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Illinois Free Banks, 1851-1865

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Free banking had been consigned to oblivion until Friedrich Hayek proposed the concept of "denationalized currency." Study of free banks, therefore, helps to render a full understanding of American financial history. This essay, by melding economic issues with overall historical trends, seeks to investigate free banks' historical background and their influence on Illinois. Employing tools from economics and history, this paper analyzes the accounting statements of Illinois free banks and examines related indices such as discounts on banks notes, prices of exchanges, and banks' life span to assess their performance. The development of free banking, furthermore, was intertwined with the confrontation between the Whig-Republican and Democratic parties, economic changes in the nineteenth century, and the rise of corporations, as well as the transportation revolution. On the whole, investigating Illinois free banks helps to assess the performance of the free banking system, allowing us to get a glimpse of nineteenth-century Illinois history from the perspective of its free banking experience.

With the destruction of the Second Federal Bank, eighteen states established their own state banks, which were called free banks. These states included seven states in the West, five states in the South, and six states in the Northeast; that is, free banks spread through each region of the United States (see Table 1). Though this banking system had been introduced by eighteen states out of thirty-three, free banking thrived in only ten states, and, after operating for approximately twenty years, free banks finally ceased operation with the advent of the National Banking System. However, debates around the free banking system have lingered. Because it did not have a central bank, many people questioned whether a free banking system was secure and safe.

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Table 1
States With and Without Free Banking Laws By 1860

States with	Regions	Year laws passed	States without
Michigan	Midwest	1837 [a]	Arkansas
Georgia	South	1838 [b]	California
New York	Northeast	1838	Delaware
Alabama	South	1849 [b]	Kentucky
New Jersey	Northeast	1850	Maine
Illinois	Midwest	1851	Maryland
Massachusetts	Northeast	1851 [b]	Mississippi
Ohio	Midwest	1851 [c]	Missouri
Vermont	Northeast	1851 [b]	New Hampshire
Connecticut	Northeast	1852	North Carolina
Indiana	Midwest	1852	Oregon
Tennessee	South	1852 [b]	Rhode Island
Wisconsin	Midwest	1852	South Carolina
Florida	South	1853 [b]	Texas
Louisiana	South	1853	Virginia
Iowa	Midwest	1858 [b]	
Minnesota	Midwest	1858	
Pennsylvania	Northeast	1860 [b]	

Source: Arthur J. Rolnick and Warren E. Weber, "New Evidence on the Free Banking Era," *American Economic Review* 73 (Dec. 1983): 1082.
[a] Michigan prohibited free banking after 1839 and then passed a new free banking law in 1857.
[b] According to Hugh Rockoff, very little free banking was done under the laws in these states.
[c] In 1845, Ohio passed a law that provided for the establishment of "Independent Banks" with a bond-secured note issue.

Economists usually point to wildcat banks to assess the stability of the free banking system. The name "wildcat" perhaps originated from the picture of wildcats engraved on the bills of a Michigan bank that was regarded as irresponsible and unsound.[1] Or it was applied to banks located in inaccessible places where only wildcats roamed.[2] During the free banking period, wildcat was used more generally to describe banks that ran their business recklessly. Hugh Rockoff gave a systematic definition, which has been used by many scholars researching free banking. It

[1] George Washington Smith, *A History of Southern Illinois: A Narrative Account of Its Historical Progress, Its People, and Its Principal Interests*, (Chicago, Ill., 1912), 415; viewed 8 Oct. 2008. URL: http://www.archive.org/details/historyofsouther03smit.

[2] Gerald P. Dwyer Jr., "Wildcat Banking, Banking Panics, and Free Banking in the United States," Federal Reserve Bank of Atlanta *Economic Review* 81 (Dec. 1996): 1–20; viewed 11 Oct. 2008. URL: http://www.frbatlanta.org/filelegacydocs/ACFCE.pdf.

consists of three parts: first, wildcats tended to locate themselves in remote areas, with the purpose of discouraging redemption in specie; second, these banks were apt to issue far more bank notes than they could redeem, a strategy that would make them great speculative profit; third, they were likely to bring huge losses to note holders, disrupt commerce, and hinder the economic development of their communities.[3] Thus, if wildcats existed in a large number, the free banking system would by no means be secure and sound.

In Illinois, the free banking period started in 1851. Wildcat banks became so rampant that "no man is safe sleeping over night with one dollar of Illinois currency in his pocket. . . . There is great danger of a mob in our city. The day laborers will never be content to work for 'wildcat' which is not worth thirty-three and one-third cents on the dollar. . . ."[4] Some scholars agree with this observation. In *Banks and Politics in America*, Bray Hammond depicts the Illinois free banking experience as a failure: "In 1851 a free banking law fashioned after New York's was submitted to popular vote and approved. Illinois then had an experience with wild cat banks that was similar to Michigan's."[5] Hence, according to some historians of the period, the performance of Illinois free banks was not satisfactory.

However, most contemporary researchers assume that Illinois free banks operated successfully. They believe that political factors rather than problems with the banks resulted in the collapse of this system. For example, Andrew J. Economopoulos examined three aspects of Illinois free banks in his article: their life span, location, and whether they entered the banking industry for an opportunity for profitable speculation. He concluded that only one bank had all the three characteristics of wildcat banks defined by Rockoff; that is, Illinois free banks were quite sound. Bank failures at the end of the free banking period, he argued, should be attributed to falling prices of Southern state bonds, a decline that was an immediate result of the Civil War.[6] Gerald P. Dwyer, Jr., has the same opinion. He argues that no evidence indicates that Illinois free banks conducted fraudulent business causing great losses to note holders. Their exit from the banking industry should not be ascribed to dissatisfaction

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[3] Hugh Rockoff, "American Free Banking before the Civil War: A Re-Examination," *Journal of Economic History* 32 (March 1972): 417-20, at 417; "The Free Banking Era: A Reexamination," *Journal of Money, Credit and Banking* 6 (May 1974): 141-67, at 141.

[4] This is the description taken from the Chicago newspaper *The Democrat*. See Andrew J. Economopoulos, "Illinois Free Banking Experience," *Journal of Money, Credit and Banking* 20 (May 1988): 249-64, at 251.

[5] Bray Hammond, *Banks and Politics in America from the Revolution to the Civil War* (Princeton, N.J., 1957), 618.

[6] Economopoulos, "Illinois Free Banking Experience," 249-64.

voiced by citizens there but to the heavy tax imposed by the federal government in 1865.[7]

Nevertheless, if free banks were as secure as contemporary researchers insist, why did people living during that period accuse them of fraud and speculation? Conversely, if most free banks in Illinois conducted wildcat business, why do they appear to be sound when scholars resort to statistical analysis? This essay seeks to answer these questions by examining the performance of Illinois free banking. It concludes that the great failures of free banks in 1861 were not simply induced by factors outside the banking system; wildcat banks played a crucial role in those events. The national crisis of 1857 served as a starting point for wildcat banks.

In the first section, I will investigate Illinois free banking law and the several amendments that set basic rules for the operation of free banks. The second section will separately describe the performance of free banks during the periods 1851-1858 and 1859-1861. In the third section, I will explore the factors contributing to the failure of free banks in Illinois in 1861.

The Beginning of the Free Banking System

Illinois had established several state banks since 1819, but the experience proved to be a total disaster. Consequently, banks of issue were prohibited after 1842, and Illinois did not have its own incorporated banks until the first free banking law was passed in 1851. Thomas Ford, mayor of Illinois, proposed that Illinois was a place where there were no cities, no trade, no manufacture, and no punctuality in the payment of debts; early banks were doomed to failure.[8] However, conditions were dramatically different at the end of the 1840s. The year 1848 marked a new epoch in Illinois history, a time when

> agriculture was revolutionized in many of its aspects; urban life discarded more and more of the traces of the frontier; the prairies were filled up by a progressive population which flowed in from every corner of the new and the old world; industry developed into new and untried fields; and the state came to take a front rank among Mississippi valley commonwealths.[9]

Chicago was prosperous, leading the commercial development of the whole West. Three great avenues—the Great Lakes, the Illinois and Michigan canal, and the Galena and Chicago Railroad—facilitated its

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[7] Dwyer, “Wildcat Banking, Banking Panics, and Free Banking in the United States.”

[8] Thomas Ford, *History of Illinois* (Chicago, 1854), 173; viewed 13 Sept. 2008. URL: http://lincoln.lib.niu.edu/file.php?file=ford.html.

[9] Arthur Charles Cole, *The Era of the Civil War, 1848-1870*, vol. 3 of *Centennial History of Illinois*, 5 vols. (Chicago, 1922), 1; viewed 27 Sept. 2008. URL: http://www.archive.org/details/centennialhisto03illi.

external trade with other states and countries; Chicago, in place of St. Louis, gradually became the great marketplace of the West. The internal commerce of Chicago was also booming, thus developing commercial specialization. It was observed that at that time the city's commerce was "conducted through the agency of six exchange dealers and bankers, thirty-two forwarding and commission merchants and produce dealers, and fourteen wholesale groceries, fifty-five lumber dealers, besides a large number of wholesale and retail dealers in dry goods, groceries, hardware, greensware, boots and shoes, harness and leather, drugs, books, etc. etc."[10]

As Alfred Chandler noted, "Specialization in finance was a natural concomitant of specialization in other commercial activities."[11] Thus, commercial progress demanded a professional financial system, a developed banking system in particular. However, Illinois had been afflicted by incompetent banking facilities. Without banks of issue for nearly ten years, foreign currencies such as Ohio "red banks," Indiana "shinplasters," and all sorts of "rag" money from outside flooded in and dominated its money market. It was estimated that in 1850, St. Louis had a bank circulation of nearly half a million dollars in Illinois, most of which was of "unquestionable legality but doubtful soundness."[12] Diversity of currencies produced confusion in transactions on the one hand; on the other hand, it increased the cost of capital. The legal rate of interest was advanced to 10 percent in 1849, but little money could be had even at that price. Money handlers usually violated the law and charged 15, 20, and even 25 percent. Therefore, the people of Illinois had to pay annually in the form of interest not less than $600,000 to foreign financial institutions.[13]

The state's economic development was controlled by other states; the economic profit that should have gone to Illinois banks went to out-of-state institutions, all of which a thriving Illinois could abide no longer. In the constitutional convention of 1847, the banking issue became one focus

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[10] "Annual Review of the Trade and Commerce of Chicago for the year 1850: Imports by Lake. Exports by Lake. Receipts by Canal. Shipments by Canal. Received by Railroad. Forwarded by Railroad. Shipments by Lake. Receipts by Canal. Receipts by Railroad. Imports. Receipts. Shipments by Canal. Lumber Trade Along Canal, Lockport. Joliet Morris. Ottawa. All Other Places Coastwise Exports. Exports to Oswego. Exports to Ogdensburgh. Exports to Canada," *Chicago Daily Tribune*, 28 Dec. 1850. (The *Chicago Daily Tribune* [1847-1858], the *Chicago Press and Tribune* [1858-1860], and the *Chicago Tribune* [1860-1872] were read online from the Proquest "Historical Chicago Tribune" database.)

[11] Alfred D. Chandler, Jr., *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, Mass., 1977), 28.

[12] Theodore Calvin Pease, *The Frontier State, 1818-1848*, vol. 2 of *Centennial History of Illinois*, 94; viewed 27 Sept. 2008. URL: http://www.archive.org/details/centennialhisto03illi.

[13] Ibid., 92.

of the delegates' attention. According to their party principles, Whigs were considered to be the spokesmen of banks, and Democrats insisted on an anti-bank provision. In the convention, ninety-one Democrats were elected to seventy-one Whigs, and Democrats were dominant in political affairs.[14] As a result, the new constitution still prohibited the establishment of banks of issue, but it left a chance for those in favor of banks: it proposed that no act authorizing corporations or associations with banking powers should go into effect unless it was "submitted to the people at the general election next succeeding the passage of the same and be approved by a majority of all the votes cast at such election for and against such law."[15]

Business leaders refused to let go of this opportunity. In 1848, a convention was held in Chicago, where representatives of the leading commercial and financial interests of the state drafted a memorial to the legislature and the governor, urging them to abandon their attitude of hostility toward banks and to provide the state with a system of banking to supply some type of convenient and convertible circulating medium. Their appeal was successful, and a general banking law with the purpose of establishing a free banking system was passed in the legislature of that year, to be submitted to the people at a general election.[16] The next general election would have taken place in 1852, but the legislature deprived all the county treasurers of their offices and provided that their successors should be elected in 1851. This change in the law made it possible to submit the measure of free banking a year earlier, a situation that shows how economic motives drove merchants and politicians to prompt the birth of their own banking system.[17]

The proposition was voted upon by the people at the November 1851 election. The general banking law received 37,626 votes in favor and 31,321 against; thus the law was passed by a margin of 6,305.[18] Table 2 presents the vote by counties, which suggests the underlying cause of the opposition to the general banking law.[19] It shows that people in northern

[14] Janet Cornelius, *A History of Constitution Making in Illinois* (Urbana, Ill., 1969), 20; viewed 7 Oct. 2008. URL: http://www.archive.org/details/historyofconstit00corn.

