THE CRASH OF THE BANK OF UNITED STATES

*Benjamin M. Anderson**

By the fourth quarter of 1930 the trouble with the Bank of United States gave occasion to grave concern.

The Bank of United States was a bank which ought never to have existed, and which certainly ought never to have had the name it had. One leading banker of New York went personally to Albany to protest against the giving of such a name to that bank or to any other bank, and was told that there was a political debt to pay.

In the period 1924 to 1929, with excess reserves and rapid bank expansion, it was easy for plungers and speculators to grow rapidly. There was a heavy discount on sound banking, and a high premium on reckless plunging. One watched it with apprehension, afraid not merely that bankers would lose their judgment but also that in many cases moral standards would crack. In many cases judgment went bad, and in more cases traditional practices, sound and tested, turned out to be bad practices in such an abnormal money markets as then existed. But the great majority of American bankers kept their integrity and tried to adhere to established and approved banking practices. However, it was an era in which the bold speculator and promoter could gain ground rapidly at the expense of the conservative banker, and it was a period in which departures from convention and approved banking practices would seem to be brilliant strokes of genius — while the new era lasted.

The Bank of United States grew very rapidly down to 1929. The name itself meant, as it was designed to mean, to many of the ignorant people of Europe, that this was the national bank, the state bank, the official bank of the United States. Deposits came to it from a great many of those people and from a great many of the ignorant poor on the East Side of New York. And a great deal of business was brought to it, too, by men engaging in speculative activities who could get the desired accommodation from this bank which other banks of New York would not give.

Loans against mortgages were generally looked upon at askance by great New York banks. The first principle of commercial banking is to know "the difference between a bill of exchange and a mortgage". Second mortgages and third mortgages were notoriously improper documents in a bank's portfolio or as a collateral to its loans. But the Bank of United States went in heavily for these. It had an affiliate also — the Bankus Corporation. This was engaged in many yet more questionable transactions, including manipulation of the stock of the bank and loans against the stock of the bank. In addition to the utterly unsound banking practices, there were definitely criminal acts for which the head of the bank subsequently went to prison — not unaccompanied.

When the first mortgages grew shaky, when the second and third mortgages had no market, and when the bank's stock was crashing, the Bank of United States and its affiliate, the Bankus Corporation, were in grave peril. Depositors grew very uneasy and they made heavy withdrawals of funds.

Unsuccessful efforts to save the Bank of United States. The great New York clearinghouse banks, the Federal Reserve bank, and the state superintendent of banking, Joseph A. Broderick (who had no part in giving the name to the bank and whose job was primarily salvage), made strenuous efforts to save the situation. The great clearinghouse banks were prepared, in the interest of preserving the good name of banking in New York, to stand part of the losses. On Monday, November 24, 1930, it was announced that there would be a merger of the Bank of United States with the Manufacturers Trust Company, the Public National Bank & Trust Company, and the Interstate Trust Company, with J. Herbert Case, Federal Reserve agent and chairman of the Board of Directors of the Federal Reserve Bank of New York, as the head of the merger.

This looked like an admirable solution of the problem. The financial community breathed a great sigh of relief when it appeared that J. Herbert Case thought that the situation could be solved in this way. It appeared that the aggregate capital funds of all these banks would suffice to absorb the losses and still leave a strong institution. But the agreement was a contingent agreement, and the other banks were to have time to scrutinize the assets of the Bank of United States. As they did, the merger became impossible. The officials of the other banks and J. Herbert Case could not assume responsibility for such a mess. The problem remained. The clearinghouse continued to work hard upon it.

A conference, lasting beyond midnight, of leading New York bankers sat with superintendent Broderick on the night of December 10 and the early morning of December 11. A plan was worked out by which a wholly new management, under the presidency of the head of one of the small but sound banks of the city, was to take over the Bank of United States with a guaranty of the great clearinghouse banks against loss.

