ADDRESS OF

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We Americans I think are generally rather prone to what might be called doctrinaire positions, that is, we frequently take the position that one method of doing something is the logical and only method and that all other methods are wrong even though we find that other methods are in use in other countries with evident success. Ours is a big country and we are rather bumptious about its great progress and general success. We do not easily see, or if we do see, we are often rather unwilling to admit its shortcomings or to provide remedies. Then when something gets so bad as to force itself on our attention and becomes a subject of rather general agitation we too frequently think that the only remedy consists in passing more laws. Our banking system which grew up originally under state charters has been generally described as an independent unit banking system, with every community large enough to require banking accommodation served by its own local banking corporation. So strongly wedded have most of our bankers been to this system that not a few of them have denounced branch banking as monopolistic and un-American, and some of them appear to believe that the only reason why Canada is not larger than the United States today is because Canada has branch banking.

Now, persons who have given a good deal of time to the study of banking in other countries as well as our own are of the opinion that branch banking has served Canada very well, and has promoted the development of its great West instead of retarding it. We find, in fact, that interest rates in the prairie provinces of Canada are generally somewhat lower than interest rates in our adjoining states, and we find, furthermore, that a tremendous amount of money has been lost through bank failures in such states as North and South Dakota, Montana and Idaho, while just across the border in Canada there have been no failures during recent years. If the agricultural and economic depression of 1920-21 was the cause of a great number of bank failures in the great agricultural sections of the United States why did it not cause an equal number of failures across the line where conditions were practically the same? It seems obvious that our banking system itself must have been at least somewhat at fault - that it was not strong enough to stand up under adverse conditions. Looking back into our banking history we find that after every period of business depression many small banks have failed, while as a rule the larger banks in the larger cities have stood the test. You are doubtless familiar with the figures presented by the Comptroller of the Currency, Mr. Pole, in his annual report and in his recent addresses showing that some two-thirds of the bank failures in this country are of banks of small capitalization, $25,000 or less, and that about an equal percentage of the bank failures occur in small towns, towns of 2,500 and less. These figures and their classification by capitalization and by size of communities have been furnished from time to time by the Division of Bank Operations of the Federal Reserve Board and have been published from time to time in the Federal Reserve Bulletin.

No less than 5,642 banks were closed in the years 1921 to 1929, inclusive, most of them in agricultural communities where the people could least afford to lose. "During the last 10 years," said the Comptroller, "and continuing at the present, bank failures have been a blight on the Mississippi Valley, the South, the Southwest and the Northwest. There are agricultural counties in which every bank has failed." There were 349 failures during the first four months of this year ending April 30th, of which 92 occurred in the month of April. The latest figures show about the same proportion of failures of banks with small capitalization and in small towns. This whole exhibit of failures is a disgrace to the country and certainly should not be permitted to continue if a remedy can be found, whether the remedy is popular or unpopular in the banking fraternity. It is something that business men should take more interest in than they have generally shown in the past.

The problem is not acute in the northeastern states. New England, New York and Pennsylvania have had very few bank failures but they are not so entirely exempt as to make the subject wholly without interest. Two failures have occurred in the Boston Federal Reserve District since the first of January, one in the New York District, two in the Philadelphia District, seven in the Cleveland District. It is interesting to note that all the other districts run into two figures, excepting one, San Francisco, the largest of those with two figures being the Chicago District with 93 failures and the smallest the Dallas District with fourteen. Coming down to the San Francisco District we find only three. The Pacific Coast, therefore, appears to rank with relation to bank failures at least somewhat with the Eastern states, but there we find throughout the great State of California branch banking very highly developed, which at least raises the presumption, the district being largely agricultural, that branch banking may have something to do with the contrast between that district and the agricultural districts of the South and Middle West.

I have been credited with having been something of a pioneer in advocating branch banking as a remedy for bank failures, but branch banking has been recognized as a remedy and has been recommended many times in the past. After the great panic of 1893 we find that two Comptrollers of the Currency in succession, Mr. Eckles and Mr. Charles G. Dawes, recommended branch banking, particularly in the smaller communities. Mr. Dawes recommended that branches be allowed in towns of 2,000 or less, but he coupled this recommendation with a rather violent argument against a general or nation-wide branch banking development and did not follow it up.

