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Banking integration and (under)development: A quantitative reassessment of the Italian financial divide (1814-74)

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Banking Integration and (Under)development: A Quantitative Reassessment of the Italian Financial Divide (1814-74)

Maria Stella Chiaruttini, University of Vienna

Abstract:

When in 1860 Southern Italy was annexed to the Kingdom of Italy, it suddenly found itself within a larger national market characterised by high levels of public debt, a new currency and increased competition in banking. Monetary problems, the depreciation of public bonds and the loss of pre-eminence of the Southern public banks to the advantage of the Piedmontese National Bank, the predecessor of the Bank of Italy, are increasingly often taken as evidence of the harmful effects of financial integration on the Southern economy. This paper, focusing on the banking side of the story, argues, on the contrary, that the South benefited significantly from its integration with the North and that the relative underdevelopment of its credit markets was not due to a policy of 'internal financial colonialism' pursued by Northern capitalists with the backing of the Italian state, but to different economic conditions and the long-lasting impact of the poor banking policies implemented under the Bourbons.

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1. Financial Integration and the Italian North-South Divide: A Research Agenda

In Europe, over the last decades, growing supranational integration has been accompanied by the resurgence of regionalist feelings within the EU member states themselves. The most spectacular example of this is Catalonia, but in Italy too tensions between regions have been mounting since the creation in the early 1990s of the 'Northern League for the Independence of Padania' [i.e. the Po Valley], a party whose racist outbursts against Southern Italy have been bitterly resented there. Although in the last years the early separatist ideology has given way to federalist ambitions, in the elections of 2018 the Italian electorate clearly split along regional lines: the North, voting for Salvini's League and the South for the 'Five Star Movement' (M5S).

At a national level, both parties are sympathetic to regionalist aspirations. As its original name makes clear, the League was agitating until recently for the independence of Northern Italy, while in the South the M5S has endorsed Neo-Bourbon movements – the Italian equivalent of the Neo-Confederates in the United States – which reinterpret the history of the Italian unification as a war of conquest and colonial subjugation of the Bourbon Kingdom of the Two Sicilies by the Northern Kingdom of Sardinia.¹ At an international level, both parties lean towards Sovereignism and have been highly critical of European integration. Apparently, the M5S has recently abandoned its Euroscepticism,² while the League, currently the strongest Italian party, is dusting off the rhetoric of anti-Europeanism in the midst of the Covid-19 crisis.³

What Northern independentism, Neo-Bourbonism and Sovereignism have in common is a deep-seated distrust of political and economic integration, be it at a national or supranational level. In Europe, for obvious reasons, the discourse against the European Union is mainly centred on the Eurozone and a common monetary and fiscal framework which – depending on the viewpoints – would either burden Northern taxpayers with Southern debts or subject Southern countries to the tyranny of foreign lenders. Against this background, in Italy, too, the cultural crusade against national unification has started to insist on the negative repercussions that financial integration with the North allegedly had for the Southern economy in the nineteenth century.

This is hardly surprising given the impressive long-term cleavage between Northern and Southern Italy as shown by most credit indicators, such as loans and deposits shares, number and types of banks, extension of branch networks, interest rates and access to credit.⁴ And the question whether this financial gap simply reflects secular economic stagnation or, instead, it was financial factors which affected the historical evolution of the North-South divide is more than legitimate given the economic literature on growth and financial deepening,⁵ although seldom addressed by scholars.⁶ Ironically, this issue has received much more attention by Neo-Bourbon ideologues. In a highly polemical book drawing on the work of Capecelatro and Carlo, the journalist and political activist Nicola Zitara ascribes the collapse of an idealised Southern credit system and, together with it, of the entire Southern economy to a war of economic extermination waged against the South by Northern capitalists and

¹ Pescosolido (2017b).

² Only a few years ago, on the blog of the party founder Beppe Grillo (2015) the euro was labelled 'a suicidal project'.

³ ANSA (2020).

⁴ Banca d'Italia (1990); Brancati (1989); Cannari and Gobbi (2010); Messori (1997); SVIMEZ (2011).

⁵ Levine (1997, 2005).

⁶ An exception is A'Hearn (2005).

financiers led by the National Bank (*Banca Nazionale*) – the Piedmontese bank of issue predecessor of the Bank of Italy – following Unification.⁷ According to this theory, the penetration of the Southern market by the National Bank at the expense of the local public banks of issue inherited from the Bourbons resulted in the channelling of Southern savings to the North in order to finance industrial investment there. The North-South divide would thus stem from both a decapitalisation of the South and a disproportionate investment in the North. The theoretical underpinning of this approach is clearly dependency theory, which postulates that ‘private foreign investment is invariably exploitative and invariably detrimental’ to peripheral countries.⁸

While the editorial success of the Neo-Bourbon literature has spurred also economic historians to react and engage in the public debate over the origins of the North-South divide with renewed fervour,⁹ the few scholarly works addressing its financial aspects seem to lend some support to revisionist claims. Monetary unification took its toll on the Southern economy. Foreman-Peck and Vicquéry have both argued that Northern and Southern Italy did not constitute an OCA in the nineteenth century and that the loss of monetary sovereignty might have contributed to the emergence of the North-South divide in the long run.¹⁰ In the short term, the introduction of the lira instead of the ducat was ill-conceived and badly executed.¹¹ It took years to withdraw and replace the old Southern currency, while Italy’s unsustainable public debt eventually led to the introduction of note inconvertibility, lasting with only a short break for the rest of the century. As regards fiscal policies, the Two Sicilies had an unblemished record, unlike the Kingdom of Sardinia and unified Italy. As shown by Collet, before Unification yields on public bonds in the South were the lowest in Italy, while thereafter the risk premium increased substantially.¹² Moreover, despite the legal unification of the public debt of all annexed Italian states in 1861/2, investors continued for a while to price Southern bonds differently, reflecting fears of a possible political breakdown of the new, overindebted country.

Banking history also paints quite a flattering picture of the South, highlighting the achievements of Neapolitan finance since the early-modern times and in particular the long-lasting success of the Bank of Naples (*Banco di Napoli*) and the Bank of Sicily (*Banco di Sicilia*) – both founded under the Bourbons – despite the initially unsupportive attitude of the Italian government.¹³ Therefore, if we simply patch together all these partial contributions, it might seem that the South was indeed harmed by financial integration with the North. More research is needed in all directions, but no answer can, in fact, be given to this question if we don’t distinguish between its fiscal, monetary and banking aspects, rather than conflate them.

As regards fiscal policies, we should investigate if the Bourbon system of mild taxation, high but stable public debt, low public investment and systematic drainage of resources from the provinces to the capital¹⁴ was preferable to the Piedmontese and later Italian system of high taxation, high debt and high public investment, and to what

⁷ Capecelatro and Carlo (1972); Nicola Zitara (2011).

⁸ Ray (1973), p. 7; Moore (1973).

⁹ Daniele and Malanima (2011); Felice (2013); Lupo (2015); Pescosolido (2017a).

¹⁰ Foreman-Peck (2006); Vicquéry (2017).

¹¹ Chiaruttini (2018).

¹² Collet (2016).

¹³ Costabile and Neal (2018); Asso (2017); Demarco (1958, 1963); De Rosa (1989, 1992); Giuffrida (1972, 1973).

¹⁴ Ostuni (1992), pp. 325–7.

extent the new state privileged the North in terms of taxation and expenditure.¹⁵ What is certain, however, is that fiscal reform, albeit painful, was not altogether harmful. After Unification, Southern taxpayers were saddled with higher taxes, while low-yielding Southern public bonds were converted into depreciated Italian ones. Yet, in real terms higher debt meant also higher public investment, for instance in railways, previously virtually non-existing in the South, and the selling-off of state property, eagerly purchased by Southern landowners. In financial terms, higher debt meant a larger market to invest in, while the initial capital losses due to debt conversion were partly compensated by higher yields on later purchases and arbitrage opportunities on the more volatile Italian public bonds.¹⁶

As far as monetary policy is concerned, the disadvantages of losing monetary independence and ending up in an inflationary paper money regime have to be weighed against the advantages of monetary integration at a national but also international level thanks to Italy joining the Latin Monetary Union in 1865.¹⁷ Moreover, if replacing the silver ducat with a de facto limping gold standard was equivalent to a depreciation (silver was appreciating at the time of Unification but had to be swapped with gold at the then unfavourable bimetallic ratio of 15.5:1), all those Southerners who had access to the international market were nonetheless able to realise the market value of their silver holdings even in the most turbulent period of recoinage.¹⁸

Finally, banking integration implied the reform of the Bourbon system of public banking, the southward expansion of the Piedmontese National Bank and the introduction of new banking institutions, from joint-stock banks to savings banks and mortgage lending. Though apparently the most benign of these reforms, banking integration has been the most demonised by revisionists. In principle, there are good reasons to claim that banking integration was a traumatic process in the South. First, banking and monetary reform were intertwined. The banknotes of the National Bank were in fact the only ones to be declared inconvertible legal tender from the introduction of paper inconvertibility in 1866 to the first comprehensive banking reform in 1874, which replaced them with inconvertible governmental paper money issued by a banking consortium. In hindsight, therefore, the creation of an integrated payment system from 1860 onwards through the nationwide expansion of the branch network of the National Bank eased the government's task of declaring note inconvertibility to break free of budget constraints.

Second, prior to Unification the backbone of the Southern banking system had been the Bank of the Two Sicilies (*Banco delle Due Sicilie*, Bank of Naples since 1862) and its offspring, the Bank of Sicily, two large public banks which suffered under the competition of the National Bank and were even threatened with closure by the new government in the early 1860s.¹⁹ The ascent of the National Bank – which the Italian government tried at first to impose as the country's central bank and later favoured with the exclusive privilege of inconvertibility – at the expense of the Southern public banks might appear particularly problematic in light of the fact that the latter were initially much larger than the former in terms of reserves and note circulation (Figure 1).

¹⁵ For an early, though controversial, contribution to this last topic, see Nitti (1900).

¹⁶ On the integration of Italian public debt markets, see Toniolo, Conte and Vecchi (2003).

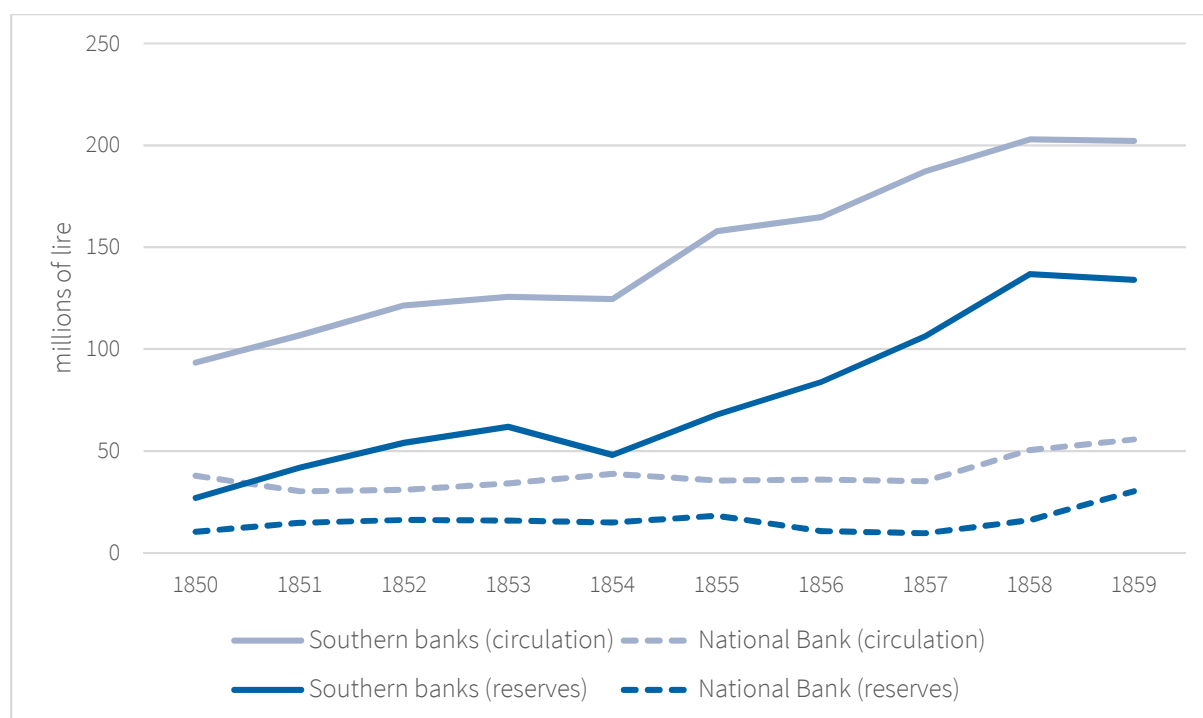
¹⁷ Cf. Timini (2018); Flandreau (2000).

¹⁸ Fratianni and Spinelli (2001), pp. 140–2.

¹⁹ Demarco (1958, 1963); De Rosa (1989); Giuffrida (1972).

Hence, the revisionist thesis that the Piedmontese bank eventually became a market hegemon only thanks to the backing of the state, which systematically favoured it instead of its Southern competitors, does not seem too outlandish. The heart of the matter here is not only the alleged distortion of market competition to the advantage of a bank closer to political power but also the fact that a bank with market power and a nationwide branch network might be able to distort regional development through a discriminatory credit policy, privileging Northern borrowers in the allocation of savings collected throughout the country. In fact, this working hypothesis is just the banking equivalent of Nitti's thesis of the transfer of fiscal resources from the South to the North during the Liberal Age.²⁰

Figure 1. Metal reserves and note circulation of the Southern public banks and the National Bank



Note: For the sake of comparability, all the amounts in the paper are expressed in lire.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; Demarco (1958); Giuffrida (1972).

