Chronological Overview

Chapter One -- Pre-FDIC

On average, more than 600 banks failed each year between 1921 and 1929. Those failures led to the end of many state deposit insurance programs. The failed banks were primarily small, rural banks, and people in metropolitan areas were generally unconcerned. Investors and other businessmen thought that the failing institutions were weak and badly managed and that those failures served to strengthen the banking system. A major wave of bank failures during the last few months of 1930 triggered widespread attempts to convert deposits to cash. Confidence in the banking system began to erode, and bank runs became more common. In all, 1,350 banks suspended operations during 1930. Some simply closed their doors due to financial difficulties, while others were placed into receivership.

As liquidity pressures eased during the early months of 1931, the number of bank failures declined sharply. Unfortunately, that decrease was short-lived. Great Britain abandoned the gold standard in September 1931, and some depositors feared that other countries might follow suit. Foreigners with bank accounts in the United States rushed to convert deposits to gold, primarily in the New York money market. The effect was a liquidity crisis that caused the failure of 2,293 banks in 1931, or nearly four times the average annual number of failures during the 1920s. Losses incurred by depositors in 1931 ($390.5 million) exceeded losses incurred by depositors for the entire six-year period between 1921 and 1926 ($383.6 million.)

Congress created the Reconstruction Finance Corporation (RFC) in January 1932, and on February 27, 1932, passed the Glass-Steagall Act. Those two pieces of legislation led to the beginning of an improvement in the banking situation. In the months that followed passage of the legislation, both the number of bank failures and the amount of depositor losses dropped significantly. Failures during 1932 declined to 1,453, and losses to depositors in that year were half those of 1931.

During the winter of 1932 and through 1933, banking conditions again deteriorated rapidly. Although it is probably not possible to point to a single factor that caused the calamitous events of that period, general uncertainty with respect to monetary and banking conditions undoubtedly played a major role. In states that had declared bank moratoriums, banks accelerated withdrawals from correspondents in an attempt to strengthen their positions. Currency holdings increased significantly, partially in anticipation of additional bank moratoriums.

Franklin D. Roosevelt was elected president in November 1932, and rumors circulated that his administration would devalue the dollar. Concerns about the future of the dollar created even greater liquidity pressures. Banks increased speculative holdings of foreign currencies, gold, and gold certificates. That period was unlike the one a year earlier of international monetary instability and conversion of foreign deposits to gold caused by Great Britain's abandonment of the gold standard.

This time many of the conversions to gold from deposits and Federal Reserve Notes came from domestic sources. Those demands placed considerable strain on New York City banks and, ultimately, on the Federal Reserve Bank of New York.

Sudden withdrawal demands in certain parts of the country started a panic of massive proportions. State after state declared bank holidays.[1-1] The panic reached a peak during the first three days of March 1933 following the failure of an estimated 4,000 banks so far that year. As one of his first official acts, President Roosevelt proclaimed a nationwide bank holiday beginning on March 6, 1933, which lasted four days. The financial system was on the verge of collapse, and both the manufacturing and agricultural sectors were operating at a fraction of capacity. Administration officials quickly began to draft legislation designed to resolve the banking crisis.

The Emergency Banking Act legalized the national bank holiday and set standards for the reopening of banks after the holiday. That act expanded the RFC's powers as a means to deal with the crisis then threatening the banking system. It authorized the RFC to invest in the preferred stock and capital notes of banks and to make secured loans to individual banks. The President subsequently issued a proclamation extending the holiday in order to allow time for officials to reopen the banks. Several hundred banks soon reopened for business. As the reopenings proceeded, public confidence increased significantly and widespread hoarding ceased.

President Roosevelt signed the Banking Act of 1933 on June 16 of that year. Section 8 of that legislation amended the Federal Reserve Act to create the Federal Deposit Insurance Corporation. A temporary plan for deposit insurance began for 13,201 banks on January 1, 1934, with coverage of deposits up to $2,500. Coverage was increased on July 1, 1934, to $5,000 for each depositor in an insured institution.

The Banking Act of 1935 terminated the temporary federal deposit insurance plan and inaugurated a permanent plan. It revised the entire deposit insurance law and made substantial changes in the plan for deposit insurance originally enacted on June 16, 1933. Table 1.1 shows all commercial bank suspensions from 1921 through 1933.

[1-1] The term "holiday" was used to imply a break in banking operations. Banks were closed for the entire day on each day that a holiday was declared.

Table 1-1

Commercial Bank Suspensions
1921 - 1933
($ in Thousands)

Year	Number of Suspensions	Deposits ($)	Losses Borne by Depositors ($)	Losses to Depositors as % of Deposits in All Suspended Banks	Losses to Depositors as % of Deposits in All Comm. Banks
1921	506	172,806	59,967	34.70	0.21
1922	366	91,182	38,223	41.92	0.13
1923	646	149,601	62,142	41.54	0.19
1924	775	210,150	79,381	37.77	0.23
1925	617	166,937	60,799	36.42	0.16
1926	975	260,153	83,066	31.93	0.21
1927	669	199,332	60,681	30.44	0.15
1928	498	142,386	43,813	30.77	0.10
1929	659	230,643	76,659	33.24	0.18
1930	1,350	837,096	237,359	28.36	0.57
1931	2,293	1,690,232	390,476	23.10	1.01
1932	1,453	706,187	168,302	23.83	0.57
1933	4,000*	3,596,708	540,396	15.02	2.15
Total	14,807*	$8,453,413	$1,901,264	22.49	

*Estimate.

Source: Federal Deposit Insurance Corporation: The First Fifty Years.