[15] George William Dowrie, *The Development of Banking in Illinois, 1817-1863* (Urbana, Ill., 1913), 134; viewed 26 Sept. 2008. URL: http://www.archive.org/details/developmentofban00dowrrich.

[16] Ibid., 135.

[17] Ibid., 138.

[18] "For Banks—Against Banks in 1857: Southern Counties. Northern Counties. Central Counties . . . ," *Chicago Daily Tribune*, 9 June 1857"

[19] These data are taken from the *Chicago Daily Tribune* of 1857. A long time has passed, and data on the issue are not easy to identify and interpret. These numbers may not be exact and in agreement with those from other sources. But they are not far off and discrepancies would not affect the argument that they reflect the opinions of voters in different regions.

Illinois favored accepting the new banking law: 80 percent of voters were for it; in the central part, 69 percent of voters favored free banks; in southern Illinois, however, only 16 percent favored the free banking law.

Table 2
Votes by Counties

Counties	For	Against
Northern	10,034	2,587
Central	10,937	4,927
Southern	966	4,926

Source: "For Banks—Against Banks in 1857: Southern Counties. Northern Counties. Central Counties . . . ," *Chicago Daily Tribune*, 9 June 1857.

Economic interests may be one reason for this situation: northern Illinois was thriving on well-developed commerce, while agriculture occupied a leading position in southern Illinois. The major customers of banks were business people, and farmers need less currency. There were only two exceptions in the northern counties: Jo Daviess and St. Clair. People of the former voted 294 for banks, and 990 against; people of the latter 226 for, and 1,779 against.[20] The reasons were that miners, the majority of the residents of Jo Daviess, were hostile to bank notes, for their products were always in demand for gold and silver; and the Germans in St. Clair had been accustomed to a metallic currency in their home country, and they could obtain specie from St. Louis and German immigrants. Therefore, they hardly felt the urgency to form native banks.[21]

In 1851, the first free banking law, *An Act to Establish a General System of Banking*, was passed. It included forty-one sections concerning all the conditions for establishing a free bank, rights as well as obligations of those banks, penalties, and measures to supervise them. People were allowed to associate to open a bank as long as a minimum of $50,000 could be collected as capital. In addition, applicants had to deposit with the state auditor some state stocks as security. Bankers had no right to print bank notes by themselves. They would receive a certain number of notes according to the average market value of deposited stocks in the New York market within the preceding six months. The value of Illinois stocks would be estimated at 20 percent less than their market value.[22] When securities decreased in value or became insufficient for redemption of their notes, banks were required to replenish their stocks or surrender an equal

[20] "For Banks—Against Banks in 1857."

[21] "Banking System in Illinois—Who Opposed It," *Chicago Daily Tribune*, 6 June 1857.

[22] "The Free Banking System," *The Bankers* (Dec. 1854), 449.

amount of bank notes.[23] Banks had to pay on demand in specie as note holders presented their notes at the counter, so they had to keep a certain amount of specie on hand. If they failed to do so, note holders could protest the said notes one by one and their stocks would be sold in New York by the auditor; the proceeds would be used to pay note holders after the grace period.[24] In order to supervise free banks effectively, the law required banks to submit reports to the Auditor quarterly.[25] In addition, the rate of interest charged by banks could not exceed 7 percent per annum.[26]

The free banking law passed in 1851 had a shortcoming, however: note holders had to protest each note individually. This process was time-consuming, especially at a time when transportation was not fully developed, thus discouraging note holders from protesting the notes. Also, the law did not prescribe the amount of specie banks should have on hand for redemption. Nor did it set an upper limit to prevent banks from over-issuing. In spite of these deficiencies, the general banking law was effectively designed to protect note holders' interests. The credit of free banks was totally attached to prices of state stocks they deposited, and thus attached to the credit of states whose stocks they purchased. Bank notes printed and countersigned by state officials produced a unified currency, thus lowering the cost of collecting information about the quality of currencies and making transactions more convenient. All of these restrictions served to lower financing costs for businessmen and all others. Moreover, the law was strict, for the amount of notes issued by each bank could not be greater than the market value of their securities, a regulation that decreased risks created by wildcat bankers. Therefore, free banking supplied the Illinoisans with a convenient, cheap, and secure circulating medium; "as a system of legitimate banking the new law was without proper checks and requirements relating to location, capital and redemption, but as a system for furnishing a safe circulating medium, it was well guarded. . . ."[27]

In the succeeding ten years, there were four amendments to the General Banking Law of 1851. These acts gradually made up for some deficiencies existing in the original one. The first amendment passed in 1853; it aimed at prohibiting the circulation of unlawful money—foreign notes and issues of private businesses—that still haunted Illinois long after

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[23] Ibid., 457-58.

[24] Ibid., 453.

[25] Ibid., 458.

[26] Ibid., 459.

[27] John Jay Knox et al., eds., *A History of Banking in the United States* (New York, 1900), 723; viewed 26 Sept. 2008. URL: http://www.archive.org/details/historyofbanking00knoxrich.

the establishment of the free banking system.[28] In 1855, two issues concerning banks were discussed fiercely: one was the low interest rate charged by banks; the other was the definite premium amount of specie kept on hand.[29] However, the amendment of 1855 paid little attention to these debates. It merely designed the way banks in liquidation retired their notes, thus making only a slight change on the banking law of 1851.[30]

The New Banking Law of 1857, in contrast, implemented some substantial corrections. It required banks to be located at places with a population of at least five hundred people, which reduced the possibilities of wildcats undertaking speculative business.[31] As bankers usually paid note holders with depreciated coins, it also demanded banks to redeem notes presented to them with the "legal coin of the United States."[32] Compared with the law of 1851, which commanded banks to redeem notes in "lawful money," the new law narrowed the range of facilities bankers could employ to pay note holders.[33] Thus, we can say the new banking law protected note holders' economic interests more effectively. Moreover, when protesting bank notes, note holders no longer needed to present or receive redemption of each note separately.[34] That the amount would be treated as a whole removed one obstacle for note holders who wanted to redeem their notes. In addition, the legal value of all stocks, Illinois stocks included, was required to be assessed at a rate 10 percent less than the market value of such stocks.[35] The law also stipulated that the number of notes received by banks should be equal to 90 percent of the stocks' legal value, so in comparison with conditions under the law of 1851, bankers received less from the Auditor, leaving a slim chance that bankers would receive capital gains on notes issued; on the contrary, bankers would suffer severely when the prices of stocks dropped dramatically.[36] In addition, the

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[28] "Supplementary Bank Law of Illinois," *Bankers' Magazine and Statistical Register* 4 (Dec. 1854): 463.

[29] "Amendment of the General Banking Law," *Chicago Daily Tribune*, 4 Jan. 1856.

[30] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 144.

[31] "New Banking Law of Illinois," *Chicago Daily Tribune*, 24 Feb. 1857.

[32] "Amendments to the General Banking Law: Remarks of Hon. J. H. Danham, of Cook," *Chicago Daily Tribune, 27* Jan. 1857; "New Banking Law of Illinois."

[33] "The Free Banking System," 455.

[34] "New Banking Law of Illinois."

[35] Ibid.

[36] In his paper of 1988, Andrew J. Economopoulos wrote, "In the same month (1857), the legislature amended the law requiring the auditor to issue bank notes on all bonds equal to 90 percent of the bond's legal price (still the bond's six-month average) with a maximum amount of notes per bond limited to the bond's par value rather than market value. Although the law seemed to increase the margin of security on non-Illinois bonds, it also opened the door to wildcat banking opportunities" (see Economopoulos, "Illinois Free Banking Experience,"

rate of interest or discount was adjusted to 10 percent; the Auditor had to confirm that banks had "a bona fide cash capital of at least 50,000 dollars actually put in good faith for the purpose of remaining in such Bank or Association as capital" before issuing bank notes to them.[37] In these ways, the act of 1857 compensated for the weaknesses of prior acts.

Another amendment was passed in 1861, laying out stricter restrictions on opening a bank. First, only stocks of the state of Illinois could be deposited with the Auditor as security for circulating notes, and they were received at par value; second, the capital for forming a bank was limited to $10 million, and banks had to have a bona fide cash capital of at least $25,000. In addition, banks could not be located at places with fewer than 1,000 inhabitants.[38] This was the final free banking law of Illinois, one that made it more difficult for banks to enter the market.

Under free banking laws, more than 150 banks existed and conducted banking business in Illinois. However, at the beginning of the free banking system there was no hint of its flourishing; not a single application was filed with the Auditor for several months after the passage of the act. It is said that the Auditor was willing only to issue bank notes to the full value of stocks of the United States or of the states of New York, Ohio, Kentucky, and Virginia, none of which was quoted at less than 106 on the New York stock market. In addition, Illinois securities were received at 80 percent of their market value.[39] The stringency of the stock provisions discouraged the formation of banking associations so much that the newspaper the *Chicago Democrat*, an opponent of the system, boasted that the law would

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253-54). But comparing the two acts of 1851 and 1857, we find discrepancies with his view. The fourth Section of 1857 free banking law is as follows: "The Second Section of an Act entitled an 'Act to establish a general system of Banking,' approved February 15, 1851, is hereby amended, so as to provide that all the Stocks of the Stocks of the United States, and of the several States, on which interest is regularly paid, including the Stocks of this State deposited with the Treasurers, under the provisions of the last named Act, shall be valued at a rate ten percent less than the market price of such Stocks: Provided, that such Stocks shall, in no instance, be received at a rate above their par value." These provisions should be interpreted as follows: when the market value of stocks was lower than par value, the amount of notes received would not exceed 90% of their market value; it is when 90% of the market value of stocks was higher than their par value that the maximum amount of notes received by banks should be equal to their par value, which was the same as the prescription of 1851 free banking law. Moreover, comments supporting those of Economopoulos could not be found in other papers and monographs on Illinois free banking, so his remarks may be a misinterpretation; the new banking law did not open "the door to wildcat banking opportunities," but rather closed another window to them.

[37] "New Banking Law of Illinois."

[38] "The New Banking Law: Article One. Article Two. Article Three. Article Four. Article Five. Article Six . . . ," *Chicago Tribune*, 18 Feb. 1861.

[39] Knox et. al., eds., *A History of Banking in the United States*, 139.

soon become a dead letter.[40] However, there was one bank jumping the hurdles and establishing a foothold in the virgin land of free banking: the Merchants and Mechanics' Bank of Chicago, which was formed in December 24, 1851.[41] Following its steps, free banks sprung up in the ensuing years.

Table 3 shows the distribution of free banks in Illinois between two regions: northern Illinois and southern Illinois. Sangamon County, where Springfield is located, serves as the dividing line (this county was treated as a part of southern Illinois).

Table 3
Banks Opened in Different Regions

Year	1851	1852	1855	1857	1858	1859	1860	1861	1862	1863
North	1	25	7	3	7	0	13	0	1	2
South	0	7	3	21	3	2	53	2	0	1
Total	1	32	10	24	10	2	66	2	1	3

Source: Warren E. Weber, "Listing of all State Banks with Beginning and Ending Dates;" viewed 18 Nov. 2008. URL: http://www.minneapolisfed.org/research/economists/wewproj.cfm.

In the beginning, banks had a tendency to operate in northern Illinois. Out of thirty-two banks newly established in 1852, nine were located in Chicago and five in Springfield. Only after close to a decade did banks spread to southern Illinois; during the most active year (1860), 80 percent of newly formed banks were located in southern Illinois. This tendency reveals that at the start of the free banking era, the primary purpose of forming banks was to serve the economic development of Illinois, especially of Chicago.