While fundamental to assessing the overall effects of national financial integration in the South, this paper leaves aside the fiscal and monetary question to focus on banking and, in particular, on the role played by the banks of issue. More specifically, it provides a first attempt, on the basis of available data, to quantify the efficiency of the Southern system of public banking and the impact on the Southern credit markets of the penetration of the National Bank during the first years after Unification. In Section 2 I illustrate the workings of the Bourbon banking system, highlighting its shortcomings in comparison with the Piedmontese one. In Sections 3 and 4 I analyse the development of the Southern credit markets in the years between Unification and the banking reform of 1874 – which marked a turning point in the balance of political power between North and South –, investigating possible pitfalls and opportunities related to the activities of the National Bank. Section 5 concludes refuting the claim that

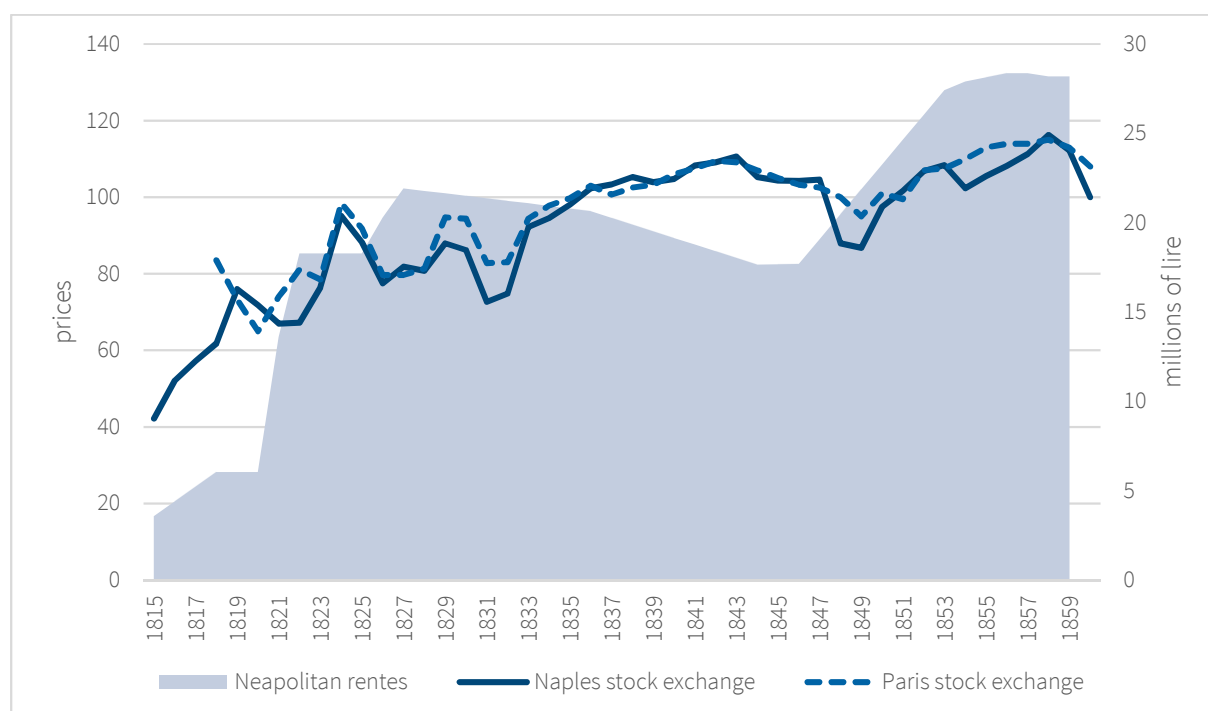
²⁰ Nitti (1900).

banking integration disadvantaged the South. In fact, the available evidence suggests that it fostered credit development to an unprecedented degree.

2. Southern Banking Under the Bourbons

At first sight, financial conditions in the Two Sicilies prior to Unification seemed to be rosy. In the early nineteenth century the government had accumulated substantial public debt, part of which held abroad. However, it always proved to be a very reliable borrower. Instead of raising taxes to service its debt, it kept public spending low, even to the detriment of badly needed infrastructure investment. Public debt was increased only when absolutely necessary, for instance to crush the constitutional insurrections in 1820/1 and 1848/9, otherwise it was kept stable or even reduced. As a result of this prudent policy, from 1835 onwards the Neapolitan *rentes* traded above par both in Naples and Paris (Figure 2).

Figure 2. Total amount of Neapolitan *rentes* (right) and their annual average prices on the Naples and Paris stock exchanges (left)



Source: Author's calculations based on data on public debt interpolated from Correnti and Maestri (1858); Demarco (2000); Ostuni (1992); Schisani (2010). Price data from Schisani (2001).

The Two Sicilies also had the largest coin circulation in Italy, both in aggregate and per capita terms.²¹ More interestingly still, the South had the largest paper circulation, consisting of the notes issued by two public deposit banks, the Bank of the Two Sicilies and what would later become the Bank of Sicily. Their notes (*fedi* and *polizze*)

²¹ Chiaruttini (2018), p. 3.

were not bearer notes but rather transferable deposit certificates akin to cheques.²² Issued by governmental banks, backed by an implicit state guarantee, received in payment and exchanged into coin at every tax office, they circulated freely across the whole country, even without being legal tender. Besides being the State Treasurer and lending to the government, the Bank of the Two Sicilies also offered credit facilities to private clients, operating as a pawnbroker and, through its Discount House, discounting bills of exchange and making advances on public securities.²³ Furthermore, Naples boasted the only Italian branch of the Rothschild House and was home to one of the few stock and commodity exchanges in Italy.

All that glitters is not gold, however. The low yields on public debt were the result not only of cautious fiscal policies but also of excess demand due to administrative provisions which prompted investment in public debt securities,²⁴ conservative investment attitudes which privileged investment in land and public debt,²⁵ and, last but not least, the credit facilities offered by the Bank of the Two Sicilies. The Rothschild branch itself had initially been established at the urging of Vienna to rescue the Bourbons from bankruptcy and enable them to issue new debt on a large scale in order to pay for a six-year long Austrian military occupation, called upon by the Neapolitan king to quell the 1820/1 constitutional uprisings.²⁶

Since then, one of the chief concerns of the government had been to curtail public debt even if at the cost of prolonged austerity. While on international markets it built its reputation upon scrupulous repayment, domestically it heavily relied on the Bank of the Two Sicilies. The Bank, in fact, not only invested in public securities on which interests were rarely paid punctually²⁷ but its Discount House devoted most of its resources to directly finance the Treasury (Figure 3). Moreover, besides this form of direct support, the Bank encouraged private investment in public securities by making advances on them at favourable rates and discounting Treasury bills. Needless to say, the government was particularly interested in shifting these credit activities away from private bankers towards its public bank so as to de facto concentrate ownership of public securities in its own hands.²⁸

Just as the high prices of Neapolitan *rentes* should not be taken as an unmistakable indication of economic prosperity, so too the size of the Bourbon banks should not be taken as evidence of flourishing financial markets. In the 1830s, the Neapolitan stock exchange had witnessed a flurry of activities, with many new joint-stock companies listing for the first time. Within a few years after the bubble burst, however, most of them delisted. Investors remained sceptical for years about new ventures and the Neapolitan exchange was reduced to little more than a commodity exchange fully controlled by a clique of large merchant bankers.²⁹ Similarly, all the attempts made in the 1850s by foreign financiers, among whom the Pereire brothers, to launch a first investment bank

²² On the early history of Neapolitan deposit banking and the issuing of *fedeli*, see Costabile and Neal (2018).

²³ The Bank of the Two Sicilies, founded in the early nineteenth century, was divided into two main departments, one offering payment services and pawn loans to private clients, and another managing the payments of public administrations and a Discount House dealing with both the Treasury and the general public.

²⁴ See Cordova to Cavour, 17 July 1860 in Cavour (2005), p. 1345; Magliani [1857], p. 20.

²⁵ According to the Rothschilds, the Great Book of the Public Debt in Naples was 'a savings bank where everyone deposits the first hundred pennies he can afford to part with' (Gille [1967], p. 248).

²⁶ Schisani (2010).

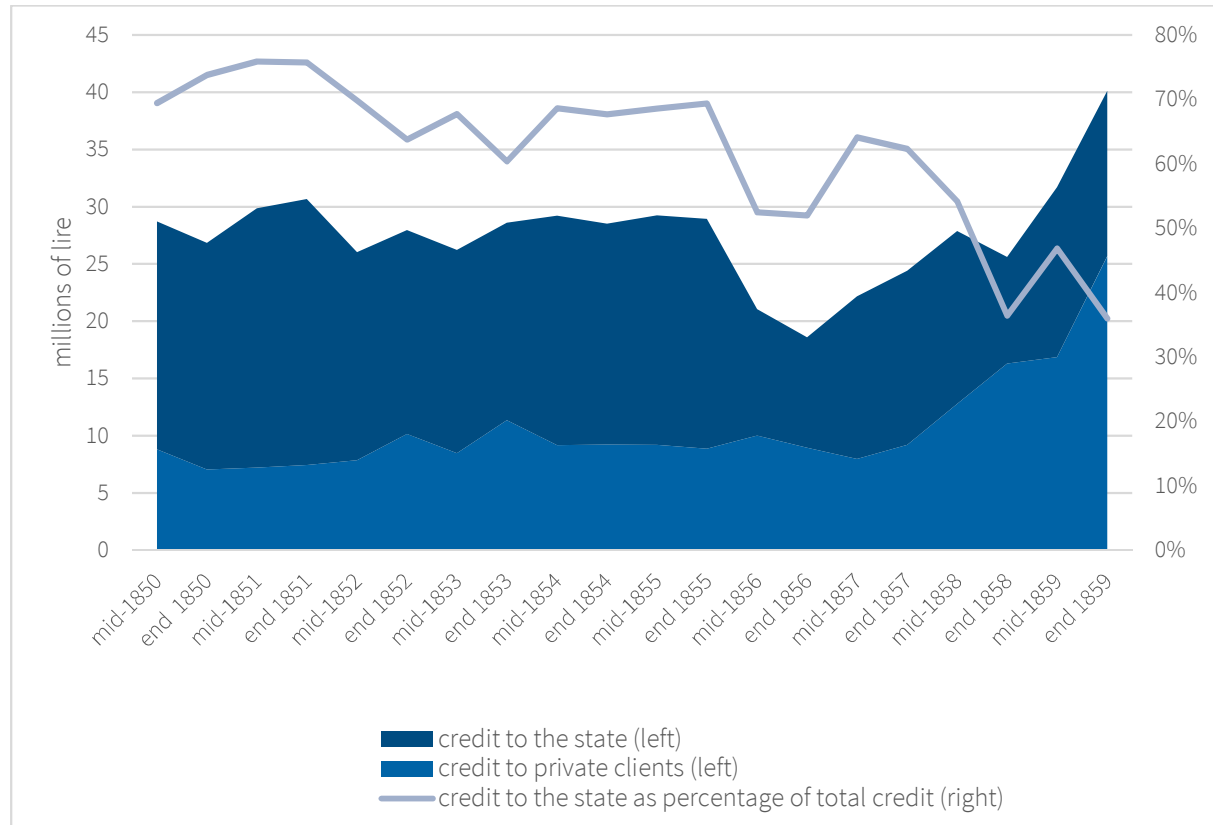
²⁷ E.g. ASBN/PBDS/AD app./46 ex 68/2. See also Demarco (1858), pp. 272–3; Demarco (1963), p. 388.

²⁸ ASN/MF/III/13587, correspondence between the Finance Minister and the Bank, Apr.–May 1860.

²⁹ Schisani (2001).

floundered due to the wariness of local investors and the hesitation of the Crown – motivated by foreign policy and fiscal concerns – in sponsoring the large public investment projects needed to keep the new bank afloat.³⁰

Figure 3. Credit granted by the Discount House of the Bank of the Two Sicilies to the private and the public sector



Note: Data do not represent annual credit volumes, which are not available, but total credit outstanding.
 Source: Author's calculations based on data from ASBN/PBDS/AD app./23.

On the eve of Unification, therefore, the banking landscape of the South had not changed much since the Restoration.³¹ Save for the Bank of the Two Sicilies, it was still made up of merchant bankers whose profits largely depended on commodity trade, public orders and tax farming.³² The Rothschild branch itself, though enjoying a special relationship with the government and playing a key role in connecting northern European and Mediterranean finance, had clearly to scale down its ambitions and adapt to the local market conditions.³³ Outside Naples, the government promoted the establishment of corn banks (*monti frumentari*), but apart from these primitive credit institutions lending in kind, the Southern provinces by and large lacked even savings banks, which were by contrast rapidly spreading across the other Italian regions.³⁴

Sluggish financial development was the joint result of an oligopolistic logic at play in the private sector and of a short-sighted policy focussing too narrowly on public indebtedness. While establishing a joint-stock bank in the

³⁰ Gille (1967), pp. 243–51.

³¹ Gicca (1859), p. 134.

³² Davis (1982).

³³ Schisani (2009); Rovinello (2005).

³⁴ Avallone (2013); Demarco (1963), pp. 431–8; De Simone (1993).

capital was an arduous task owing to the competition of a privileged public bank and incumbents of the calibre of the Rothschilds,³⁵ the large Neapolitan merchant bankers pulling the strings of commodity trade countrywide had little incentive to promote credit development in the provinces. In its self-assigned role of public banker, the state could have played a crucial role in fostering financial deepening across the entire kingdom by opening its own bank branches, but an excessive concern about public finances prevented it from doing so.

Indeed, extending the credit activities of the Bank of the Two Sicilies outside Naples was a burden for the state, which had first to endow the new branches with an operating fund. Moreover, as will be discussed below, bank branches would have eased specie outflows from Naples to settle regional trade imbalances, an unwelcome outcome for both the Treasury and the Neapolitan merchant community. Thus, despite decades of universal requests from provincial towns demanding a branch of the Bank of the Two Sicilies, the Bank opened but three branches in Palermo (1844), Messina (1846) and Bari (1858). The Sicilian branches later became an autonomous bank in 1850 (renamed Bank of Sicily after Unification), when the island was granted administrative autonomy after the quelling of the Sicilian secession of 1848/9. They were, however, not even allowed to discount until 1859 and had to limit themselves to collecting deposits and issuing notes, since the Sicilian Treasury, burdened with heavy debts towards Naples for the crushing of the insurrection, lacked for years the means to provide them with the endowment legally necessary to start their lending operations.³⁶

The near absence of a network of bank branches resulted in a concentration of coin in Naples, Palermo and, to a lesser extent, Messina. Regional trade imbalances were often settled in notes, issued on bank deposits in the main cities and eagerly sought after by provincials, who, lacking a bank branch in their own town, were not able to obtain paper money by simply depositing their coins and withdrawing notes there but instead had to trade, directly or indirectly, with the main cities to acquire them.³⁷ Due to their artificial shortage, notes stayed in circulation for many years and perpetuated the financial dependence of the provinces.

