Lessons from the History of U.S. Banking and Regulation

Since inception, commercial banking in the United States has been regulated. It began at the state level, progressively moved to the national level and then to increasing amounts of regulation at both the state and national level. Along with a steady growth in regulation has been the steady growth in the federal safety net. Yet, as this book clearly illustrates, banking has also become increasingly unstable over time. Indeed, perhaps the most stable time in banking history was the minimally regulated antebellum era; there were far fewer failures and crises were not systemic but, rather, largely isolated. Certainly, the world we live in today is much different from the antebellum era but we still must reconcile how banking has become both more regulated and more unstable. This chapter attempts to offer an explanation through the lens of history.

More specifically, this chapter first considers the evolution of increasing regulation and the tendency to increasingly rely on regulation as the response to each crisis. This is accomplished by comparing the nature of regulation from the antebellum era to the present. Second, a similar consideration is given to the increasing federal safety net in commercial banking. Third, this chapter attempts to shed some light on why, over time, there has been an increased appetite for regulatory responses to crises. Fourth, using the historical evidence from earlier chapters, this chapter illustrates the trend of increasing fragility in commercial banking and also offers a way to understand why the instability is increasing. Finally, this chapter offers a few closing thoughts on the implications for the future of commercial banking, given the tendency towards regulation induced instability in banking markets.
Increasing regulation throughout history

Since the antebellum era, there has been a significant growth in the scope of banking regulation. What began as state regulated enterprises are now regulated by multiple agencies that are at the state and/or federal level depending on the nature of the bank charter. Figure 8.1 illustrates the real expenditures federal regulators devoted to finance and banking regulation over the past 50 years. While expenditures do not always correlate with influence, it is interesting to note that since 1990, expenditures increased 45.5 percent and since 2000 they have risen over 18 percent.1 Though there is not similar data for earlier periods, it is obvious that bank regulation has been expanding since the origin of U.S. banking almost 230 years ago.

Analysis across all periods

A more precise picture of the expansion of bank regulation is captured by comparing the summary regulation tables from Chapters 3 through 7 (Tables 3.3, 4.12, 5.13, 6.4, and 7.4). These tables provide a brief summary of the significant regulation for each banking era. As it was rare for deregulation to take place, one may largely think of these tables

Figure 8.1  Real Spending on Federal Finance and Banking Regulation: 1960–2010

Note: In millions of 2000 dollars. 2010 value estimated.