The Performance of Illinois Free Banks, 1851-1861

In 1857, a national economic crisis occurred that considerably influenced the economic development of Illinois; the condition of free banking also greatly changed after 1857, so that year is used as the dividing line in examining the performance of Illinois free banks. To assess their performance, it is not enough to depend on historical records or simply analyze historical data; one must view them together to achieve this purpose.

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[40] Ibid., 139.

[41] "Bank Items," *The Bankers' Magazine and Statistical Register* 2 (July 1852): 81.

Historical records indicate that Illinois free banks performed well during the period 1851-1857. They encountered several crises, but every time they managed to sustain themselves and even grow.

The first challenge free banks had to face was being overwhelmed by foreign currencies. By 1853, such currencies still furnished the major part of Illinois circulation, threatening the infant free banking system. In 1853 Illinois passed the first amendment to the general banking law purporting to drive foreign money out of Illinois. The Board of Brokers of New York City, with similar organizations in St. Louis and Chicago, cooperated to enforce this act. As a result, the Wisconsin Marine and Fire Insurance Company and other institutions withdrew their notes from circulation; issues of Illinois free banks came to be used more generally and, for a brief time, established a good reputation both at home and on Wall Street, where the notes of nine free banks were accepted at a discount of 0.75 percent, helping foster people's confidence in Illinois banks as well as their notes.[42] Moreover, it proves that during the first two years, Illinois free banks were sound and secure; otherwise, they would not have gotten the help from other states, and their bank notes would not have been accepted on Wall Street at such a low rate.

During the summer of 1854, free banks met the first heavy blow, which was caused by "a panic of short duration but characterized as the worst since 1837."[43] The root of this crisis was the extensive railroad construction in the Midwest, which first drained the money market and then later the stock market. As a result, the price of Virginia and Missouri stocks, the major part of securities deposited by Illinois banks, fell to 95 and 93 cents on the dollar. A feeling of distrust seized note holders, and runs on Illinois banks occurred. Unprepared for this situation, many banks were compelled to suspend specie payments.[44] Six banks ceased operation, four of which were situated in Chicago, but the shutdown did not bring any losses to note holders, whose notes were fully redeemed by bank commissioners.[45]

Outside the state, distrust of the credit of Illinois banking institutions also prevailed. However, in some places such as St. Louis, where the notes of most Illinois banks were being used, bankers and brokers still supported Illinois currencies. They issued a circular to the public in

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[42] Information from *Thompson's Bank Note Reporter* and *Clark's Counterfeit Detector*. See Knox et. al., eds., *A History of Banking in the United States,* 142; "Indiana and Illinois Currency," *Bankers' Magazine and Statistical Register* 2 (March 1853): 739.

[43] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 144.

[44] Ibid.

[45] "Illinois Banks," *The Western Journal and Civilian; Devoted to Agriculture, Manufactures, . . . ,* 12 (Sept. 1854): 739; "Article1—No Title," *Bankers' Magazine and Statistical Register* 4 (Dec. 1854): 490; "The Broken Banks of Illinois," *Chicago Daily Tribune*, 4 April 1855, p. 2.

November 16, 1854, and said, "in the opinion of the subscribers, bankers and brokers of St. Louis, we regard this feeling as wholly unnecessary and unwarranted by the real condition of the great majority of these institutions" and at their counters, they would make no unusual discrimination against notes of Illinois banks with credit.[46]

The next shock to Illinois banks came in 1857. Another monetary panic swept the whole nation. The cessation of railroad-building madness was deemed one cause of this crisis, but the pivotal occurrence was the failure of the Ohio Life Insurance and Trust Company.[47] In Illinois, many banks had deposited stocks of this company with the Auditor, so they had to replenish additional securities after its failure.[48] Worse, the national crisis resulted in decreasing demand for Illinois products. As a result, commercial activities nearly stagnated there, thus casting negative effects on Illinois free banks. In 1857, approximately fourteen banks ceased operation, including four Chicago banks and three in Springfield.[49]

The 1857 crisis produced a general distrust of Illinois free banks. In September of that year, at their counters Detroit banks started to charge 5 percent on Illinois money and charged 3 percent on deposit in September.[50] As for St. Louis, in October, its banks refused a million and a half of Illinois currency circulating there.[51]

However, the heavy shadow overhead did not totally destroy the confidence of other states in Illinois free banks. Although Illinois currency was not bankable in St. Louis, the *St. Louis Republican* still commented that Illinois banks were in good condition and they stood upon a substantial basis. "They are better than any stock banks that were ever made. They have the credit of a state to back them."[52] Moreover, Wisconsin continued to receive all the currency of Illinois banks.[53]

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[46] "Illinois Banks," 739.

[47] Hammond, *Banks and Politics in America*, 709-10.

[48] Knox et. al., eds., *A History of Banking in the United States,* 725.

[49] "Banks of the United States: Location, Name, President, Cashier, and Capital of each. May, 1857. Maine. New-Hampshire. Vermont. Massachusetts. Boston, Mass. Rhode-Island. Providence, R.I. Connecticut. New-York. New-York City. New-Jersey. Pennsylvania. Philadelphia. Delaware. Maryland. Baltimore. District of Columbia. Virginia. North Carolina. South Carolina. Georgia. Alabama. Illinois. Free Banks. Indiana. Free banks. Bank State of Indianan. Kentucky. Louisiana, Michigan. Mississippi. Missouri. Ohio. Tennessee. Texas. Wisconsin. Nebraska," *The Bankers' Magazine* 6 (June 1857): 977.

[50] "Article 4—No Title," *Chicago Daily Tribune*, 7 Sept. 1857.

[51] "Financial: Illinois Currency at St. Louis. New York. Meeting of the Boston Merchants. Baltimore and the Virginian Banks. A Blue Day at St. Louis," *Chicago Daily Tribune*, 7 Oct. 1857.

[52] Ibid.

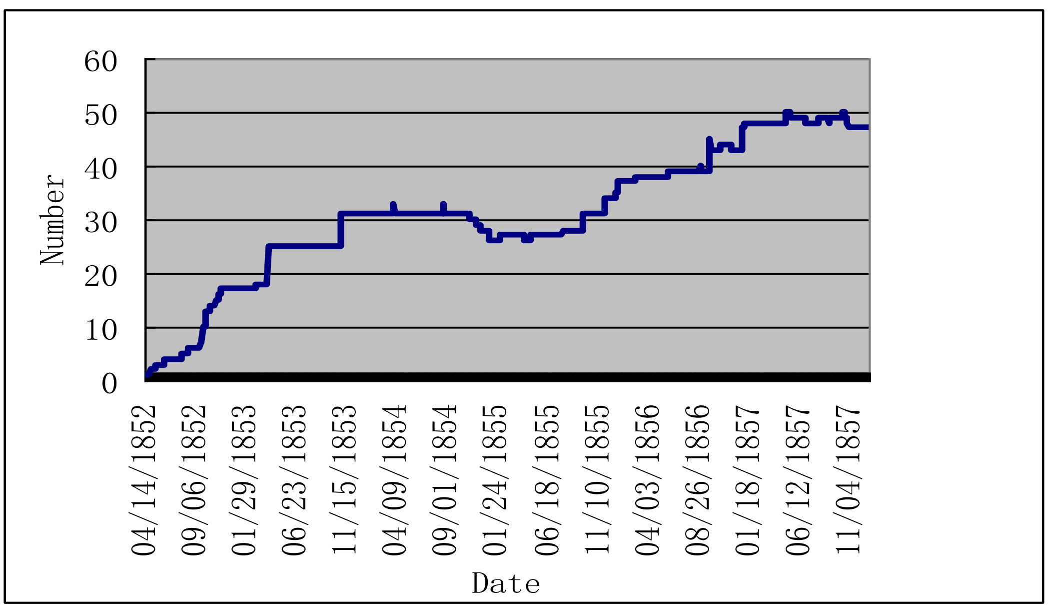
[53] "Front Page 33—No Title," *Chicago Daily Tribune*, 2 Oct. 1857.

Simultaneously, reports about wildcat banks emerged in Illinois. The *Chicago Daily Tribune* claimed that a few wildcat banks existed in Illinois. Those banks had no fixed places of business, did not pretend to redeem their notes, and paid no heed to the Commissioners' demand to replenish their securities. Nevertheless, the newspaper admitted that wildcats were still few in number.[54]

On the whole, the historical descriptions indicate that the performance of Illinois free banks was satisfactory during this period. Although they encountered economic crises and thus aroused criticism, their bank notes continued to be accepted by other states and to maintain a good reputation. Data may be able to depict the performance of Illinois free banks more objectively. This part of the essay analyzes the data that can be used to reveal whether Illinois free banks were stable and whether they had provided Illinois with a secure circulation.

During 1851-1857, approximately seventy free banks entered the banking industry. Figure 1 displays the total number of banks in operation on selected days during this period. There are ups and downs on the curve, but no sharp rises or drops, except in the beginning years; therefore, the operation of free banks could be described as stable.

Figure 1
Numbers of Banks, 1851-1857



Source: Weber, "Listing of all State Banks with Beginning and Ending Dates."

[54] "Illinois Banking—Necessity for Decided Action," *Chicago Daily Tribune*, 29 Dec. 1857.

In addition to their stability, the security of free banks and of the bank notes they issued is also an important indicator in assessing their performance. I next examine this aspect in terms of locations, life span, and possible losses that free banks caused to note holders.

The location of free banks

Information about sixty-eight banks formed during the 1851-1857 period was available. Table 4 is drawn from it.

Table 4
Banks and Population

Population[a] / Year (Entry)	0-200[b]	200-500	500-1,000	1,000-10,000	Over 10,000	Total
1851	0	0	0	0	1	1
1852	2	0	3	18	9	32
1855	0	0	0	9	1	10
1857	6	6	2	11	1	26
Total	8	6	5	38	12	69

Source: Banks: Weber, "Listing of all State Banks with Beginning and Ending Dates"; Population of 1850 and 1860: U.S. Census Bureau; viewed 17 Oct. 2008. URL: http://www2.census.gov/prod2/decennial/documents/1850a-25.pdf; http://www2.census.gov/prod2/decennialdocuments/1860a-01.pdf.

[a] For banks opening before the year of 1855, data are taken from the Census of the United States in 1850, while for those that began their business in and after 1855, the Census of 1860 was the data source.

[b] The population of some places is unavailable in both censuses. The assumption is that the population in these places was too small to list, so they are included in the range 1-200.

The amendments of 1857 and 1861 restricted banks in places with a population less than 500 and 1,000, respectively, so those two numbers should be reasonable indices to show whether banks were established in inaccessible locations. In addition, Economopoulos' paper defines locations with a population of two hundred or less as "remote places." Thus, this number also serves as an index to examine whether banks were located in remote places. Table 4 reveals that during 1851-1857, out of the sixty-eight free banks, 28 percent were located in places containing fewer than a thousand inhabitants and 20 percent in locations with a population less than five hundred. Of the fourteen banks located in places with a population not exceeding five hundred, only two were formed in 1852: the Bank of Peru and the Illinois River Bank of Taylor and Coffing. Both of them were situated in the city Peru, whose population is unavailable in the

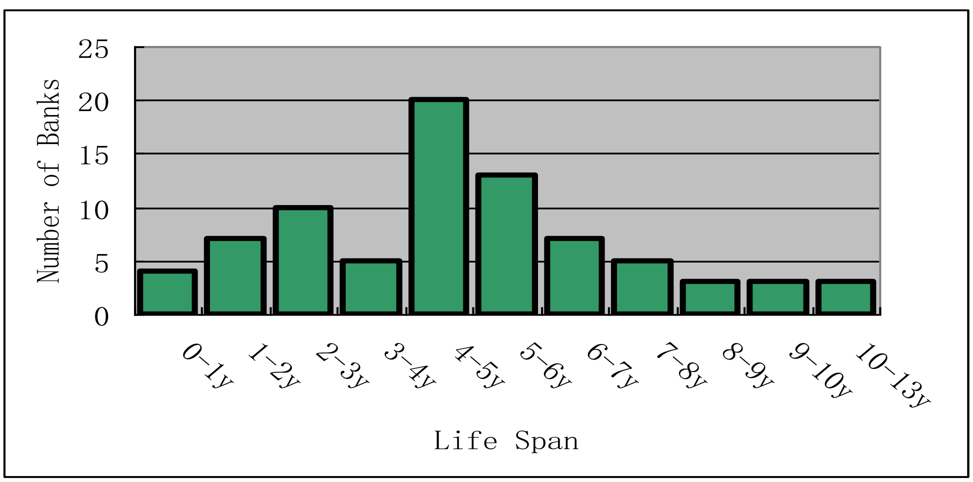
1850 census, but the number of inhabitants in this place in 1860 was 3,139. In contrast, all of the remaining twelve banks were formed in 1857.