This dependence was further exacerbated by the fact that in the provinces note conversion was ensured not by branches of the Bourbon bank but by tax collectors. Excess supply of notes resulting from provincial trade surpluses did not automatically translate into specie outflows from Naples to meet the local demand for note conversion, as would have happened in the presence of a bank branch, legally bound to unconditional conversion. Rather, notes had to be exchanged into coin by local tax collectors out of their specie surpluses or by private moneychangers at a discount. The government did of course send additional funds in cases of too large a demand, as it was not in its own interest to let notes depreciate, but most of the time it tried to delay specie transfers. Implicitly, conversion at par at a provincial level simply relied on provincials accumulating enough specie from their trades to pay taxes in coin and thereby replenish the local state coffers. The care taken by the Bank and the government to make the mechanism of note conversion work, but not too smoothly, helped retain specie in the capital, while

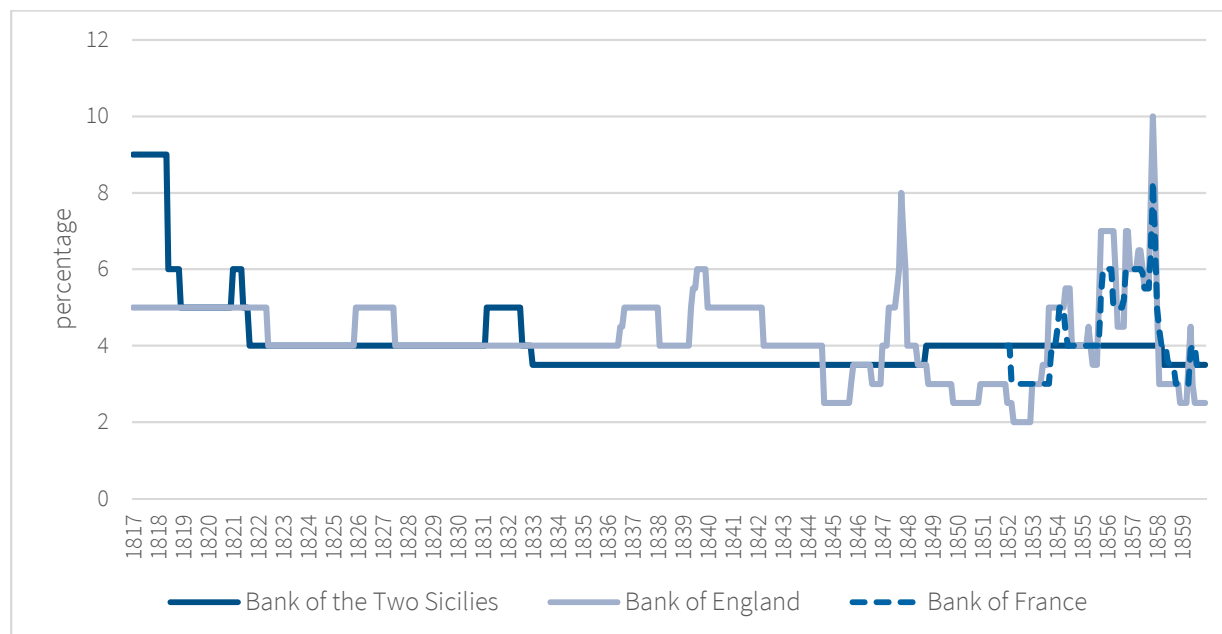
³⁵ Avallone (2013), p. 260; Demarco (1958), pp. 238–42, 273–6.

³⁶ Giuffrida (1972), pp. 73–95, 119–128.

³⁷ Tax collectors did also exchange specie into notes but at their own discretion.

providing a convenient pretext to delay the establishment of branches, deemed unnecessary given the change service already provided by tax officials.³⁸

Figure 4. Discount rates of the Bank of the Two Sicilies (Discount House), the Bank of England and the Bank of France



Source: Author's calculations based on data from Demarco (1958); NBER Macrohistory (XIII: Interest Rates); Rogers (2013).

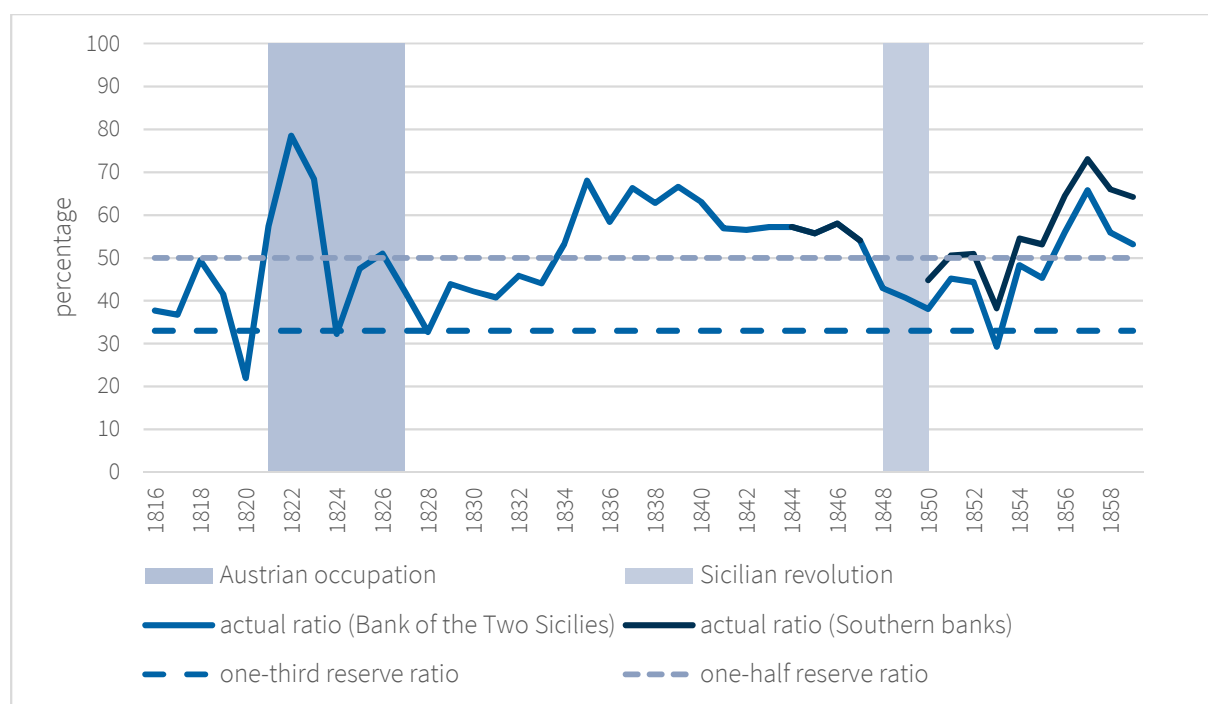
Another pretext to deny the establishment of bank branches was to question their market potential.³⁹ As shown in Section 4, the rapid credit development in the Southern provinces after Unification seems to discredit this argument. Yet, just from a purely logical point of view, only two options are possible: either the Bank and the government were right and a bank branch could survive only in four cities in the whole South, or they were wrong. In neither case can revisionists rejoice, either because of the South's economic backwardness or because of an utter policy failure. Fostering banking development in the provinces, although initially expensive, would have increased the total amount of bank deposits, deposits which could have been reinvested to stimulate the local economy. And even assuming that the government was not interested in local development, it would nonetheless have had more resources at its own disposal to channel them – through a careful management of specie reserves countrywide – to wherever it pleased. (After all, this is exactly what revisionists accuse the National Bank of having done thanks to its branch network, namely collecting large deposits nationwide and distributing them asymmetrically.) Credit development, in turn, by boosting economic growth, would have further contributed to strengthening public finances. In the medium-long term, therefore, the government would have better achieved its own aims *with* rather than *without* a proactive banking policy. But launching such a policy would have required vision and the courage to sacrifice the short-term gains ensured by the status quo, namely lower costs and specie retention in Naples.

³⁸ E.g. Demarco (1958), pp. 350, 368, 392. Clearly, that between the Southern provinces, petitioning for a bank branch also in order to improve their access to credit, and the government, claiming that a bank branch was unnecessary since some payment services were already provided by tax officials, was to a large extent a dialogue of the deaf.

³⁹ E.g. Demarco (1958), pp. 391–3.

Solvency and liquidity were thus prioritised over growth and efficiency. If concentration of coin and banking activities in Naples enabled the central government and the largest businessmen to borrow at extremely favourable rates (Figure 4), this came at the cost of a savings glut due to the disproportion between the amount of deposits and on-site investment opportunities. Indeed, although targeting a fifty per cent reserve ratio – a very conservative threshold for a privileged bank so widely trusted –, the Bank of the Two Sicilies was often unable to invest its excess reserves (Figure 5). In Sicily, where the local public bank offered only deposit and payment services, idle deposits accumulated on a gigantic scale.

Figure 5. Reserve ratio of the Bank of the Two Sicilies and the Bank of Sicily



Note: The reserve ratio is calculated as the ratio between metal reserves and sight liabilities.

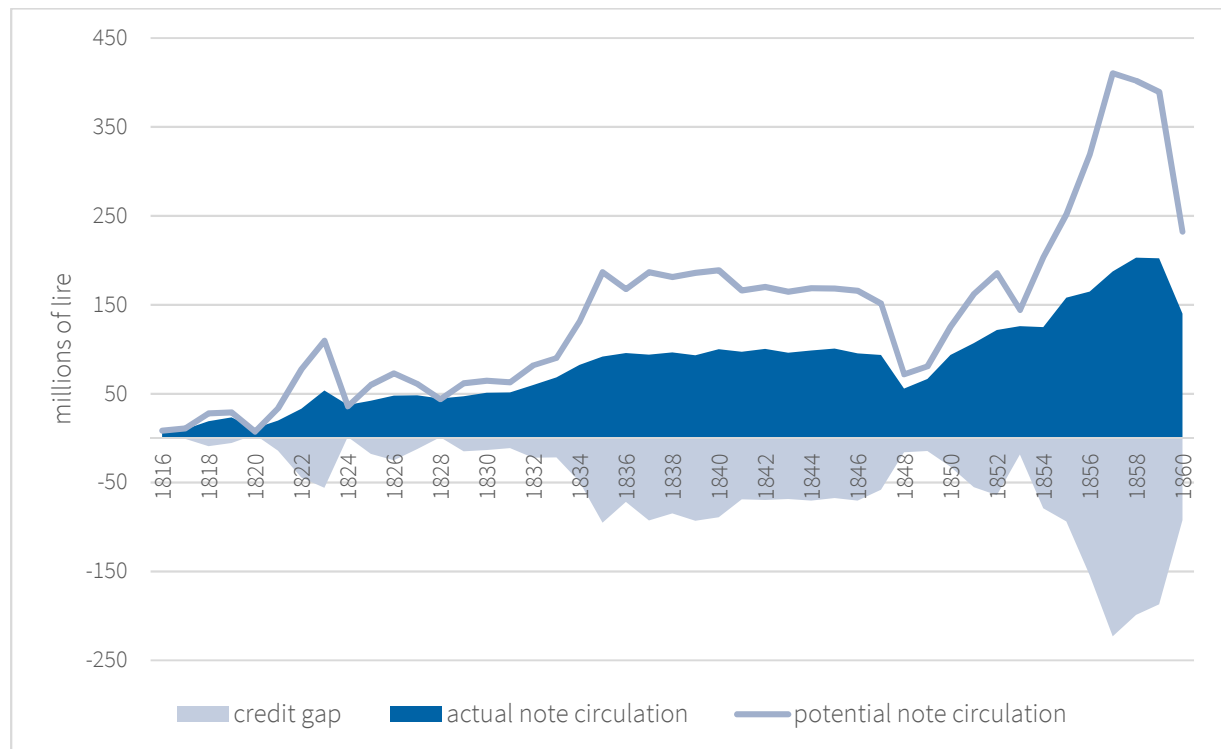
Source: Author's calculations based on data from Demarco (1958) and Giuffrida (1972).

Reversing the argument of revisionists, one could argue that the most striking feature of the Southern monetary system was not the abundance of money but its shortage. In fact, the Bourbon monetary policy was much more restrictive than the total amount of note circulation would at first suggest. If we assume a standard one-third reserve ratio – as prescribed by the National Bank statute, for instance –, we can see that the total note issue of the Bourbon banks could have been much higher. Which means that they could have lent much more generously leveraging their sizeable reserves. The difference between their actual and potential note circulation is thus an indicator of the amount of extra capital ('credit gap') that could have been created and invested in the kingdom (Figure 6). This credit potential, however, existed on paper only, because there was no banking infrastructure that could convey money where it was most needed.

Cash hoarding on such a scale was possible only because of the public nature of the Bourbon banks, which, as privileged institutions, attracted a disproportionate amount of deposits and at the same time – sheltered from market forces, paying no interests to their depositors and without shareholders to whom to pay dividends – could

afford the luxury of idle funds better than any private enterprise. Yet, if public banking arguably played a distortive role in banking intermediation, high inequality coupled with a rentier attitude in the private sector probably magnified this policy failure.

Figure 6. Actual and potential note circulation of the Bank of the Two Sicilies and the Bank of Sicily and total credit gap (difference between actual and potential circulation)

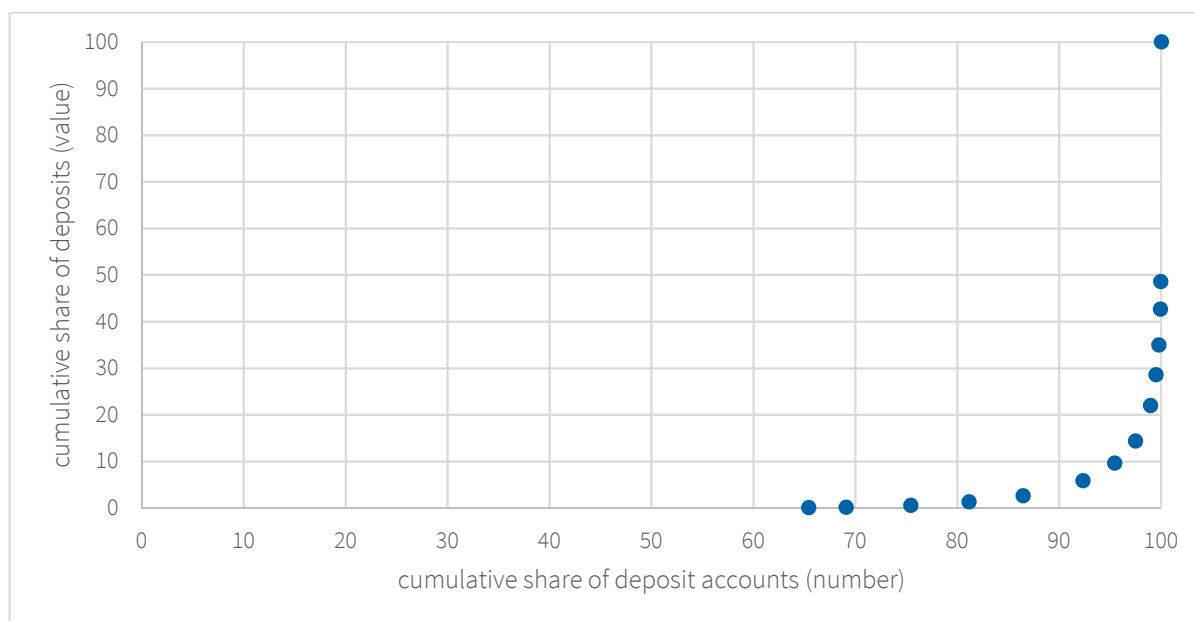


Source: Author's calculations based on data from Demarco (1958).

Although we lack comprehensive studies on inequality in the South during the nineteenth century, recent research on literacy, poverty and welfare points to high levels of inequality.⁴⁰ This seems corroborated also by the distribution of bank deposits (Figure 7). On the eve of Unification, roughly 80,000 citizens had an account with the Bank of the Two Sicilies. Sixty-five per cent of them had, however, less than 3 lire on average on their account, as against thirty clients with more than 3 million.

⁴⁰ Cappelli (2016); Ciccarelli and Weisdorf (2018); Felice (2013), pp. 41–50; Felice and Vasta (2015); Vecchi (2011).

