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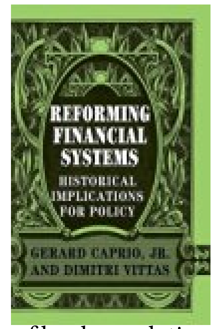
in the Humanities & Social Sciences

Gerald Caprio, Jr., Dimitri Vittas, eds. *Reforming Financial Systems: Historical Implications for Policy.* New York: Cambridge University Press, 1997. x + 222 pp. $49.95 (cloth), ISBN 978-0-521-58115-8.



Reviewed by Michael Haupert (University of Wisconsin-La Crosse)
Published on EH.Net (December, 1997)

Reforming Financial Systems is a volume of collected papers presented at a 1994 seminar entitled "Financial History: Lessons of the Past for Reformers of the Present." The essays in this volume address a number of interesting questions that have long challenged financial historians. Any student of financial history will find at least one essay of interest in this volume.

The essays are contributed by leading scholars in the field, and the topics cover a wide geographical and historical canvas, encompassing a variety of financial systems and topics. They range from broad, historical overviews, such as the Forrest Capie piece on the evolution of central banking, to the more specific, such as Randall Kroszner's discussion of free banking in Scotland as a model for emerging economies. All of the essays are fairly brief, thus they are not in-depth studies of the topic which they address, but they do serve as nice overviews of various topics, and all include useful bibliographies from which an interested reader can proceed. As a result, the book would serve well as a supplementary textbook in a financial history course.

The essays can be divided into three categories: general topics in banking, country-specific examples of financial institutions, and comparative studies. The first category includes the aforementioned Capie essay and one by Anthony Saunders and Berry Wilson on contingent liability banking. The second includes the Kroszner essay, Frank Packer's historical overview of the prewar Japanese banking system, Sam Williamson's study of the development of industrial pensions in twentieth century America, a case study of the U.S. securities market by Richard Sylla, and an historical overview of deposit insurance in the United States by Eugene White. The final category includes comparative studies of bank regulation in Canada and the United States by Michael Bordo, thrifts in the United States and Europe by Dimitri Vittas, and a look at universal banking in Germany and the United States by Charles Calomiris.

In their introductory chapter, the authors nicely synthesize the lessons to be learned from each of the essays. While covering a diverse selection of topics and geographical regions, they do have a common theme. They stress two general lessons for contemporary government authorities and financial reformers: diversification and proper incentives. Regulators and overseers need to insure in some way that financial institutions diversify their risks. As the editors correctly note, most banks–and banking systems–encounter solvency problems because they fail to diversify. While it seems rather obvious to students of financial history, officials focusing on short-run performance can overlook this important fact.

The essays in this volume illustrate the numerous methods of ensuring diversification that have been employed throughout history, ranging from competitive banking to unlimited liability to branch banking to holdings of international assets. What works in one banking environment will not necessarily work as well in another, a truism as far as historians are concerned but a point not always appreciated by contemporary policy-makers. The point emphasized by the authors in this volume is that while the options are diverse, the lesson is straightforward: diversify.

Creating incentive systems that will induce proper behavior by bankers as well as depositors is the second general lesson extolled in these essays. Again, a wide variety of incentive systems have been employed throughout history. This seems to indicate that just about anything can work–as long as it is properly employed. However, a word of caution to contemporary policy-makers is provided by the editors when they point out that "the temptation to draw lessons from history can be overdone. Sometimes history does not teach clear lessons, or stated differently, one has to be extremely careful in applying the so-called lessons ... a better acquaintance with history is a necessary ingredient in this endeavor" (p. 3).

Each essay is followed by a transcript of the discussion that followed each paper presentation. I did not find these discussion summaries particularly enlightening. The transcripts are poor substitutes for actual participation in the discussion and do not add much to the papers they follow. This, however, is a minor quibble, since you can always skip them. I think their main value is to serve as a memory jog to those who were at the conference but did not take notes during the discussions.

Perhaps the most important and enduring lesson these authors offer contemporary policy-makers is that reform takes time. This advice is directed specifically to central bankers by Forrest Capie in his essay on the evolution of central banks, but, as this collection of essays illustrates, anything worthwhile seems to be worth waiting for. It is an important lesson for government officials who are often guilty of focusing on short-run results for political reasons to the detriment of the long-run stability of the financial system.

This volume is sure to please financial historians no matter what their specialty. In addition, it should appeal to scholars of contemporary monetary regimes, especially those focusing on developing financial institutions. Finally, it should be required reading for all government officials involved with the regulation of financial institutions.

Citation: Michael Haupert. Review of Caprio, Gerald; Jr.; Vittas, Dimitri, eds., *Reforming Financial Systems: Historical Implications for Policy.* EH.Net, H-Net Reviews. December, 1997.

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