"HOPE" AND LINCOLN BANKING HISTORY

by Steve Brown

Since the parallels between President Lincoln and Obama will be stark during today's inauguration ceremonies, we wanted to highlight a little known fact that, when it comes to banking, President Lincoln was one of the founding fathers of modern banking. Since this assertion isn't widely touted and the fact that President Obama may be on a similar restructuring path, let's consider the history.

Back in 1839, a recession was in full swing due to the popping of a land bubble brought on by the expansion of the railway system. Railroad bonds defaulted by the hundreds which caused many banks that held this paper, including the Bank of the United States, to become insolvent. Lincoln, a Senator from Illinois at the time, was a long time proponent of railroad expansion, as well as an advocate for free trade. However, by 1841, he realized to temper his free trade notions in order to balance growth and regulation. The pure free-trade movement did much to restore economic growth and when combined with lower interest rates, resulted in yet another bubble in 1855 that was centered on industrial growth in the North. By 1857, another recession occurred and a bank liquidity crisis ensued.

After Lincoln was elected President in 1860, the anti-nationalists launched secession from the union and a civil war was the result. In order to strengthen the economic backbone of the country, Lincoln disconnected from the gold standard and created a national currency for the first time in order to add liquidity to the system. He then issued Treasury notes in which to help finance the war. Finally, he expanded the railway system to the mid-Atlantic region in order to promote industrialism.

By 1861, Lincoln now developed a "banking problem." Since he was long a proponent of state's rights and state banking, there was a huge push to nationalize banks along the European model. Several banks, such as the Bank of New York, were helping finance the war, but were gaining power at the same time becoming national in scope. In order to control this movement, Lincoln compromised and agreed to formalize the state and national system we have today. Lincoln backed and got passed the National Currency Act and the National Bank Act of 1864.

The legislation established the OCC and made it a requirement for banks to apply for a charter before opening and subject themselves to ongoing regulation. The Bank Act was a composition of the best of banking laws from each state and included minimum capitalization, reserve, credit management, reporting and ownership requirements. The OCC limited interest rates on loans to each state's usury laws (or 7% if no such laws were present). Any bank caught exceeding this interest limit would forfeit the loan and refund to the borrower twice what had been paid in interest. The Bank Act also established the start of what would become the fractional reserve system as banks were required to leave monies on deposit with the Treasury that would then be loaned out to finance the war effort.

Under Lincoln, the banking system was forever changed. While many back then derided the President for over-regulation, history has shown that the combination of banking, trade, agricultural and educational reform enacted under Lincoln, gave the US one of the greatest periods of industrial growth the world has ever seen. Hopefully, President Obama can channel a similar feat.

TARP CPP S-CORP CAPITAL MODEL

We will release our updated TARP capital model for s-corp banks tomorrow. If you would like to receive a copy via e-mail, check back to this space tomorrow to register.

BANK NEWS

Bank Failures

The FDIC closed National Bank of Commerce ($431mm, IL) and Bank of Clark County ($446mm, WA). Deposits in both banks will be assumed by Republic Bank of Chicago and Umpqua Bank, respectively. The demise of both banks were a result of credit quality and concentration issues.

FHLB Pittsburgh

Due to write downs associated with GSE preferred stock and mortgage backed holdings, the Home Loan bank became the latest FHLB to potentially fall below capitalization limits. Since OTTI impairment gets complicated when dealing with FHLB stock, it is unclear if banks that purchased equity will need to take the charge.

FDIC

The Temporary Liquidity Guarantee Program will be extended to insure new senior unsecured bank debt over 10Y (up from 3Y) in an attempt to stimulate consumer lending.

Home Foreclosures

From 2007 to 2008, the states with the most homes in some stage of foreclosure were NV (+7.3%), FL (+4.5%), AZ (+4.5%), CA (+4.0%) and Co (+2.4%). Meanwhile, states with the lowest percentage change were VT (+0.0%), WVA (+0.1%), SD (+0.1%), ND (+0.1%) and MS (+0.2%). Overall, the US average was a +1.8% change.

RDC Update

Celent projects 67% of all banks will have adopted remote deposit capture, deploying slightly more than 350k machines.