Figure 7. Distribution of deposits of the Bank of the Two Sicilies (Lorenz curve)



Source: Author's calculations based on data from Demarco (1963).

Credit conditions in the Two Sicilies stood in sharp contrast to those in Piedmont-Sardinia. During the first half of the nineteenth century, the financial landscape in the Northern kingdom had been equally dull, with a small public debt, a few banking houses and an absolute monarchy not very keen on financial innovation. The fiscal crisis of 1848/9, triggered by the First War of Italian Independence, however, had forced both the newly-formed constitutional government and the banking community to radically reshape the country's financial system. The pillar of the new system became a private bank of issue founded with Turinese and Genoese capital, the National Bank, which in the mind of its shareholders and of Prime Minister Cavour was to become the local equivalent of the Bank of France. Due to parliamentary opposition to central banking, the Piedmontese government never succeeded in granting it legal privileges such as the legal tender status for its banknotes and the management of the Treasury service. Informally, however, government and bank were able to establish a close working relationship.

Over the 1850s, public debt continued to rise because of growing military expenditure in preparation for a future confrontation with Austria and of infrastructure investments in strategic sectors like railways. With the encouragement of the government, the banking community was eager to seize the opportunity of founding new joint-stock companies and banks investing in industrial undertakings and speculating on the stock exchange. Unlike in the Two Sicilies, this development was accompanied by both international integration – thanks to substantial foreign investments – and domestic integration – thanks to the creation of a nationwide network of bank branches. The National Bank, in fact, – constantly under the threat of potential competition as a private institution – quickly expanded in the provinces in order to pre-empt regional markets and spread its notes. Its provincial branches were not only offering deposit and payment services, like the Southern public banks, but had to lend, if they wanted to survive. The presence of a bank branch, in turn, not only supported the establishment of local companies but also of new, specialised banks that could rely on the National Bank for rediscounting.

Unlike the Southern banks, the National Bank always struggled to remain liquid for many reasons. Its notes did not enjoy any legal privilege (save that of temporary inconvertibility at the time of the First and Second War of Italian Independence), its by-laws did not entitle it to offer interest-bearing deposits⁴¹ and, most importantly, Piedmont-Sardinia was subject to constant capital outflows due to its structural trade deficit, foreign debt service and international arbitrage on bullion.⁴² However, if neither the Kingdom of Sardinia nor its central bank were as rich as the Kingdom of the Two Sicilies and its deposit banks, they exploited the lesser resources at their disposal to the fullest. Figure 8 compares reserves, circulation and credit provision of the three banks on a per capita basis. Until the mid-1850s, the Bank of the Two Sicilies and the Bank of Sicily had a comparable amount of reserves, roughly double than those of the National Bank. Thereafter, while the Piedmontese bank was losing reserves, their vaults were being flooded with coin, to the point that the Bank of Sicily alone commanded much larger reserves than the National Bank, both in aggregate and per capita terms.⁴³ This asymmetry in specie holdings was – unsurprisingly – reflected in the respective circulation of notes.

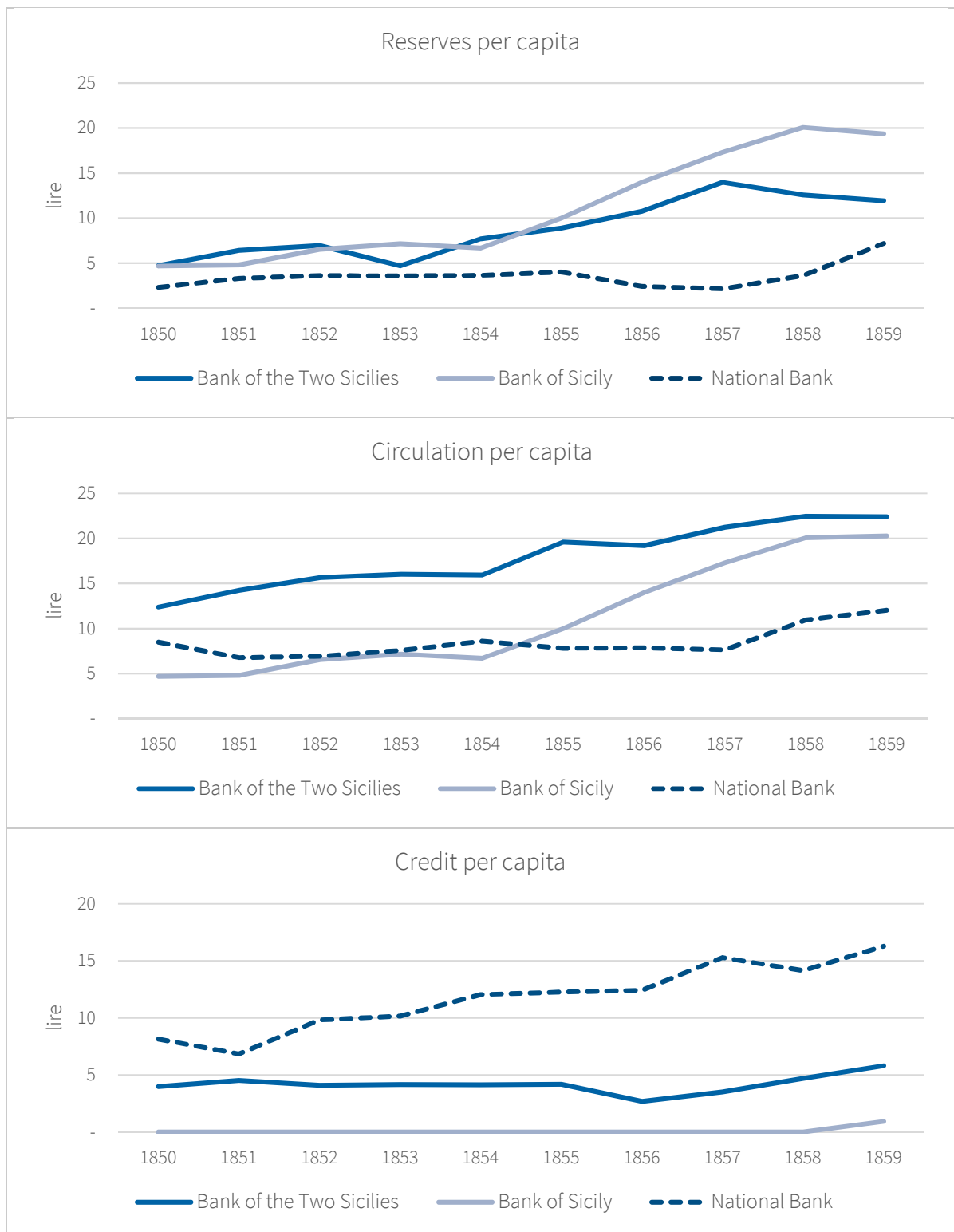
In contrast, the picture changes completely if we compare credit activities. Thanks to massive capital injections and foreign loans, the National Bank was able to constantly increase its lending, which vastly exceeded that of the Bank of the Two Sicilies – stagnating for almost a decade –, not to mention the Bank of Sicily, which started to discount timidly only a year before Unification. However, if the Bourbons are to blame for their short-sighted banking policy, so too are Southern and, particularly, Sicilian capitalists, who, instead of depositing their monies into a public strongbox, could have either used them to found a new bank, or simply invested or lent more privately, had they wanted to. In terms of counterfactuals, it is therefore almost irresistible to wonder what Sicily's growth might have been, had its public bank worked as the National Bank did, or, conversely, why, despite Sicily's larger wealth, a bank like the latter never materialised.

⁴¹ Paying an interest on deposits was considered a dangerous practice for a bank of issue, since it increased its financing costs, pushing it to pursue riskier investments to the potential detriment of note convertibility. As we will see in the case of the South, however, it was considered an acceptable – though exceptional – means to raise funds in a fragile banking environment.

⁴² On the development of Piedmontese financial markets during the 1850s, see Chiaruttini (2019); Conte (1990); Decugis (1979); Di Nardi (1953).

⁴³ The surge in metal reserves in the South – which was on a silver standard, unlike Piedmont, which was a bimetallic country – was also the result of international bullion arbitrage on silver.

Figure 8. Metal reserves, note circulation and credit of the Bank of the Two Sicilies, the Bank of Sicily and the National Bank



Note: See Fig. 3.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; ASBN/PBDS/AD app./23; Demarco (1958); Giuffrida (1972).

3. Foreign Banking After Unification: Risks

The previous section has shown that, while it certainly cannot be said that the Bourbon South was an impecunious country – at least not for Italian standards –, its banking system was such to retard, rather than expedite, growth. In this part, I will discuss how the traditional system based on the Bourbon public banks evolved after Unification and which role the National Bank played in this context. I choose 1874 as the end point of my analysis because that was the year of a first comprehensive banking reform, which – by transferring the issue of inconvertible paper money from the National Bank to a consortium of all Italian banks of issue including the Southern ones – re-balanced the position of the former vis-à-vis the latter.⁴⁴ The period from 1860 to the mid-1870s is indeed the most relevant if we want to discuss the issue of ‘internal colonialism’ as regards Southern Italy. In those years the influence of the Historical Right, closer to Northern interests, was the strongest while the South’s position the weakest. The region was ravaged by brigandage and loyalist guerrilla fighting for the restoration of Bourbon rule and only in the mid-1870s, when the military emergence was over, the South’s political weight at national level began to increase with the ascent of the Historical Left. This power asymmetry was reflected also in banking, for it was in those early years that the government tried to impose the National Bank as the only note issuing bank, although it eventually failed in its attempt owing to regional resistance.

Almost all Italian policies towards the South in the wake of Unification have been variously criticised by contemporaries and historians alike, from the top-down impositions of Piedmontese institutions and eventual demise of regional autonomies, to the overnight shift from Bourbon protectionism to Cavourian free trade and to the brutal repression of brigandage.⁴⁵ The Piedmontese ‘Unification package’ also included the expansion of the National Bank, which quickly broadened its branch network countrywide. Canonical works on Southern banking, echoing a narrative largely crafted by the Southern banks themselves, highlight the pitched battle the National Bank fought against them and extol their survival to the benefit of the South, although governmental backing, most tangibly embodied in the privilege of note inconvertibility (*corso forzoso*) granted from 1866 to 1874 to the National Bank alone, inevitably relegated them to a subordinate position.⁴⁶ That Southern banks passed through hard times is beyond question. As the public banks of a defeated government, in the first years after Unification they were forced to lend massively to the Italian Treasury and struggled to survive in a highly precarious environment amidst banking runs – shortly before and after annexation –, monetary chaos and various attempts to reform or even liquidate them altogether to establish the principle of the monopoly of note issue dear to the Right (and the National Bank). What is less clear is if their fate coincided with that of the Southern credit market.

Although North and South now belonged to one country, the southward expansion of the National Bank can be interpreted, to some extent, as an instance of foreign banking. The National Bank, which needed both a larger capital and a broad consensus to bolster its claims to the monopoly of note issue, did open its board to directors

⁴⁴ In Italy until 1893 there were three other banks of issue – two in Tuscany and one in Rome – besides the National Bank and the Southern ones. The Southern banks lost the privilege of note issue only in 1926.

⁴⁵ Probably the most recent contribution pointing the finger at the economic policies of the new state in Southern Italy and one of the very few scholarly works espousing the revisionist thesis of the ‘extractive character’ of the Piedmontese ruling class is De Oliveira and Guerriero (2018).

⁴⁶ Demarco (1958, 1963); De Rosa (1989); Giuffrida (1972).

coming from all major Italian cities and issued new shares for regional investors. However, in terms of top management and ownership it clearly remained a Northern institution (Table 1). Its lifelong Director General, Carlo Bombrini, was Genoese, 12 out of 21 directors in its Superior Council represented Northern head offices and only 31,250 new shares were issued for Southern investors, as against the 166,250 held by Northerners from Liguria, Piedmont, Lombardy and Venetia.

In the last decades, the penetration of foreign banking in emerging markets, especially in Latin America and even more spectacularly in Central and Eastern Europe has been the subject of countless studies. Before the Global Financial Crisis, foreign banking was generally considered beneficial, while afterwards concerns have started to resurface.⁴⁷ The main benefits usually ascribed to foreign banking are increased competition, better access to credit, improved bank performance and the introduction of new products, technology and know-how.⁴⁸ Moreover, foreign banks might be less vulnerable to the domestic business cycle.⁴⁹ However, foreign banking also entails potential risks. Foreign banks might acquire substantial market power, ‘cherry-picking’ the best borrowers and leaving domestic banks to scramble over bad ones,⁵⁰ or, more simply, cause financial contagion and capital flight.⁵¹ Foreign banks moreover can have more difficulties in adapting to a new economic environment.⁵²

Table 1. Shareholdings in the National Bank: distribution across regions

Year of capital increase	Shares of total capital by region				
	Liguria and Piedmont	Lombardy	Venetia	South	others
1849	100.0				
1852	100.0				
1859	80.0	20.0			
1865	66.2	16.6		17.2	
1867	60.0	15.0	8.1	15.6	1.25
1872	60.0	15.0	8.1	15.6	1.25

Note: In 1872 the bank’s capital was raised for the last time before the establishment of the Bank of Italy in 1893. Figures are calculated on the assumption that shares issued for regional investors continued to be traded on the regional market.

Source: Author’s calculations based on data from De Mattia (1978).

If we examine the behavior of the National Bank in the South from all these perspectives, it emerges that benefits outweighed costs. The costs were mostly related to the fact that the National Bank did, in a sense, cause financial contagion. In 1866, shortly before the Third War of Italian Independence broke out, note inconvertibility was declared not only to relieve public finances but also to enable the National Bank to bail out a few large Northern banks, then in deep waters – like the Treasury – because of the attempts of French investors to get rid of Italian

⁴⁷ Claessens and van Horen (2014), p. 297.

⁴⁸ Bonin et al. (2005); Claessens (2006); Jeon et al. (2011); Micco et al. (2004).

⁴⁹ Barba Navaretti et al. (2010); Crystal et al. (2002); Fiala and Havranek (2017).

⁵⁰ Brown et al. (2011); Detragiache et al. (2008); Gnos and Rochon (2004/5); Song (2004), pp. 29–30.

⁵¹ Adams-Kane et al. (2017); Dekle and Lee (2015); Jeon et al. (2013).

⁵² Weller (2001).

securities. Note inconvertibility, in turn, resulted predictably in capital flight. Like the other Italians, Southerners too suffered from the introduction of note inconvertibility and the ensuing monetary turmoil, with the difference that the epicentre of the banking crisis had been in the North and that the 1866 war was fought to acquire yet another Northern territory (Venetia). Nonetheless, the richest among them profited nicely, as they used their cash to buy public bonds, whose price was then free-falling domestically and abroad, at an additional discount owing to the premium on specie.⁵³

Especially in the early years, when the destiny of the old Bourbon banks was still uncertain, there were also instances of ‘cherry-picking’. The National Bank was indeed able from the very beginning to ally itself with the wealthiest merchant bankers in the South – among whom Rothschild⁵⁴ – by offering them a seat on its local boards, thus forcing the Banks of Naples to turn to smaller and less reliable clients in order to stay in business.⁵⁵ To a large extent, however, this is the way competition is supposed to work: those who make the best offers attract the best clients and if there are not enough good borrowers for all the banks on the market, it simply means there are too many or too large banks.