In May 1902, Mr. James B. Forgan, Chairman of the First National Bank of Chicago, one of the leading bankers for many years in the United States, delivered an address on branch banking before the Bankers Club at Milwaukee, which attracted considerable attention. Mr. Forgan declared that the development of banking in the United States had been diverted from its natural course by erroneous politics and policy and added:

> "Had banking, as in the case of other lines of business, been allowed to work out its own destiny untrammeled by politics and free from subordination to government necessities a system would ere this have been established which would have made itself felt as a potent factor in the financial affairs of nations. We would also now have a system that would stand together for the public benefit in times of financial distress. As it is today we have no banks that will compare in financial strength and power with those of other countries. While actively competing with other nations in the fields of commerce and industry, it must be admitted that in the world's finance we are away behind in the race; nor does our system even satisfactorily provide for our own domestic requirements. The need of coalition among our unit banks is urgent."

The passage of the Federal Reserve Act and the development of the Federal Reserve System have changed some of the worst conditions that Mr. Forgan complained of, and we have had coalitions in the large cities which <u>have</u> given us banks which do compare in financial strength and power with those of other countries. It is claimed that we have one or two banks in New York since the latest mergers larger than any bank in any other country - but there is still urgent need of coalition among our small unit banks in the agricultural sections of the country. Mergers have gone a long way, possibly too far, in the big cities but they have been practically forbidden to country banks. If you attempt to merge two banks in towns located ten or twenty miles apart in the same county but not within the same municipal limits you cannot under federal law keep both offices open. The McFadden Act of February 1927 permits mergers and branches in cities where state banks can have branches but prohibits mergers and branches in country districts if the banks belong to the Federal Reserve System even though state laws permit and encourage branches.

This prohibition has had a rather serious effect in one of our southern Federal reserve districts, the Richmond District, where considerable numbers of country banks, some of them rather sizeable, have withdrawn from the Federal Reserve System in order to enter branch banking organizations under state laws. This development has been mostly in North and South Carolina, and Governor Seay of the Federal Reserve Bank of Richmond has stated in a recent letter that "The aggregate deposits of banks which have relinquished membership because of the present status of the law relating to branch banking was about $75,000,000" - during 1929 and to date of letter in 1930. Further commenting upon these conditions in a letter dated May 20th, Governor Seay says, "The extent to which branch banking shall be permitted, that is, whether it shall be country-wide or shall have commercial or Federal reserve zones may be debatable; but I do not think it is any longer debatable as to whether member banks in the Federal Reserve System shall be able to establish branches throughout states which permit their own state banking institutions to establish branches."

This statement it seems to me should have general endorsement. There is no reason that I can see why national banks and member state banks should not be allowed the same privileges with relation to branch banking that are allowed to state banks in the states where branch banking is permitted. A few banks have been lost to the Federal Reserve System in other Reserve Districts through the branch banking restrictions of the McFadden Act, one of them here in the State of Maine. It is obvious, of course, that the recent rapid development of branch banking in the Carolinas has been chiefly due to economic reasons. Many small banks have failed within the last five years and the people have turned to branch banking as a remedy. Why try to restrain such a natural and necessary movement by law?

The general conception of branch banking on the part of many of the bankers who have participated in the debate on the subject is that of a "reaching out" of banks in the large cities into the country. That conception was recently expressed by Mr. C. T. Zimmerman, President of the First National Bank of Huntingdon, Pa., in an article, published in the "Bankers Magazine," in which he said, "Merging of city banks in order to handle larger financing is doubtless justifiable in this trend, but to enable them to reach out for control of country banks is not justifiable." It didn't seem to occur to Mr. Zimmerman that country banks could merge if allowed to have branches, without reference to, or connection with any large city. The Comptroller's proposed amendment to the banking laws might well prohibit banks in central reserve cities, that is New York and Chicago, from establishing branches outside city limits, unless in immediately adjoining suburban territory - for two reasons. In the first place, they never would put branches in small towns where bank failures mostly occur. Their idea of branch banking is to have branches only in the larger cities, which would not accomplish anything so far as the prevention of failures is concerned. Furthermore, they have no need of branches as they already do a very large part of the best business all over the country without the expense of maintaining branches. In almost every small city and in many of the rather large cities there are large industries and people of wealth who find the local banking facilities too small for their purpose and, therefore, carry accounts in New York or Chicago. This brings up the Comptroller's point that to permit branch banking in "trade areas" would decentralize credit, that is, would create banking institutions in what New York sometimes calls the Hinterland large enough to handle much of the business now forced into New York because our unit banks in a very great number of places are too small to handle it.

