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BOOK REVIEWS

John Orbell and Alison Turton, **British Banking: A Guide to Historical Records** (Aldershot: Ashgate, 2001. 674 pp. £55.00)

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This guide to the historical records of the British banking community, published under the auspices of the Business Archives Council in their series *Studies in British Business Archives*, is a magnificent achievement. The authors, supported by a network of relevant bank archivists, local record office staff and librarians, are to be congratulated on their rigour, thoroughness and, above all, their patience, in producing such an attractive, informative and useful guide. The volume is effectively a new edition, substantially expanded and revised, of an earlier much-used volume published in 1985 as *A Guide to the Historical Records of British Banking*, edited by Leslie Pressnell and John Orbell. That guide was a pioneer in collating, contextualising and commenting upon the nature and location of a wide range of historical material extant on British banks and their varied operations. In the intervening years, much new material has been located and the use of bank archives has been extended into new areas, encompassing not only well-established research themes in economic and financial history, but also broader social and cultural questions about business organisation and management. The new guide provides coverage of sources relevant to all these concerns, in addition to expanding the treatment of British overseas banks, merchant banks, discount houses and a range of professional and trade organisations relevant to the banking industry.

The volume begins with a clear and concise introduction to the structure and evolution of the British banking system by John Orbell. This is a vital aid to those new to the field, especially if approaching bank archives as potential sources for historical questions framed outside the specialisms of economic or financial history. Orbell's introductory comments, for example, explain the role of the bill of exchange as the key financial instrument of industrialising Britain, as well as its widespread use in financing international trade via the 'bill on London'. His remaining discussion is organised around the nature and operations of the following institutions within British banking: the Bank of England, the clearing banks in both London and the country, merchant banks, discount houses and overseas banks. In general, these themes are very well handled, although the distinctiveness of the Scottish banking system, particularly during the eighteenth and nineteenth centuries, is somewhat underemphasised. As a guide to *British* banking there was perhaps more scope to draw contrasts between the experience of England and Wales vis-à-

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vis Scotland, particularly the role of Edinburgh and Glasgow as key banking centres and organising nodes for widespread branch networks long before branch banking became common south of the border.

A second introductory essay by both authors outlines in detail the nature of bank archives, paying close attention to the original purposes for which distinct classes of records were created and indicating the range of uses to which such records can now be put. The coverage here is wide, indicating the value of bank archives in addressing the following areas of historical enquiry: business organisation, performance and profitability; employment practices and social welfare; architecture and building management; provision of services to customers at every level, from the individual to large companies and governments. The exposition of these themes is a model of clarity and serves to emphasise to newcomers and established users alike that banking records have a central place in the historical reconstruction and analysis of modern British economy and society. A substantial bibliography, covering individual bank histories and more general works, is also included.

The records themselves are listed from A to Z, ordered by the most recent name by which each particular bank was/is known. Although in general each entry is relatively compact – a necessity with the inclusion of over 700 archive collections – the authors nonetheless manage to convey a strong sense of the place and purpose of each bank within the broader canvas of some four centuries of banking history. Indeed, the brief histories that preface each entry in the guide will no doubt prove one of the most useful and enduring features of the work, allowing those unacquainted with a particular institution to gain a ready summary of its nature as a banking institution, whilst also allowing those designing comparative projects to identify banks with similar historical functions, capital base or geographical location. Brief sources for each historical note are provided where possible, before the listing of the records extant and their location. As the authors admit, significant problems were evident in standardising the record listings between banks, a problem compounded by the different traditions followed between archives and, of course, by the highly uneven survival of historical materials themselves. Despite such problems, the creation of the entries has been handled with great skill and attention to detail. One of the most useful aspects of the new guide lies in the extensive and complementary series of indexes. By listing each entry by company name, place(s) of business, type of bank or association, and archive repository, the immense amount of work that lies behind the production of the guide is easily accessed at the research planning stage.

The guide is expensive, though given its size and comprehensive nature this is perhaps to be expected. In any event, this is one publication that will repay its initial cost time and time again. For students, academics, archivists, local historians and all those who possess an interest in the history of this key sector of the British economy, the guide will prove an indispensable tool in the identification, conceptualisation and prosecution of historical problems within the traditional paradigms of economic and monetary history and beyond.

