Sen. Douglas' Speech 2/22/
before Senate

stitute is adopted, that the Senator from New York will not offer his amendment.

With that in mind, I ask unanimous consent that on Monday, beginning at 12 o'clock, debate upon the pending bill be limited as follows: That no amendment may be offered which is not germane; that the Senator from North Dakota [Mr. LANGER] shall have 1 hour for the discussion of his two amendments, and that the Senator from Georgia may have 1 hour, if he so desires, in opposition to those amendments—that is, that the time be limited to two hours, and be divided equally between the Senator from North Dakota and the Senator from Georgia; that, as to all other amendments and substitutes, and as to the bill itself, debate shall be limited to 30 minutes.

Mr. CASE. Mr. President, will the Senator yield?

Mr. McFARLAND. I yield.

Mr. CASE. That is with the understanding, is it not, that there shall be no restriction on any other amendments which may be offered, if germane to the bill?

Mr. McFARLAND. There will be no restriction, except as to germaneness. It is merely a restriction on debate, that is all.

Mr. LANGER. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. CHAVEZ in the chair). Does the Senator from Arizona yield to the Senator from North Dakota?

Mr. McFARLAND. I yield.

Mr. LANGER. Has the distinguished majority leader conferred with the minority leader, the Senator from Nebraska [Mr. WHERRY], about this matter?

Mr. McFARLAND. I believe we mentioned it to the minority leader, and I may say I conferred with the Senator from Ohio, who was very much interested. As I understand, it would have been agreeable to him to proceed today; but I also understand the procedure now suggested is agreeable to him. That is my understanding, though I have not asked the Senator.

Mr. LANGER. Mr. President, will the Senator yield further?

Mr. McFARLAND. I yield.

Mr. LANGER. What troubles me most regretfully, is the fact that the Senator from Nebraska [Mr. WHERRY], as minority leader, requested me not to agree to any unanimous-consent request, unless preceded by a quorum call. That is the custom. It would be very difficult to obtain a quorum today.

Mr. McFARLAND. A quorum call is not required for an agreement of this kind.

Mr. LANGER. Mr. President, if the Senator will yield further, I may say this is a very important bill.

Mr. McFARLAND. Mr. President, would the Senator from North Dakota mind contacting the distinguished Senator from Nebraska by telephone to ascertain whether he has any objection to the request?

Mr. LANGER. I shall certainly be glad to call his office, if the Senator will wait.

Mr. McFARLAND. We shall wait.

Mr. LEHMAN. Mr. President, I wish to say that at the time I submitted my amendment to House bill 1, providing for national life insurance benefits to members of the Armed Forces, I made this statement:

> At this point I should like to say that I was and I am in favor of the provisions contained in S. 84, a bill introduced by the chairman of the Senate Finance Committee. S. 84 provided that any serviceman who dies or has died in line of duty on or after June 27, 1950, shall be presumed to have been covered by a national service life insurance policy in the amount of $10,000. Obviously, the intent of this bill was to protect those Korean veterans who die in the service of our country who have not taken out a national service life insurance policy. S. 84 affected neither existing national service life insurance policies nor the rights of future veterans to those policies. However, the seeds of the idea contained in S. 84 have apparently germinated and grown in H. R. 1 into a plant which, while it contains worthwhile fruits, threatens certain rights which servicemen have enjoyed in the past. If the Senator from Georgia wishes to substitute the provisions of S. 84 for those of H. R. 1 at this point, I shall be happy to support such a move.

I merely wish to reiterate that statement, and to say that if the Senator from Georgia [Mr. GEORGE] will substitute his bill, S. 84, my cosponsors and I shall be glad to support it.

Mr. GEORGE. Mr. President, I may say that I have prepared an amendment to strike out all after the enacting clause of House bill 1 and to substitute Senate bill 84, which amendment I shall offer at the proper time.

Mr. CASE. Mr. President, will the Senator yield for a question?

Mr. GEORGE. I am glad to yield.

Mr. CASE. Would it be possible in the meantime, to have the amendment printed, so that if we follow the suggestion of the distinguished majority leader, it will be available to Senators on Monday?

Mr. GEORGE. Yes.

Mr. McFARLAND. Mr. President, I suggest that no one seems to be opposing the substitute, and we might therefore at least proceed that far with the consideration of the bill now, and we could then take up the amendments of the Senator from North Dakota on Monday. As I understand, no one objects to the substitute, everyone is agreeable to it, and we could take it up with the understanding that the Senator from North Dakota could offer his amendments to the substitute.

Mr. CASE. Mr. President, if I may pursue the matter a little further, the Senator from North Dakota, of course, may speak for himself, but it simply occurs to me that if it is a complete substitute, the question ought to be resolved whether it would be in order and whether it would be possible to amend it without a motion to reconsider.