It does not seem to be clearly understood that the unit banking system, carried to such an extreme as we have carried it in this country, forces banking business into the big cities and particularly into New York that could and should be done elsewhere, and also fosters speculation by forcing money into Wall Street to be loaned to brokers that might frequently be loaned, if not at home, at least to industries in the same state or in the same general neighborhood. Some economists have recognized this fact, but I think it was never forcefully presented until Comptroller Pole's recent address. It's truth can be amply proven. Early in 1926 there was formed in South Carolina a combination of three banks under the auspices of the Bank of Charleston, which after the necessary consolidations became the South Carolina National Bank. Interests connected with the Bank of Charleston, of which Mr. R. S. Small was the president, acquired control of the Norwood National Bank of Greenville in the Piedmont section and the Carolina National Bank in Columbia, in the center of the state. These three banks became state banks for a brief period and were consolidated under state laws, the

Greenville bank and the Columbia bank becoming branches of the bank in Charleston. They were then converted into a national bank with branches under the provisions of the Act of 1865 (a wise provision of law unhappily repealed by the McFadden Act in 1927). In a circular letter issued to the shareholders of the Bank of Charleston, N.B.A., in January 1926, Mr. Small stated that it was planned to consolidate these three banks into one corporation, in order, first, to be able to compete with the larger institutions in the North and East for the best class of business in the state and, secondly, he said,

> " It is a fundamental principle of banking that loans should be diversified, but there has not been in the smaller communities throughout the country a proper recognition of what diversification is. In a community like this practically all of our enterprises are dependent upon the results of agriculture, so that the failure of our crops is reflected in losses among our business institutions, and no matter how we may divide our loans among the various kinds of business, the fact that all the businesses are more or less dependent upon agriculture, in the last analysis, means that all our loans are dependent upon agriculture, so that no real diversification is obtained. The demand for money in one locality, such as this, is seasonal, which means that we have a big demand at one season and a small demand at another, resulting in our having to borrow at one season and to lend on call in New York at another, both of which processes are expensive. Through operating in Greenville we diversify our loans by having a number of them dependent upon an entirely different set of conditions, which insures a diversity, not otherwise obtainable, and in addition, the seasonal demand in Greenville for funds is exactly the opposite from Charleston, with a result that it will avoid, to a large extent, the necessity of borrowing at one season and lending on call in New York at another, thus giving us greater diversity and a more uniform demand."

Here is a distinct recognition of the fact that money was loaned on call in New York either from Greenville or from Charleston which could have been loaned in the state if the institutions in both sections of the state could work together. Greenville, as you know, is a manufacturing town and the peak of demands in that section would naturally come at a different time from the peak of demands at Charleston on the seacoast. I understand that the expectations outlined in this circular letter in 1926 have since been realized and that the institution is successful. That similar conditions obtain in many other states and sections is proven by the testimony of the group bankers recently summoned to the hearing before the Banking and Currency Committee of the House of Representatives. Every one of them stated that they were able through their larger organizations to keep business at home that had before been forced to New York or Chicago. As Mr. Deckor phrased it "We are tired of having the cow fed in Minnesota and milked in New York."

Much interesting information was brought out in these hearings before the Banking and Currency Committee of the House of Representatives on the general subject of branch, group and chain banking. The hearings were the result of the recommendations made by the Comptroller of the Currency in his annual report, and his interesting and very able statement was heard first. When he had presented all his facts and recommendations it seemed to me that there was evidence of considerable change of opinion on the part of several of the members of the Committee, and as the hearings progressed it became evident that there was a rather general feeling that some extension of branch banking would be advisable. Almost all the witnesses, including some of those who came to oppose branch banking, admitted under questioning that there were some places where branches would serve better than small separate corporations. Mr. A. J. Viegel, Banking Superintendent of the State of Minnesota, in a recent statement, mentioned 154 places in that state which previously had supported banks where there are now no banking accommodations whatever, principally because of failures. About one-half of them he said should have some kind of banking service, but he said he could see no way of safely serving them except through branches.