King's College, London IAIN S. BLACK

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Ben S. Bernanke, **Essays on the Great Depression** (Princeton, NJ: Princeton University Press, 2000. 272 pp. 48 tables, 10 line illus. $37.50)

Elmus Wicker, **The Banking Panics of the Great Depression** (Cambridge: Cambridge University Press, 2000. 192 pp. 5 line diagrams, 45 tables, £11.95)

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The Great Depression continues to intrigue financial, monetary and macroeconomic scholars. The puzzles have been numerous. First, what event, or set of events, was responsible for the worldwide depression? Second, why did the United States Federal Reserve fail to conduct open market operations? Was its failure to do so pernicious; that is, did it contribute to the magnitude of the output contraction? Third, what was the role of the banking panics? Did the panics contribute to the contraction? And fourth, why did the recovery stretch over the entire decade of the 1930s?

Two recently published books, *Essays on the Great Depression* by Ben Bernanke, a recent appointee to the Board of Governors of the Federal Reserve System, and *The Banking Panics of the Great Depression* by Elmus Wicker touch upon all four puzzles. Bernanke's book is a collection of nine essays divided into two parts; one titled 'Money and Financial Markets', the other 'Labor Markets'. Wicker's book, a compilation of two previous studies and two new ones, is more narrowly focused on the four banking panics of the depression.

Bernanke's effort is the more encyclopedic and provides insights into each of the four puzzles. With respect to 'What caused the depression', Bernanke buys into a consensus which has emerged among economic historians that shies away from identifying a particular shock, or collection of shocks, as responsible. Instead, it was the system, namely a design defect in the international gold standard, that transformed a run-of-the-mill recession into a worldwide depression. The defect, discussed in two essays 'The gold standard, deflation, and financial crisis in the Great Depression: an international comparison' and 'Deflation and monetary contraction in the Great Depression', stemmed from an asymmetry in gold standard rules. Gold standard countries typically placed minimum statutory limits on the gold reserves of their central banks but did not place maximum limits. The result was a potential deflationary bias as those countries experiencing an outflow of gold at any point in time would be compelled to accumulate gold in order not to violate the minimum limit, while the inflow countries would be under no analogous compulsion to limit their accumulation. Significantly, this design defect proved of little significance under the classical gold standard of the nineteenth century where a for-profit central bank, the Bank of England, was at the centre. 'The Bank of England of course had to hold enough gold to ensure convertibility, but as a profit-making institution it also had a strong incentive not to hold large stocks of barren gold' (p. 75). In contrast, the Federal Reserve was founded as an explicitly non-profit institution, which had 'little or no incentive to avoid accumulation' (p. 75). And it was this disincentive 'to avoid accumulation' that, according to Bernanke and other

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economic historians, made possible, if not inevitable, the stockpiling of gold by the Fed (and the other key player, the Bank of France) during the early depression years.

The emphasis on a systemic design defect leads naturally into a resolution of the second puzzle. If the Federal Reserve's management was simply responding to the incentives built into the system, then it hardly seems fair to blame them for poor monetary policy. Bernanke's only qualification is in the pre-1931 period when the Fed 'actually managed to convert positive reserve inflows into negative growth in the M1 money stock' (p. 111).

The Fed, at least the Board, also gets off easy in Wicker's analysis of the four banking panics of the Great Depression. Relying on an assortment of newspaper accounts and various banking data series, some of which are self-constructed, Wicker is able to highlight the role of individual banks in key regions that gives a portrait of each panic that is richer than what could be revealed by aggregate data. His finding that each of the panics tended to be regional in origin and scope largely absolves the Fed of any blame. In fact, in Wicker's view, the Fed deserves a fair bit of praise because, prior to the Fed's creation, panics had been triggered by liquidity problems originating in the New York money market. That the New York market operated relatively smoothly during the depression years suggests that the Fed must have been doing something right. In particular, Wicker points to the Fed's success in smoothing the spikes in interest rates that had been such a prominent feature of nineteenth-century panics.

The power of Wicker's micro-approach is perhaps best illustrated in his analysis of the September–October 1931 panic. The conventional story line, forcefully advanced by Friedman and Schwartz, is that Britain's departure from gold in late September triggered an outflow of gold from the United States. The Fed reacted in October by increasing the discount rate in two steps from $\frac{1}{2}$ per cent to $3\frac{1}{2}$ per cent. The rate increase 'was accompanied by a spectacular increase in bank failures and in runs on banks' (Friedman and Schwartz, 1963, p. 317). But Wicker is quick to note that 'To accompany does not imply to cause (p. 93). And a detailed examination of the data on bank suspensions and the hoarding of currency by Federal Reserve District and by state indicates that 'substantial hoarding and increases in bank suspensions occurred *before* the Fed raised the discount rate' (p. 94). So much for the thesis that the Fed's discount policy caused the panic.

In the end, the Fed does not completely escape Wicker's arrows, however. An ideal policy in the late 1931 panic, as well as in the others, would have been for the Fed to purchase enough government securities to restore depositor confidence thereby forestalling bank suspensions. In Wicker's framework, the Fed's failure to do so was more one of omission than of commission. So blame the Fed if you want, but *only a little*.