Undoubtedly, the National Bank also acquired market power. Its notes, thanks to the privilege of inconvertibility, enjoyed a special status and the Southern banks were no longer able to sustain such a large circulation as before Unification nor could they command the same amounts of metal reserves.⁵⁶ They lent less than the National Bank and the branch network they started to develop in the 1870s remained far smaller than that of the latter. However, if in comparative terms they had become second-rank institutions, their absolute lending volume increased substantially (Figure 9). Furthermore, as will be discussed later, the National Bank wielded market power at a national level, while in the South its market share was comparable to that of its local competitors. The net result of the encroaching of the National Bank on the Southern market was thus the partial replacement of Southern deposit notes with its own banknotes and a surge in lending by all three banks due to heightened competition.

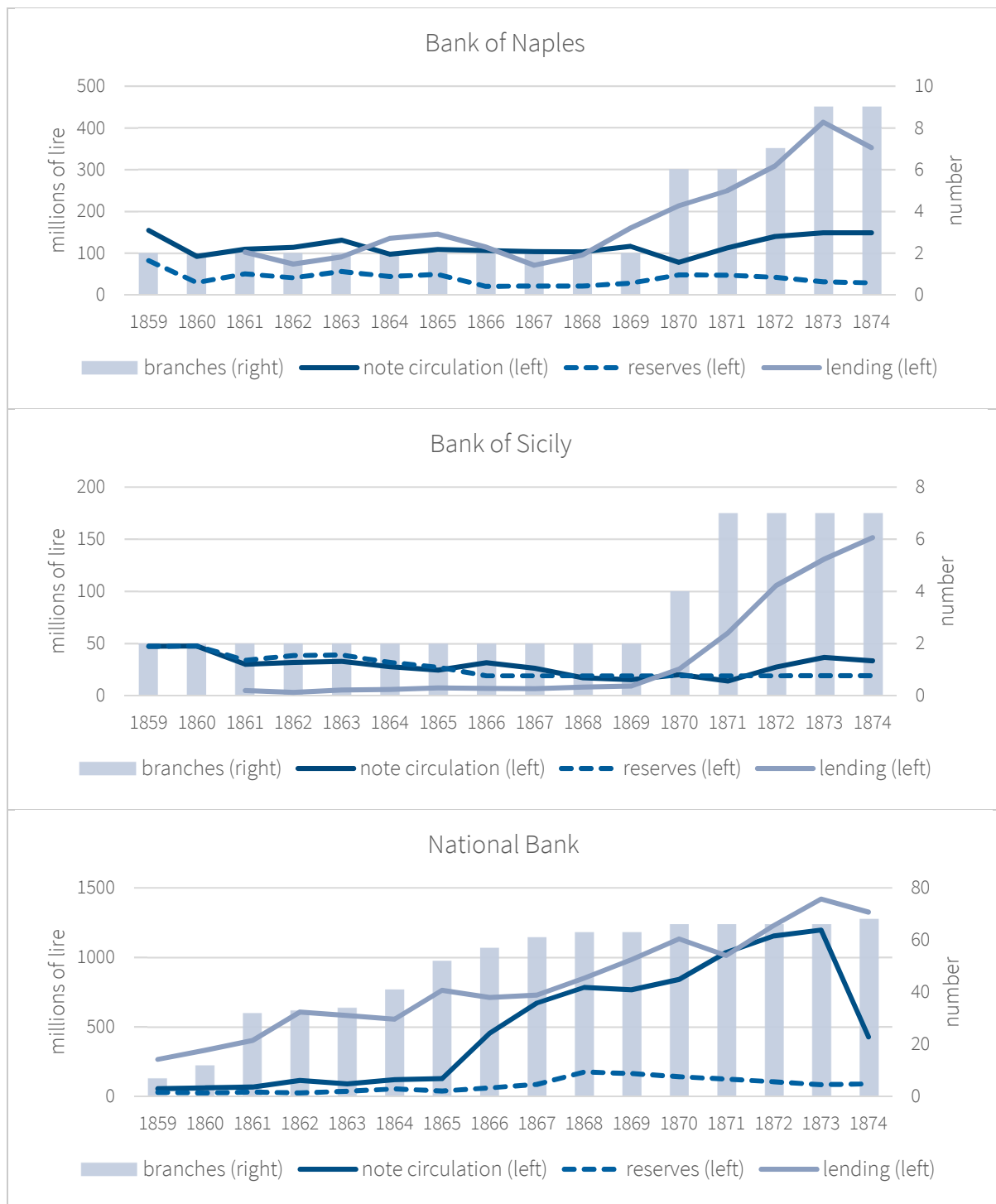
⁵³ Chiaruttini (2018); see also Fig. 15.

⁵⁴ The Rothschild branch in Naples was closed in 1863, since after Unification and the transfer of the capital to Turin it was easier and more economical to supervise Italian financial markets directly from France.

⁵⁵ Banco di Napoli (1868), pp. 145–6; Banco di Napoli (1869), p. 65; Camera dei Deputati (1869), 3rd vol., p. 208; Demarco (1958), pp. 455–7; De Rosa (1989), pp. 131, 134.

⁵⁶ Although during the *corso forzoso* the note circulation of the National Bank was extraordinarily high, thereafter – albeit much reduced – it continued to exceed that of the Southern banks thanks to the larger business volume of the former.

Figure 9. Metal reserves, note circulation, annual lending volume and branch network of the Bank Naples, the Bank of Sicily and the National Bank all over Italy, before and after Unification



Note: Data on credit volumes include discounting and advances but not ancillary activities of the Southern banks – such as mortgage lending and, in the case of the Bank of Naples, pawn lending and the management of a savings bank – that were not offered by the National Bank. Direct loans to the Treasury by the National Bank during the *corso forzoso* – reflected in the massive increase of its note circulation – are also excluded from credit activities.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; ASBN/RA; De Mattia (1967); Giuffrida (1973).

Leaving aside market indicators, one may wonder if the ascent of the National Bank marginalised the Southern banking community, shifting the control over Southern business affairs to the North. This certainly happened to a certain extent. As mentioned above, Southerners were a minority within the institution which was going to become Italy's central bank. On the National Bank Superior Council, which included three representatives from each head office, they were underrepresented because there were only two head offices in the South, Naples and Palermo; yet this choice largely reflected the uneven financial development of Southern cities inherited from the Bourbons. They were also underrepresented as shareholders, but, while the enthusiastic oversubscription in the South of the capital increase of the National Bank in 1865 suggests that the latter could have been more generous in the regional allocation of its new shares, thereafter Southerners did not increase their participation in the bank's capital through purchases on the secondary market and in Naples and Palermo trade in the stock of the National Bank languished for years.⁵⁷ The lesser role played by Southerners within the National Bank, therefore, cannot be simply attributed to a discriminatory policy against them.

Moreover, we should not forget that, though Northern in capital, the branches of the National Bank were Southern in management, for local boards were formed of Southern notables and businessmen in charge of daily business, and that for all strategic decisions the Southern representatives on the Superior Council also had their say. More importantly, if Southerners were not in full control of the National Bank business in the South, they could now manage the Banks of Naples and Sicily free from central government interference. In fact, after the first attempts the Italian government made to liquidate the Bourbon banks or reduced them to little more than *monts-de-piété* so as to ease the transfer of their deposits to modern credit institutions like the National Bank, it renounced such plans in the face of bitter opposition from the South. Instead, it decided to retain only supervisory power and entrusted them to representatives of the local administrations and business associations, while preserving their public character.⁵⁸

Thus, if the former Bourbon banks lost their hegemonic position in the South, the Southern businessmen running them gained autonomy from the Finance Ministry – not even needing to invest money in the very banks they managed because of their public character. Furthermore, a great many more than before were given the chance to contribute to the financial development of the South and of the new country. Indeed, Neapolitans and Palermitans were now able to extend their influence to the entire nation by serving on the National Bank Superior Council as well as by managing the Banks of Naples and Sicily, which since the 1870s had started to open their first branches outside the South, while for their part Southern provincials were being co-opted on the local boards of three different banks of issue instead of being left – as in the past – to their own devices.

Apart from the risk of financial contagion, cherry-picking and market power, we should also examine whether the National Bank was underinvesting in the South and channeling Southern savings to the North, thus contributing to distorting regional growth rates. Since the National Bank was controlled by Northern bankers and businessmen whose economic interests were much broader than those of pure shareholders only caring about the most profitable

⁵⁷ Camera dei Deputati (1869), 1st vol., p. 12; ASBI/RD/BNRI/RA; De Mattia (1978), pp. 762–4.

⁵⁸ De Rosa (1989), pp. 6–7, 14–9; Giuffrida (1973), pp. 7–19.

allocation of the bank's resources, this might seem a plausible hypothesis. A preliminary study of available data, however, lends little support to this conjecture.

First, we cannot expect the National Bank to be able to unfairly discriminate against Southerners because of its weak market power at regional – rather than national – level. As mentioned before, the penetration of the National Bank in the Southern market never transformed it into a regional hegemon but rather spurred competition from the incumbents. As shown in Figure 10, during the 1860s the National Bank came to manage 80 per cent of all bank branches⁵⁹ in the South, but by the mid-1870s it only controlled 50 per cent of them in Sicily (7 branches) and 63 per cent (15 branches)⁶⁰ on the southern mainland. This balance then remained almost unchanged all over the 1880s, save for the Bank of Naples, which slightly increased its share of branches. In terms of lending volumes, however, over 15 years the Bank of Naples was able to keep more than 50 per cent of the market on the southern mainland, a percentage which was slowly eroded only in later years, while in Sicily, after the first years in which credit activities were confined to Palermo (as discussed below), the National Bank had to content itself with roughly 45 per cent of the market once the Bank of Sicily began opening its own branches and lending on a grand scale.

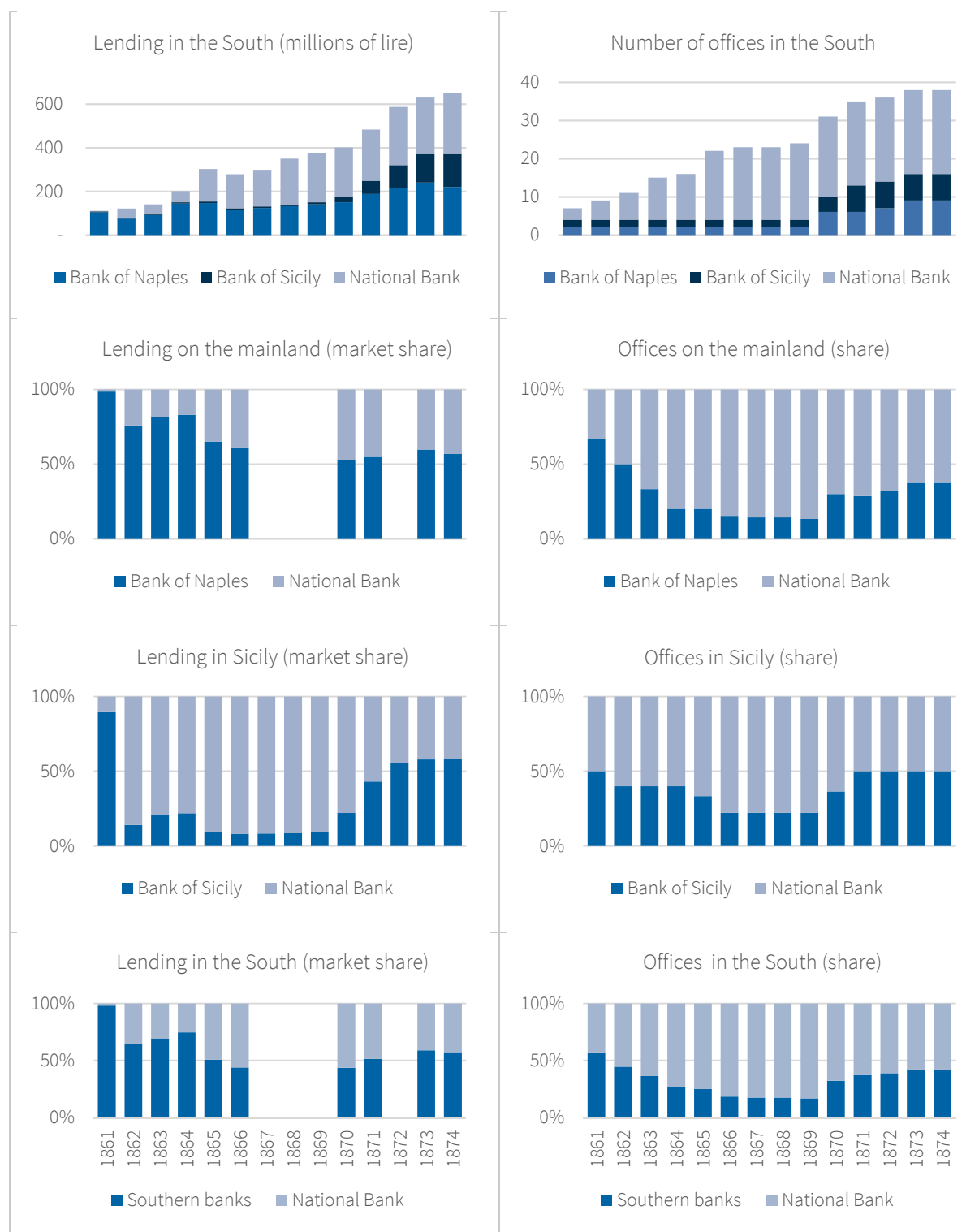
We can therefore distinguish two periods. In the 1870s, when the Southern banks started to develop their own branch network, the National Bank had a smaller market share than its local competitor and in most Southern towns where it had a branch there was now also one either of the Bank of Naples or Sicily. Because of direct competition, the banks offered roughly comparable conditions to depositors (see Section 4). In this context, the National Bank would have found it difficult to collect sizable deposits in a Southern town while curtailing credit unfairly. Had it done so, local businessmen would have simply turned to the Bank of Naples or Bank of Sicily branch for credit and would have been very likely to transfer their deposits to them too, apart from minimum balances needed to settle payments nationwide through the National Bank. Moreover, as the branch network of the Southern banks remained virtually confined to the South until the 1874 banking reform (and even thereafter it expanded mostly within regional borders), savings collected by the Southern banks were necessarily reinvested locally, thus thwarting any 'colonialist' attempt by the National Bank.

The only decade in which the National Bank could have successfully pursued a strategy of credit undersupply was therefore the 1860s. Indeed, only in those years was the National Bank in a position to distort both sides of the equation – deposit collection and credit supply – given that most Southern towns were then still devoid of credit institutions and local private lenders were certainly no match for it. Furthermore, its power was all the greater as in 1862 it began offering interest-bearing accounts, akin to sight deposits though requiring a few-day notice for very large withdrawals – a facility it granted only to a few clients outside the South.