Mr. McFARLAND. Yes; we shall take care of that.

Mr. GEORGE. It would be subject to amendment in the first degree. In other words, the Senator would not be cut off by any technical rule.

Mr. LANGER. Mr. President, I may say I have conferred with the distinguished minority leader, who says it is customary not to agree to a limitation of debate without first having a quorum call. He said it was his opinion that it would be impossible to proceed without a quorum call. However, I should be perfectly willing to proceed as far as possible, this afternoon, if desired.

Mr. McFARLAND. I think we might proceed at least to the extent indicated.

Mr. GEORGE. Mr. President, I send to the desk an amendment in the nature of a substitute, to the bill, H. R. 1, and ask that it be read.

The PRESIDING OFFICER. The clerk will state the amendment.

The LEGISLATIVE CLERK. It is proposed to strike out all after the enacting clause and insert:

> That any person in the active military or naval service, or reporting for such active service under orders of competent authority, who, on or after June 27, 1950, and before the expiration of 120 days after the date of enactment of this act, while in such service or while reporting under orders for such service, dies or has died in line of duty, shall be deemed to have applied for and to have been granted national service life insurance in the amount of $10,000, and such insurance shall be deemed to be or to have been continued in force to the date of death of such person: *Provided*, That the amount of insurance herein granted, when added to any other insurance in force under the World War Veterans' Act, 1924, as amended, or the National Service Life Insurance Act of 1940, as amended, shall not in the aggregate exceed $10,000: *Provided further*, That the insurance herein granted shall be payable in 240 equal monthly installments, with interest at 3 percent per annum, to the following beneficiaries and in the order named:
>
> (A) To the widow or widower of the insured, if living and while unremarried;
>
> (B) If no widow or widower entitled thereto, to the child or children of the insured, if living, in equal shares;
>
> (C) If no widow or widower entitled thereto, or child, to the mother or father of the insured, if living, in equal shares.

Mr. McFARLAND. Mr. President, I temporarily withdraw my unanimous-consent request.

Mr. GEORGE. Mr. President, the substitute offered leaves undisturbed the existing world war insurance, national service life insurance, but it does protect all the men who have been called into the service and who, in response to a call from competent authority, may have been killed while en route to report for duty, from June 27 last year and for a period of 120 days after the enactment of the act, by giving to them automatic insurance in the sum of $10,000. Then, within 120 days or after discharge, at any time in life they are entitled to apply for insurance and to receive Government insurance, as we speak of it, for the veterans, just as those who went into World War I and World War II were, without upsetting the insurance program we have worked out with some degree of care, I take it, for our veterans.

House bill 1, for which the substitute is offered, merely provides for an indemnity in the sum of $10,000. The theory of House bill 1 is that from the time of the passage of the bill national service life insurance, world war veterans' insurance, and all other forms of Government insurance will cease, except as to those veterans who have policies in force and effect, and except as to those who return from any present service or future service disabled to the extent that they cannot procure ordinary life insurance from a private company. In other words, the theory of the House bill is to end Government insurance for the veterans.

The Committee on Finance at first undertook to amend H. R. 1. A series of amendments were made. At the end it was voted to report H. R. 1 with these amendments, but I, as chairman of the committee, and the senior Senator from Ohio [Mr. TAFT], reserved the right to offer a substitute. Subsequently I conferred with more than a majority of the Finance Committee, and this morning had a conference with several members of the committee, at the conclusion of the hearings before the committee, and I feel that I am authorized for the committee to offer this substitute to H. R. 1.

It was the sense of the committee that we should not deprive the soldiers who go into service now, or who went in last June, of all the rights to Government life insurance enjoyed by the soldiers of World War II and World War I, all of our soldiers, and that the occasion and time had not arrived for the discontinuance of our system of Government insurance.

Moreover, Mr. President, we did not believe and do not now believe that the House program, if followed, would work any substantial economy. It is asserted by the House that it would, and that was the theory upon which the House passed the bill, but it is questionable, highly questionable, whether it would result in substantial economies, because the national life insurance must be carried on for the veterans who now have policies, and who may never enter military service again, as many of them will not, and it must also be carried on, even under the theory of the House bill, for those who have received service-connected disabilities which render them uninsurable according to the ordinary insurance standards established by private companies.

Mr. President, that being true, it would seem to the committee that there is very little reason why we should pass H. R. 1, provide this new system of indemnity, and discontinue Government insurance for the veterans. For that reason I have offered the substitute.

The PRESIDING OFFICER. If the Chair may make a suggestion to the Senator from Georgia, in order to clear the parliamentary situation unanimous consent should be requested that the substitute be regarded, for the purpose of amendment, as the original text, and that the committee amendments be withdrawn.

Mr. GEORGE. I make that request.

