

For release at 3 P. M.
Eastern Standard Time
Friday, April 26, 1957

Remarks by

Wm. McC. Martin, Jr.

Chairman, Board of Governors of the Federal Reserve System

In Accepting the Degree of Doctor of Laws
at the
Convocation of the University of Pennsylvania Council marking
the 75th Anniversary of the Founding of the
Wharton School of Finance and Commerce

Philadelphia, Pennsylvania
April 26, 1957
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Seventy-five years ago an increasing need for greater business learning was given farsighted recognition in the founding of the Wharton School of the University of Pennsylvania as the first school of business education in an American college.

There was an immediate need to give Americans of the late 19th century college training in business, just as the medieval colleges had given men training in theology, law and medicine. That need sprang from a transition still incomplete at the time, the transition of this country from a predominantly agricultural economy to the leading business and industrial nation of the world.

But there was recognized, too, a longer-range need -- the need to learn more about the world of business and the nature of the economic process. This was a new sort of recognition, as measured in the history of man, a recognition of the rise of the business civilization.

Since the business civilization is an ancient form to those of us living today, we are often inclined to accord the contempt bred of familiarity to some of its manifestations and to some of the grey-flanneled men who personify its shortcomings in current literature.

Yet, only a couple of centuries ago the business civilization, or, more precisely, the market system that would furnish its cornerstone, was just coming into recognition as a new way of

life that offered a promise of material advancement and individual freedom such as men had never known before.

The market system lifted men's hearts when they first saw in its development an alternative to the other two systems around which society had been organized from time immemorial.

One of these systems, prevailing in India until recent years, employed the forces of tradition to ensure the execution of the countless jobs that had to be done to keep society going -- disagreeable jobs as well as pleasant ones. By custom and usage, jobs were assigned from father to son for generation after generation, and men did the work deemed appropriate to their caste.

The other system antedating the market system was that of authoritarian rule, in which the whip of centralized power drives workers to the necessary tasks. It was used in ancient Egypt to build the pyramids. It is used in modern Russia to execute the Soviet's five-year plans.

Against these age-old systems of social control, the market system must have appeared to men of vision as a magnificent achievement in social engineering, for it provided a mechanism for sustaining and maintaining an entire society by the free and voluntary activity of its individual members. It constituted a way of life affording to the individual a dignity unknown under the older social systems. In the market system, each man would be guided to

his work by the hope of reward rather than the lash of authority or the chains of caste. Yet, though each might freely go wherever he thought his fortune lay, the interplay of one man in competition with another would result in accomplishment of all the tasks society needed done.

The transformation of this country from a wilderness to a highly developed business civilization in so short a time demonstrates the results that can be obtained through a system which is directed toward releasing rather than shackling the energies and abilities of the individual.

The advantages of a system where supply capacities and demands and needs are matched in open markets cannot be measured in economic terms alone. In addition to the advantages of efficiency in the use of economic resources, there are vast gains in terms of personal liberty. Powers of decision are dispersed among the millions affected, instead of being centralized in a few persons in authority.

The basic concept of the market system has remained with us since the founding of the nation. It has remained the cornerstone of our society down to this day, although we have done some extensive remodeling of the structure as a whole from time to time.

Some of the remodeling we have done in the past has been for the admirable purpose of correcting structural defects and

distortions that were warping the system. Competitive, freely functioning markets are one thing, and rigged markets another. Rules and regulations to prevent rigging are necessary and essential to a sound structure.

Other remodeling has come about because the American people have refused to accept economic goals as their sole objective. That was true in older generations, as well as our own. Let it be said, to our credit, that American economic action has often been determined by balancing material advance against other human objectives.

When the Wharton School was founded in 1881, the population of the United States numbered about 50 million, and rural dwellers outnumbered their urban brethren by nearly three to one. But well under way was the growth and movement that has carried our current population to more than 170 million and put city dwellers in the majority -- despite the swing to suburbia -- by a ratio of nearly two to one.

In 1881, if the phrase "party line" had any meaning at all to the students and faculty of the new business school, it was as a reference to that comparatively new and still rare instrument, the telephone. We did not have electric lights, much less automobiles, gasoline tractors, airplanes, radio, television, wonder drugs, air conditioning, frozen fruits, vegetables, meats -- and waffles, too -- or even such words as automation and electronization.

The wonder is not that we have these things, for the American people, working under their free enterprise system, have produced and are producing material abundance as no people in history. Yet, great as are the wonders of production that have been achieved in the American system, still greater are the wonders of distribution. There would be little gain in convenience, comfort or luxury for Louis XIV or Charles II, or for Antony and Cleopatra, in living today. Our mass production and distribution system could not do much for them. It can and does provide abundance for the mass of people. It is a system for the many rather than for the few. It has provided greater equality in worldly possessions than any socialist or communist society has done, or showed the slightest prospect of doing.