⁵⁹ For the sake of brevity, with the expression 'bank branch' I refer to the bank branches of the banks of issue, including also head offices if not mentioned otherwise.

⁶⁰ Sixteen counting Benevento.

Figure 10. Annual lending volume, branch network and market shares of the Bank of Naples, the Bank of Sicily and the National Bank in the South, 1861–74



Note: Data on credit volumes include discounting and advances, see Fig. 9. Local credit supply from the Bank of Naples in 1867–9 and 1872 has been interpolated in the first panel to the left. Benevento is not counted as a Southern branch of the National Bank, as the town did not belong to the Two Sicilies.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; ASBN/RA; De Mattia (1967); Giuffrida (1973).

Unfortunately, only piecemeal evidence survives of the amount of bank deposits in the South in those years. They suggest, however, that the discrepancy between the larger number of branches the National Bank had on the southern mainland and its lower lending volume compared to the Bank of Naples in the 1860s (Figure 10) was not due to the National Bank draining savings from the Southern provinces through its branches and then lending too little. In fact, scattered data on interest-bearing deposits and more comprehensive data on sight deposits show that in the South the National Bank was collecting large deposits only in the main cities and even there the amount of sight deposits was far below the average in the North. Indeed, the very introduction of interest-bearing deposits – a rather unorthodox practice for a bank of issue – testifies to the difficulties it had in financing its operations in the region.⁶¹

For instance, Table 2 shows that the amount of interest-bearing deposits in Milan alone was higher than in the whole Sicily. In Cagliari – not an affluent city in a poor region, Sardinia – the National Bank collected more deposits in this form than on the southern mainland, with the obvious exception of Naples. In Sicily, excluding Palermo, 74 and 16 per cent respectively of those deposits came from just two cities, namely Messina and Catania.

Table 2. Interest-bearing deposits of the National Bank, in thousands of lire

	Naples	Palermo	Southern branches		Milan	Ancona	Cagliari
			mainland	Sicily			
1862	2,924	2,405	5	1,035	-	-	-
1863	3,015	3,622	807	1,326	-	-	-
1867	8,217	5,215	516	5,570	12,547	3	640

Note: Data on branches exclude the head offices in Naples and Palermo.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; Camera dei Deputati (1869), 1st vol.

If we look at sight deposits, the contrast is even starker (Table 3). In Venice, which at that time was certainly not a burgeoning financial centre – as the comparison with the non-Southern head offices further makes clear –, the National Bank usually collected more deposits than in either Naples or Palermo. And it cannot be claimed that sight deposits in the South were so low because there, unlike in the North, clients could simply choose to deposit their money at an interest. In fact, for that Northern savers had just to turn to their many savings banks, for instance. They need not avail themselves of the National Bank as a strongbox to safekeep their money. We may therefore assume that their bank balances were commensurate with their actual payment needs. Rather, the main reason why sight deposits in the South were so low is simply that the wealthy Palermitans and Neapolitans were still making most of their payments through the Southern banks, as their still large circulation clearly suggests (Figure 9).

⁶¹ Demarco (1963), p. 403.

Table 3. Average sight deposits of the National Bank, in thousands of lire

	Naples	Palermo	Turin	Genoa	Milan	Venice	Florence	Rome	Branches
1861	11	5	1,595	845	1,144				212
1862	91	43	1,728	885	1,771				682
1863	45	45	4,698	1,671	1,757				864
1864	48	58	3,280	1,148	1,707				1,766
1865	58	91	2,140	1,065	1,983		764		1,432
1866	52	158	1,725	2,539	1,464		2,091		1,406
1867	78	69	1,482	1,426	1,127	23	2,874		1,655
1868	64	40	2,218	1,243	1,155	86	2,123		2,118
1869	57	72	1,723	959	1,106	89	5,306		1,882
1870	53	79	2,002	2,363	1,581	80	3,063		1,886
1871	56	42	1,859	3,150	1,497	200	2,903	107	2,212
1872	52	56	2,164	2,822	2,345	49	683	192	3,240
1873	37	59	2,192	2,483	1,801	71	566	78	3,080
1874	37	52	2,462	4,077	2,081	39	517	155	2,822

Note: Disaggregate data for branches (excluding head offices) are not available.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA.

The few data available show that the National Bank – unlike its Southern competitors – was far from being awash with Southern savings. Moreover, it was not in its best interest to use this money to finance its operations in the North (where it already collected enough funds in the form of equity and deposits), for the very simple reason that in the 1860s it still aimed at replacing the Banks of Naples and Sicily so as to obtain the monopoly of note issue. In order to succeed, it desperately needed to spread its notes in the South – something it could only do by lending. Data, again, seem to confirm this presumption. We see, for instance, that in 1867 – the only year for which data on deposits are complete – for every lira of sight and interest-bearing deposits, Naples, Palermo and Milan were getting respectively 5.4, 5.6 and 5.5 lire in discounts and advances. In the rest of the South, where deposits were much lower, for 1 lira of interest-bearing deposits the National Bank branches overall provided credit for 12 lire.

The case of Sicily is even more illuminating. Table 4 compares the amount of deposits of the National Bank on the island and of the Bank of Sicily with the total volume of their annual lending activities. Albeit incomplete, figures clearly show that the National Bank was lending much more than the Bank of Sicily in the 1860s. In those years, because of its large loans to the government, the Bank of Sicily had ceased discounting in Messina and was only lending in Palermo,⁶² but even there it was much less active than the National Bank until 1870. Nevertheless, most deposits still concentrated in its vaults rather than in the National Bank's, so that for every lira collected in Sicily the National Bank provided credit for 4–7 lire, while the Bank of Sicily only for a few cents.

⁶² Camera dei Deputati (1869), 1st vol., p. 52; Giuffrida (1972), pp. 167–71, 176–80, 189–94.

Table 4. Total deposits and annual lending volume of National Bank in Sicily and the Bank of Sicily, in millions of lire

Years	National Bank (Palermo)			National Bank (Sicily)			Bank of Sicily		
	deposits	credit	credit / deposits	deposits	credit	credit / deposits	deposits	credit	credit / deposits
1861	0.00	0.05	10.61	0.00	0.58	126.27	34.05	5.01	0.15
1862	2.45	6.97	2.85	3.48	19.72	5.66	38.49	3.23	0.08
1863	3.67	9.97	2.72	4.99	21.96	4.40	39.09	5.61	0.14
1864	-	8.48	-	-	21.90	-	31.91	6.09	0.19
1865	-	38.11	-	-	71.11	-	27.40	7.48	0.27
1866	-	38.71	-	-	82.37	-	19.10	7.14	0.37
1867	5.28	29.73	5.62	10.85	76.60	7.06	19.10	6.87	0.36
1868	-	31.85	-	-	91.93	-	19.10	8.39	0.44
1869	-	28.84	-	-	92.16	-	19.10	9.31	0.49
1870	-	27.36	-	-	91.14	-	19.10	25.76	1.35
1871	-	21.20	-	-	79.52	-	19.10	60.18	3.15
1872	-	22.87	-	-	84.28	-	19.10	105.64	5.53
1873	-	29.55	-	-	95.59	-	19.11	130.93	6.85
1874	-	39.50	-	-	108.82	-	19.11	151.60	7.93

Note: Since data on deposits are not available for the Bank of Sicily, the amount of metal reserves has been used in its stead, which, reserves typically being lower than actual deposits, only reinforces the claim made in the text about their sub-optimal use. Deposits for the National Bank in Palermo include both sight and interest-bearing deposits, while for its other Sicilian branches we have data only on the latter kind of deposits. The amount of sight deposits at branch level was however probably not very high, see Tab. 3.

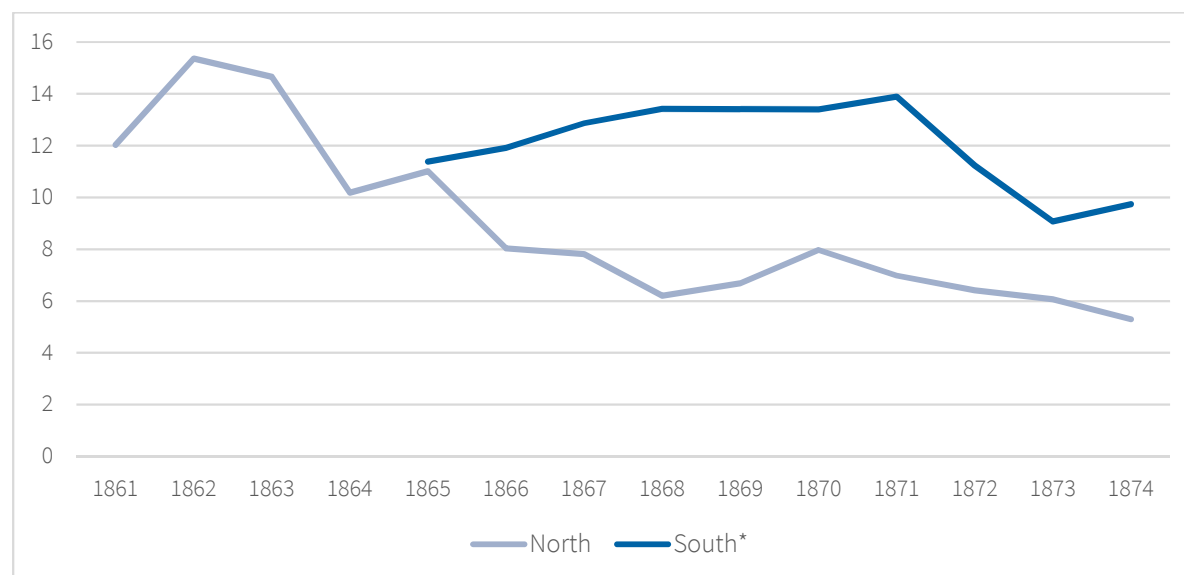
Source: Author's calculations based on data from ASBI/RD/BNRI/RA; De Mattia (1967); Camera dei Deputati (1869), 1st vol.

Besides deposits – which neither in the North nor in the South did ever provide the bulk of its funds – in order to finance its business the National Bank could primarily count on its circulation, its equity and, marginally, on idle funds it could touch upon from the Treasury's current account, on specie flows linked to its management of the national mints and on foreign rediscount facilities.⁶³ For all of these categories, we know the regional origin only of deposits and capital. If we look at equity figures, for every lira they invested in the bank's capital, Southerners received much more credit than Northerners (Figure 11). If we sum capital and liabilities in the form of deposits, in 1867 the South was slightly disadvantaged compared to the North but not if compared to Lombardy or Venetia on their own. For every lira the National Bank raised in the South, either as capital or deposits, it supplied credit for

⁶³ Even during the *corso forzoso*, the National Bank could not finance itself only by issuing inconvertible notes. Its statutory reserve ratio was still binding, if we exclude the amount of notes loaned directly to the government.

5.2 lire, while in the North for 5.8 lire. In Liguria and Piedmont, the ratio increased to 6.5 and 7.8 lire respectively, but in Lombardy it decreased to 5 lire, while in Venetia – just annexed in 1866 – it was as low as 1.7 lire. As a rule of thumb and contrary to revisionist conjectures, therefore, both North and South in aggregate could borrow in proportion to the money lent to or invested in the National Bank.

Figure 11. Regional loan-to-capital ratios of the National Bank



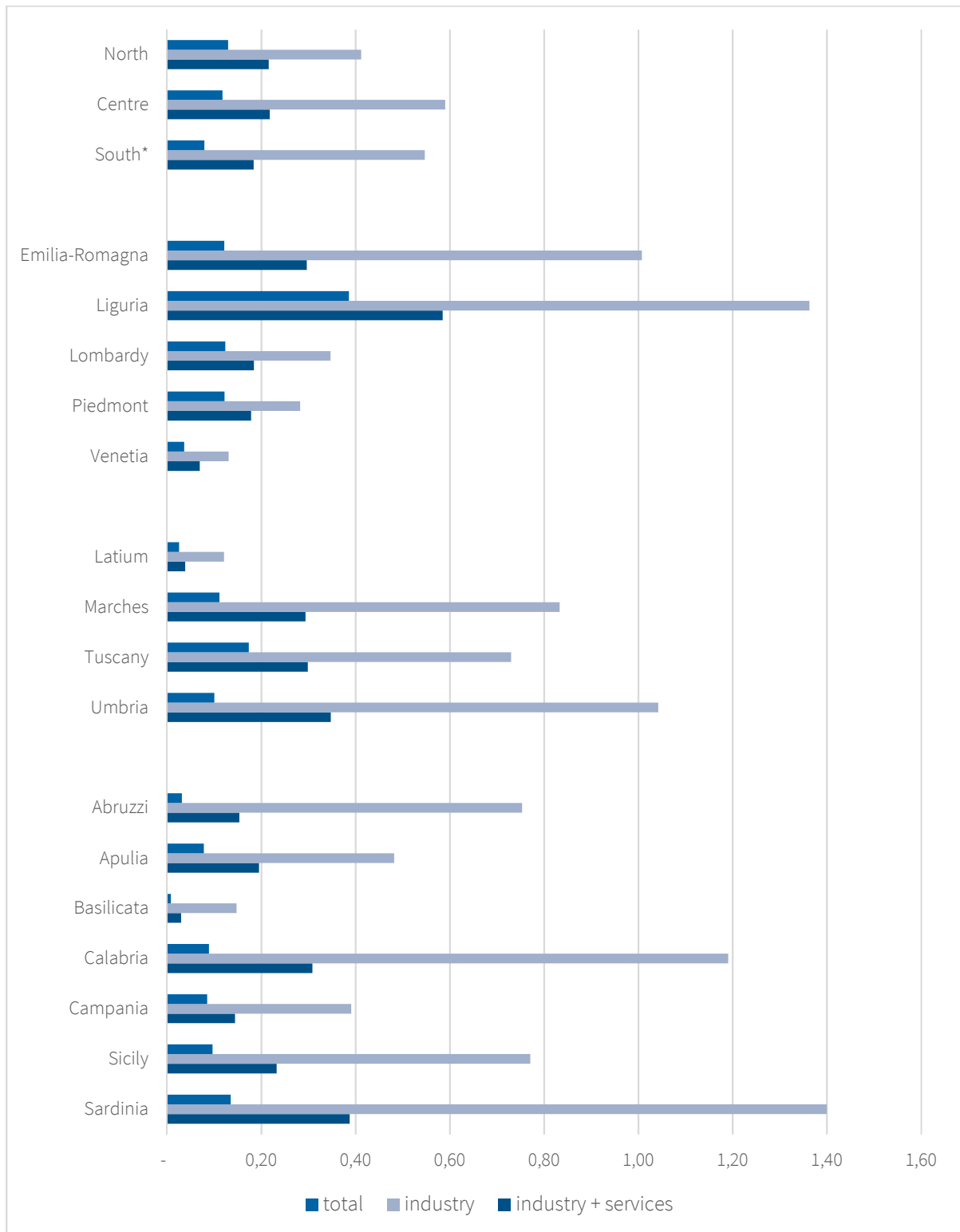
Note: The regional loan-to-capital ratio is calculated as the ratio of the regional annual lending volume to the paid-in capital brought in by regional shareholders. South* excludes Sardinia.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA and De Mattia (1978).

