CANADIAN BANKING PRACTICE.

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XXIX.

It will be interesting to trace the working of this part of the banking machinery. There are various kinds of drafts. The simplest of all is that wherein the bank draws on one of its branches. Even in these the profit made is not by any means uniform. There are a number of things that enter into the calculations.

The extent of the actual profit made by the bank, apart from the commission charged, depends, first, on the nature of consideration given by the purchaser for the draft. He may give a cheque on a standing deposit of his, in which case the effect of the draft is to redeem a deposit liability. He may give a cheque on, or notes of, another bank in town, in which case the bank is put to no expense in collecting them. He may give the bank's own notes, his payment saving it to that extent from the expense of bringing in its notes for counter purposes, in which case there is a collateral profit to be added to the commission charged on the draft.

He may give sundry bank notes, in which case there is an expense involved in shipping them away, and the actual profit is reduced by that extent. He may give a cheque on an outside point, itself subject to a commission charge, in which case it sometimes happens that double commission is received and no actual transfer of funds takes place. He may discount a note, in which case the draft is the form in which the bank makes the advance.

Profits Vary According to Method of Payment.

Then the profits are affected by the manner in which payment is made for the draft by the branch at the other end. Does the payee deposit the amount to his credit? Then the bank holds the funds. The transaction as a whole results in no loss of deposits, but, perhaps, a gain. It may result in the bank's lending money at 7 per cent., or higher, the proceeds going on deposit at 3 per cent. Does the payee present the draft at the counter, demanding cash? Then the bank gains in circulation, for it pays out its own notes. This circulation will be bad, indifferent, or good, according to the length of time the notes remain outstanding. Does the draft come in through another bank? Then it has to be settled for in legals or hard cash.

Another factor affecting the profits is found in whether the general trend of currency is towards or away from the two branches directly concerned in the transaction—the drawer branch and the drawee branch. Usually the transaction is most profitable when the transfer is made in the direction contrary to the general trend of currency, and least profitable when made in the same direction as the general trend.

To illustrate: Take two branches, A and B. A uses more currency than it receives, and is constantly shipping it in. B receives more than it uses, and is constantly shipping out. If A were to issue a draft on B, the transfer would be made contrary to the general trend. A would probably receive currency from the purchaser of the draft, lessening the amount it would require to ship in. B would pay out currency, lessening the amount it would require to ship away. Expenses might be reduced at both ends. On the contrary, if B were to draw on A, the expenses might be increased at both ends.

Payment in Big Settling Centres.

Another point to be borne in mind is that, no matter what branch may be drawn upon, payment will, in most cases, be made, ultimately, by a branch in one or other of the big settling centres, Montreal, Toronto, Winnipeg. The practice of the banks in the small places is to settle their differences by drafts on these places; and that means that everything between banks, practically, is settled and paid for in the big cities. That is one reason why the supply of "legals" and gold is concentrated at the central branches.

But, though all these things enter into the profit and loss calculation when a draft is sold, the bank cannot allow for them in its negotiating with the customers. To be on the safe side it must assume that the funds will have to be transferred in every case to the branch on which the draft is drawn. The collateral gains and losses have to be taken as they come. One of the results of over-competition in banking is a tendency among the banks to forego or reduce their commissions on remittances, transfers, and drafts, with the idea that the collateral or extra profits will suffice to bring them out on the right side.

At the best, this is a haphazard kind of banking. It is a real service the banks do for their customers when they collect for them moneys payable in other places, and when they make payments on their customers' behalf in the sundry cities and towns where the customers have payments to make. Because the banks are able to make a great many of these collections and payments at little or no cost is no reason why they should perform the services without charge.

Benefit of Branch System.

Their ability to perform them economically is very largely due to the establishment of complete systems of branches and the gathering together of large volumes of business, wherein it happens every day that many debit and credit transfers offset each other. It would certainly seem that the bank stockholders were properly entitled to a considerable share of the benefits resulting therefrom.

It quite frequently happens that customers desire to get drafts on points where the bank has no branches. If other banks are represented in these places it is open to the bank to use them. It may be that there is represented another bank with which the bank has a general arrangement for the reciprocal encashment of each other's drafts at par. In that case the draft is drawn on an agreed-upon branch, and across the end is written a request for the other bank to pay it at par.

Drafts Payable at Other Banks.

If there is no bank at a point whereon a draft is wanted, with which a reciprocal arrangement is running, all that can be done is to add to the amount which the customer wishes to remit ten cents or thirteen cents, or 1-10 or 1/8 per cent, and to request one of the banks located there to cash it less that commission. In the first case the bank retains the whole of the commission received from the customer, but pays the other bank through extending par facilities to all of its branches; in the second, it divides up the commission with the other bank, or makes an extra charge on the customer buying the draft. It has been found in practice that the real cost to the bank is about the same in both instances.

Another form of drawing is when the draft is drawn on a bank with which the bank maintains a running balance. Then the bank occupies the same relation to the drawee bank as its own customers occupy towards itself. These accounts or balances with other banks are generally on the basis of quid pro quo. The one institution maintains a balance with the other, or pays it in some other way, for the privilege of drawing at par on a complete set of branches.

New York and Foreign Exchange.

When a customer desires to remit money to some place in the United States, the bank can meet him by giving him a draft on New York. As New York is the great settling and reserve centre of the United States, the banks in practically all the cities, towns, and villages keep accounts with one or more New York banks. Thus it has become the practice for banks practically all over the Union to pay New York drafts at par.