The PRESIDING OFFICER. Is there objection to the request? The Chair hears none, and it is so ordered.

Mr. O'MAHONEY. Mr. President, I assume no attempt is to be made to have the amendment acted on today.

Mr. McFARLAND. We should like to have the amendment acted on today, and that will leave the bill open for the amendment of the Senator from North Dakota, if the Senate takes a recess until Monday, and we will make that much progress.

Mr. O'MAHONEY. The statement of the Senator from Georgia, as usual, is most persuasive. I have no doubt that the substitute is all that it has been described to be, but there are only a few Senators upon the floor, we have not had an opportunity to examine the substitute, and those of us who were advised yesterday that H. R. 1 would be the first order of business today assumed that H. R. 1, as amended by the committee, had the support of the entire committee.

It now appears that the substitute is an altogether different amendment, and I am persuaded that, in the interest of the veterans, and in the interest of getting substantial and valuable legislation, we should not attempt at the session today to substitute this amendment for the bill which was formally reported and recommended by the Committee on Finance, in the absence of Senators who may have views quite different from those which have been expressed.

Mr. McFARLAND. Mr. President, will the Senator yield?

Mr. O'MAHONEY. I yield to the Senator from Arizona.

Mr. McFARLAND. I call the Senator's attention to the fact that it was stated yesterday that this bill would be disposed of today, and I presumed that any Senators who were interested in the bill would be present today. It is my understanding that the substitute now offered is entirely agreeable to everyone.

Mr. O'MAHONEY. I have no doubt that it is. I desire to inquire of the Senator from Georgia whether it is the intent formally to adopt the amendment now offered as a substitute at this time, without recourse on the part of Senators when the Senate reassembles at its next session.

Mr. GEORGE. No; we do not ask for final action. I offered the substitute with the usual request, that it be considered as the original text so that amendments might be offered to it. I am perfectly willing to have the substitute printed and lie over until Monday, so far as I am concerned.

Mr. O'MAHONEY. I think that would be the better practice.

Mr. GEORGE. I do not insist upon it, however.

The PRESIDING OFFICER. Does the Chair correctly understand that the Senator from Georgia asks that the amendment lie over, and that it be the pending question the next time the Senate meets?

Mr. GEORGE. That is my request, if it is agreeable to the majority leader. I ask that the substitute be printed.

Mr. McFARLAND. The amendment would be the pending question, having already been offered. Unanimous consent is not required.

Mr. GEORGE. If consent could be had limiting debate, it would be agreeable to me.

Mr. CASE. Mr. President, will the Senator yield?

Mr. GEORGE. I yield.

Mr. CASE. I must confess some unfamiliarity with the procedure in the Senate with respect to this kind of substitution. Am I correct in assuming that if the unanimous-consent request is not acted upon it would still be within the province of Senators on Monday to object to the proposed substitute for the original bill reported by the committee?

Mr. GEORGE. Oh, yes; if no action is taken.

Mr. LEHMAN. Mr. President, will the Senator yield?

Mr. GEORGE. I yield.

Mr. LEHMAN. I merely wish to say that the bill which has been offered by the distinguished chairman of the Committee on Finance as a substitute fully effectuates the purpose of the amendments which I offered last week. The substitute bill would give continued protection to the men and women who are entering the armed services of the country, to exactly the same degree to which veterans of World War I and veterans of World War II have been protected. In addition thereto, of course, the substitute bill contains an indemnity feature in the event of death on the battlefield, or through injuries sustained in connection with war duty. The bill effectuates fully the purposes of the amendments which were proposed by me. Therefore, I wholeheartedly support the substitute bill and hope it will be passed by the Senate.

CONTROVERSY BETWEEN THE FEDERAL RESERVE SYSTEM AND THE SECRETARY OF THE TREASURY

Mr. O'MAHONEY. Mr. President, there has been a current assumption by certain columnists and editorial writers to the effect that if the price of bonds of the Federal Government were permitted to decline upon the open market, the result would be to discourage banks throughout the country from making loans to clients who seek loans. There is a similar assumption, that if interest rates were raised they would somehow tend to deter loans by banks. Both these assumptions were controverted upon a factual basis by Dr. John D. Clark, of the Council of Economic Advisers, when he appeared before the Joint Committee on the Economic Report on February 2, 1951. He pointed out that unless by manipulation or otherwise bonds of the United States were driven very much below their current prices there would be no effect upon the ability and desire of the banks to make current attractive loans. He also pointed out that in recent history the high prices paid by the public for commodities in common use throughout the country and, in fact, the inflation which has taken place, have occurred at a time when there was practically no change in the volume of money. Therefore, he was challenging the second assumption ,that changes in the volume of money would have any discernible effect upon prices.

