CHANGING THE U. S. BANKING SYSTEM.

The newly organized Federal reserve banks of the United States and the Federal Reserve Bank at Washington have begun operations this week. Much is expected from the new departure in the way of improvement of the U. S. banking system, but there is to be no haste or pressure for the full exercise of the functions of the new system. It starts with a partial deposit of the capital of the reserve banks, which is to be held by the member banks in each case in proportion to their own capitalization. This produces a capital fund of about $3,300,000 in the New York institution and $18,000,000 or so in the reserve banks of the twelve districts, out of an authorized amount of over $106,000,000. Another installment will be paid in at the beginning of February after which the residue will be subject to call at intervals up to 6 per cent. of the capital and surplus of the members. This will be determined by what may prove to be the needs of the situation, and it is anticipated that the full amount may not be required. Next comes the transfer of a part of the reserves of the member banks to the reserve institutions in proportions which have already been made familiar. This will provide a fund for the discount and currency operations of the system which are expected to get into effect at once and increase in volume as it gets settled down to regular working. Three years will be required for a complete adjustment to the new reserve basis.

GREATER MOBILITY.

One of the most useful results of the transition from the old system to the new, and one which will be immediately availed of, is that of giving greater mobility to one of the chief assets of sound banking, the commercial paper held as security for current business loans. This as defined and prescribed will have a character of practically assured safety. At first this paper, offered by member banks for rediscount by the reserve banks, may be deposited with the reserve agents and count as one-half the reserve to be there deposited. This is one of the features of operation that it is thought should be conducted with care, as it will in itself be a substitution of credit for cash in reserves and it is doubtful how far it should be carried. Weakening reserves by mingling cash and credit and making the former do double duty is a questionable policy at best. Of this discounting and rediscounting process much is expected in the way of facilitating exchange operations in domestic trade.

ELASTIC CURRENCY.

Another feature of the new system of which much is expected is that of applying an elastic element in the circulating currency of the country. The bond-secured bank notes will remain for a long time as the main body of the credit currency, but they will be gradually diminished in volume while the requirement for such currency is likely to increase. The result will be an elastic margin of the new Federal reserve notes, which will expand and contract according to the requirements of business, as they may be issued in the rediscount of commercial paper, which must be deposited as security and will be constantly maturing and being replaced, and must be redeemed in gold coin on demand, a reserve of 40 per cent. being held for the purpose, and the Government credit also standing behind the notes with an obligation of final redemption in gold. There is no reason to apprehend that this will not be an entirely safe as well as useful credit currency. It will be especially useful in meeting the fluctuating requirements of the "crop-moving season." Provision is made that after two years from the passage of the reserve act the reserve banks may begin a process of taking over bonds deposited to secure issues of national bank notes and replacing these with their own notes. This is expected to go on for about thirty years while the bonds are maturing, after which the member banks will cease having circulating notes of their own.

Among other useful functions which the new banking system is expected to exercise is that of facilitating foreign exchange by dealing in acceptances and bills of exchange based upon export and import transactions.

ON THE ROAD TO RUIN.

It appears that the total issues of new currency and bank money in Germany during August and September, to avoid a technical moratorium and to make possible the Government loan, amounted to at least $1,100,000,000. The depreciation of the Reichsbank note in neutral money markets is of course to be attributed to this inflation, which has been accompanied by a suspension of specie payments. Though the depreciation has not yet reached a serious figure it is hardly open to question that the German Government, by adopting the policy of a forced issue of legal tender, has entered upon a path which, if long enough pursued, says an American authority, must wreck the whole fabric of German finance and credit. That the Allies have abstained from resort to any similar expedient gives their economic position an enormous superiority over that of Germany. All the combatants must go on spending vast sums, and the vital question is which can last longest at that game. It was the judgment of the British Chancellor of the Exchequer, Mr. Lloyd George, that the last few hundred million might win this war. "The first hundred millions our enemies could stand just as well as we could, but the last they could not." Considering the paralysis of Germany's foreign trade, the consequent closing of factories and workshops tributary to that trade, and the drying up of the revenue which it yielded to the Government, there is no denying the fact that for the economic struggle of the war Germany is less adequately prepared than her adversaries.

DOUBLE THE RATE OF INTEREST.

Professor J. S. Nicholson says that, "the difference between the German and the British banking systems is shown by the rates at which the two Governments have been able to issue their loans, the German rate being very much higher than the British. Not only is this the case, but the German loan, being received in depreciated paper, adds so much to the real cost.

"Taking everything into account, it seems likely that the money borrowed by Germany during the first six months of the war will require double the rate of interest paid by the British Government. This high rate of interest in Germany means so far a relative breakdown in public and banking credit. As the war progresses the higher command of the money power will begin to be alarmed, and the lower commands of the money power will begin to feel the pressure of diminished resources."