

MORE LIBERTY BONDS, OR MORE INCOME?

BY

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There are undoubtedly thousands of Americans who are to-day puzzled in endeavoring to determine how many Liberty bonds they should buy. It is not intended in this article to formulate rules by which one may accurately decide his duty in this matter. That decision must be made by each individual according to his ability, his personal needs, and his patriotic impulses. But some light may be thrown on the subject by presenting various aspects of the question which may not have occurred to the reader. The question certainly involves perplexities which many who are unacquainted with the relations of Government finances to the security markets find difficulty in solving to their own satisfaction. Needless to say the financial officers of our Government are confronted with like perplexities, only from quite a different standpoint. The individual is considering his own comforts, or, possibly, what he believes to be his necessities. His viewpoint is a narrow one compared with that of the Secretary of the Treasury, who is charged with the duty of borrowing a large part of the money required for the prosecution of the war but who, at the same time, must so shape his plans, within the limits imposed by Congress, so that the business of the country which is essential to winning the war, may proceed and even be extended without being hampered for lack of capital. But the money must be raised!

In the early months of the war, the Treasury was required to provide funds without any accurate measure by which the amount could be determined. Congress was appropriating billions for war purposes. We were promptly called

upon to make large advances to the governments which are allied against Germany, but no one knew, or could estimate, how rapidly the funds appropriated by Congress could be spent by the various departments of the Government, so that, necessarily, the borrowing policy of the Treasury could only be mapped out in a tentative way until experience disclosed at what rate war materials could be produced and money be actually spent.

Since late in 1917, advances to allied governments and our own expenditures by the army and navy departments, have become more stable and regular. Those who are raising funds can estimate with more certainty how much will be disbursed over a given period; in fact, the Government's financing has developed a rhythm which permits a fair judgment of requirements for periods of from four to six months in advance. Assuming that expenditures will shortly amount to \$2,000,000,000 a month, and that it is possible for Congress to levy taxes which will produce a total of, say, \$8,000,000,000 for this fiscal year, there will still remain \$16,000,000,000 to be raised by borrowing. The success of these borrowing operations will depend primarily upon the extent to which our people are willing to economize and then upon the extent to which they are willing to turn over the fruits of their economies to the Government. Unexpended income is generally represented in this country by unused balances in the bank. The Government needs those idle bank balances and asks its citizens to hand them over to the Treasury in exchange for interest bearing bonds. Therefore, successful borrowing by the Treasury will depend upon the amount of those idle bank balances and upon whether their owners will be willing to exchange them for Government bonds.

The bonds recently issued by the Government, known as the Third Liberty Loan, bear interest at 4 1-4% and were offered at par. It was, therefore, quite natural that anyone having idle funds in bank should ask him-

self the question, - Is it my duty to buy a 4 1-4% Government bond at par when I can buy other good bonds and stocks which will pay me a return of 6% or 8%, or even more?

Each investor must be his own judge in deciding between his duty to his Government and his own real needs in the way of income. It is not difficult, however, to state some simple examples which may be an aid in arriving at a decision, and the importance of the decision will be appreciated when one realizes that the sum of all of these decisions by all of the investors in the country is what will make war loans successes or failures.

Possibly the first point to consider in choosing between a subscription to Liberty bonds or the purchase of other bonds or stocks which pay a higher return, is whether an investment in some other security may aid or hinder the Government in the prosecution of the war. There is no choice whatever between investing in the war bonds of the Government or in new issues of securities made by enterprises which are engaged in operations which are of no assistance to our war activities. At this time no citizen has a right to divert surplus income to the creation of nonessential industries when that income is needed by the Government for war purposes. That question has already been answered by our Government for every investor. Capital Issues Committees have been appointed, pursuant to Act of Congress, to determine whether it is or is not in the public interest to allow any given issue of new securities to be offered to the public. When bankers offer bonds or stocks which are advertised as having been submitted to the Capital Issues Committee and approved by that Committee as not incompatible with the public interest, it may clearly be understood by the investor that our Government has passed upon the question as to whether investments in such securities will aid or injure the Government's war finance program, and, so far as the investor is concerned, he need make no further inquiry as to whether that particular security is or is not suitable for

investment at the present time. Its issue has received the Government's approval. He may feel justified, because of his own needs and those of his family, in purchasing securities of that class on the ground that it affords indirect aid to the prosecution of the war. There are, however, few in this country who are able by practicing economy to increase their savings fund at this time who cannot also afford the trifling sacrifice of additional income involved through the purchase of Liberty bonds rather than some other investment, and their satisfaction in rendering direct aid to the Government will certainly more than offset the slight loss in income. But this does not answer the investor's question as to whether he may not purchase some existing security which pays a higher return than Liberty bonds. Here a nice question arises which will be discussed later.