Mr. President, I desire to invite the attention of the Senate and of those who may read the CONGRESSIONAL RECORD to the entire text of Dr. Clark's testimony before the Joint Committee on the Economic Report, and I therefore ask unanimous consent that his statement be printed in the RECORD as a part of my remarks.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

JOINT COMMITTEE ON THE ECONOMIC REPORT HEARINGS UPON THE 1951 ANNUAL ECONOMIC REPORT OF THE PRESIDENT, FEBRUARY 2, 1951

STATEMENT UPON MONETARY POLICY BY JOHN D. CLARK, VICE CHAIRMAN, COUNCIL OF ECONOMIC ADVISERS

The diversity of view of monetary policy which has been exhibited in recent discussion and here today is not surprising. We are now dealing with the problem in an environment which has never before been experienced.

The policies and theories developed in a period when, as Dr. Seltzer said, business loans constituted the bulk of investment of the banks. Today it exists in a situation where the banks hold billions of dollars of Government securities which, whatever price manipulation may take place, will always be liquid and can be turned into cash upon a moment's notice.

It exists in a period when great institutional lenders likewise hold billions of dollars of these liquid assets and when business itself is a source of credit far beyond any situation that existed before.

Businessmen do not have to go to banks in order to get loans before they can initiate a project even though later in the course of the project they may want to resort to banks for part of the funds.

These are new situations which have greatly upset the assumptions upon which monetary policy has been developed in the past century and a quarter. We also have the new situation of an enormous public debt which, because it has been handled successfully, seems now to be looked upon by many people as a tame domestic animal which does not hold within it the seeds of violent disturbance to the economy, and therefore we do not have to do much about it.

That is not the character of the national debt. If it is not handled prudently, if we take such action that some important offering of Government securities is a flop on the market, we will soon learn that the Government credit can be destroyed by imprudent debt management.

These are the two new situations which have to be considered in considering monetary policy today. Obviously we have an opportunity to come to different conclusions about proper monetary policy. Certainly the lessons of the past have very little to guide us in determining what we are to do in a situation which is so greatly different from that of other years.

The breadth of this diversity of view is illustrated by a couple of statements which have been brought to the attention of the committee. One I am not certain that you have had. It is a statement issued this week by some of the most important members of the faculty of Chicago University, of the department of economics. To show how strongly these respectable authorities support the most rigorous view of monetary policy, I want to read just a few lines:

"The price rise of the last 6 months could almost certainly have been largely or wholly avoided by effective monetary action."

Approaching the subject from that standpoint they come to this conclusion of what the policy should be today:

"The Federal Reserve System should at once announce that it will conduct its operations with an eye single to their effects on the supply of money and credit and on the level of prices."

In demanding "an eye single" upon one and only one objective, they exclude all idea of monetary policy being related to the problems of debt management in this period when the public debt certainly is going to be a matter of daily concern. "It should at once begin to sell Government securities to whatever amount is necessary to bring about a contraction in the currently swollen credit base, and it should persevere in this policy to the point that the inflation is checked, even though one of its incidental effects is a rise in the interest rate on Government securities."

Last week you heard Mr. Eccles state a very simple theory of monetary policy based upon the idea of the direct relation between the volume of money—including currency and bank deposits and savings deposits—and prices.

As I understood him, his view was that you could influence prices in either direction by changing the volume of money. That seems to be the view expressed by the Chicago economists. The simple fact is that prices in July, August, and the first part of September had their most rapid price advance when there was almost no change in the volume of money, and had slowed down and there was relatively little price advance from the middle of September until the end of November when there was a very rapid increase in bank loans and in the volume of money outstanding.

That is the very reverse of the situation implied by these theories.

In 1939 the Federal Reserve Board made a very frank statement to the American people of the monetary theories held by the Board. I will read a single short sentence which was repeated in that report more than once:

"The Board finds it impossible to believe that prices can be controlled by changes in the volume and cost of money."

Before you suggest that that was at a time when we were interested in bringing about price increases, and that the very general and universal terms used by the Board at that time must be interpreted as applying only to efforts to come out of a deflationary condition, let me hurry to tell you that the illustration they used, out of experience, to justify this conclusion, was the events from 1926 to 1929 which, as you may recall, was not a deflationary period.

The CHAIRMAN. Was that a Board statement?

Mr. CLARK. Yes, sir.

The CHAIRMAN. Not the statement by any individual members?

Mr. CLARK. That was a Board statement, published in the Federal Reserve Bulletin in April 1939. The Federal Reserve position today is not so easily determined. They have not made an equally candid statement of the theories behind their operations.

