April 18, 1944

(Hearing called off)

DRAFT OF STATEMENT BY CHAIRMAN ECCLES
BEFORE THE HOUSE BANKING AND CURRENCY COMMITTEE

Mr. Chairman and Members of the Committee:

Four weeks ago I appeared before the Senate Committee on Banking and Currency to discuss the extension of the emergency price control act. My conviction about the importance of the extension of this act without restrictive amendments and for a sufficient time after the war to allow industry to swing into full production has not changed since then. I shall be glad, however, to restate briefly the more important points in my earlier statement and to add a few supplementary remarks.

The fact that there is no serious disagreement about continuing the legislation is a tribute to your statesmanship. It would be tragic if price stability became an issue in party politics. The line against inflation must be held. Special interests must be subordinated to the general good. But we must also realize that each minor revision aimed at eliminating this or that irritation or removing small inequities, while in itself of little importance, may in conjunction with other minor changes drive a fatal wedge into our stabilization program. I think this is the real danger against which we must guard. There is, of course, room for improvement in the administration of the act--it would be miraculous indeed if so enormous a venture as the control of wartime prices and rationing could be accomplished without difficulty. The evidence shows that improvements are being made and that further improvements can be expected within the framework of the existing legislation. I have full confidence that Mr. Bowles is doing everything he can to improve the operations of the programs and to make adjustments wherever they can be made safely.

The record so far has been good,--extremely good when compared to that of World War I. The cost of living has increased by only 26 per cent from August 1939 to February of this year, and for 12 straight months it has remained stable. In comparison the increase in the corresponding period of the first World War was 65 per cent, notwithstanding the fact that rate of war expenditures now is six times that in World War I. In view of this record, it is only common sense to let well enough alone. Changes here or there might produce minor benefits, but if once opened for amendments, the risks of serious damage to stability are too great to take.

Price controls during the war

We are about to enter the decisive phase of this war. All our strength must be concentrated to bring it to its earliest victorious conclusion. On the home front this means a continued all-out production effort, an effort which is impossible if our attentions are distracted by concern over the effects of rising prices. We are all aware that large inflationary potentials exist in the form of liquid balances held by individuals and business firms and in the form of demands for higher prices and wages by producers and workers. If controls are weakened and potential inflationary forces are released, the execution of the war production program would be seriously disturbed. The proper allocation of manpower and resources would be disrupted and confusion would be inevitable.

A break in the inflation barriers would not only interfere with war production; it would work havoc with our war finances. During

the three fiscal years ending June 30, 1944, it is estimated that the federal government will have collected a total of $213 billion of receipts. Of this, only $78 billion will have been obtained from taxes, leaving $135 billion or 64 per cent obtained in the form of loans. For the current fiscal year, the Treasury expects to raise over $40 billion in borrowing. To relieve the pressure of consumers' demand upon prices and to minimize further increases in the money supply, it is important that these loans be drawn as much as possible from the average citizen, and as little as possible from the banks. Our system of war finance thus rests squarely on the people's willingness to lend to their government. They have been willing to do so because of their complete confidence that the purchasing power of the money invested in government securities will not decline. Only if the public is firm in its faith that the value of their investments will not be placed in jeopardy, either now or after the war, can the problems of financing the war and refunding the debt continue to be met successfully. Nothing must be done which might tend to shake this confidence because without it, and without adequate taxes, we would have to rely more and more upon borrowing from the banks, which would lead us into an inflationary spiral and to disaster. By assuring that effective price control will be continued, you will contribute immeasurably to the success of our financing program, and to the restoration of vigorous enterprise after the war. By maintaining prices you will save the government billions of dollars in additional expenditures which would have to be made if prices, and hence the cost of war materials were permitted to rise.

Finally, effective price and rationing controls must be kept intact because they are an inherent part of the stabilization program which without them could not survive under the impact of potential pressures of incomes and costs. It is only through a firm all-round stabilization policy that interest groups can be given assurance that they can join in support of the general goal without risking losses to themselves. It is only on the basis of such a general "truce" in the struggle for competitive advantage that fullest cooperation can be obtained. Failure to obtain full cooperation at home means a potential loss at the battle front in morale if not in supplies of munitions.

Price controls in the transition period

Price and rationing controls are not only needed for the remainder of the war, but they will also be of crucial importance for the period of transition to peacetime production. I have urged for this reason that the price legislation be continued not only for one year, but until the war is won and the transition to peacetime production has been accomplished.

It is exceedingly difficult, to be sure, to foresee what our economic circumstances will be when the war ends, since much will depend upon the course of military events and the wisdom of the economic policies followed during the remainder of the war. History tells us, however, that the peak of inflationary pressure is seldom reached during the war itself but comes after the war when people, tired of wartime controls and restraints, want to satisfy long pent-up wants denied during the war and rush into the markets before industry is prepared to supply peacetime products in sufficiently large quantities.