Hence, before 1857, banks had never conducted business in isolated places, a strategy that would have indicated they were for speculative profit. In contrast, the performance of banks formed in 1857 was not that satisfactory: more banks were located in remote places, and thus they were easy to be treated as wildcat banks. However, there may be another explanation; that is, the crisis of 1857 drained specie from Illinois owing to a lack of commerce; as a result, banks tended to hide themselves in remote places to avoid redemption in specie. Their original purpose, thus, may not have been speculative.

The life span of free banks

Life span is also an index to indicate the stability of free banking. Usually speculative banks existed for less than a year, because in the first year they could enjoy the privilege of tax exemption.[55] A short life span, in turn, would increase the instability of the free banking system and thus the risks of note holders. Figure 2 shows the life span of Illinois free banks formed before 1858.

Figure 2
Life Span of Free Banks, 1851-1857



Source: Weber, "Listing of all State Banks with Beginning and Ending Dates."

A problem with banks' life span arises: some banks ceased operation and then restarted some time later. They had the same name and the same location, but it is unclear whether they were the same banks. Probably some went into liquidation for a certain period in order to replenish securities with the State Auditor but in fact had never wound up business.

[55] "Stock Quote 4—No Title," *Chicago Press and Tribune*, 6 Jan. 1859.

Hence, this essay can only approximately estimate banks' life span. For example, the Marine Bank of Chicago opened in 1852 and disappeared from the banking list in 1862; however, in 1863 it was on the list again. The exact time when it closed is unknown. In this essay 1865 is deemed as the last year free banks existed, for the federal government imposed heavy taxes on them, and most surviving free banks were driven out of the banking industry in that year. Therefore, its life span is estimated as 10-11.

Figure 2 clearly shows most Illinois free banks operated for four to six years. Nine of them existed for more than eight years. Four banks existed for less than one year and another seven were in operation less than two years, but only one of them, the Bank of Hutsonville, lay in a remote place.

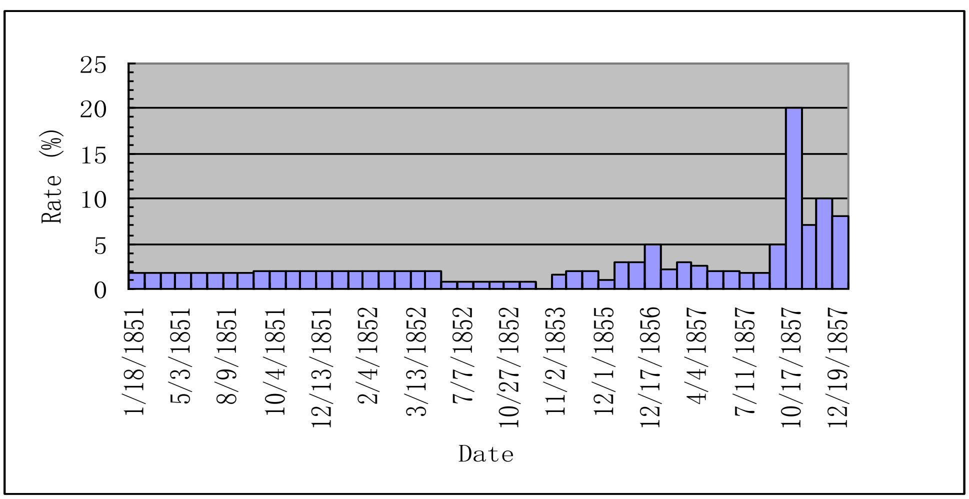
Losses caused to note holders

The most important factor to determine whether banks were secure or not was the losses they had brought to note holders. Discounts and exchange rate are two indices to measure the losses people had to bear when bank notes were in circulation. However, after banks wound up, if they could not redeem their notes as usual, that would cause losses to note holders as well.

Discounts mostly reflect redemption costs and the risk premium; that is, if banks were in inaccessible places or in bad condition, discounts on their notes would increase. In such cases, as long as bank notes were in circulation, they were depreciating.

Figure 3 presents the discount rates on Illinois bank notes in New York from 1851 to 1857. Discounts were higher in the first year, but this fails to imply that Illinois free banks were unsecure. Just as Gary Gorton argues,

Figure 3
Modal Discounts on Illinois Free Banks in New York, 1851-1857

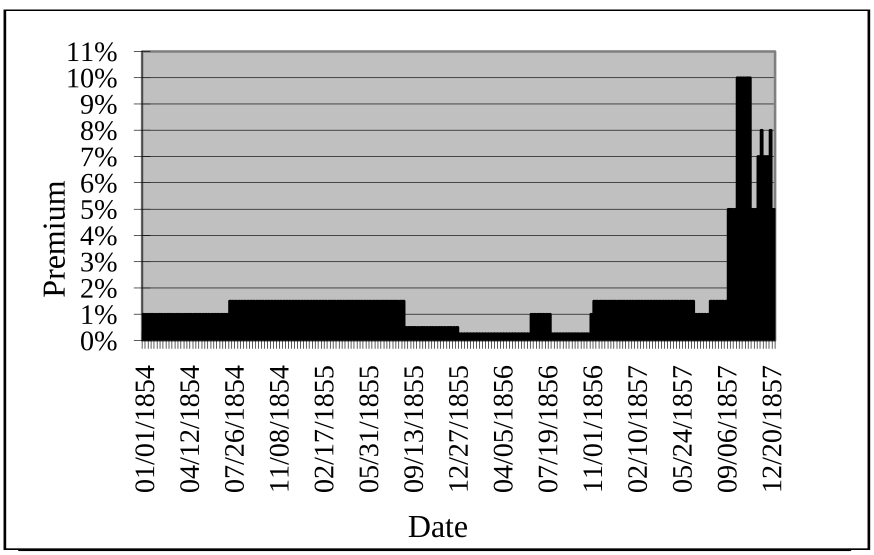


Source: Warren E. Weber, "Quoted Discounts on State Bank Notes in New York, Cincinnati, and Cleveland, selected dates, 1827-1858"; viewed 18 Nov. 2008. URL: http://minneapolisfed.org/research/economists/wewproj.html.

in the beginning "By redeeming the notes of new banks with high discounts and observing whether these banks can honor their obligations, note holders learn whether new banks are riskier than other banks at thatlocation."[56] Thus, the high discount rates just mean that the reputation of Illinois free banks failed to form in the note market in the first year. That discount rates later decreased to less than one percent displays a risk premium of close to zero, indicating that the reputation of Illinois free banks had been formed, and note holders had more confidence in their issues. When the national crises of 1854 and 1857 struck Illinois, discounts increased again, indicating that distrust of Illinois free banks rose among the note holders. Therefore, the related data agree with the historical records.

Prices of foreign notes against Illinois bank notes is another important index to estimate potential losses brought to note holders in Illinois, where economic development mainly hinged on agricultural trade. If the premium on foreign notes was too high during the busy months of commerce, merchants, farmers, and all other participants would bear a heavy loss. In Chicago, prices of New York notes were published every week, as is reflected in Figure 4.

Figure 4
Prices of New York Exchange, 1854-1857



Source: "Stock Quote 42—No Title," *Chicago Tribune*, 1 Jan. 1861.

The information offered here is in accord with the conclusion above; that is, the performance of free banks was commendable before the crisis

[56] Gary Gorton, "Reputation Formation in Early Bank Note Markets," *Journal of Political Economy* 104 (April 1996): 346-97, at 350.

of 1857. In the summer of 1854, a national panic took place, and the premium increased by 0.5 percent, but it soon fell back. Agricultural products hit the market in fall and winter; during this period Illinois money was in great need, and thus prices of foreign notes against it dropped, causing the low premium of New York notes after August 30, 1855, and that of the period from August 2 to October 25, 1856. However, the value of Illinois bank notes decreased rapidly and severely in 1857, and more fluctuations occurred as well. Fortunately, most commercial transactions fell into stagnation, so losses for farmers and merchants were not enormously high.

Redeeming their issues in specie was the major task of Illinois free banks, even when they were in liquidation. When banks failed, the Auditor was entitled to auction stocks they deposited as security in New York. Proceeds from selling those stocks would reimburse note holders of such banks.

Out of the three failed banks with remote locations and a short life span, only the People's Bank at Carmi has information still available. The bank started to redeem its bank notes in January 1858, and the loss on the notes was trifling, because the bank had $127,500 worth of bonds to redeem notes worth $110,300. Its securities paid 94 percent on the dollar.[57] Though detailed information about the other banks is lacking, it is certain that they brought no great losses to people, because most failed banks were able to reimburse their note holders dollar for dollar during this period.[58] More than that, note holders of the Rushville Bank were fortunate enough to have all their notes on hand exchanged at par for gold.[59] There was only one case in which note holders bore economic losses owing to their bank notes: the Stock Security Bank of Danville went into liquidation in 1857, but its securities depreciated so rapidly that the note holders received only 88 cents on the dollar. This was the first instance where proceeds from the sale of stocks failed to fully reimburse the note holders.[60]

On the whole, from the information collected above, it is safe to conclude that free banks in Illinois were stable and sound before 1857. The majority of them had no characteristics of wildcat banks at all. Moreover, their currency brought little loss to note holders, either in circulation or in redemption. Although the national crisis of 1857 cast negative effects on their operation, the performance of free banks was generally satisfactory.

In January 1859, bank commissioners submitted a bank report, in which they expressed their satisfaction with the performance of Illinois free banks. They assumed that a system "which had withstood the test of two successive years of financial depression should receive the stamp of

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[57] "ILLINOIS MATTERS," *Chicago Daily Tribune*, 5 Jan. 1858.

[58] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 145, 150.

[59] "ILLINOIS MATTERS."

[60] Dowrie, *The Development of Banking in Illinois, 1817-1863,* 150.

approval from the public."[61] They did believe that the crisis of 1857 helped Illinois win a larger share of public confidence than any events during the previous period. Governor William H. Bissell held the same opinion as the bank commissioners. Not only did he claim that free banks in the past years were successful, but he also proposed that they needed no amendment to the free banking law in the future. Apparently this view was shared by most people. That is why 1859 became the only year in Illinois history that the free banking law was not amended.[62]

But during the next four years, people lost faith in Illinois free banks. The feeling of distrust that prevailed in 1857 transformed into aversion, within and without. In January 1859, the *Detroit Tribune* claimed that Illinois money had a downward tendency, and forwarders in that city advertised that they would no longer receive it in payment for produce or freight. At the same time, the board of directors of the State Bank of Indiana also decided to throw out Illinois notes by an almost unanimous vote. Their excuse was that many Illinois banks were located in "inaccessible points and the cost of procuring redemption or exchanges were greater than the holders of the currency are willing to submit to."[63]

However, this was only a start. In August of that year, the *Milwaukee Sentinel* of Wisconsin reported that the reputation of Illinois currency deteriorated in the East because banks in Illinois placed many obstacles in the way of redeeming their bank notes.[64] At the end of 1859, the *Cincinnati Gazette* criticized Illinois banks with many harsh words. It said that Illinois was "cursed with an inferior currency." Irresponsible bankers and financial sharpers were "growing rich at the expense of the industrial classes." They opened banks with two or three thousand dollars, purchased securities, issued notes, and paid their customers an inferior currency instead of gold as they promised. Their issues were called money, but the value of their bank notes fell short by 1.5 percent of that of gold. Thus, the note holders were taxed to sustain the bank; Illinoisans lost half a million per year owing to their banks.[65]

Rejection of Illinois notes persisted in 1860. The *Janesville Gazette* of Wisconsin implied that all the banks of Janesville would not receive Illinois money on deposit and would buy them at a discount rate from 1.5 percent to 1 percent in January 1860. It also signified that Illinois money had not been received in Milwaukee and Madison for several months because they were inconvertible.[66]

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[61] Ibid., 154.