Another example may be used to illustrate the state of mind of an investor who must consider his own personal necessities. He may be a poor man who has been dependent upon a small salary or a small income from a nest egg of investments accumulated after long years of toil; he may have saved a small part of this income, or, possibly, some of his investments paying a high rate of interest may have been repaid at maturity. He is conscious of the fact that it costs him more to live, with prices at their present high level, than it did before the war. Must he make the sacrifice involved in accepting 4 1-4% interest instead of a higher rate, possibly even 6% or 8% which he may have been receiving until his old investments were repaid? This is necessarily one of those doubtful cases where each man must decide according to his present needs, as contrasted with the needs of his Government. If economies can be practiced which will not interfere with the maintenance of his health, or that of his family, or with the education of his children, or with continued efficiency in his work, he is justified, and, possibly, required as a matter of duty to forego a larger income in order that his Government may have his support. By this sacrifice he assumes his share of the burden of the war. On

the other hand, if it really involve impairment of health, or efficiency, or the loss of education for his children, such a person is, doubtless, warranted in making investments of a character that will pay a higher return so as to maintain the standard of living that is essential for the welfare of that individual, and of his family, and, through them, of the nation. But, in selecting an investment which pays a higher return, it is desirable, if possible, to pick out some new issue and, of course, a sound security, which has received the stamp of approval of the Capital Issues Committee, so thereby he gives support to some enterprise which is engaged in work that directly or indirectly promotes the prosecution of the war, and which needs new capital. If this is a fair statement of the position of a man with an income of, say, twenty-four hundred dollars a year, who is able to save two hundred dollars; it is still hard to justify withholding his savings from the Government. Two hundred dollars invested at 4 1-4% produces \$8.50 a year and at 7 1-2% \$15.00 a year. He foregoes an additional income of \$6.50 per annum, which even the poorest man can afford, and it must not be overlooked that the income from his new investment is free of any taxes whatever. This may seem an insignificant contribution to the Government's war effort, but 10,000,000 people making an investment of this size can furnish the Government with \$2,000,000,000, which is one-third of the probable amount of the Fourth Liberty Loan.

A third class of investors, now a much larger one than is realized, comprises those patriotic men and women who have abandoned business or professional occupations to enter the army or navy or Red Cross, or other branches of the service, in consequence of which their incomes have been greatly reduced and often the good-will of a business or of a professional practice jeopardised for all time; frequently, in fact, notwithstanding that these men and women may have dependent children to support. Let us take as an illustration a

successful young lawyer who has built up a practice which has been paying him \$10,000 a year; he has accumulated, say, \$10,000 by economy and saving; he has a wife and children. In surrendering his practice to enter the Government's service, his income may be reduced to a salary of \$2,000 a year or less. His income from his securities may bring this up to \$2,700 a year. In winding up his practice he collects outstanding bills from his clients totaling \$10,000 and must decide whether to spend this money in maintaining his former standard of living or to invest it in some security paying a high return so as to help mitigate the hardship of enforced economy, or to buy Liberty bonds. A man of strong character, with a family loyal to the purpose for which he has made the sacrifice of his practice, may be able to readjust his plan of living to an income of \$2,700 a year, plus the \$425. additional income from the Liberty bonds that he buys, and still be perfectly happy and comfortable and feel that he is doing his duty both to his family and to his Government. On the other hand, he may be tempted to believe that in order to educate children who are at school and college, and to maintain his own health and efficiency, it is necessary to obtain a larger income than is possible by the investment in Government bonds. There is certainly no reason why that man should be condemned for risking the future of his family, the education of his children, or even his own health, by declining to make the additional sacrifice of income involved in the purchase of a 4 1-4% Government bond. But he has already made a sacrifice of great proportions and while the nation can well afford to insure his efficiency by permitting him to obtain the largest income possible from an investment in some security issued by a corporation which is engaged in war work, the chances are that one who makes such sacrifices as this can be relied upon to make the small additional sacrifice of income involved in purchasing the war bonds of his Government.