The most difficult puzzles are the ones seeking to explain the output contraction – its causes, propagation, magnitude and duration. With respect to propagation, one might anticipate substantial agreement between Bernanke and Wicker. After all, Bernanke's bank credit channel thesis (presented in the chapter 'Nonmonetary

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effects of the financial crisis in the propagation of the Great Depression') relies on disruptions to the financial system as an important propagating factor and seems to be in tune with Wicker's focus on panics. But interestingly, Wicker is lukewarm. He refers to Bernanke's work on only two occasions and concludes that evidence for the credit thesis is highly ambivalent.

The second half of Bernanke's book, five chapters devoted to 'Labor Markets', sheds considerable light on the issue of why it took a decade for the United States' economy to recover from the depression. At the heart of several chapters is a measure of work effort as the product of the average workweek and employment. During the 1930s the American economy relied heavily on shorter workweeks as a way of reducing labour input, due primarily to New Deal pro-union legislation. One implication, supported by the 1930s data, is that the real wage will tend to be countercyclical – rising during economic slowdowns. Since union-induced high wages are normally associated with decreased aggregate output supply, one might think that Bernanke would use his finding to argue that the New Deal was responsible for prolonging the recovery from the Depression. Indeed, Harold Cole and Lee Ohanian recently have advanced this provocative thesis in a series of articles. But surprisingly, Bernanke comes to the opposite conclusion. The New Deal 'was a period of economic growth … with a real wage *push* engineered in part by the government and the unions' (p. 253). The higher wages 'to some extent *paid for themselves* through increased productivity of labor' (p. 253). Let us just say that we have not heard the last word on the New Deal debate.

My overall assessment: these books are powerhouses. Bernanke is the master of applied macroeconomics. Not only is he technically proficient but his ability to place his results in a larger macroeconomic context is unparalleled. In contrast to Bernanke's technical virtuosity, Wicker's style is to undertake painstaking searches of the data and then present them in simple tabular form. It is amazing how much Wicker is able to deduce from an unadulterated presentation of the 'facts'. His careful narrative overturned much of what I 'knew' – for example, that discount rate increases triggered the late 1931 panic – about the depression-era panics. The many hours I spent with Bernanke and Wicker were pleasurable and intellectually rewarding.

University of Kentucky MARK TOMA

Gerard Caprio, Patrick Honohan and Joseph E. Stiglitz (eds), **Financial Liberalization. How Far, How Fast?** (Cambridge: Cambridge University Press, 2001. 318 pp. £35.00)

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The book consists of three parts. The first, 'Analytics', comprises two essays by Caprio, Hanson and Honohan and Honohan and Stiglitz. The second presents empirical work based on cross-country econometrics. The third entails several case studies of financial liberalisations.

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The analytical essay reviews briefly the reasons for, and against, financial liberalisations, arguing that financial liberalisation is always better than financial repression for the reasons already explained by McKinnon, Levine and others. The question that this book addresses is why, though financial liberalisation is the best choice in theory, in practice its implementation often precedes violent and disruptive crises. The reasons for these undesired events must be searched for in the particular circumstances of implementation, which differ from country to country. The case studies must make clear these circumstances. The reasons why history may diverge from the established theory are not new: poor sequencing of liberalisation measures; macroeconomic imbalances that were not solved before the financial liberalisations were implemented; bad regulation; and an insufficient institutional legal framework. Notwithstanding all this, Caprio, Hanson and Honohan argue that the case for liberalisation of interest rates is much more compelling than that for its fixing, although the liberalisation must be undertaken with some caution. They write: 'Having a substantially liberalized financial system is clearly the only viable way forward for any country that wants to participate fully in the benefits of economic growth' (p. 28). Removal of controls, for example, may be slow rather than rapid under some circumstances.

Honohan and Stiglitz, in the second essay within the same section, argue strongly for fixing rates on deposits, which would induce bank managers to behave in a less risky way when deciding about the composition of their portfolios. They distinguish between financial repression and financial restraint. Financial restraint, however, may include among its tools some 'price (interest rate) controls'. This control should not be used as it has been done in the past to achieve economic goals but only to achieve prudential goals (see Honohan and Stiglitz, p. 53). Whatever the goal pursued by fixing the rates, if the policy advice is to fix them, financial liberalisation should not be implemented. The authors (one of them common to both essays) do not seem to be aware of the contradiction.