[62] Ibid.

[63] "Bank Items," *The Bankers' Magazine and Statistical Register* 8 (June 1859): 994.

[64] "Financial and Commercial: Monetary," *Chicago Press and Tribune*, 8 Aug. 1859.

[65] "Illinois Banking," *Chicago Press and Tribune*, 16 Nov. 1859.

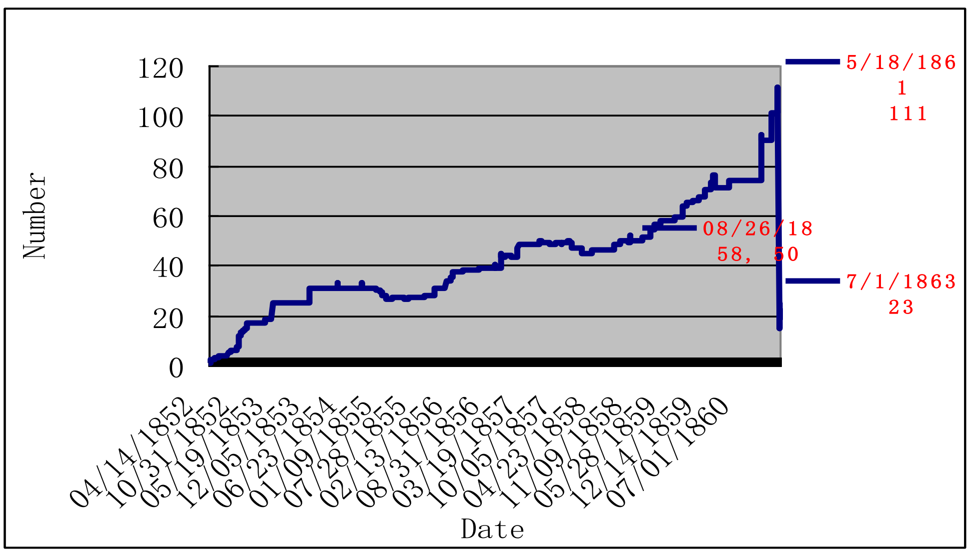
[66] "Stock Quote 6—No Title," *Chicago Press and Tribune*, 28 Jan. 1860.

Illinoisans lost trust in Illinois free banks as well. On December 7, 1860, business leaders in Chicago convened in Bryan Hall to discuss their "vicious currency system." They criticized the performance of Illinois free banks and assumed all sister states had a currency better than theirs.[67] Complaints about banks were also voiced by the *Chicago Tribune*. In 1861, the *Chicago Tribune* observed that the abundant crops were of good quality, commercial activities were active, and the economic condition better off; the only hindrance to prosperity was their "villainous currency," so the newspaper appealed to remove that obstacle.[68]

The descriptions during this period reveal that the performance of Illinois free banks deteriorated after 1857. They were not as sound and secure as before. As a result, the banks were unable to facilitate and stimulate commercial development; on the contrary, they and their bank notes appeared to be an obstacle to it.

Figure 5 presents the number of banks at specific dates during 1851-1863. Although the economy of Illinois was bogged in depression after the crisis of 1857, the free banking industry seemed to be much more prosperous than before 1857. During the four years from 1858 to 1861,

Figure 5
The Number of Illinois Free Banks, 1851-1863



Source: See Appendix to this essay.

approximately 81 banks were newly formed. At the peak of the craze for establishing banks, 111 banks had simultaneously been in operation, twice of the total number of banks formed in the previous six years. Banks

[67] "THE CURRENCY MEETING: The Solid Men of Chicago in Council. RESOLUTIONS, SPEECHES, ETC." *Chicago Tribune,* 8 Dec. 1860.

[68] "MONETARY :PREMIUM AND UNCURRENT FUNDS," *Chicago Tribune*, 25 Jan. 1861.

rushed into the banking industry within three years and then retreated in one and a half years, indicating the instability of the free banking system from 1858 to 1861.

The following section again employs the three indices—Illinois free banks' location, life span, and losses they caused to note holders—to examine the stability and security of the banking industry.

The location of free banks

According to Table 5, 60 percent of the eighty-one banks were situated in places with a population less than one thousand. Although the free banking law of 1857 set the bottom line of the number of inhabitants in free banks' locations as five hundred, 40 percent of banks still chose remote locations with a population less than five hundred; 25 percent of them even opened at points where the number of inhabitants was less than two hundred. By contrast, from 1851 to 1857, only 28 percent of the free

Table 5
Banks and Population

Population / Year (Entry)	0-200*	200-500	500-1,000	1,000-10,000	Over 10,000	Total
1858	4	1	2	2	1	10
1859	0	2	0	0	0	2
1860	15	8	14	28	1	66
1861	1	1	0	0	0	2
Total	20	12	16	30	2	80

Source: Weber, "Listing of all State Banks with Beginning and Ending Dates"; Population of 1860: U.S. Census Bureau; viewed 19 Oct. 2008. URL: http://www2.census.gov/prod2/decennial/documents/1860a-01.pdf.

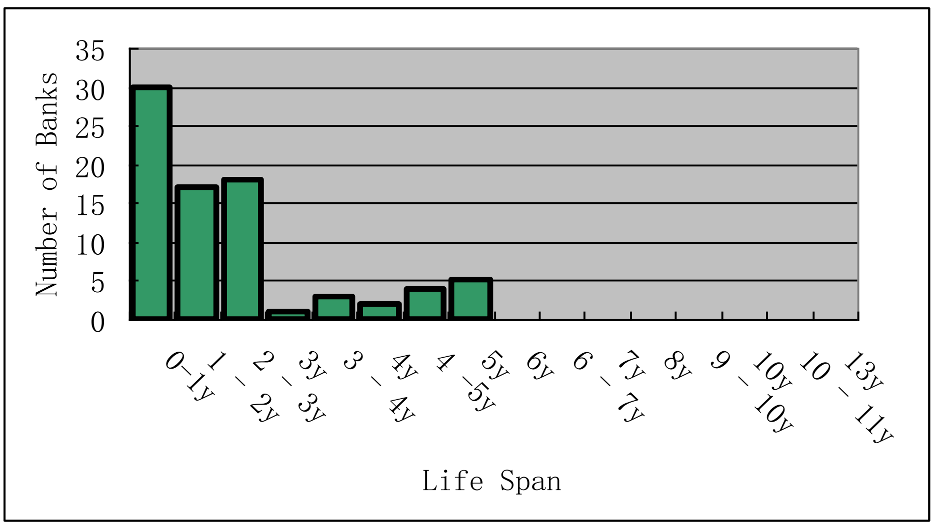
*The population of some places is unavailable in both censuses, so it is assumed that the population in such places was too small to list, and thus they are included in the range 1-200 in this paper.

banks were located in places where inhabitants were less than one thousand people, and 20 percent where they were less than five hundred. With floods of immigrants, the total population of Illinois was increasing, but banks preferred relatively isolated places. In addition, the major number of these banks was established in 1860, a year that saw the largest number of newly opened banks. These data imply that banks formed after 1858, in 1860 in particular, were by no means as secure as those before.

Life span of free banks

Figure 6 clearly indicates that among all the banks that had started since 1858, thirty banks had a short life span of less than a year; another seventeen banks had been in operation more than one year but less than two years. The longest life span is five years, which, however, was the average life span of banks opened during 1851-1857. Moreover, banks located in remote places tended to have short life spans. For instance, twenty-four banks whose life span was less than two years were situated in places with a population less than one thousand. Seven of the banks that were located in places with a population less than five hundred were in operation less than a year; another eight of such banks were in operation for one to two years. Located in remote places and exiting from the banking industry in a short time, those free banks are easy to associate with wildcat banks.

Figure 6
Life span of Free Banks, 1858-1861



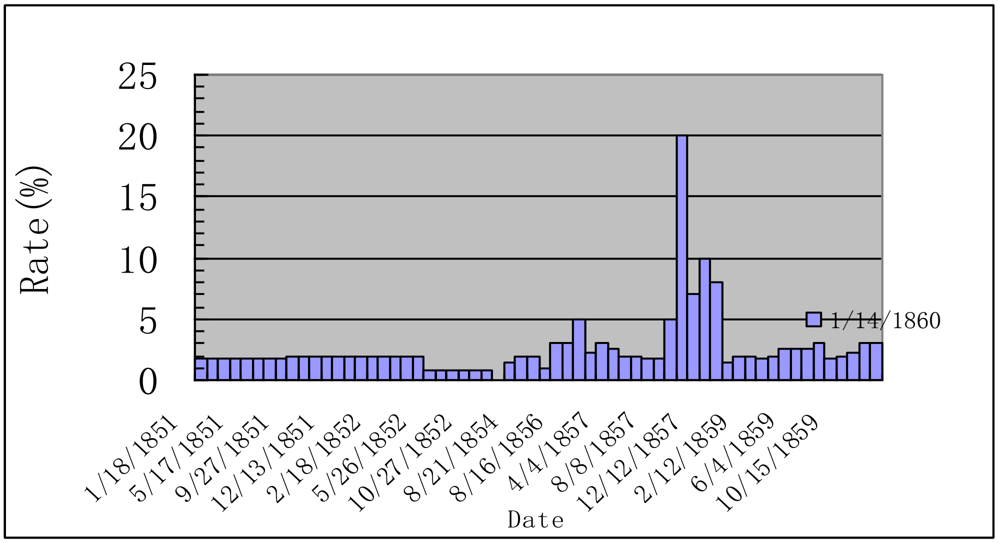
Source: Andrew J. Economopoulos, "Illinois Free Banking Experience," *Journal of Money, Credit and Banking* 20 (May 1988): 249-64.

Losses caused to note holders

Note holders were most concerned with the losses free banks caused them, so this is a crucial factor in assessing the performance of free banks. This section again uses discount rates, exchange rates, and redemption rates when banks were in liquidation to estimate the possible losses incurred by free banks. Discounts in New York, 1851-1860, are shown in Figure 7.

Owing to the nationwide economic recovery from the crisis of 1857, the discount rates on Illinois bank notes fell back during 1858 and 1860, but the rates fluctuated more often and became higher than these of 1851 and the first half of 1852. Because discounts reflect redemption costs and

Figure 7
Modal Discounts on Illinois Bank Notes in New York, 1851-1860



Source: Weber, "Quoted Discounts on State Bank Notes in New York, Cincinnati, and Cleveland, selected dates, 1827-1858."

the risk premium, the rise in discount rates reveals that those banks were located in inaccessible places or that note holders distrusted Illinois free banks. In June 1860, the situation was worse. It was calculated that the discount rates of 97.5 percent of Illinois bank notes were 2.25 percent or even higher.[69] Luckily for those banks, their banks notes were received at par in Chicago at that time. At the end of 1860, however, a number of Illinois bank notes were gradually rejected by Chicago banks: notes from seven banks, including American Exchange Bank at Raleigh, Bank of Aurora, Bank of Commonwealth at Robinson, Bank of Raleigh, Corn Exchange Bank at Fairfield, National Bank at Equality, and State Bank of Illinois at Shawneetown, were first thrown out. By May 18, 1861, as table 6 shows, the New York and Chicago market only accepted a few banks' bank notes at par. The majority of Illinois free banks were rejected in both places. If note holders had purchased their bank notes at par and held depreciated notes of more than one bank, they would suffer a lot. Though it is not easy to calculate the average loss rate of all note holders, some researchers estimated that it was 22.2 percent, much higher than that of Wisconsin, which was only 7.2 percent.[70]

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[69] Dwyer, "Wildcat Banking, Banking Panics, and Free Banking in the United States," 13.

[70] Ibid., 16.