A fourth type to consider is the man of large income who spends but

a fraction of it and has large amounts to invest every year. This man should have little difficulty in his decision - if he is engaged in some business directly promoting the prosecution of the war, which requires for its necessary development the employment of increased amounts of capital, he should not, of course, hamper the efficiency of his business by withholding from it the capital which possibly he, alone, can furnish by so employing a portion or all of his surplus income. This applies to the manufacturer of war materials particularly. On the other hand, if he is a retired capitalist, with an income beyond his needs, it is unquestionably his duty to the nation to invest every dollar of the surplus which he accumulates in the bonds of the Government, beyond, possibly, a moderate amount in new security issues bearing the stamp of approval of the Capital Issues Committee, which he may consider safe.

These are only a few of a great variety of types of possible investors who face a decision which is vital to the nation and they are referred to simply for illustrative purposes. There are, however, principles of great importance underlying the whole question of the purchase and sale of securities by investors in these war times, which should be considered by every investor before he decides what he shall do with his savings.

When one buys a security in the security market, it may be that the seller, in turn, will invest the proceeds in Government bonds. On the other hand, it may be that the person selling the securities desires funds for some purpose not at all related to the war, or, in fact, to waste in quite unnecessary living expenses or extravagances. The buyer can hardly stipulate with the seller as to how the latter shall spend the money, but can he take the risk of the seller's intentions? Of course the existence of a security market where investment securities are bought and sold is a facility which in many ways aids Government financing, and, deprived of that facility, the Government would

encounter difficulties which would not arise if a security market did not exist. An active market where the ownership of securities can be promptly shifted from one person to another is one of the means by which those who desire to buy Government bonds, and are willing to sell existing investments for the purpose, are enabled to do so without delay and often without great loss. Not every sale of investment bonds and stocks is, however, inspired by that desire, although these constant transfers of investments do to some unknown extent result in the transfer of bank balances from those who have accumulated them without expectation, and, possibly, without ability to buy Government bonds, to the ownership of those who are able and willing to do so. When the Government places a Liberty Loan, all those who have money to invest are brought under the influence of a great campaign of education, which is, in fact, a great selling campaign. Those who have accumulated the bank balances by selling their investments are just as subject to the influence of the campaign as are those who in the first instance accumulated the bank balances by thrift or otherwise and later transferred them to other persons in exchange for securities. It can hardly be claimed, therefore, that the available investment fund of the nation is reduced as the result of such transfers of securities. The important thing is to reach all owners of idle bank balances, however those balances may have arisen, with the Liberty Loan propaganda and induce them to buy Government bonds; those who can not afford to invest in low-rate securities making it possible for others who can afford to do so by purchasing from them the securities which they are willing to sell. To illustrate this point, if we assume that the total value of all investment securities in this country aggregate 350,000,000,000 at the time of a Liberty Loan offering; that at the same time the total of idle bank balances in the country aggregates \$6,000,000,000; and that the Government is inviting subscriptions to \$6,000,000,000 of Liberty bonds, it makes no difference in the result whether the \$6,000,000,000 is turned over to the Treasury in exchange for Liberty bonds

by those who originally accumulated the \$6,000,000,000 or by others who have acquired those bank balances by selling the portion of the \$50,000,000,000 of securities which they formerly owned. This process of shifting of ownership between investors, as stated above, does, indeed, to some extent, facilitate the Government's borrowing operations. But there is another aspect of the security markets, which bears on this matter, where influences may arise which could be highly detrimental to the Government's borrowing program. Suppose a large number of people with idle funds became interested in the market in a speculative way, rather than simply as purchasers of investment securities; and because they believed that stocks and bonds would advance, were led to use their surplus income as margin for the purchase of securities which they could not fully pay for, and, in consequence, borrowed heavily from the banks in order to carry them. Such a movement might gain speculative headway and result in a general advance in security prices, particularly those of a speculative nature. People in this country only too readily develop an insatiable appetite to buy securities "for a rise." The result of such a movement would be a great increase in bank loans; - speculators can borrow more money on stocks as they advance in price, and generally do; bank credit would, as a result, be absorbed and the surplus earnings of many individuals, which might have been applied to the purchase of Government bonds, would be used as margin in speculative operations which would serve only to clog the banking machine. This would clearly be a diversion of investment funds from legitimate to illegitimate purposes when it is considered that the nation is at war and needs those funds. It may, in general, be said that the existence of a security market, where investment securities may be readily bought and sold, is a good thing, probably even an essential thing in order to preserve the stability of financial affairs during war time; - but that on the contrary, the existence of a speculation which attracts capital to speculative operations is

