REMARKS BY THE DISCUSSANT

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George Green has given us an interesting narrative of policy formulation and implementation in the Citizens Bank of Louisiana. The 'Citizens Bank' Green tells us was largely concerned with the mobilization of funds for long-term argicultural and commercial mortgage credit. Initially, such funds were generated by two sources: an exchange of $12 million of the Bank's equity for $14 million of locally-held land, structures, and slave mortgages, and a $47 million debt issue sold to European investors. The latter exchange was consummated only upon the endorsement of these bonds by the State of Louisiana. A comparison of bond contracts before and after state endorsement suggests the state's subsidy was approximately $850,000.

The behavior of the bank during the period 1836-38 is contrasted with bank policy from 1839 to 1842. The first 'epoch' was marked by successful bond sales in the European market, and thus corresponds to a large and continuing specie inflow. Edmund J. Forstall, a figure not unknown to business and economic historians--I cannot ascertain the difference--presided over the bank throughout this period. His tenure was marked by strict adherence to "sound banking", i.e., substantial specie and commercial paper reserves and loan activity constrained by the bank's paid-in capital and accumulated retained earnings. Liquidity dificulties began for the bank in March 1837; the 'nonliquidity' of the bank's commercial paper reserves was a major source of difficulty. Forstall's inability to continue 'sound money' policies--largely the result of exogenous shocks to the Louisiana money market during 1837, brought the suspension of specie payment in March of that year. Forstall's desire to limit the credits of stockholders to a constant fraction of the bank's paid-in capital was overruled in April of 1838. His resignation the following August brought the end of epoch one in the bank's history.

Green views the period August 1838 to August 1842 as characterized by *ad hoc* responses to several crises. This period was characterized by continued expansion of credit to bank stockholders, and by a portfolio increasingly weighted by long-term commerical securities. The later 'epoch' is not to be regarded as one of 'easy credit.' Despite its concern for stockholders, the bank failed to get involved in a branch bank project encouraged by the state legislature. The increasingly 'illiquid' position of the bank, coupled with shocks to international and interregional exchanges, resulted in a series of unusual transactions by the bank; among these was the cotton speculation of 1839. In may 1842, the resumption of specie payment by other New Orleans banks forced the Citizens Bank to follow suit. The resultant large specie outflow forced its liquidation within the year.

What were the determinants of the bank's failure? Historians have suggested mismanagement and 'inherent difficulties of property banking' as explanations. Green argues the evident success of modern 'mixed banks' may be sufficient cause for rejecting Redlich's 'inherent disadvantage' notion. An alternative explanation has 'external disadvantages' as its basis, these being: (1) limited portfolio options, (2) poorly developed capital markets, (3) instability of public preferences for specie, and (4) an unregulated money supply.

I am not a student of banking history. Nonetheless, I would advance the following criticisms of Green's paper. First, the paper is short on its presentation of the bank's financial statistics. Second, insufficient attention is paid to the temporal ordering of exogenous shocks and the several policies implemented by the Bank. For example, it would appear that the Bank of England's actions in 1836 brought on the specie difficulties of the Citizens Bank in 1838; and yet those actions coincided with the period for which the 'sound money' policy "worked reasonably well". Third, what evidence can be provided to the period 1838-1842 as one of 'tight-credit?' Certainly the bank's disinterest in branch banking must be weighted more carefully against its expansion of credit to stockholders and its increased holdings of long-term commercial securities.

I have one final comment on Green's paper. Nagel has shown us that historical inference may be regarded as a counterpart of the predictive testing of universal conditions (scientific laws). The former asserts the truth of these laws; the latter attempts their falsification. If we are to pursue explanations of the behavior of business firms by means of collecting and organizing singular statements, then careful attention must be given to the truth of the 'laws of economics' which underlie our presentation. I see no such attempt in this paper. And, as such, I remain skeptical toward the asserted explanation for the failure of the Citizens Bank of Louisiana.

Van Fenstermaker's study of commercial banking in the early nineteenth century is a cautious and original piece of research. Using the reports of state chartered banks in five states--Massachusetts, Pennsylvania, Virginia, North Carolina and Mississippi--he has developed estimates of dividends flows and the value of paid-in capital for the period, 1807-1830.