Table 6
Value of Illinois Bank Notes in Different Markets, 1861

Number of banks with different discounts / Value(cents/dollar)	New York Market	Chicago
Par	9	6
90 and above	14	16
80 and above	16	19
70 and above	15	9
60 and above	11	9
50 and above	11	14
40 and above	1	0
Rejected	37	38
Total*	114	111

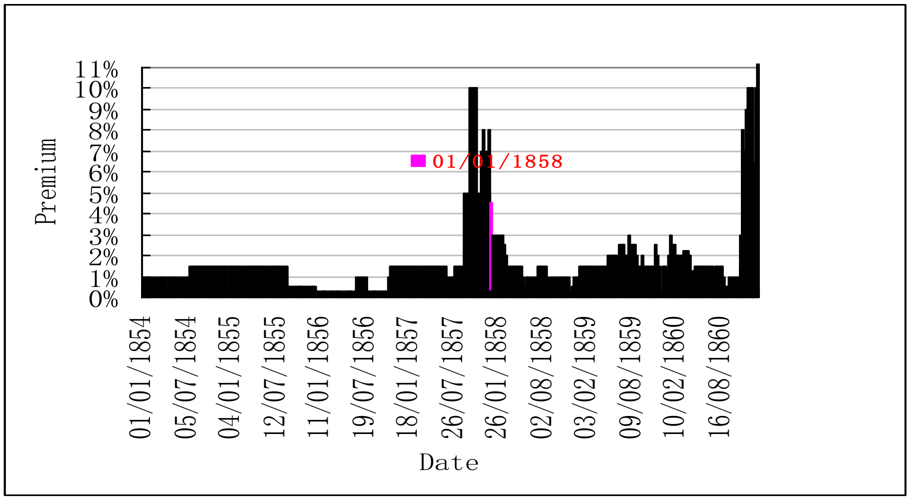
Source: "Complete list of Illinois banks, giving their securities and real value, accurately computed, based on the market, price of bonds at the latest dates. This list will be corrected from day to day, according to the fluctuation of the stock market," *Printed Ephemera Collection*, portfolio 18, folder 4a; viewed 7 Oct. 2008. URL: http://hdl.loc.gov/loc.rbc/rbpe.0180040a.

* New York market received notes of Illinois banks at different discount rates from these of Chicago. Moreover, some banks had been closed and their notes were out of circulation in Chicago, but they still circulated in New York. For instance, Banks of Peru, Bank of Ottawa and Commercial Bank of Chicago had been out of business in 1861, but New York market still received their notes at par. That's why the total number of banks is different between the two places.

The price of New York exchange against Illinois bank notes is also an important index. Figure 8 shows the rates from 1854 to 1861. In the first two months of 1858, Illinois gradually recovered from the destructive effects of the economic crisis. The premium of New York money to Illinois currency returned to the level before 1857 and remained at 1 to 1.5 percent for most of the time. There were approximately five months when the premium stayed at 2 percent. However, during the fall and winter, the busiest months of the agricultural trade, the premium was one percent higher than that before 1857. This means that farmers had to bear more losses than before. Worse still, at the end of 1860, the prices of exchange began to rise sharply; that is, Illinois bank notes depreciated to a greater extent, meaning that more and more note holders lost faith in Illinois free banks.

Finally, note holders would suffer from economic losses when banks were in liquidation. According to the accessible data, the majority of banks failed in 1861; only four banks out of eighty ceased operation before 1859. The four banks closed before 1859 were Bank of Rockford, Dupage County Bank, Exchange Bank of H.A. Tucker & Co. and Phoenix Bank at Chicago. The Exchange Bank of H.A. Tucker & Co. voluntarily went into liquidation and redeemed its paper in 1858, as did the Bank of Rockland. Information about the other two was unavailable. George Dowrie concluded that before

Figure 8
Prices of New York Exchange, 1854-1861



Source: Data for 1854-1860: "Stock Quote 42—No Title," 1 Jan. 1861; data for 1861: "Stock Quote 8—No Title," 29 Jan. 1861; "Stock Quote 8—No Title," 8 Feb. 1861; "Stock Quote 5—No Title," 18 April 1861; "Important Currency Movement," 15 May 1861: all *Chicago Tribune*.

1860, the state and federal stocks that Illinois free banks deposited with the Auditor fully protected the free banking system, so that "the securities of but one fell short of providing for redemption in full of all outstanding issue."[71] Charles Garnett also proved that, after two years of hard times from 1858 to 1860, only six of fifty-four downstate banks had gone out of existence. "All these institutions, with the exception of the Danville bank, had redeemed their notes and caused no losses to the holders."[72]

However, note holders were no longer fortunate in 1861. Because of the large number of failed banks, the new Illinois banking law passed in 1861 provided that the Auditor could redeem bank notes with the securities deposited for banking purposes. When a note holder presented bank notes to him, the Auditor could calculate the ratio of the notes against the total number of circulating notes surrendered by that bank and pay the note holder the same proportion of that bank's securities.[73] At a

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[71] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 158.

[72] Charles Hunter Garnett, *State Banks of Issue in Illinois* (Urbana, Ill., 1898), 54; viewed 7 Oct. 2008. URL: http://www.archive.org/details/statebanksofissu00garnrich.

[73] "The New Banking Law: Article One. Article Two. Article Three. Article Four. Article Five. Article Six. . . ."

time when stock prices were dropping sharply, this provision undoubtedly increased the economic risk of note holders. For instance, during October 1861, the par value of presented bank notes was $279,089, but the holders received bonds whose value was only $160,419.80.[74] In 1862, according to the price of their securities, only four banks redeemed their notes at par; three banks redeemed their bank notes at 90-95 cents on the dollar; eight banks redeemed their bank notes at 81-90 cents, eleven banks at 71-80 cents, twenty-five banks at 61-70 cents, and thirty-eight banks at 50-60 cents.[75] It is estimated that the loss rate was 44 percent as a result of the Auditor's reimbursing note holders with securities. However, a large number of note holders sold their bank notes or securities to brokers, thus causing a second heavy discount. Therefore, though it is difficult to calculate the exact number, the loss rate would be much higher than 44 percent.[76]

On the whole, note holders suffered great economic losses in holding, circulating, and redeeming Illinois bank notes. During the debate on a new bank bill before Congress, Senator John Sherman reported that as a result of the bank failure of 1861 and 1862, note holders had directly lost 3 to 4 million, not counting "the indirect loss of as many millions more by derangement of business and ruin to private interests."[77] Before the establishment of free banks, Illinoisans had lost $600,000 every year as a result of the monopoly of foreign institutions, whereas before the end of the free banking system, they bore losses greater than that. Because Illinois free banks grew unsecure and brought great economic losses to society, the banking industry of Illinois during 1858-1861 was by no means a success.

The End of the Free Banking System

Some researchers, including Arthur Rolnick, Warren Weber, and Andrew Economopoulos, employed the falling asset hypothesis to interpret the Illinois free banking experience in 1861: bond prices of southern states dropped dramatically with the Civil War, thus prompting note holders to demand specie payment. Simultaneously, bank commissioners demanded additional capital from banks influenced by the falling bond prices. Unwilling bankers would rather exit the banking market, leaving their note holders with depreciated stocks, than pay on demand and replenish the amount of securities deposited to the Auditor.[78] Consequently, approximately ninety banks failed in only one year; there were only seventeen

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[74] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 173, footnote 170.

[75] Ibid., footnote 140.

[76] Ibid., footnote 170.

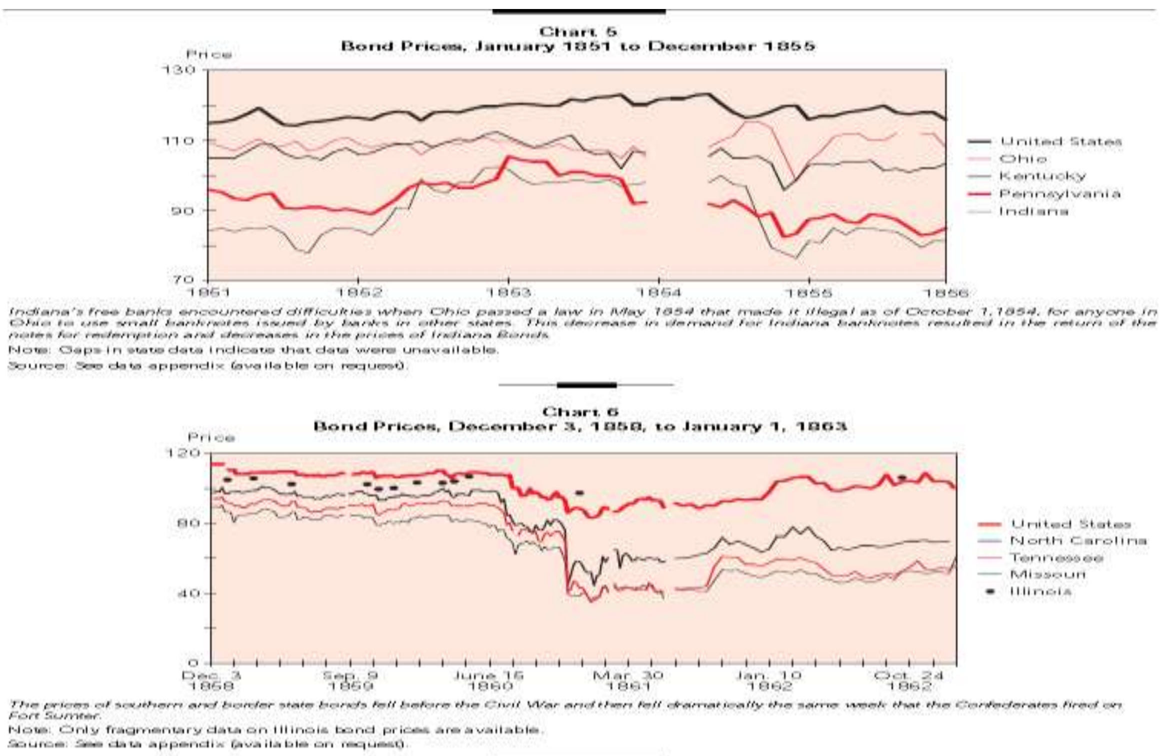
[77] "The New Bank Bill," *Chicago Tribune*, 9 March 1863.

[78] See Arthur J. Rolnick and Warren E. Weber, "New Evidence on the Free Banking Era," *American Economic Review* 73 (Dec. 1983): 1080-91; Economopoulos, "Illinois Free Banking Experience," 249-64.

banks in 1862 and twenty-five banks in 1863. According to these researchers, free banks themselves were sound and prudent; factors outside the banking system sealed their fate.

This theory could also explain other phenomena. Figure 9 shows that bond prices began to drop in the summer of 1860. Simultaneously, the discount rate rose, and New York money was purchased at a higher premium. At the end of 1861, Chicago began to reject free banks in other parts of Illinois and accept their bank notes at discount. All of these phenomena could be ascribed to the distrust of Illinois free banks aroused by falling stocks prices.

Figure 9
Bond Prices, December 3, 1858, to January 1, 1863



Source: Gerald P. Dwyer Jr., “Wildcat Banking, Banking Panics, and Free Banking in the United States;” Federal Reserve Bank of Atlanta *Economic Review* (Dec. 1996), 1–20; viewed 11 Oct. 2008. URL: http://www.frbatlanta.org/filelegacydocs/ACFCE.pdf.

However, there are still several questions this theory failed to answer: if free banks were really as sound and secure as current scholars described, why did more than sixty banks open during 1859 and 1860, which was a difficult time for the banking industry? Outside Illinois, bank notes were rejected; within the state, business was completely paralyzed owing to the economic crisis. Moreover, because of crop failures, Illinois agricultural commerce fell into stagnation and failed to recover until the second half of 1860. Hence, one wonders what drove so many banks to enter the banking industry in panic and depression.

There seems to be only one answer: most banks were not formed for regular banking purposes from 1859 to 1860; they were wildcat banks. The crisis of 1857 gave them a chance to earn extensive profits during the general suspension of specie payment. Banks could issue as many notes as they liked; thus, even regular banking institutions could make illegal profits legally against such a background. That is why only approximately twenty banks possessed the characteristics of wildcats, but nearly ninety failed in 1861.

At the beginning of the economic crisis, people still held faith in the economy of Illinois. The *Chicago Tribune* claimed that agricultural commerce dominated the state's economy. Since crops were immense and the quality of products surpassed all previous years, people need not worry about their economy.[79] Unfortunately, just when Illinois nearly recovered from the crisis, crop failures hit the state. The crop of 1858 was both small and poor in quality because of frost. That of 1859 was good, but meager in amount.[80] These crop failures had a great impact on the Illinois economy: there had been few agricultural transactions since then.