There was much interesting testimony from the representatives of the new group banking organizations in Minneapolis and St. Paul, in Detroit and in

Buffalo. Mr. Decker and Mr. Wakefield who head the two leading group banking organizations in Minneapolis and St. Paul, controlling banks in a territory where failures have been numerous and disastrous, presented rather convincing arguments that their group systems have served a very useful purpose. Both of them denied that they would convert their group banks into branch banks if authority were given them to do so, but they both admitted that their groups included only rather sizeable banks located in rather sizeable towns, and that it would be an advantage if their banks could have branches in the smaller places not now touched by them. Mr. Lord of the Guardian-Detroit group made similar statements, but was rather more willing to admit that branch banking would be more economical and might give better service. With few exceptions the banks in his group are located in cities not smaller than 10,000. Several of the group bankers admitted that if branch banking superseded group banking it would probably result in lower interest rates in the smaller group towns. All of them, however, declared that the banks in their combinations were independent units, each managed by its own local board of directors and each retaining its local pride, even though the stock of the local banks is all owned by holding companies. All thought the group system had some marked advantages, by comparison with branch banking. In the case of all of these new group banking systems the stock of the local banks has been exchanged for stock in the holding companies, so that the old stockholders may be said to retain an interest in their own banks and to have acquired an interest in all the other banks of the group. Mr. Wakefield of the First Bank Stock Corporation said that his group had started to buy control of banks for cash, but had found that did not work well. People were unwilling to sell for cash but were willing to exchange their stock for stock in the larger corporation. In the Guardian-Detroit group, the holding company stock carries double liability, just as bank stock does.

This system of group banking is new and is certainly different from what has been known for many years as "chain banking" where one man or a group of men have purchased for cash the control of a number of banks. As conducted in the Minneapolis-St. Paul district, in the Detroit district and by the Marine-Midland group of Buffalo, the groups bear a very strong resemblance to branch banking. The men representing them all declared that no single bank in the system could or would be allowed to fail. They declared also that if any individual or industry in any community had need for loans larger than the loaning limit of the local group bank of the community such loans would be taken care of within the group. I agree with Comptroller Pole that this development of group banking should not be checked by law unless something better can be substituted for it. We pass too many restrictive laws. What we want now is something constructive.

This kind of group banking not only resembles branch banking, but probably would have been called branch banking in the days of the old state banks before the Civil War. One of the model branch banking organizations of that period was the Bank of Indiana, of which Hugh McCulloch who became the first Comptroller of the Currency was the president. If you look into the history and structure of the old Bank of Indiana you will find that its branches were pretty nearly independent. As originally organized, the Bank of Indiana was not much more than a board of directors, appointed by the Legislature, with certain supervisory and directory powers, while the branches were independently organized banks with separate stock. The Bank of

Ohio was also a group of pretty nearly independent banks bound together under a modification of the New York safety fund principle. In those days, of course, the emphasis was on giving security to note issues, but the principles are the same when applied to security for deposits. Deposit banking was something which grew up in the cities and was not much understood for a long time outside of the cities. The notion that depositors did not need any special protection persisted for many years after the National Banking Act was passed, and Mr. Thomas P. Kane in his book "The Romance and Tragedy of Banking," published in 1922, declared that with all the numerous amendments of the National Banking Act passed since 1864 not one "can be said to have had for its object the increase of the security of depositors in national banks" until the Federal Reserve Act was passed.

The resemblance of the group banks of today to the branch banks of the days before the Civil War suggests that with proper legal recognition and direction they might be developed into branch banking institutions somewhat of the old type - the branches retaining a considerable amount of independence, but being jointly responsible for the debts of every branch in the group as was the case in the old Bank of Indiana, and each group supervised and in a measure controlled by a central board of directors, under governmental supervision. Possibly such a system of branch banking - a sort of compromise between group and branch banking - would meet the chief objection of many of the ardent opponents of branch banking. I mention this merely as a possibility, and without much confidence that such systems would take care of the very small towns where most of the banking failures occur. It should serve to bring to mind that branch banking need not necessarily be of one pattern. Branch banking can be organized so as to give the branches a certain amount of independence, and can be organized without any "parent bank" - simply a group of banks in different places operating under one corporation. The head office, where the directors meet and where the corporation books are kept, need not be a bank. I am not quite sure that there must be a "head office" - at any rate one of the institutions in the South operating two banking offices - banks recently consolidated - maintained in recent letters to the Federal Reserve Board that there was no "parent bank" involved, and no "head office." Therefore, they thought they should be allowed to remain in the Federal Reserve System. I thought so myself but our Counsel could not be convinced.