Most noteworthy of all, perhaps, the American people and the American system of free enterprise have come a bit closer to abolishing poverty and its attendant evils than any one has ever come before. This is an unfinished task, however, and one that requires the use of our minds as well as the gift of our hearts.

The founding of the Wharton School demonstrated recognition that the business process is a rational process, not a mystical or magic one, and the faith that men can master and improve it by the exercise of reason, sharpened and clarified by the discipline of objective study. It is fortunate that we have this school and its

counterparts in other universities, for the need for rational economic thought is one of the most important of our time.

We do not have to look far for an example of that need. It is evident in a suggestion often made these days that if only the Federal Reserve's monetary policy were changed we could have more new homes, more rapid construction of vitally needed schools, hospitals, and other community facilities, more new automobiles, and more new highways to relieve the traffic jams we have already.

Well, it would certainly be a fine world indeed if, by merely opening wider the spigot of credit, the Federal Reserve could increase the flow of goods and services sufficiently to meet all human wants at any time. If the Federal Reserve possessed such magic, I assure you it would use it. But of course there is no such magic, and all of us will be better off if we do not act as if there were.

What is this Federal Reserve policy that some people are so anxious to change?

It is a policy of endeavoring, at all times, to assure monetary and credit conditions that will foster high levels of business and employment, maintain the stability of the currency, and promote sustainable growth in the economy.

It is a policy of combating, with equal vigor, the excesses of inflation and deflation alike. It is a policy that recognizes that inflation compounds its own cruelties by bringing deflation with its

further cruelties -- the cyclical progression we have suffered many times in the past with consequences heavy in human hardship.

Operations in execution of that policy must, of course, be adapted to the particular circumstances of an economy which, like everything else in life, is always changing. The recent record illustrates the point.

In 1954, when production was falling away from capacity and unemployment was rising, the Federal Reserve System followed a policy of combating deflation by facilitating an expansion of credit and an increase in the money supply so that idle resources might be brought back into use.

In 1956, with employment at peak levels and the economy pressing against the limits of capacity with booming intensity, the Federal Reserve System followed a general policy of combating inflation by holding further expansion of credit within the limit of resources available for use.

I do not want you to think I am claiming the System was endowed with special wisdom in either of these instances. It was, in fact, simply adhering to a realistic principle with respect to the money supply laid down long ago by the great common sense philosopher who founded this university.

Benjamin Franklin, back in 1729, wrote it down in these words:
"There is a certain proportionate quantity of money requisite to carry

on the Trade of a Country freely and currently; more than which would be of no Advantage in Trade, and less, if much less, exceedingly detrimental. "

In Benjamin Franklin's own lifetime, virtually every American was to learn -- the hard way -- the fact that there can be such a thing as too much money in the economy as well as too little. Their experience is recalled in a bitter saying we still use: "not worth a Continental. "

Since its early days, the American republic has grown enormously in complexity as well as size, but the fact remains that the capacity of any economy to produce goods and services is, at any given time, limited by the resources, human and material, that are currently available. The further fact remains that, when the economy is running at peak levels, creation of more money cannot produce more things; it can only push up prices.

Over most of the last two years, our economy has been straining its capacity under the influence of inflationary pressures. Total expenditures in terms of money have increased more than the physical output of goods and services, and buying demand, based in part on credit expansion, has been trying persistently to increase expenditures even more. This strain on the economy has been reflected in rising prices and costs, pushed up by actual spending, and rising interest rates, pushed up by the borrowing demands of those who wish to spend still more.

These things have been happening because business concerns, governments, and individuals have wanted to borrow and spend more money than they were willing and able to save in order to buy more things than can yet be produced. Basically, credit has been made tighter, and therefore more expensive, by a single phenomenon -- the development of a credit rush reminiscent of the California gold rush a little more than a century ago.

In these difficult circumstances, it has been helpful to have discussion, debate, and critical appraisal of monetary policy, and I hope we will have the benefit of more of it as time goes on.

The Federal Reserve is not infallible or perfect, and it is a good thing to keep people aware that there is no magic in monetary policy -- or any other policy or power of government -- that can ensure prosperity for everyone, in perpetuity.

It is a good thing to hold the light of reason to the illusion that economic difficulties -- and social injustices as well -- can be cured, effortlessly and painlessly, by the simple process of pumping up the supply of money and credit.

If we examine and continuously study our business civilization earnestly and honestly, I am confident that, along with our deeper knowledge, we will find strength to do greater and finer things than we have yet done. And, in doing them, we will find new faith both in our system and in ourselves.

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