As well as I have been able to ascertain the theoretical position of the Board at this time, it is this: They still hold to the view expressed in 1939 that you cannot control prices by bringing about changes in the volume of money or in the cost of money, the cost of credit. They first moved into the theory of restricting availability of bank credit, which has been mentioned here today, by finding methods which will induce banks to hold their Government securities. You see it is a new problem they are dealing with, one they did not have in 1939 to any large degree. They would induce banks to hold their Government securities by giving them a better yield thereon, a policy which Professor Musgrave, in his report to you, which has been published, speaks of as buying off the banks from using their credit machinery to endanger the public welfare.

The difficulty with that is, as has been pointed out by some of these gentlemen today, that every bank in America has plenty of Government securities which it can dispose of in the market without being much concerned about these changes in yields. The banks hold a large proportion of short terms which are not very much affected by the moderate changes in yields which you can bring about.

The Reserve Board now has a much more sophisticated theory of controlling bank credit under this condition of large bank holdings of Government liquid securities. It is that they will perhaps be able to dissuade the banker from disposing of his Government securities if he has to take a book loss thereon.

I cannot quote anything officially from the Board itself on that, but this is the explanation given by Mr. Louis Brown, a director of the Federal Reserve Bank of New York, when he undertook to explain the recent policy maneuvers of the Federal Reserve System.

By using open-market operations to bring about an increase in the yield, which means a decline in the market price, of Government securities, including short terms, the banker will be persuaded not to take a book loss in selling some Governments to build up his reserve in order to make some business loan which is offered to him.

The suggestion has been made here that bankers do not think that way and do not act that way. But quite irrespective of that, I do not think that the banks of the country can possibly be put in that squeeze. The little bank that supports me when the Government is not employing me is not entirely typical in that respect, but it is not such a bad example. It is one that I happen to know about. Every week, we subscribe for $200,000 of bills which mature in 13 weeks. $200,000 happens to be just 10 percent of our required reserve.

So every week we have $200,000 of bills maturing. All we have to do in any week to increase our reserve by 10 percent is simply not to subscribe for new bills that week. And in 3 weeks we can increase our reserve by 30 percent. The Treasury is going to continue to use these short-term securities in our total debt structure. They will always be available to the banks.

You could not possibly drop prices on the financial markets low enough—unless you are ready to completely destroy the debt structure—so that any banker is going to be under any particular difficulty of meeting requests that he make attractive loans. We are caught in this trap and we cannot get out of it, by these methods. The bankers do have liquid assets which they are able to turn into reserves and you cannot stop them by market manipulation.

The view of the Council upon this tough problem has been presented under two of the three groups of circumstances with which your committee has been concerned during the past year. Last February Mr. Keyserling and I, as the surviving members of the Council of Economic Advisers, in response to your request for a report upon a number of questions, including monetary policy, furnished you our views which you have published in the hearings on the 1950 Economic Report of the President.

In November we again made a report in response to the request of the staff that we contribute to this very valuable staff report that has been published within the last few days. The first time we were dealing with problems of monetary policy in a period of peacetime inflation. We told the committee that our approach to the problem is not and cannot be limited to the monetary aspect, nor to the obvious need to protect the Treasury in managing the public debt. Under the Employment Act of 1946 our approach has to be much broader to consider the total problem of stabilization and not merely the monetary problem and the debt-management problem. We are continually concerned with the problem of economic growth. We look upon the cost of capital as being no different from any other cost of production and we believe that it is always desirable to have costs of production, including the cost of capital, held at as low a point as social policy will permit or will bring about.

Therefore, we were not in favor of monetary policies that were directed to increasing the cost of capital and thereby limiting economic expansion. But in a period of inflation, under ordinary peacetime conditions, a period which is found to come to an end either through effective policies being applied to it or through the crash which otherwise is the normal result of inflation, we think that it is entirely permissible to tighten credit.

And for that reason, ever since the Federal Reserve Board presented the proposal in 1947, we have vigorously supported the plan for a special reserve, to be held at the option of the bank in short-term Government securities.

In November the committee was considering the situation that then was dominated by the needs of the defense program following the attack in Korea, a very long-term program so far as we can tell. The one change that we then made, and for that reason made, in our recommendation was to tell you that under the conditions following the Korean attack we looked upon the continued expansion of the economy as being far more important than it would have been in another period of inflation.

For that reason, we were not in favor of tightening credit, although we did believe that it was still true that the Federal Reserve Board always should have among the tools in its armory of antiinflationary policy the right to establish the special reserve requirement when conditions called for such action.

Now we are in the third situation. The Chinese attack has aggravated the problem of preparedness and has accelerated the defense program. We immediately shifted from the original position we had taken that it was not necessary to have wage and price controls. Now we thought it was necessary to have wage and price controls. And a second change which that new condition makes in my mind is that if now business loans, the extension of bank credit, are creating a dangerous situation, there is no sense in trying to attack the danger by the use of the awkward, indirect, and indiscriminate control of credit. We should do with respect to credit what we are doing with respect to other sectors of the economy, and that is to apply direct control of the volume of credit.