Over the period 1790-1830 the author observes an increase in the capital stock of state banks on the order of 5500 percent. The suggestion of high profitability for bank stock--based on this rapid increase and on substantial 'institutional holdings'--seems unwarranted. Indeed, the second of these suggests only stability of those earnings. Average annual dividend rates are observed to be highest in Mississippi and lowest in Massachusetts. A plausible explanation for this divergence in equity rates of return is offered in the form of a positive relation between those rates and the availability of specie relative to bank notes and deposit liabilities.

Since dividends were often paid in the notes of the bank declaring them, a comparison of dividend rates cannot be made directly. Van Fenstermaker performs a regional deflation of the dividends, making use of bank note discounts in Philadelphia. As expected, the deflation calculations reduce the regional variability in these rates. The last section presents time series observations of bank equity returns for each state, 1807-1830.

My comments on Van Fenstermaker's paper are several. Each is intended as an extension of the author's discussion--a discussion I find thorough and useful. However, the word profitability should be dropped from the paper's title. The discussion relates exclusively to the dividend/paid-in stock (at book value) ratio. Further, the comments on Pennsylvania dividend taxation as a deterent to returned earnings seem to purvey a slightly incorrect interpretation. (Apparently, Pennsylvania banks needed only to pay some dividends. Under this system, I find it difficult to ascertain whether retained earnings would rise, fall, or remain constant.) Additionally, I would appreciate more emphasis on spatial and temporal variation of dividend rates. I hold to this view since the estimated rates appear quite consistent with advanced propositions about factor market integration. The observed variations provide us, then, indirect information on these propositions.

Finally, I think this paper raises an interesting point in method: How does one obtain statistical averages from samples with but a few elements? I provide no answer. Can one apply subjective weighting schemes based on 'feelings' about the data? Should one always use the sample mean? These questions deserve some consideration.

I find myself in almost complete agreement with the substantive content of Vedder's discussion of federal deposit insurance, shifts in 'depositor confidence,' and bank failure rates prior to 1930. The proposed measure of 'depositor confidence' is the deposit-currency ratio (hereafter referred to by the symbol D/C). One observes a secular increase in D/C from 1920 to 1929. In the fall of 1930 began a series of banking 'crises' which lasted until April 1933. Coincident with the large number of bank failures was a large fall in D/C. This decline in 'depositor confidence' forced many banks to convert assets into reserves at a time of low prices for those assets, further aggrevating general economic decline.

Federal deposit insurance legislation was not contained in the Roosevelt administration's legislative program; its presence in the Banking Act of 1933 can be attributed to Henry Steagall. The intent of this legislation was the addition of a 'stabilizer' to the money market, and not the protection of small time deposit accounts.

The proposed legislation did not become effective until January 1, 1934. Prior to that time the rate of bank failures fell rapidly and D/C became stable. The advent of FDIC operation in 1934 corresponds to substantial increase in D/C, a slowing of bank failures, and a decline in postal savings. So much for the first year of the FDIC. What, asks Vedder, are the longrun effects of deposit insurance in the United States? Surely the stable growth of D/C--conditioned by deposit confidence under the ledislation--has made the conduct of monetary policy easier. (No comment is offered here on the quality on that policy). Insured state nonmember banks have likely become subject to more extensive examination. The FDIC has additionally assumed the 'bad assets' of 'troubled banks,' and has promoted mergers between these banks and more stable banks.

The increased stability of the environment within which the banks operate should have produced a shift in bank portfolio composition toward long-term loans. This phenomena has yet to be observed, but, says Vedder, the FDIC is not to be held responsible for its non-occurrence. As evidence, we are given statements by Leo T. Crowley and K. A. Randall. Suggested alternative explanations are: pegged interest rates and higher reserve levels.

I have several questions for Vedder: Have you given sufficient attention to the background material on FDIC legislation? (How, for example, does Senator Glass's role in the legislation relate to his oft-cited views on banking reform?) Have FDIC examinations for state nonmember banks resulted in different standards? If the intent of the legislation was to curtail bank failures, can we assign critical importance to any one of the FDIC's functions that tend to accomplish this goal? Answers to these questions are available. A reading of Golembe's Political Science Quarterly (1960) article, provides one with an excellent discussion of the origins of the legislation. Bank examinations are carried out on some agreement between state bank regulatory agencies and the FDIC. Whether the content of these examinations has changed radically, I cannot say; nor does Vedder. Answers to these questions and their extensions can only come from a more complete analysis of the actual FDIC operations and their impact in some list of cases. I do not find that analysis here. Nor do I find material which supplements the extensive discussion of Friedman and Schwartz.