If there is no evidence that the National Bank was funnelling Southern savings to the North, we may still ask whether its lending activities were proportional to the size of the local economy. If we compare total regional lending of the National Bank to regional value added in the first year, 1871, for which we have both census data and a well-developed branch network, we see that indeed the National Bank lent relatively less in the South (Figure 12). At that time, however, the South had the largest agricultural sector in Italy: 58 per cent of regional value added as against 41 per cent in the North and 47 per cent in Central Italy.⁶⁴

⁶⁴ Felice (2019).

Figure 12. Ratio between total credit supply by the National Bank and total and sectoral GDP in 1871



Note: South* excludes Sardinia. Benevento is also excluded, see Fig. 10.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; GDP data by courtesy of Emanuele Felice, see Felice (2019).

As we shall see at the end of the paper, the South had also a weaker financial sector if compared to the rest of the country. It is therefore of little surprise that a bank of issue, whose primary business was short-term lending to finance, commerce and, to some extent, industry,⁶⁵ lent less in an agricultural than in an industrial region. Ideally, we should therefore compare National Bank lending to value added in financial services, wholesale commerce and industry. Unfortunately, available GDP estimates do not yet allow such a comparison at a regional level.⁶⁶ As a second best, since the main clients of the National Bank were bankers, we could tentatively compare total lending with the size of the financial sector alone, using census data on employment in banking and finance at provincial level as the ratio's denominator. We would thus obtain a very fine-grained but also unreliable picture, since those statistics are in many cases highly suspect.

As a further option, there is data on the number and size of joint-stock companies, but this does not lead us much further, because in most provinces where the National Bank operated no company was recorded. Moreover, at that time each town had its own mixture of companies and individual operators which was still very loosely linked to its business volume, making data on companies a poor choice as denominator. Faute de mieux, we can take industrial value added as the ratio's denominator. According to this indicator, we can see that the National Bank was investing significantly in the Southern economy. If we take the value added in industry and services, the picture blurs, and unsurprisingly so, since services represent an omnium gatherum of activities, many of which have nothing to do with trade and business borrowing. However, even in this case, if we look at single regions, no pattern of systematic discrimination based on geography emerges: Calabria, Sicily and Apulia in the South received more credit than Lombardy, Venetia or Piedmont in the North (Figure 12).

These data alone can of course neither tell us how much credit Southern entrepreneurs were receiving from the whole banking system – including private banking – compared to other Italians, nor whether ten years after Unification the South's lower industrial output was partly the result of still insufficient credit provision at an aggregate level. What figures do suggest, however, is that the National Bank was not pursuing a discriminatory policy at the expense of the South, but, conversely, that it contributed significantly to finance Southern businesses.

4. Foreign Banking After Unification: Opportunities

The previous section has discussed the potential drawbacks of the expansion of the National Bank in the South and argued that they mainly consisted in the exposure to the financial crisis of 1866. In this section we will examine the actual benefits of this expansion in more detail. They are all related to increasing competition: on the one hand the very survival of the Bourbon banks prompted the National Bank to quickly extend its services across the whole South, on the other the former had to rapidly adapt to the new business environment.

As predicted by the literature on foreign banking, the National Bank was responsible for the introduction of new products and business practices, above all the issue of banknotes. Banknotes and deposit certificates could

⁶⁵ Camera dei Deputati (1869), 1st vol., pp. 20–1.

⁶⁶ See Battilani et al. (2014).

serve similar needs but were two different means of payments. Banknotes were anonymous and standardised and – in the case of those issued by the National Bank – accepted all over the country thanks to the nationwide extension of its branch network. The deposit notes of the Southern banks were in contrast registered certificates of any denomination transferable by endorsement which could also include specific conditions for payment and, more importantly, could be refunded in case of theft – a non-trivial advantage in a region plagued by urban crime and brigandage.⁶⁷ Furthermore, in the mid-1860s the Bank of Naples introduced its own bearer notes to compete with the National Bank on the same ground.⁶⁸ Thus, Southerners were able to choose between different means of payment. Once the Southern banks also started to build their own branch network across the South and in the rest of Italy, the advantages of being able to choose between different kinds of paper instruments further increased, as they were now all – albeit to various degrees – national in reach.

As mentioned above, besides new means of payment both the National Bank and the Southern banks introduced savings accounts.⁶⁹ Previously, the Southern banks had been able to collect large deposits at no interest because they were the only ones issuing paper money under an implicit state guarantee.⁷⁰ With the arrival of the National Bank, however, all this changed and the three banks of issue had suddenly to compete for funding. Although the interest rates offered on short-term deposits were modest (2.5 per cent), this was a welcome innovation given the South's traditional lack of safe assets other than public bonds in which to invest.

Conditions for being admitted to discount were roughly similar for all banks of issue. There were, however, small differences (with regards to the maturity of bills, number of signatures and the like) that, without leading to actual market fragmentation, enabled clients to choose the best services according to their own needs.⁷¹ Furthermore, increased competition for discounting encouraged the Banks of Naples and Sicily to venture in new markets. So, they welcomed the government's proposal to engage in mortgage lending (*credito fondiario*), which was a major breakthrough in a mostly agricultural region like Southern Italy,⁷² while the Bank of Naples was also entrusted with the management of a savings bank.⁷³

Under the competition of the National Bank, Southern banks not only started to expand territorially and offer new services, but also improved their business practices. Heir to a tradition of deposit banking dating back to the sixteenth century, they were traditionally overstaffed, poor supervised and struggling with a complex accounting system. The competition with the National Bank, a more modern institution, finally forced them to keep abreast of the times and implement several internal reforms in their governance structure, accounting system and personnel management.⁷⁴ Even more importantly, the Southern banks became much more efficient in investing their funds, with a ratio of lending volume to reserves converging to that of the National Bank (Figure 13).

⁶⁷ Di Martino, Felice and Vasta (2020), pp. 5–6.

⁶⁸ De Rosa (1989), pp. 61–2, 109–13.

⁶⁹ Ibid., pp. 199–204; Giuffrida (1973), p. 19. The Bank of Naples was even managing its own savings bank in Naples, whose activities have not been considered in this paper (see below in the text).

⁷⁰ Camera dei Deputati (1869), 1st vol., p. 38.

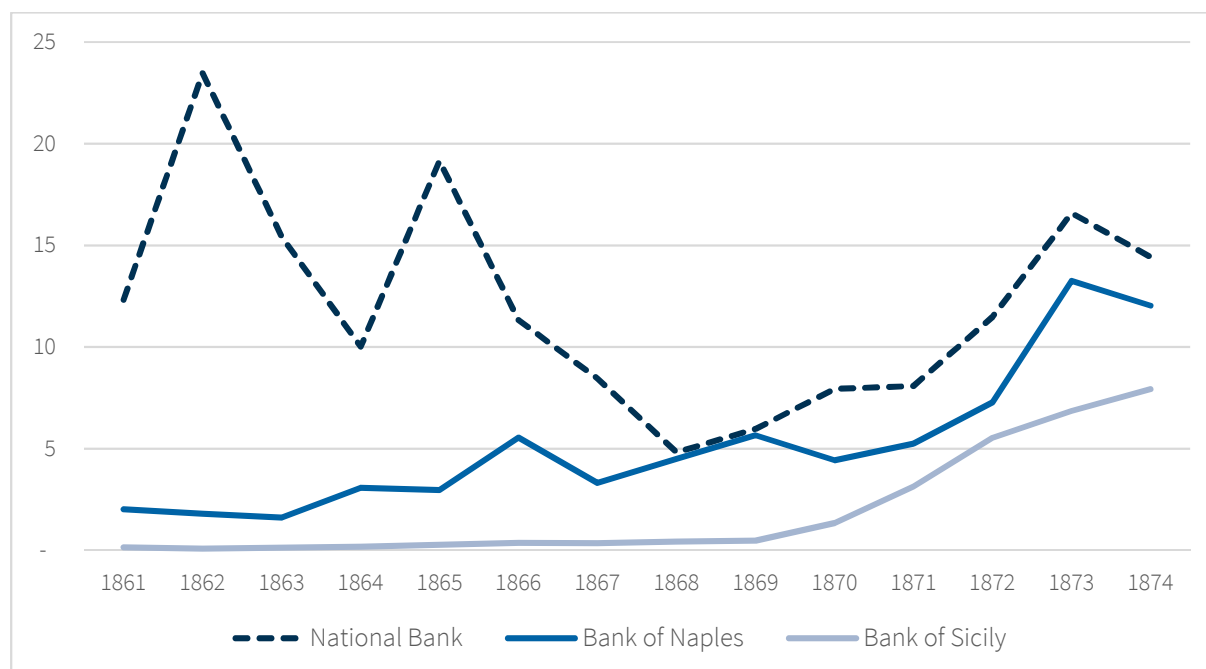
⁷¹ Chiaruttini (2019), p. 268.

⁷² De Rosa (1989), pp. 47–58, 243–54; Giuffrida (1973), pp. 194–8.

⁷³ Demarco (1958), pp. 448–51; De Rosa (1989), pp. 34–8.

⁷⁴ Demarco (1958), pp. 460–4; De Rosa (1989), pp. 268–77; Piluso (2017), pp. 29–35.

Figure 13. Loan-to-reserve ratio of the National Bank, the Bank of Naples and the Bank of Sicily



Note: The loan-to-reserve ratio is calculated as the ratio of the annual lending volume to metal reserves.

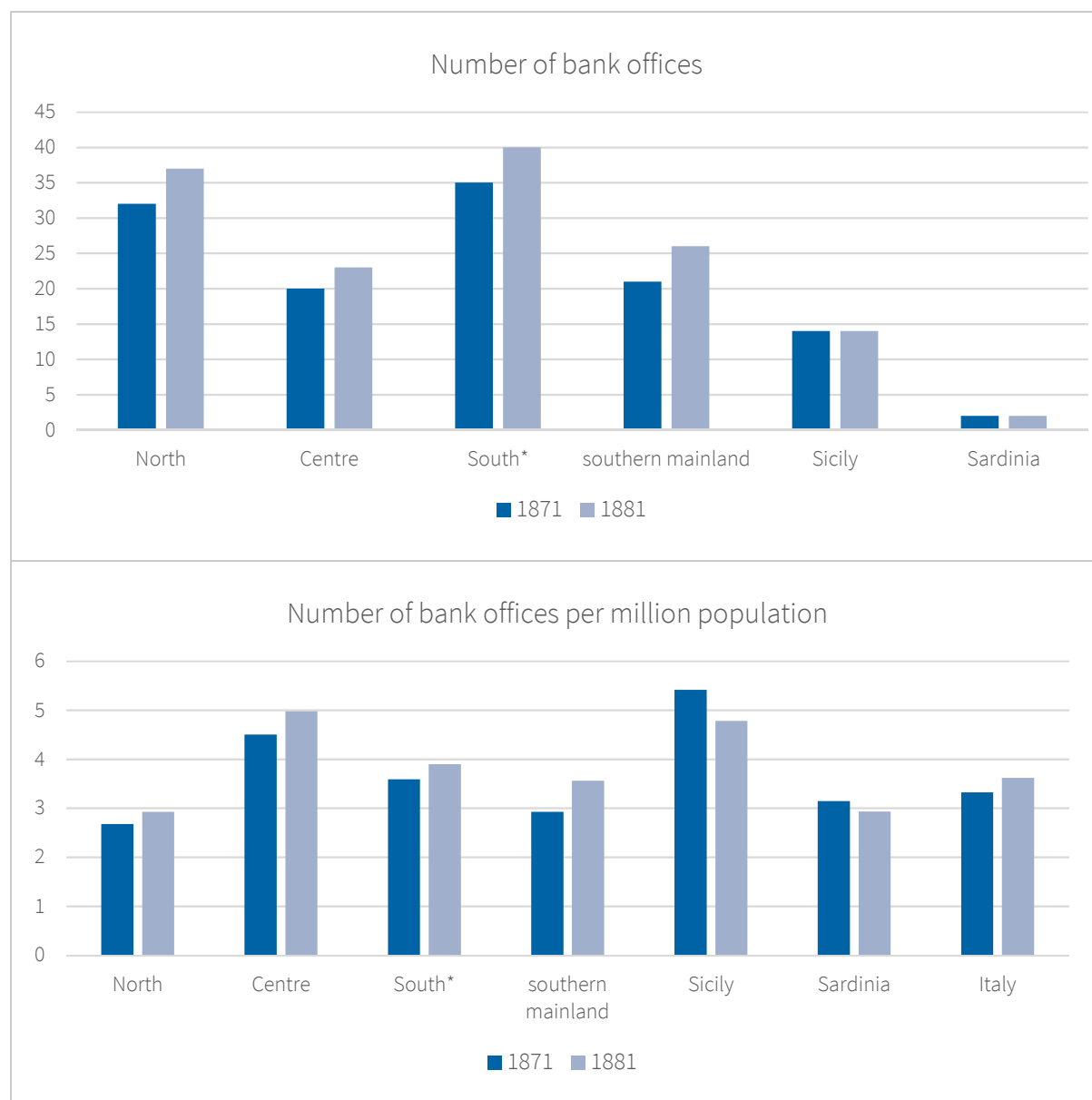
Source: Author's calculations based on data from De Mattia (1967).

Nowhere, however, were the benefits of 'foreign' banking more strongly felt than in the Southern provinces, which all of a sudden, thanks to the branch network of the National Bank, had access to discount facilities under the same conditions – in terms of interest rates and eligibility – of Naples and Palermo. Immediately after Unification, the National Bank opened three branches in Sicily (Palermo, Messina, Catania), followed by four others by 1866. On the southern mainland, apart from Naples, by 1874 it was present in 14 towns. From the mid-1860s until the creation of the Bank of Italy in 1893, the South (excluding Sardinia) could boast one third of all its branches. In terms of branch density, in 1871 Sicily had as many National Bank branches per million inhabitants as the North (2.7), while the southern mainland fared only slightly worse (2.1).⁷⁵

The National Bank, however, also contributed indirectly to financial deepening in the South by triggering the competitive reaction of the Banks of Naples and Sicily. If we take into account the branch networks of all the six Italian banks of issue (two Tuscan banks active only regionally, the Roman Bank only present in Rome and the two Southern banks, which had a few offices outside the South), it turns out that the South had the highest number of bank branches in Italy, with Sicily having the highest branch density and the southern mainland more branches per million inhabitants than the North (Figure 14).

⁷⁵ The ratio increases to 2.2 if we include Benevento, see note to Fig. 10. Counting Benevento, by 1874 the National Bank was present in 16 cities on the southern mainland.