And when it is suggested, as Mr. Eccles argues with me, that the problems of direct control of the volume of loans which banks may make is an administrative impossibility, I have to say that we certainly are wasting our time in talking about such things as controlling prices of 4,000,000 business institutions and fixing the wages of 60,000,000 workers if the problems of controlling 14,000 banks, the institutions more subject to control than any others in our Nation, is too big a job for us to handle. That is a personal view. The Council has not had occasion to pass upon it.

I say "if it is necessary to act." Last week, when the committee had an executive hearing, I stated my view that there is probably no great problem in this matter of bank credit, that the situation has already been carried into a pattern which will not only stop the increase in bank credit but will soon create a plethora of funds seeking investment.

Two days after I made that forecast to you the president of a building and loan association, in an address at one of their conventions, besought them not to establish limits upon deposits which they would accept. And the problem arose because those institutions already are finding it impossible to find outlets for savings and for new investment funds.

If you looked at the schedule that Don Woodward gave you at your hearing the first of the week, you may have noticed that he came to the conclusion that in 1951, without any changes in prices, the inability of consumers to find goods to buy would mean that consumers' savings would be in excess of $25,000,000,000 this year. What are they going to do with the money? It will not be put into houses. That is a kind of a saving or a method of saving. What are they going to do with the funds? What will be done with the funds of these corporations which are going to begin to establish reserves for these higher taxes that the President has proposed today, and which will not be payable until the beginning of next winter?

They will not let those funds lie idle in the banks. I am sticking by my forecast, Mr. Chairman, that by the middle of the year you are not only not going to have any problem of expansion of bank credit but you are going to have such a drive upon the Government security markets by those seeking the only outlet available for their funds that it will be absolutely impossible through any rational open-market operations to prevent interest rates from going down.

Mr. DOUGLAS. Mr. President, may I ask whether the Senator from Wyoming has concluded his remarks on the question of bank credit and prices?

Mr. O'MAHONEY. Yes; I was making only a preliminary comment in order to introduce the testimony of Dr. Clark, so that it would be available to anyone who wished to read it.

Mr. DOUGLAS. Mr. President, in view of the fact that the Senator from Wyoming has raised the issue, and in view of the great importance of the subject, I am constrained to do what perhaps I should not do; namely, discuss the alleged points of difference between the Federal Reserve Board, on the one hand, and the United States Treasury, upon the other.

REAL ISSUE IS MONEY SUPPLY, NOT INTEREST RATES

It is sometimes represented to the public that this difference is only over interest rates. It is sometimes said that it is the purpose of the Treasury to maintain the price of Government bonds above par and to keep the interest rate low, in order to keep at a minimum the debt charges upon the Government and also upon private borrowers.

It is also being said that the Federal Reserve System, on the other hand, is trying to increase the interest rate. If that were the issue, there is no doubt as to where public sympathy would lie, and probably justly lie.

No one desires a high-interest rate in and of itself. A high interest rate would increase the total volume of payments which the Government would have to make on the outstanding public debt; a low interest rate is not only favorable so far as interest payments are concerned for the Federal Government, but it encourages private borrowers to demand large quantities of capital, and, hence, stimulates capital investment.

However I do not think this states accurately the real issue before us. The real issue is inflation. The real issue is the degree to which we will permit prices to rise, and the degree to which the Federal Reserve System will hold or arrest this upward movement. Next to the questions of foreign policy and defense, the threat of inflation is perhaps the most serious problem which we face.

Mr. O'MAHONEY. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. O'MAHONEY. When the Senator said that there is no issue, per se, about the interest rate, I asked one of the pages to bring me a copy of this morning's Washington Post. In it I read the following statement in the column written by Marquis Childs:

> If the inflationary drift is to be checked, certain steps must be taken just as quickly as possible. Neither Congress nor the Truman administration can escape the responsibility.

With that statement I am in complete agreement. Steps should be taken to control inflation, but the question is whether I was correct in saying that certain columnists and others have assumed that a change in the interest rate would have certain beneficial effects.

Mr. Childs goes on to say:

> No. 1 on fiscal policy, the administration must find some way to switch from the stubborn determination to keep interest rates at the present low levels.

That statement in itself, I think, is an assumption.

> Virtually all economists on the outside, including observers from abroad who follow economic trends here, are agreed on the need for a rise in the Government interest rate in order to check the flow of credit into the banks.

I think that explains the reason why I made the statement which I did—that there is an assumption that a change in the interest rates will have some immediate effect.

