Banking, (New York, 1936); Davis R. Dewey, State Banking Before the Civil War, (Washington, 1910); Bray Hammond, Banks and Politics in America, (Princeton, 1957); Davis R. Dewey, The Second United States Bank, (Washington, 1910); Walter B. Smith, Economic Aspects of the Second Bank of the United States, (Cambridge, 1953); Ralph C. H. Catterall, The Second Bank of the United States, (Chicago, 1903). Examples of a state banking history and the history of one bank are: Robert C. Weems, Jr., "The Bank of Mississippi--A Pioneer Bank of the Old Southwest, 1809-1844," (unpublished Ph.D. dissertation, Columbia University, 1951); Walter W. Chadbourne, A History of Banking in Maine, 1799-1930, (Orono, 1936).

[2]Carter H. Golembe, "State Banks and the Economic Development of the West, 1830-1844," (unpublished Ph.D. Dissertation, Columbia University, 1952), and J. Van Fenstermaker, The Development of American Commercial Banking: 1782-1837, (Kent, 1965).

[3]Harold F. Williamson, The Growth of the American Economy (Englewood Cliffs, 1951), p. 236.

[4]Albert Gallatin, Considerations on the Currency and Bank-System, (Philadelphia, 1831), p. 28.

[5]Van Fenstermaker, pp. 13, 77, 80, 84, 87, and 91.

[6]Weems, pp. 757-766.

[7]Williamson, p. 236.

[8]Acts of the General Assembly of Pennsylvania, VI (1814), c. 3902, pp. 154, 173.

[9]Weems, pp. 757-766.

[10]Donald L. Kemmerer and C. Clyde Jones, American Economic History, (New York, 1959), p. 202.

APPENDIX

Table 5

RATIO OF BANK NOTES AND DEPOSITS TO
SPECIE IN FIVE STATES, 1807-1830

Year	Massachusetts	Pennsylvania	South Carolina	North Carolina	Virginia
1807	4.47				6.01
1808	3.53				4.65
1809	4.44				2.84
1810	3.38				5.72
1811	3.79				6.21
1812	1.87				3.68
1813	1.57				5.01
1814	1.74				14.57
1815	1.96	19.20	18.46		18.73
1816	3.39	7.74	18.36		3.78
1817	3.81	6.72	4.29		
1818	4.94	7.33	6.46		
1819	4.20	4.49	5.93	6.36	
1820	4.52	3.78	6.55	4.67	
1821	2.77	4.20	6.19	4.67	
1822	6.73	5.16	3.61	7.09	
1823	6.05	4.84	8.39	5.65	
1824	4.68	4.70	14.06	4.31	
1825	9.16	4.43	14.49	7.73	
1826	7.18	5.34	13.57	10.42	
1827	6.70	5.84	13.83	6.27	
1828	8.73	6.45	8.61	11.12	
1829	9.63	5.64	16.77	10.58	
1830	9.14	5.06	9.39	12.53	

Sources: Massachusetts Legislature, Schedule Showing the Condition of Banks in Massachusetts, 1803-1837, Boston, 1837; Pennsylvania Legislature, Senate Journals, Harrisburg, 1815, pp. 39-49, 1816, pp. 35-57, 1817, pp. 93-125, 1818, pp. 169-200, 1819, pp. 99-128, 1820, pp. 179-211, 1821, pp. 157-187, 1822, pp. 142 167, 1823, pp. 157-182, 1824, pp. 123-139, 1825, pp. 108-130, 1826, pp. 122-147, 1827, Vol II, pp. 548-574, 1828, Vol. II, pp. 332-359, 1829, Vol. II, pp. 432-461, 1830, Vol. II, pp. 426-455: Jaob Maudlin Lesesne, "The History of the Bank of the State of South Carolina," Unpublished Ph.D. dissertation, University of South Carolina, 1948, pp. 189-190; South Carolina Legislature, Erratum: The following table should be included in the Appendix beginning on page 82.

Table 4

ANNUAL AVERAGE DIVIDEND RATES FOR CHARTERED BANKS
IN SIX STATES, 1807-1830

Year	Massachusetts	Pennsylvania	South Carolina	North Carolina	Virginia	Mississippi
1807					7.50	
1808	7.50				8.00	
1809	7.08			10.00	6.50	
1810	7.50			10.00	7.00	
1811	7.96			12.00	10.00	6.00
1812	7.14			7.50	12.00	7.00
1813	5.84			7.50	12.00	9.50
1814	5.68			9.20	9.21	10.00
1815	6.44	7.45	16.45	9.00	10.14	12.00
1816	5.74	7.52	16.00	9.90	10.86	16.00
1817	5.96	7.68	13.12	8.60		10.50
1818	6.68	9.24	11.90	9.90		14.00
1819	6.54	6.10	9.60	7.30		9.00
1820	6.34	5.70	8.40	6.30		8.00
1821	5.30	5.42	7.23	7.10		9.50
1822	5.96	4.66	10.04	6.90		9.00
1823	5.94	6.01	9.46	7.50		8.00
1824	5.87	5.61	9.72	7.60		9.00
1825	5.82	4.22	9.62	7.80		10.00
1826	5.90	4.44	5.89	7.60		10.00
1827	5.52	6.18	6.27	6.30		17.00
1828	5.68	5.90	9.27	3.90		10.00
1829	5.84	5.98	9.69	3.10		13.00
1830	4.98	6.38	9.70	3.70		10.00