"Whether you like it or not," said Mr. Decker of Minneapolis in his recent statement to the Banking and Currency Committee, "size is fundamental in many lines of business. It certainly is in the banking business." Now, keeping always in mind the main purpose of making our country banks large enough to take care of a larger share of the local business, some of which now goes to New York, and large enough and with diversification enough to be able to stand up in adverse times, what limits should be set, with relation to capital and to extent or number of branches? Mr. Henry Dawes, former Comptroller represents the extreme position of opposition to branches, but admits the necessity of larger banks. He cites the fact that 88 per cent of the failures of the last nine years have been banks with a capital less than $100,000, and recommends that no banks be chartered in the future with a capital less than $100,000. If I understood his recent statement to the Banking and Currency Committee he would not permit smaller country banks to consolidate so as to obtain the requisite capital, if consolidation involved the maintenance of more than one office, in different places. His idea seemed to be that unless a town or community was large enough to maintain an independent bank with a capital of $100,000 it should depend on the nearest large town - i. e., it should be deprived of convenient banking service. Mr. Dawes took the ground apparently that we must either have nation-wide branch banking, or none at all outside of cities. "It seems to me," he said, "there is no room for compromise on this subject and that a determination should be reached as to whether the United States wishes to embrace a national system of branch banking or to preserve its coordinated independent units. It cannot do both."

I disagree wholly with this dogmatic position. There was more branch banking in the United States 100 years ago, in proportion to population and banking resources, than there is today, and there always has been some branch banking in the United States. In fact there always has been some branch banking in the National Banking System, and I think it can be shown that not quite all of it came in through conversion of state banks. There is no clear evidence that the Congresses of Civil War days in enacting the National Banking Act had any intention of prohibiting branch banking, and I am informed that the Comptroller's office did not finally pass upon the question until 1902. In 1911 Attorney General Wickersham delivered an opinion adverse to branches in the case of the Lowry National Bank of Atlanta, an opinion later much modified by Attorney General Daugherty who Oct. 3, 1923, found in favor of additional offices within city limits. The matter was never definitely decided by the Supreme Court, the St. Louis case in 1924 having turned on enforcement of a state law. Now and then National banks opened outside offices and sometimes they withstood the Comptroller's criticisms for a considerable period. The Citizens National

Bank of Newport, New Hampshire, was given a certificate by the Comptroller on March 27th last for the operation of a branch at Warner, in an adjoining county, on the ground that the branch had been operated for the past 25 years. There are today (April 8th figures) 273 banks in the United States maintaining 570 branches outside so-called city limits without counting California. Twelve of them are National banks maintaining 28 branches. North Carolina heads the list with 34 banks maintaining 66 outside branches. California has two less banks (32) with outside branches, but the number of branches is much greater, 547, of which 313 are branches of National banks. Of the banks maintaining outside branches 52 are in New England, 22 of them in Maine, the Maine banks maintaining 57 branches. The Maine law, permitting branches in the county of the parent bank and any adjoining county seems to me excellent, and the limit it provides would be sufficient, I think in any Eastern state. In Western states where there is much less diversification of industries the limit should doubtless be much wider, perhaps in some districts comprising more than one state.

Branch banking can be limited in any way desired - by territory to be covered, by number of branches to be allowed each bank, or by the size of the places in which branches may be organized. As four-fifths of all bank failures have occurred in places of less than 2,500 inhabitants the law might provide that no more unit banks should be incorporated in places of less size, branches to be authorized instead. There is no reason why we should decide now with relation to what kind of banking may seem desirable to the people fifty or 100 years from now, and no reason why we should not apply a desirable and well proven remedy within limits now because of fear that some future generation may decide to enlarge the limits.

Banks have a common law right to establish branches. This was generally recognized in the early days of our nation's history. In many states they have lost this right through restrictive legislation, some of it not originally intended to prohibit branches. The obvious thing to do is to repeal some of the restrictions and allow some freedom of natural development. I do not believe that there would be any rapid or dangerous development, if the establishment of branches were permitted within trade areas as the Comptroller suggests. I do not believe that any Comptroller would permit a dangerous or a very rapid development, and the history of branch banking where long authorized by state laws seems to indicate (with the single exception of California) that development would proceed slowly anyway. Branch banking is really a country bank proposition. New York and Chicago bankers are generally opposed to it (witness the testimony of Mr. George W. Davison of the Central-Hanover) having learned many years ago that correspondent banking serves them best. As long as the banking units out in the states can be kept comparatively small the biggest and best business must come to the big cities, and the country banks themselves through their correspondent accounts must furnish a large part of the funds with which this business is taken care of. The present system suits Wall Street bankers exactly, and why should they worry over the continued failures of a lot of little banks off somewhere in the distant prairies?

I suggest as the first amendments necessary to remedy the present disgracegul situation with relation to bank failures that national banks be given the same privileges with relation to branches that state banks have, and second that in all states national banks should be permitted to establish branches through consolidations in trade areas, which might well start with the limits of the present Maine law, with discretion to the Comptroller for extension where necessary in order to secure the diversification essential to safety.