Mr. DOUGLAS. I think the Senator from Wyoming is correct, as he almost invariably is. There are some who believe that a change in the interest rate will have these effects. But I think this misstates the real issue, which is whether we shall have any control over the total volume of credit. The interest rate is merely a consequence of the relative supply of credit in relation to demand.

THE MEANING OF INFLATION

What do we mean by inflation? To every housewife who goes to market it is painfully apparent in the rising cost of living. To every school teacher, to every Government worker, to millions living on retirement funds and countless millions more who are counting on their savings, to every individual who depends for existence on a fixed income, it brings up a nightmare of fear that the dwindling purchasing power of the dollar will put them on a starvation level. To the churches, the universities, to the millions investing in insurance, it is a living threat to their security. And what about the pensions which Congress has voted for those of our Armed Forces, who have been wounded on the fighting fronts? What about payments of the pensions for which labor has fought so hard and the social-security payments? These pension payments are in terms of fixed money amounts and, if prices go up and the value of the dollar goes down, the security which it was intended they would give becomes a mirage.

Mr. KILGORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. KILGORE. Does not the Senator find that one of the most serious complaints received is that having to do with the constantly rising cost of foodstuffs?

Mr. DOUGLAS. Yes. That is a very important element.

Mr. KILGORE. Could the Senator explain to me how, if in any way, the curtailment of credit would affect the price of foodstuffs? I can understand that people going in debt to buy automobiles, refrigerators, and things of that kind are dependent on the ability of the banks to lend money. I was wondering if the Senator could explain that feature.

Mr. DOUGLAS. If the banks lend large quantities of money for wage payments, salary payments, and various outlays of that kind, the result is to give the people more money with which to buy food. So the increase in the general supply of money spreads through the entire economy. Increases in the prices of individual commodities may start with specific causes, but they can be made possible only if there is a large volume of credit to float the increase.

It may be said also that a recent Federal Reserve survey of bank loans shows that three-fifths of the expansion of business loans went to commodity dealers and to processors, with loans to cotton dealers predominating. So the speculators and dealers have been furnished with abundant supplies of credit, which, in turn, has permitted them to bid up prices in the face of a more or less constant supply of these commodities.

Mr. KILGORE. The Senator has no doubt read, in the same column to which the Senator from Wyoming has referred, of the housewife in Washington who strenuously objected because the price of eggs had increased 3 cents a dozen between the time she picked up the eggs on the counter and the time when she reached the checking counter to pay for them.

Mr. DOUGLAS. Thank God, we are not in the condition which existed in Germany, when men would carry their pay to the store on bicycles, rather than walk with it, because they knew that the money would be worth much less by the time they got to the grocery store. That was hyper-inflation.

INFLATION DESTROYS DEMOCRACY

Every historian knows that inflation has been a great destroyer of the vast middle classes and of governments. It has paved the way for dictatorships and overthrow of democratic institutions. By wiping out the middle classes and separating society into the two classes of the propertyless on the one hand and the rich speculators on the other, it paved the way for fascism and communism on the continent of Europe. It is a destroyer almost as evil as war itself. In the eyes of those who want to destroy democracy and capitalistic institutions it is a cheap way of achieving their collapse. It costs the enemy nothing in lives or treasure. It is really a supreme folly for a nation which is arming against the threat of invasion from without to let this invader, inflation, bring ruin from within.

Mr. O'MAHONEY. Mr. President, I dislike to interrupt the Senator from Illinois, but will he yield?

Mr. DOUGLAS. I am delighted to have the Senator interrupt.

Mr. O'MAHONEY. The Senator is always very kind. I wish to explain to him that the Committee on Interior and Insular Affairs, of which I am chairman, is holding a hearing this afternoon. I called witnesses to appear at two-thirty, so it will be impossible for me to remain in the Chamber during the Senator's discussion. I shall be deprived of some very valuable information, I know, when I leave; but I want the Senator to realize why I am compelled to absent myself from the Chamber at this time.

Mr. DOUGLAS. The Senator from Illinois well knows that the Senator from Wyoming never runs away from a fight. I hope the Senator will forgive me, therefore, if I take a rather strong position, which, I understand, differs from his on certain points—with, of course, no reflection upon the Senator from Wyoming in his absence.

Mr. O'MAHONEY. I understand the view of the Senator from Illinois, and I quite agree with what he is now saying about the importance of controlling inflation. No one could hold more firmly to the belief than I do that Congress should take immediate steps, and strong steps, to control inflation; but I am strongly of the opinion that those steps cover a wide front. They involve many courses of policy, and particularly they involve the need for early and high taxation——

Mr. DOUGLAS. On that point the Senator from Illinois is in complete agreement with the Senator from Wyoming; but I think we may disagree as to whether the Federal Reserve System should be constantly pumping fresh purchasing power into our banking system, and thus inflating the currency in that respect. On that point we may differ.