In the cross-country studies, Honohan concludes that 'there is evidence for an increase in the general level of real interest rates as financial liberalization progressed, and this increase was more pronounced than the contemporaneous increase in industrial country rates' (p. 53). This appears to be one of the most important contributions of the book. Demirguc-Kunt and Detragiache find the probability of a crisis following liberalisation higher when regulation is weak and the institutional structure is inadequate.

The case studies deal with particular episodes of financial liberalisation in postwar Europe, South Korea, Mexico, Russia, India and Indonesia, and Uganda. In chapter six, Cho sees the reasons for the failure of South Korea's financial liberalisation process in the bad sequencing of the liberalisation of interest rates, implemented in various phases and which allowed short-term rates on deposits to be free whereas long-term rates remained subject to regulation. This, in turn, led to firms' debt structures to become short term. The expansion of the market for commercial paper, a result of the very high short-term interest on these instruments, contrib-

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uted, in his interpretation, to excess investment by firms because depositors' (presumably households') money placed in trust accounts by banks was used to rediscount commercial paper which, in turn, was used to finance risky investments by chaebol. What is missing here is the role played by the accumulation of assets within the corporate non-financial sector in the expansion of the commercial paper market. As a matter of fact, business sector deposits held in trust accounts rose from 5,819b. won in 1992 to 54,977b. won in 1997 (Bank of Korea, Flows of Funds, Total of financial transactions). Given the growth of the commercial paper market to about 70,000b. won in 1997, the contribution of corporate investment to the expansion of this market appears evident. It was both the securitisation of debts and a financial structure with many layers, rather than just the short-term nature of the debt contracts, which increased the correlation of default risk, thus making the environment more fragile and causing a rapid spreading of the crisis.

The failure of Mexico's financial liberalisation was instead due, according to the authors, to macroeconomic circumstances accompanying the process, which saw a substantial increase in spreads and a rather inefficient privatisation. These elements notwithstanding, the major responsibility for the failure of this experiment is to be found in macroeconomic instability, inflation and external imbalance. The authors do not take up the issue of whether financial liberalisation itself might have contributed to macroeconomic instability. High spreads in a country where most firms still rely mainly on bank debt as a source of finance might have fuelled inflation through the formation of prices by mark-up over costs. The boom in consumption and imports could have been fuelled by a change in the distribution of income favouring the wealthy, who could enjoy higher rents in the financial sector.

The Russian case is still more compelling as a failure since liberalisation not only failed to give all the benefits promised by theory, such as financial deepening, increase in efficiency and growth, but in practice destroyed the whole monetary economy with exchange significantly based on barter. The fault lay again in the way liberalisation was implemented, particularly in excessively low barriers to entry into the financial sector and the lack of an adequate institutional background.

The chapter devoted to the experiences of Indonesia and India describes these two experiments as partly successful, though the efficiency of the financial sectors has not greatly increased and the practice of directed credits has survived in both cases. The reason why they are considered half-successful cases, I presume, is that these financial liberalisations were accompanied by a good (or not so bad) record in output growth. Even in these cases, as in the preceding ones, the nexus, this time favourable, between the financial liberalisation and the macroeconomic scenario is not clear.

As a nice surprise to the reader who reads to the end, one successful case is presented: Uganda. Unfortunately, this shows all the bad signs that the reader has already become familiar with from the previous studies: high real interest rates; high segmentation in financial markets; and persistence of directed credits and rents. As in the other cases, success is attributed to macroeconomic performance *after* financial

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liberalisation. At the end a doubt arises: is it consistent to justify failures and successes alike by resorting to macroeconomic circumstances? If it were so, then one should conclude that financial liberalisation does not matter at all. In particular, it does not become clear whether the macroeconomic circumstances that made the realized liberalisations unsuccessful, or successful, were exogenous events or consequences of the liberalisation measures themselves.

The empirical part makes clear that the consequence of liberalisations has everywhere been high real interest rates. Starting from this point, the essays do not explain how this has contributed to the occurrence of crises and instead refer to often cited specific circumstances, such as bad sequencing; insufficient or bad regulation; or macroeconomic imbalances, to show why history does not agree with theory in matters of financial liberalisation. The finding of the empirical part – that everywhere real interest rates have risen – could have offered a clue to link the analysis with the book's historical parts, but this route has not been followed. The reason might be that the increase in interest rates is considered either, according to the neoclassical perspective, for its effect on planned investment or, according to the monetarist perspective, on expected and actual inflation, never as affecting the distribution of income and power among interest groups.

On the whole the book offers valuable contributions to the history of financial liberalisations in many countries. It also finds that most liberalisations undertaken have been unsuccessful. It fails, however, to give convincing reasons as to why this has happened, apart from the so often mentioned macroeconomic circumstances or institutional deficiencies.

University of Macerata, Italy DOMENICA TROPEANO

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