The crop failure exacerbated the scarcity of money. A reporter in Illinois described the situation: "nobody could pay; everybody mortgaged and chattel-mortgaged, until at the moment of writing, I believe the times are as distressing as they were in the year 1837."[81] Table 7 confirms his observation. In contrast with the year 1857, three banks newly opened in 1858, but the amount of specie decreased by 63 percent. In 1859 the situation was a little better; in 1860 the number of banks was 65 percent more than in 1858, but the amount of specie still stayed at the level of that year. In such a case, though Illinois free banks secured their bank notes with state stocks, "they were utterly unable to redeem their bills in coin." As a result, "with a degree of wisdom and courage seldom seen at such times," they determined to take and pay the bills of those banks as currency.[82] The general suspension of specie payment began, and in May 1858 the *Chicago Tribune* reported that "in other parts of the state [out of Chicago], banking means anything but paying specie on demand."[83]

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[79] ". . . of the West," *Chicago Daily Tribune*, 29 Aug. 1857, p. 2.

[80] "Stock Quote 42—No Title," *Chicago Tribune*, 1 Jan. 1861.

[81] "Letter from Illinois [from a Regular Correspondent an Old California]," *Daily Evening Bulletin*, 8 Oct. 1858; viewed 19 Jun. 2007. URL: http://docs.newsbank.com/s/HistArchive/ahnpdoc/EANX/117B2CFBCAD210B8/384B38030B1C4026A3FCD3E7E09B9921.

[82] "Stock Quote 4—No Title," *Chicago Press and Tribune*, 1 Jan. 1859.

[83] "Illinois Banks," *Chicago Daily Tribune*, 27 May 1858.

Table 7
Amount of Specie, 1853-1861

Year	Number of Banks	Specie (dollars)
1853	23	419,531
1854	29	565,152
1856	36	759,474
1857	42	635,810
1858	45	233,239
1859	48	269,585
1860	74	223,812
1861	94	302,905

Source: Report Compt. Curr., 1876, see Charles Hunter Garnett, *State Banks of Issue in Illinois* (Urbana, Ill., 1898), 55; viewed 7 Oct. 2008. URL: http://www.archive.org/details/statebanksofissu00garnrich.

Therefore, since September 1857, the New York exchange prices had risen to fabulous figures in Illinois, and other states rejected Illinois bank notes at the same time because they were inconvertible. As a result, note holders sacrificed a lot because of the unredeemable bank notes, but they acquiesced in such a situation. Therefore, Illinois bank notes were still received at par in Chicago; Illinoisans passed those bank notes from hand to hand in the payment of debts, and there were no reports about runs on Illinois free banks.[84] The *Chicago Tribune* reveals the reason for people's tolerance. First, economic recovery and social development needed the free banks to produce "currency" in such a time when money was extremely scarce. Illinoisans "gave them an opportunity to furnish the people with a kind of currency, which, if not readily convertible, had real and recognized value, and without which everything in the way of settlement of domestic balances and local improvement must have come to a dead halt."[85] Second, note holders still had faith in Illinois free banks. Though banks were unable to pay in specie, their bank notes were secured by state bonds. Experience of the past years proved all bank notes could be redeemed at a trifling cost, so people learned to "offset the vice of inconvertibility against the virtue of security, which to a very large extent it is agreed on all hands our currency possesses."[86] There is another reason the newspaper failed to mention; that is, from 1858 to the first half of 1860, Illinois commerce was almost in stagnation. Although the discount

[84] "Stock Quote 4—No Title."

[85] "ILLINOIS BANKS," *Chicago Press and Tribune*, 14 June 1859.

[86] "Stock Quote 25—No Title," *Chicago Press and Tribune*, 2 Jan. 1860.

rates and the price of exchange were high, people hardly felt the harm of inconvertible currencies. That is also why, when agricultural commerce resumed in the autumn of 1860, people could no longer bear the economic losses caused by 3 percent discounts on Illinois bank notes and 2 percent premiums on New York exchanges. Thereafter, many comments in the *Chicago Tribune* eagerly favored banks redeeming in specie.

The tolerance for inconvertible currency released free banks from a heavy burden: paying on demand. Meanwhile, the need for a circulating medium created an opportunity for banks to issue as much paper money as they liked. The potential economic profits in the banking industry attracted more and more people to invest in establishing banks. Consequently, the size of Illinois free banking expanded greatly from 1858 to 1860, and the amount of circulation simultaneously swelled. In 1856, the circulation of Illinois free banks was worth $3,420,985; it rose to $5,534,945 in 1857. The value of circulation was $5,238,930 in 1858 and $5,707,048 in 1859. In 1860, the amount was $8,981,723, three million more than in 1859; in the year 1861 the amount expanded to $11,010,837.[87]

Such an amount of bank notes should have furnished adequate credit to the mercantile and manufacturing interests of the state. However, evidence reveals that these free banks failed to extend enough loans to meet people's demand for currency, for only a few banks conducted a regular banking business. Table 8 is the aggregate statement for Illinois free banks on October 1, 1860, when the free banking system was in prosperity and expanding at an unprecedented speed.

First, only fourteen of the ninety-four banks owned even enough real estate to provide a site for their place of business. And the banks invested only $116,551.40 in the real estate.[88] It could be inferred that the remaining eighty banks had either no or no fixed place of business. Therefore, in the convention held in December 8, 1860, a Chicago business man viewed such banks as wildcat banks and complained that "seventy-five of our banks have no location or a name. Why[,] take out two one dollar bills, one is located at Thebes, one at Sparta. No one but an Illinois wild-cat banker could answer the question where Thebes and Sparta are."[89]

Second, most curious is the amount of loans and discounts. Only fourteen banks conducted their own "loan and discount" business, which means only $540,876.28 of the $19 million in resources was used in this manner. With reports for a different date, however, we find the loan and

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[87] Garnett, *State Banks of Issue in Illinois*, 55.

[88] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 160.

[89] "THE CURRENCY MEETING: The Solid Men of Chicago in Council. RESOLUTIONS, SPEECHES, ETC."

Table 8
Aggregate Statement for October 1, 1860

RESOURCES

Item	Total for 94 banks
Stocks deposited as security for notes	$12,264,580.74
Real estate, etc.	116,551.60
Notes of other banks	287,111.25
Due to the bank other than loans and discounts	1,950,244.39
Loans and discounts	540,876.28
Specie	302,905.26
Deposited with other banks	3,793,753.22
Expense account	19,459.76
Checks, drafts and other cash items	37,920.21
Surplus stocks and suspended debt	85,492.21
Profit and loss	37,791.26
Total	19,436,985.74

LIABILITIES

Capital stock	$6,750,743.07
Debts other than deposits and notes	422,220.36
Deposits	807,763.82
Notes outstanding	11,010,837.00
Due other banks	64,200.72
Exchange, interest and expense account	25,628.52
Surplus bonds	286,614.26
Profit and loss	68,977.99

Source: George William Dowrie, *The Development of Banking in Illinois, 1817-1863*, (Urbana, Ill., 1913), 159; viewed 27 Sept. 2008. URL: http://www.archive.org/details/developmentofban00dowrrich.

discount business at that time was strangely small in comparison with other states and with itself before 1860.

The little state of Connecticut had less circulation than Illinois, but its loans were seventy-one times as much as those of Illinois. With similar banking size, Indiana had less commerce than Illinois, but its loans and discounts were nineteen times those of Illinois; the banking system of Wisconsin resembled that of Illinois, but its bank loans were far more than those of Illinois banks. In comparison with Illinois itself, it is also evident that the size of loans extended by Illinois free banks was small. With the increase in the number of banks, the total amount of circulation rose proportionally, but loans dropped sharply in 1860 and 1861 (see Table 10).

TABLE 9
Loans and Circulation in 1860, Selected States

States	No. of Banks	Capital	Circulation	Loans and Discounts
Connecticut	74	21,512,176	7,561,519	27,856,785
Indiana	97	4,343,210	5,390,246	7,675,861
Wisconsin	108	7,620,000	4,429,855	7,592,361
Illinois	94	5,251,225	8,981,723	387,229

Source: Anonymous, "Banks—Census Report," *The Merchants' Magazine and Commercial Review* 47 (Oct. 1862): 381.

TABLE 10
Loans and Circulation of Illinois Banks, 1853-1861

Year	No. of Banks	Circulation	Loans and Discounts
1853	23	1,351,788	586,404
1854	29	2,283,526	316,841
1856	36	3,420,985	337,675
1857	42	5,534,945	1,740,671
1858	45	5,238,930	1,146,770
1859	48	5,707,048	1,296,616
1860	74	8,981,723	387,229
1861	94	11,010,837	546,876

Source: Report Compt. Curr., 1876, see Charles Hunter Garnett, *State Banks of Issue in Illinois* (Urbana, Ill., 1898), 55; viewed 7 Oct. 2008. URL: http://www.archive.org/details/statebanksofissu00garnrich.

How did this huge amount of currency get into circulation on so short a line of discounts, and how did these banks make money? The answer is that Illinois free banks probably made money by means of usury and investing in bonds. The *Chicago Tribune* described their tricks in detail. Usually, a speculator formed a bank at a relatively remote place—say, Egypt in southern Illinois—and deposited its notes with private businesses in Chicago or some other places, where the currency was loaned to the public at high rates, yielding from 20 percent to 40 percent per annum.[90]

[90] "CURIOSITIES OF ILLINOIS BANKING," *Chicago Press and Tribune*, 23 Aug. 1860.

In such a manner, they could circumvent the Illinois free banking law, which provided that the rates of interest these banks got could never exceed 10 percent. This accounts for the "Deposited with other banks" amount aggregating to $3,793,753.22. Moreover, the banker sometimes gave an amount of money to a broker, who bought bonds with the money and "took his pay in the very bills issued upon them." The banker could obtain the interest on the bonds, which was a very handsome net income; meanwhile he need not redeem the bank notes issued on the bonds in specie.[91] Such activities explain why George William Dowrie defined free banks as "mere devices for obtaining a supply of paper money to use in connection with a private banking business where the restrictions placed upon an incorporated concern could be avoided."[92]

However, in the second half of 1860, the good old days of Illinois free banks ended. First, Illinois had recovered from the destructive impact of the economic crisis. "The western states were all favored that year with a crop of unusual abundance." The partial failure of the wheat crop in Europe, and the almost total destruction of both wheat and corn in the southern States by the drought promoted the demand for western crops. The exports of grain had been more than double those of 1859.[93] Heavy shipments of agricultural products brought in a large amount of specie and, at the same time, aroused people's discontent with the reality of Illinois: the price of exchange ought to be a little higher above par at worst, just as in the years before the crisis; however, now the premium was 1.5 percent to 2 percent, thus causing a great loss when commercial activities were active. Second, the stock market gave free banks another heavy blow. In the winter of 1860-1861, prices of southern securities began to decline because of the political situation in the South. As a result, the prices of eastern exchange against Illinois currency rose correspondingly.

Consequently, note holders of Illinois free banks eagerly demanded redemption in specie. More and more comments in the *Chicago Tribune* claimed that for three years—since the crash in 1857—this delinquency on the part of the banks had been permitted by the people, under the conviction that such a course was necessary to preserve a circulating medium of any kind whatever. "But the occasion which gave rise to it has passed."[94] In the convention held in December 8, 1860, in Chicago, business leaders expected to exert their influence on the bank commissioners "to put any bank into liquidation which fails to redeem their bills. . . ."[95]

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[91] Ibid.

[92] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 160.

[93] "THE GENERAL BANKING LAW," *Chicago Tribune*, 10 Nov. 1860.

[94] "A WORD IN TIME," *Chicago Press and Tribune*, 21 Aug. 1860.

[95] "THE CURRENCY MEETING: The Solid Men of Chicago in Council. RESOLUTIONS, SPEECHES, ETC."