an unessential and often a dangerous thing. We must not overlook the fact that the existence of a market for securities enables thousands of investors to use their securities as the basis for quite legitimate borrowings, frequently when funds are desired in order to subscribe for Government bonds in anticipation of expected savings, also when capital is required to develop industries that are essential to the prosecution of the war and when credit is needed to pay off existing debts, as well as for many other valid purposes. Without a market for securities, banks would be reluctant to lend on them and billions of dollars of investments in the hands of the people of the country, which might be usefully employed as the basis of necessary and desirable credit, would be rendered unliquid and unavailable as security for bank loans. Nor can we fail to overlook the existence of a great mass of loans now held by our banks, which are secured by bonds and stocks, and which have no relation to speculative operations whatever, where the protection of the lending banks, as to the value of the collateral, depends upon the continued existence of a market where securities can be liquidated if need arises.

The financial officers of our Government are confronted with a difficult situation which they do not control and which, under our system, they have power to influence to only a slight extent. Expenditures are mapped out by the various departments of the Government, the largest now being by the war and navy departments; they are submitted to Congress and appropriation bills result, which authorize the expenditure of the various amounts demanded by the departments, as finally approved by Congress. At no point have the Treasury Officials any legal standing to control, and they can but slightly influence, the amounts of these expenditures, outside of those relating to the administration of their own department. The Treasury, therefore, is called upon to raise money, the amount of which it has no voice in determining, and the expenditure of which it has no means of controlling. Its policy must be governed, under the archaic procedure which our Government

follows, by very simple rules. Sound financing of the Government requires that as large a proportion of war expenditures as possible be raised by taxation, but not so large an amount as to impair business enterprise, and particularly those enterprises which must be developed to high speed in order to produce goods required for war purposes. If, therefore, the Treasury is provided by Congress with a given proportion, say, one-third, of the expected Government outlay from taxation, whatever else is spent must be raised by the Secretary of the Treasury through various forms of borrowing authorized by Congress at his request. Right here the attitude of the people of the country, even more than the decisions of Treasury Officials, controls developments in future years which will be of vast importance to our welfare. If we are able to pursue a policy of gradually increased taxation as industries are able to bear it, but never raising taxes to the point where essential business is injured, and if we can raise the balance of our war expenditures from voluntary subscriptions to bonds and the bonds are paid for out of savings, the country's financial condition after the war is over will be substantially unimpaired and certainly vastly better than that of some other belligerents. On the other hand, if these voluntary subscriptions are not, or can not be made, no one for a moment would assume that on that account we must stop fighting. The war must be won and the funds must be raised to win it, even if bond issues fail. The failure of a bond issue simply means that other methods must be employed, possibly methods less sound in principle and certainly less palatable in application than those which are now being pursued. The choice of methods can not be said to rest any more upon Government Officials than upon the decision which must be made by each individual who has possibly imposed upon himself rigid economy so as to be able to buy the maximum amount of Government bonds.

No patriotic citizen, whatever his means, who can afford to pur-

chase his Government's war bonds can afford to take the risk that the hard won results of his economies will be wasted by some other individual to whom he delegates this decision. That is what he does when he turns the product of his economy over to some one else in exchange for some other kind of an investment, because that other individual may see fit to waste it.

Our success in financing the war from now on will absolutely depend upon the extent to which people are willing to economize. There is no doubt as to the results which can be achieved by such economies, whether they be voluntary or enforced. They can be made to produce, in this country of wealth, extravagance and waste, a sufficient fund of savings to absorb all the war bonds which the Government must issue in order to win the war.