But after this able young president and his associates, accustomed to clean, sound banking, looked at the assets of the Bank of United States, looked at the second and third mortgages, looked at the tangled and involved transactions they would have to deal with, they declined. They just did not know how to do that kind of banking. No other New York bank knew how to do that kind of banking.

And so it came to pass that, on Thursday morning, December 11, 1930, the Bank of United States was closed for good.

Cheap money could not help in a situation like this. To ease the shock and to relieve the plight of the depositors of the bank, the other banks of the city agreed to make loans against deposit accounts in the Bank of United States up to fifty percent of their face value.

With the announcement of the closing of the Bank of United States the stock market plunged still lower. Money remained extraordinarily cheap in this stock market crisis. Call-loan renewal rates ranged from 2 to 2.3 percent between December 13 and December 27. But cheap money could not help in a situation where it was not liquidity but confidence that was vanishing. The stock market reached a wide-open selling climax on Wednesday, December 17. Then, as is usual, it rallied, and the rally carried over through the early months of 1931. But, in the light of developments of the next two years, the American banking system was mortally wounded. By March, 1933, it lay prostrate. One rotten apple can make the entire pile of apples go bad.

---

* Benjamin McAlester Anderson, 1886-1949, author of the posthumously published treatise *Economics and the Public Welfare, A Financial and Economic History of the United States, 1914-46* (Princeton: D.Van Nostrand Co., Inc., 1949; second edition: Indianapolis: Liberty Press, 1979) from which this excerpt was taken, slightly edited by Antal E. Fekete of Gold Standard University.

Editor's comment. Professor Anderson was a distinguished scholar, historian, banker, financier, and economist. As a monetary historian he wrote about a period in which he was not only an astute observer but also a frequent participant.

What lends extraordinary timeliness to his observations about the 1930 banking scene is the now unfolding subprime mortgage crisis that has already metastasized from the United States to the rest of the world. Needless to say, in 1930 the American banks were in a far better shape than they are today when the entire banking system is guilty of unsound practices with which only isolated banks, such as the Bank of United States and the Bankus Corporation, indulged themselves eighty years ago.

Eighty years ago the fancy name of the bank was the lure to entice ignorant people to their doom. Today it is the fancy name of the product: "mortgage-backed securities", "collaterized debt obligations", "securitization of loans" and, most recently, "insuring bonds" that is supposed to do the same trick.

What makes the above reading so frightening is the fact that eighty years ago the credit of the United States was rock-solid. Today it is moth-eaten; the promises of the federal government are hardly worth the paper on which they are printed, in view of its repeated defaults and its embracing of the unconstitutional regime of the irredeemable dollar. Worse still, the credit of other countries is no better, given the fact that it is not backed by anything more solid than the credit of the United States.

Eighty years ago American institutes of higher learning offered the very best available by way of economic and banking knowledge. Today they are a sorry shadow of their former self. They are subject to bribe and blackmail. They are stooges of the banks. There is a gigantic cover-up and distortion of truth, as a consequence of our way of financing advanced studies through grants from the banks, including the twelve Federal Reserve banks, with a hidden agenda to perpetuate the regime of the irredeemable dollar.

If academia is the tamed lion of the banks, then financial journalism is their lapdog.

Eighty years ago one was afraid that moral standards may crack in consequence of questionable banking practices. Today we know that they have. The Bank of United States closed its doors for good on December 11, 1930. But it did not even have off-balance liabilities! Nor did it have *nina* mortgages! (nina = no income, no assets).

It is interesting to watch the Fed trying to meet the present crisis in the same way as it was in 1930: by administering liberal doses of cheap money. In 1930 the Fed made the crisis worse and it prepared the ground for the Great Depression. Cheap money in 1930 certainly did not stop the decline in the stock market.

Ruefully, one can say of the Fed the same what was once famously said of the Bourbons after the restoration of the monarchy in France: "they've learned nothing and forgotten nothing."

January 28, 2008.