Figure 14. Head offices and branches of the Italian banks of issue per region and million population



Note: The branches of the Tuscan National Bank (*Banca Nazionale Toscana*), the Tuscan Bank of Credit for Italian Industries and Commerce (*Banca Toscana di Credito per le Industrie e il Commercio d'Italia*) and the Roman Bank (*Banca Romana*) are all included. Benevento is excluded, see Fig. 10.

Source: Author's calculations based on data from ASBI/RD/BNRI/RA; ASBN/RA; Camera dei Deputati (1869), 1st vol.; Giuffrida (1973). Population data by courtesy of Emanuele Felice, see Felice (2019).

This does not mean that overall Southerners enjoyed better banking facilities than their compatriots, since the data only refer to the banks of issue. These figures do, however, highlight the transformative power of competition in this specific segment of the market, in an age in which banks of issue were among the largest players. Moreover, the fact that the National Bank always managed more branches in the South than the Southern banks themselves (Figure 10) implied that it was also present in smaller towns in which it would have been less profitable for the latter to invest.

To gauge the extent of credit under-provision in the Southern provinces until the very last years of the Bourbon regime is wishful thinking, but from the activity increase of the National Bank's branches in the first decade after

Unification we can at least get a sense of their prior ‘credit hunger’, even more so if one believes, as revisionists do, although apparently without much ground,⁷⁶ that the Southern economy was seriously impaired by the shock of Unification. Table 5 provides the average annual growth rate of lending per capita at branch level since 1861 excluding the first year of activity, which is always characterised by a very large growth rate due to the initial small business volume. As growth rates tend to be higher for younger branches, Table 5 groups them by years of existence (more than ten years, from six to ten, and less than six years). Clearly, the more meaningful figures are those of the oldest branches, because the growth spurt of the first years is diluted and because data are very close to the pre-Unification period.

Table 5. Average annual growth rate of the per capita lending volume of the head offices and branches of the National Bank for the period 1861–74 and years of activity until 1874

Office	Growth	Years	Office	Growth	Years	Office	Growth	Years
Bari	33.7	12	Cosenza	22.4	9	Potenza	119.0	4
Palermo	32.1	14	Lecce	19.5	10	Campobasso	69.2	5
Chieti	29.5	12	Avellino	16.8	8			
Foggia	22.5	13	Caserta	15.8	6			
Catania	21.4	13	Agrigento	15.5	9			
Reggio Calabria	19.6	13	Salerno	15.3	9			
Aquila	15.4	11	Teramo	13.2	9			
Naples	13.6	14	Catanzaro	12.6	10			
Messina	10.1	14	Trapani	11.9	9			
			Caltanissetta	10.9	9			
			Syracuse	4.3	10			
North	5.2	15	North	19.7	9	North	145.1	5
Centre	14.8	14	Centre	7.5	10	Centre	51.5	4
South*	22.0	13	South*	14.4	9	South*	94.1	5
Sardinia	9.5	14	Sardinia	-	-	Sardinia	-	-

Note: Growth rates are calculated from the second year of activity onwards. Population data are interpolated on the basis of census figures in 1861, 1871 and 1881. South* excludes Sardinia. Benevento (est. 1868; average annual growth rate: 10.2) is excluded, see Fig. 10.

Source: Author’s calculations based on data from ASBI/RD/BNRI/RA.

Among branches operating for more than ten years, Southern branches show the highest per capita growth rate. For branches with ten or less years of activity, growth rates in the South are still substantial, though growth is now higher in the North due to the excellent performance of the Lombard branches and the annexation of Venetia, a

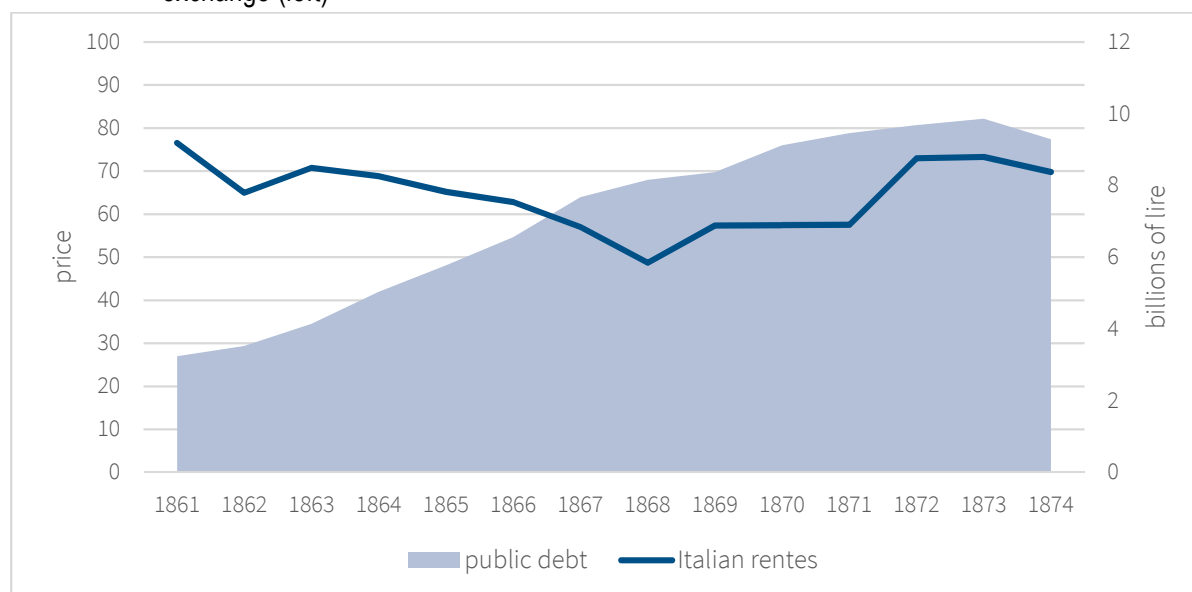
⁷⁶ See Ciccarelli and Fenoaltea (2013); Federico et al. (2019).

region with a good level of industrialisation⁷⁷ and where previously there was only one small bank of issue, taken over by the National Bank.

Despite the activism of the National Bank – motivated not by philanthropy but by the need to compete with the other banks and to assert itself as the largest issuing bank so as to claim monopoly of note issue – the financial sector in the South remained, however, less developed than in the rest of the country. Unification led everywhere to a flourishing of financial activities, including the creation of new joint-stock companies – among which many banks – listed on local exchanges and the spread of various credit institutions, like savings banks, previously almost unknown in the South. This progress notwithstanding and despite the fact that official statistics are not fully reliable and must therefore be taken with a grain of salt, they all point to a significant financial divide between North and South. Between 1870 and 1873, at the height of a speculative bubble, only 15 new banks were founded in the former Two Sicilies (South excluding Sardinia) as against 93 in the North and 30 in Central Italy.⁷⁸ In 1871, the North had 50 per cent of all cooperative banks for 66 per cent of their total capital, while the South had only 8 per cent of the total number for 4 per cent of the total capital,⁷⁹ although the region caught up in the following decades.⁸⁰

Equity markets were also severely underdeveloped, as Southern investors continued to prefer investing in public debt and land, a penchant they could indulge thanks to the large issues of high-yielding public bonds (Figure 15) and the sales of state property at equally attractive prices.

Figure 15. Total amount of Italian rentes (right) and their annual average prices on the Genoa stock exchange (left)



Source: Author's calculations based on data from Da Pozzo and Felloni (1964); Francese and Pace (2008).

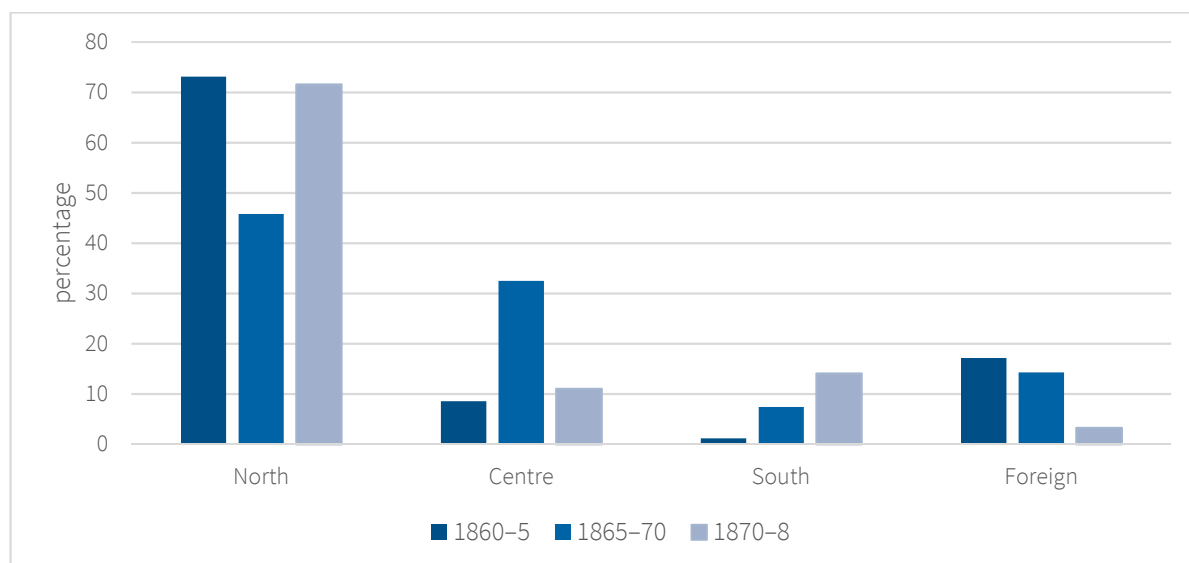
⁷⁷ Ciccarelli and Fenoaltea (2013); Felice (2019).

⁷⁸ Polsi (1993), p. 101.

⁷⁹ Ibid., p. 245.

⁸⁰ A'Hearn (2000).

Figure 16. Regional distribution of bank equity holdings (new subscriptions)



Source: Author's calculations based on data from Polsi (1993).

By contrast, very few invested in equity. In 1860–5, 82 per cent of all new shares in banking were subscribed in Northern and Central Italy against 1.2 in the South, although the situation mildly improved over time (Figure 16).

Table 6. Regional distribution of bank equity holdings (number of subscriptions) across professional classes, macro-areas and selected regions in the 1870s

	Finance	Industry and Trade	Professionals	Landowners	Others	Total
Piedmont	5.7	7.9	2.5	0.8	1.4	18.3
Liguria	7.9	19.5	2.7	1.1	1.6	32.8
Lombardy	6.5	5.5	1.7	1.7	0.4	15.8
Venetia	2.3	1.8	0.8	0.5	0.4	5.8
Tuscany-Umbria	3.6	1.8	1.3	1.8	0.6	9.2
southern mainland	1.0	1.1	0.3	1.0	0.5	3.8
Sicily	0.6	4.0	0.8	0.6	0.7	6.7
North	23.4	35.5	8.6	4.9	3.9	76.3
Centre	4.6	2.2	2.1	2.2	0.8	11.9
South*	1.6	5.0	1.1	1.5	1.3	10.5

Note: South* does not include Sardinia.

Source: Author's calculations based on data from Polsi (1993).

That investment patterns corresponded to social and economic conditions is further confirmed by the distribution of bank equity holdings across professional categories. The vast majority of investors in the banking sector were Northern industrialists and bankers, in particular from Piedmont, Liguria and Lombardy, while Southern shareholders were almost irrelevant (Table 6). However, what is maybe even more striking is the little participation of financiers among them: on the southern mainland there were as few bankers as landowners investing in bank shares and they were less numerous, for instance, than Lombard professionals (such as lawyers or engineers). In Sicily, the only significant contributions came from industrialists (likely owners of sulphur mines) and merchants. The contrast with the North is all the more glaring as in the South lived almost 40 per cent of the Italian population.

In 2005, A'Hearn found no clear support to the hypothesis that the growing divergence between Northern and Southern Italy was due to a collapse of Southern banking following the financial crisis of the early 1890s, concluding rather that the South appeared to be 'a chronically and comprehensively unhealthy environment for banks'.⁸¹ Similarly, looking at the previous period, this paper shows that if the South lagged far behind the North in terms of financial development, this was not due to the shock of Unification, at least as far as banking is concerned. In fact, Italian unification ushered in a banking revolution which, rather than increasing, helped reduce the financial gap already existing between Northern and Southern Italy, although never really managing to bridge it. This gap, in turn, originated well before Unification, was not the result of a lack of capital – as a hasty analogy with the South's current condition might suggest – but rather of its inefficient redistribution through a well-functioning credit system. This evident failure, due to poor state policies, highly hierarchical and segmented credit markets as well as presumably high inequality, made the Kingdom of the Two Sicilies unable to leverage its vast resources to the advantage of the real economy, in stark contrast with a country, like Piedmont-Sardinia, which did not command much capital but was able to multiply it through a modern banking system.

5. Conclusions

Over the last years, Southern cultural and political associations have been increasingly vocal in claiming that the Italian North-South divide stems from Unification and the top-down imposition of financial integration on the new country. According to this narrative, the Southern banking system was sacrificed to make room for the Piedmontese champion – the future Bank of Italy –, whose nationwide expansion only aimed at channelling Southern savings to the North in order to finance industrial development there, thus relegating the South to the role of an agrarian internal colony.

This paper critically revises – and refutes – such claims. Although by joining the North the South did suffer from monetary constraints and growing public indebtedness, it clearly gained in terms of credit development. The present analysis in fact suggests that differences between the Kingdom of Sardinia and the Two Sicilies in the level of financial development *did* play a role in the emergence of the North-South divide *before* national unification,

⁸¹ A'Hearn (2005), p. 38.

while thereafter the adoption of new banking institutions and practices contributed to creating a more level playing field between North and South.

The penetration of 'foreign' (i.e. Northern) banking into the Southern market made it more vulnerable to financial contagion within a macroeconomic framework characterised by higher integration at international level and excessive public indebtedness. This vulnerability was however compensated by the standard advantages usually highlighted by the literature on foreign banking, namely increased competition, easier access to credit and improved business practices. Even more importantly, banking competition led to growing integration within the Southern credit markets themselves and a more even distribution of capital at provincial level.

If we like the paradigm of 'internal colonisation', we should perhaps consider whether, with hindsight, it would better suit the North-South dynamics of post-Unification Italy or the centre-periphery relationship prevailing in the previous decades between Naples and Palermo, on the one hand, and the Southern provinces on the other. Reflecting on the amount of resources that could have been invested in the South under the Bourbons but were instead left idle because of an inefficient and fragmented banking sector would probably contribute to a better understanding of the early emergence of an economic North-South divide more than just blaming post-Unification policies indiscriminately.

While in the current political debate Italy is pitted as an undivided nation against hostile foreign institutions and the European project itself is being widely questioned, domestically its history is increasingly often recounted as one of internal colonisation. This is not, however, the picture emerging if we look at credit markets in the nineteenth century. In fact, banking history shows that financial integration following Unification, though entailing substantial costs in terms of monetary and fiscal policy, significantly contributed to mitigate rather than widen the economic divide between Northern and Southern regions. In this case at least, economic and political integration was the solution, not the problem.

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