Moreover, bank commissioners commanded free banks to deposit additional securities owing to the falling prices of southern bonds. At the end of 1860, nearly every bank in Illinois had to replenish its securities.[96] On February 14, 1861, Illinois passed another amendment to the general banking law, which proposed to establish a central redemption system. Banks had to send agents to Chicago or Springfield to redeem their notes in specie. It also set the final date for banks to replenish their securities—August 14, 1861. Failing to answer such calls, banks would be put into liquidation.[97]

Furthermore, Chicago bankers ceased to accept bank notes of other places at par, and seven banks were thrown out of Chicago.[98] In April 1861, the number of rejected banks increased to thirty-three.[99] By June 1861, Chicago bankers received only fourteen banks' notes at par and rejected all other Illinois bank notes.[100] Worse still, railway and transportation companies plunged themselves into battle against Illinois free banks. They held a convention in May 1861 and decided to appoint an executive and a corresponding committee to force "the banks of the State of Illinois to give additional security and guaranty for the redemption of their notes." Depending on whether the banks had taken necessary measures to replenish adequate stocks and had redeemed their bank notes, these companies would accept their bank notes at different discount rates. They made a list according to their evaluation of bank notes, which became the standard value of Illinois bank notes at that time.[101]

Finally, the action of the Board of Trade "put the knife into the heart of the Illinois banking system" by resolving that the business of Chicago must be conducted on a specie basis and by demanding that the banks have specie on hand to cover no less than one-third of all their liabilities.[102]

After the crisis of 1857, free banks loaned bank notes at high rates by the hand of private business, invested in southern stocks to get 6 percent interest on them, and issued more bank notes to conduct these businesses without redemption in specie. When the value of southern stocks depreciated greatly, they could purchase more stocks and compensate for

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[96] George William Dowrie, *The Development of Banking in Illinois, 1817-1863*, 156.

[97] "ILLINOIS BANKS: IMPORTANT REPORT OF THE BANK COMMISSIONERS. Twenty-three Banks Under Call. CENTRAL REDEMPTION REQUIRED To the Public," *Chicago Tribune,* 24 June 1861.

[98] "Stock Quote 5—No Title," *Chicago Tribune*, 21 Nov. 1860.

[99] "THIRTY-TWO ILLINOIS BANKS THROWN OUT," *Chicago Tribune,* 1 April 1861.

[100] "Other 10—No Title," *Chicago Tribune*, 8 June 1861.

[101] "The Railroads and the Currency: LIST No. 1, PAR. LIST No. 2, NINETY CENTS. LIST No. 3. EIGHTY CENTS. LIST No. 4, SEVENTY CENTS. LIST No. 5, SIXTY CENTS. LIST No. 6, FIFTY CENTS," *Chicago Tribune*, 21 May 1861.

[102] "THE CURRENCY QUESTION—A CALL DEMANDED," *Chicago Tribune,* 24 May 1861; "Stock Quote 9—No Title," *Chicago Tribune,* 28 May 1861.

the expense by issuing more paper money. However, the demand for redemption in specie made free banks with little or no specie unable to continue on this path. In such cases, banks not only had no chance to make excessive profits as easily as before, but they also had no ability to withstand pressures from merchants, bank commissioners, Chicago banking houses, transportation departments, the Board of Trade, and the note holders demanding specie at their counters. Having no choice, they had to exit the banking industry. As a result, approximately ninety banks failed at the same time in 1861.

The free banking experience of the later period imposed great economic losses on Illinois. Note holders suffered severely owing to high discount rates, high prices of eastern exchange, and the losses in banks' liquidation processes. Moreover, the position of Chicago as the commercial center of the West was unstable. Merchants filled their stores with goods from St. Louis and exported products there as well, because when they shipped their produce to Chicago they were paid in depreciated currency, 2 percent below par, whereas in St. Louis, they were paid with gold or its equivalent.[103] Another immediate aftermath of the free banking experience was that foreign notes flooded into Illinois once again.[104] It is interesting that what the free banking system had tried to eliminate returned as a result of the failure of that system.

Meanwhile, the old hostility to banks returned. A proposition to establish a central banking system, known as a "specie system" of banking in comparison with the "stock system," evoked a hot discussion.[105] Several local papers of Illinois, Democratic and Republican newspapers alike, put the words "Against the Banking Law on a Specie Basis" at the head of their columns.[106] They held that, "if any one, with the experience of the last three years, can think of wildcat banks and hyena bankers, without burning with indignation, he is the man who may vote to create another batch with a tenure of existence and predatory warfare upon the pockets of the people during the next quarter of a century." They viewed the whole banking system as an evil second only to the treason, rebellion, fraud, and robbery then in progress in the South.[107] As a result, Illinois failed to establish a central banking system.

It is obvious that the painful experience of free banking destroyed Illinoisans' confidence in any type of banking system. Therefore, it was quite natural that in the election of 1862, Illinois voters gave 126,538 votes

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[103] BULLION, "Illinois and Wisconsin Currency," *Chicago Press and Tribune*, 16 Aug. 1859.

[104] "Stock Quote 9—No Title," *Chicago Tribune)*, 14 June 1861.

[105] Dowrie, *The Development of Banking in Illinois, 1817-1863*, 165.

[106] " 'Against the Banking Law'," *Chicago Tribune*, 28 Oct. 1861.

[107] "THE NEW BANK LAW: OPINIONS OF THE COUNTRY PRESS. Vote it Down. 'AGAINST THE BANKING LAW ON A SPECIE BASIS.' WHY WE OPPOSE THE PROPOSED BANKING LAW," *Chicago Tribune*, 4 Nov. 1861.

in favor of entirely abolishing banks and bank paper. Illinoisans even voluntarily proposed a heavy tax on free banks sufficient to drive their circulation out and leave standing room for the government greenback.[108] In 1864, there were still twenty-four free banks in Illinois, but as a result of the national banking system and the tax on the issues of state banks, Illinois free banks gradually disappeared from the Illinois banking industry.[109]

Every step Illinois free banks made was closely associated with the state's economic progress, its commercial development in particular. The free banking system was established to seize back the power in conducting independent economic activities and to serve specialized commercial transactions. At first, free banks fulfilled their tasks by furnishing the state with a secure and convertible currency and lowering the financing costs of commercial activities. However, when commerce fell into stagnation after the crisis of 1857, free banking was bogged in chaos as well. Wildcats, grasping the chance offered by the general suspension of specie payment, entered the banking industry and made extensive profits by conducting speculative business. People needed the currency they produced at a time when money was scarce, so the community acquiesced in their conduct. However, with the resuscitation of commerce, banks' speculative activities obstructed the economic development of Illinois. In such a situation, free banks encountered heavy pressures from many sides calling for regular banking business. Consequently, most of the Illinois free banks exited the banking industry. Nevertheless, their absence aroused people's old hostility toward banks. The free banking system was abolished at the public will, and the remaining free banks gradually disappeared as well. Illinois had begun its National Banking era.

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[108] "A NATIONAL CURRENCY," *Chicago Tribune*, 13 Aug. 1862.

[109] Garnett, *State Banks of Issue in Illinois*, 52.

Appendix

Number of Banks: Figure 5

The primary source is Warren E Weber, "Listing of all State Banks with Beginning and Ending Dates;" viewed 17 Nov. 2008. URL: http://www.minneapolisfed.org/research/economists/wewproj.cfm. The data on the number of banks after 1860 are taken from "Complete list of Illinois banks, giving their securities and real value, accurately computed, based on the market, price of bonds at the latest dates. This list will be corrected from day to day, according to the fluctuation of the stock market," *Printed Ephemera Collection,* portfolio 18, folder 4a; viewed 7 Oct. 2008. URL: http://hdl.loc.gov/loc.rbc/rbpe.0180040a; "BANKS OF THE UNITED STATES.; LOCATION, NAME, PRESIDENT, CASHIER AND CAPITAL OF EACH. MAY, 1861. MAINE. NEW-YORK. NEW-YORK CITY. NEW-JERSEY. PENNSYLVANIA. PHILADELPHIA. DELAWARE. MARYLAND. BALTIMORE. VIRGINIA. NORTH CAROLINA. SOUTH CAROLINA. GEORGIA. ALABAMA. FLORIDA. ILLINOIS. FREE BANKS. INDIANA. BANK STATE OF INDIANA. FREE BANKS. IOWA. KANSAS. KENTUCKY. LOUISIANA. MICHIGAN. MISSOURI. MINNESOTA. MISSISSIPPI. NEBRASKA. OHIO. TENNESSEE. WISCONSIN. NEW-HAMPSHIRE. VERMONT. MASSACHUSETTS. BOSTON, MASS. RHODE-ISLAND. PROVIDENCE, R. I. CONNECTICUT," *The Bankers' Magazine* 10 (June 1861) (27 pages), 974; Gerald P. Dwyer Jr., "Wildcat Banking, Banking Panics, and Free Banking in the United States;" viewed 11 Oct. 2008. URL: http://www.frbatlanta.org/filelegacydocs/ACFCE.pdf; "BANKS OF THE UNITED STATES," *The Bankers' Magazine* 11 (June 1862): 12; "BANKS OF THE UNITED STATES," *The Bankers' Magazine* 13 (July 1863): 1; George William Dowrie, *The Development of Banking in Illinois, 1817-1863* (Urbana, Ill., 1913), 159; viewed 26 Sept. 2008. URL: http://www.archive.org/details/developmentofban00dowrrich.

Life Span

TABLE 1
Life Span of Illinois Free Banks, 1851-1861

Life Span	Number of Banks (Formed in 1851-1857)	Number of Banks (Formed in 1857-1865)
0 - 1	4	30
1 – 2	7	17
2 – 3	10	18
3	0	1
3 – 4	5	3
4	0	2
4 - 5	20	4
5	0	5
5 - 6	13	0
6 – 7	7	0
7 - 8	5	0

Life Span	Number of Banks (Formed in 1851-1857)	Number of Banks (Formed in 1857-1865)
8 - 9	3	0
9 – 10	3	0
10 - 13	3	0

Source: Data for 1851-1857: Warren E. Weber, "Listing of all State Banks with Beginning and Ending Dates," viewed 18 Nov. 2008. URL: http://www.minneapolisfed.org/research/economists/wewproj. Data for 1857-1865: Andrew J. Economopoulos, "Illinois Free Banking Experience," *Journal of Money, Credit and Banking* 20 (May, 1988), 249-64.

Modal Discounts

TABLE 2
Modal Discounts on Illinois Bank Notes in New York, 1851-1860

Date	Modal Discount	Count	Frequency
1/18/1851	1.75	1	1
2/15/1851	1.75	1	1
3/22/1851	1.75	1	1
5/3/1851	1.75	1	1
5/17/1851	1.75	1	1
6/4/1851	1.75	1	1
8/9/1851	1.75	1	1
9/6/1851	1.75	1	1
9/27/1851	2	1	1
10/4/1851	2	1	1
11/15/1851	2	1	1
11/29/1851	2	1	1
12/13/1851	2	1	1
1/3/1852	2	1	1
1/17/1852	2	1	1
2/4/1852	2	1	1
2/18/1852	2	1	1
3/3/1852	2	1	1
3/13/1852	2	1	1
4/24/1852	2	1	1
5/26/1852	0.75	4	2
7/7/1852	0.75	4	2
7/21/1852	0.75	4	2
7/31/1852	0.75	7	3
10/27/1852	0.75	8	4
11/17/1852	0.75	8	4

Date	Modal Discount	Count	Frequency
10/22/1853	0	0	0
11/2/1853	1.5	29	16
8/21/1854	2	35	25
1/1/1855	2	37	22
12/1/1855	1	42	41
7/2/1856	3	2	1
8/16/1856	3	2	1
12/17/1856	5	1	1
1/10/1857	2.25	59	59
2/14/1857	3	59	48
4/4/1857	2.5	60	52
5/9/1857	2	62	51
6/6/1857	2	62	59
7/11/1857	1.75	60	57
8/8/1857	1.75	62	60
9/12/1857	5	63	62
10/17/1857	20	63	55
11/28/1857	7	64	54
12/12/1857	10	65	60
12/19/1857	8	64	61
6/19/1858	1.5	59	56
1/15/1859	2	67	64
2/12/1859	2	69	66
3/19/1859	1.75	71	68
4/23/1859	2	72	69
5/14/1859	2.5	73	70
6/4/1859	2.5	74	71
7/16/1859	2.5	79	76
8/13/1859	3	78	75
9/17/1859	1.75	81	78
10/15/1859	2	83	80
11/19/1859	2.25	86	83
12/24/1859	3	90	87
1/14/1860	3	91	88

Source: Warren E. Weber, "Quoted Discounts on State Bank Notes in New York, Cincinnati, and Cleveland, selected dates, 1827-1858;" viewed 18 Nov. 2008. URL: http://minneapolisfed.org/research/economists/wewproj.html.