Also we know that at the end of this war buying power in the hands of our consumers and businesses will be enormous. I have mentioned before that in the three fiscal years ending June 1944 the federal government will have borrowed close to $135 billion. It is estimated that of this total the commercial banks and the Federal Reserve Banks will have supplied about $65 billion, thereby creating a corresponding increase of money--deposits and currency--in the hands of the public. Of the $75 billion of bonds sold outside the banks, over $30 billion will have been in the form of war savings bonds. These can be redeemed at a fixed price at any time and are thus altogether liquid. As a result of our methods of war finance, the volume of cash, deposits and other liquid assets in the hands of the public has risen to unprecedented magnitudes. By June of this year liquid assets (currency, deposits and U. S. securities) in the hands of individuals will amount to $110 billion or more, and those in the hands of business (other than banks and insurance companies) will amount to $50 billion. By June of next year, these figures may have risen to $140 and $110 billion respectively. If these enormous wartime savings are released gradually and after industry has returned to a peacetime basis, they may contribute greatly to the maintenance of prosperity. But if they are spent too soon and the price control program has been weakened unwisely in the meantime, the resulting price rise may undermine the foundations of our economy and destroy our chance for full employment and decent opportunities for those at home as well as for the returning armed forces. We must give all possible assurance to the millions of people that the value of their bonds will not be reduced and they will not lose by waiting to cash them in until the supply of goods becomes more ample.

The Federal Reserve System in particular has a vital stake in maintaining price stability during the transition period. If prices are not maintained, the System might well be placed in the untenable position of being forced to feed inflation instead of being instrumental in restraining it. Even if prices are maintained and an orderly transition to peacetime production is assured, it is likely during this period that the public will want to sell more securities than they will want to buy. This means that unless tax receipts are substantially above expenditures, the banking system will have to purchase additional government securities. Should prices start to rise, the net liquidation of securities might easily assume large proportions with the result that the Federal Reserve System might have to absorb large amounts of government securities, thereby pumping additional money into the economy and aggravating the inflation problem. This is the story of German inflation. To assure that such a situation will not arise, the continuation of effective price and rationing controls during the transition period is essential. Combined with a fiscal policy directed at maintaining taxes and balancing the Federal budget, if employment conditions permit, the government credit will remain intact.

To repeat, we cannot be certain whether in the immediate postwar period the predominant forces will be inflationary or whether the deflationary effects of a sudden and drastic cut in the Federal budget will predominate. But by maintaining price, and where necessary, rationing controls, we shall be ready to meet such inflationary pressures as may develop. If prices tend to fall rather than rise, price ceilings are rendered automatically ineffective and will do no harm.

Price control and the postwar economy

The importance of continuing a successful stabilization program not only applies to the war economy and the transition period. It will also have a profound and probably determining effect upon our chances of maintaining a high level of income and employment after readjustments to peacetime production have been made.

The millions of people owning the savings deposited with the banks of our country, the millions who are beneficiaries of life insurance policies and of the social insurance system, and all those who have purchased war savings and other bonds, as well as educational, religious and charitable institutions dependent upon income from their endowments, have all placed their faith in the future purchasing power of the dollar. Millions are saving their funds now expecting that after the war they will be able to buy homes, automobiles and other things which had to be postponed for the duration of the war. Only by maintaining price stability can their expectations be fulfilled.

But it is not only the interest of the individual owner of savings bonds that is at stake. The large volume of savings accumulated during the war will serve in the postwar period to finance the backlog of consumers' demand for durable goods which in turn will give income and employment to millions of American workers and make it possible for enterprise to maintain a high level of operation. The savings accumulated will also serve to finance postwar expansion of business enterprise and the equipment of farms. If prices are permitted to rise this potential demand is lost to the American economy and the task of maintaining a high level of employment without deficit financing will be made that much more difficult.

We all know from experience after World War I the consequences which excessive wartime increases in prices impose. By keeping prices from getting out of line domestically and in the world market, we will protect ourselves against painful readjustments at a later date. A sound postwar economy cannot be erected on the basis of the gross distortions and inequities which accompany a period of drastic price increase.

The war years have changed our conceptions with respect to the productive capacity of the American economy. The record of war production stands as a tremendous challenge to American business to provide a comparable level of peacetime production in years to come. To meet this challenge, business must be assured of price stability because the uncertainties of price fluctuations weaken business incentives to plan for the future and tend to turn enterprise into a gamble. Like other sectors of the American community, business has thus a most vital stake in maintaining the value of the dollar. Price stability is essential for a victorious peace as well as for a victorious war.

R.A.M.
K.B.W.