Sources: Massachusetts Legislature, Schedule Showing the Condition of Banks in Massachusetts, 1803-1837, Boston, 1837; Pennsylvania Legislature, Senate Journals, Harrisburg, 1815, pp. 39-49, 1816, pp. 35-57, 1817, pp. 93-125, 1818, pp. 169-200, 1819, 99-128, 1820, pp. 179-211, 1821, pp. 157-187, 1822, pp. 142-167, 1823, pp. 157-182, 1824, pp. 123-139, 1825, pp. 108-130, 1826, pp. 122-147, 1827, Vol. II, pp. 548-574, 1828, Vol. II, pp. 332-359, 1829, Vol. II, pp. 432-461, 1830, Vol. II, 426-455: Joab Mauldin Lesesne, "The History of the Bank of the State of South Carolina," unpublished Ph.D. dissertation, University of South Carolina, 1948, pp. 189-190; South Carolina Legislature, Compilations of Acts, Resolutions and Reports etc. in Relation to the Bank of the State of South Carolina. Columbia: State Printer, 1848, pp. 117, 136, 157, 264-268, 408-434; North Carolina, Department of Archives and History, Raleigh, Bank Papers, 1809-1837; Virginia Legislature, Journal of the House of Delegates 1815, p. 151; Robert C. Weems Jr., "The Bank of Mississippi--A Pioneer Bank of the Old Southwest, 1809-1844," Unpublished Ph.D. dissertation, Columbia University, 1951, pp. 757-766.

Compilations of Acts, Resolutions and Reports, etc. in Relation to the Bank of the State of South Carolina. Columbia: State Printer 1848, pp. 117, 136, 157, 264-268, 408-434; North Carolina, Department of Archives and History, Raleigh, Bank Papers, 1809-1837; Virginia Legislature, Journal of the House of Delegates 1815, p. 151.

Table 6

ANNUAL AVERAGE PERCENT DISCOUNT ON STATE BANK NOTES AT PHILADELPHIA, 1814-1830

Year	Massachusetts	Other Pennsylvania	South Carolina	North Carolina	Virginia	Mississippi
1814		3.50	7.50	7.50	7.50	
1815		5.00		5.00	5.00	
1816		7.00	5.00	3.00	3.00	
1817	(1.00)*	3.00	1.50	2.50	1.00	
1818	par	3.00	2.00	3.00	2.00	
1819	par	2.50	5.00	10.00	4.50	
1820	3.00	2.00	2.00	5.00	2.00	
1821	1.50	2.00	1.50	3.00	1.50	
1822	2.00	2.00	3.50	5.50	1.50	
1823	1.50	2.50	3.00	7.00	1.00	
1824	1.50	1.00	1.50	4.50	.50	
1825	1.50	par	1.50	3.50	.50	9.00
1826	1.50	par	1.50	4.50	.75	9.00
1827	1.50	.50	1.25	5.00	.75	6.00
1828	1.75	.50	2.00	8.00	1.00	7.00
1829	1.50	.50	1.50	3.00	.75	5.00
1830	1.00	.50	1.00	1.75	.75	5.00

*Above par.

Source: U.S. House Executive Document No. 15, 28 Congress, 1 Session (1843-44), Vol. II, pp. 1108-1128.

Table 7

NUMBER OF STATE CHARTERED BANKS
THAT REPORTED DIVIDENDS IN FIVE STATES, 1807-1830

Year	Massachu-setts	Pennsyl-vania	South Carolina	North Carolina	Virginia	Missis-
1807					1	
1808	16				1	
1809	16			1	1	
1810	15			1	1	
1811	15			2	1	1
1812	16			3	1	1
1813	16			3	1	1
1814	21			3	2	1
1815	25	35	1	3	2	1
1816	25	36	1	3	2	1
1817	26	37	1	3		1
1818	27	37	1	3		1
1819	28	32	1	3		1
1820	28	32	1	3		1
1821	28	29	1	3		1
1822	33	24	1	3		1
1823	34	21	1	3		1
1824	34	19	1	3		1
1825	41	21	1	3		1
1826	55	20	1	3		1
1827	60	22	1	3		1
1828	61	26	1	3		1
1829	66	28	1	3		1
1830	63	27	1	3		1

Sources: Massachusetts Legislature, *Schedule Showing the Condition of Banks in Massachusetts, 1803-1837*, Boston, 1837; Pennsylvania Legislature, Senate Journals, Harrisburg, 1815, pp. 39-49, 1816, pp. 35-57, 1817, pp. 93-125, 1818, pp. 169-200, 1819, pp. 99-128, 1820, pp. 179-211, 1821, pp. 157-187, 1822, pp. 142-167, 1823, pp. 157-182, 1824, pp. 123-139, 1825, pp. 108-130, 1826, pp. 122-147, 1827, Vol. II, pp. 548-574, 1828, Vol. II, pp. 332-359, 1829, Vol. II, pp. 432-461, 1830, Vol. II, 426-455: Joab Mauldin Lessesne, "The History of the Bank of the State of South Carolina," (unpublished Ph.D. dissertation), University of South Carolina, 1948, pp. 189-190; South Carolina Legislature, *Compilations of Acts, Resolutions and Reports etc. in Relation to the*

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