Mr. O'MAHONEY. May I take advantage of the good humor of the Senator, and his indulgence?

Mr. DOUGLAS. I try always to be in good humor.

Mr. O'MAHONEY. Before I leave for my committee meeting, let me say that it is my conviction that the records show that the policy which is advocated by the Federal Reserve Board does not have the effect of reducing prices in any material degree. The facts, it seems to me, are these: Beginning with Korea prices immediately began to rise, and the increase in the price of all commodities and of the cost of living was the result not of any change in the money supply, but a result of hoarding upon the one hand, of profiteering, of attempts by purchasing consumers and industries of all kinds to get in a position vis-a-vis the probable imposition of price ceilings, and the probable adoption of a rationing program. The great inflation which we suffered was due to causes altogether separate and apart from the basic point in this controversy.

Mr. DOUGLAS. I am sorry that the Senator from Wyoming is not able to remain, because if he were to remain, with his customary open mind, I am sure that he would be convinced to the contrary—that the primary reason for the large increase in prices since June has been the expansionist credit policies which have been carried through by the Federal Reserve System under the stimulus of the Treasury.

Mr. O'MAHONEY. In that connection, let me say that, to my mind, the records of the past show conclusively that a run-away inflation is not stopped by the cost of credit. During 1929, when we were suffering from a run-away inflation, call money upon the stock market reached an interest rate as high as 17 or 20 percent. Yields on Government bonds were as much as 5 or 5½ percent. To my mind, if the Senator will indulge me, the conclusive factor in this controversy is that there are $155,000,000,000 worth of Government bonds, marketable Government bonds, in the economy.

Mr. DOUGLAS. In private hands.

Mr. O'MAHONEY. In private hands; and that there are some $58,000,000,000 of Government savings bonds, which, are in effect, demand notes, in the hands of small savers. I am convinced that if any policy were adopted which would cause the price of Government bonds to decline—and that policy was advocated before our committee by Mr. Marriner Eccles, a member of the Federal Reserve Board—no man is wise enough to foresee what the effect of such a deliberate policy of reducing the open market price of Federal bonds would have upon the credit of the United States at the very moment when it is moving over the most delicate fiscal crisis in its history.

I thank the Senator from Illinois very much for having indulged me.

Mr. DOUGLAS. I am very appreciative of the contribution of the Senator from Wyoming, but I think he misunderstands the real issue, if I may say so. While some unwary persons have in the past contended that a rise in the interest rate would appreciably reduce the volume of borrowing, that is not the contention of the Senator from Illinois. The cost of interest is such a small fraction of the borrower's total cost of doing business that a rise in the rate does not have much effect upon the demand for loans. What I am going to advocate and what I think the Federal Reserve Board should do is to restrict the supply of credit at its source, and I hope to demonstrate that this cannot be done so long as the Reserve Board is compelled by the Treasury to purchase every Government bond or any Government security that comes its way. That is the real issue.

Mr. CASE. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. FREAR in the chair). Does the Senator from Illinois yield to the Senator from South Dakota?

Mr. DOUGLAS. I yield.

Mr. CASE. Would not the Senator from Illinois add to that the effect when the Secretary of the Treasury is required to buy the debentures or evidences of obligations issued by such agencies as

Federal Housing, Reconstruction Finance Corporation, or the Commodity Credit Corporation?

Mr. DOUGLAS. Those have not been very large in amount. I do not believe they have amounted to more than a couple of hundred millions. The big increase has come in the expansion of private credit. As a matter of fact, as I hope to demonstrate, the inflation has not been caused by an excess of Government expenditures over receipts. Receipts have been greater than expenditures by nearly $2,000,000,000.

No; the inflation has come through an expansion in private credit furnished by the banks, in turn made possible by the Federal Reserve, at the dictates of the Treasury.

Mr. CASE. When the Housing Authority, or the Commodity Credit Corporation, or the Reconstruction Finance Corporation obtain money from the Treasury by that method of operation, and then it goes into construction or into the purchase of commodities, does not that in turn increase the flow of money?

Mr. DOUGLAS. It does, but it is all a matter of proportion. The amount of the issues for quasi-public authorities has been very small since last May. They are a drop in the bucket compared to the total volume of private loans which have been granted by banks, and I suggest therefore that the Senator from South Dakota seek elsewhere in trying to find the cause for inflation.

Mr. CASE. The Senator from South Dakota is not trying to cover the whole subject, but the Senator from Illinois did make the suggestion that the inflation was due to certain things, and I merely wished to point out that certain laws within the past year or two directed the Secretary of the Treasury to purchase additional obligations of the Commodity Credit Corporation up to $2,000,000,000 and to purchase obligations of the Housing Agency up to $1,000,000,000. It occurred to me that amounts of that size may contribute to the inflationary picture.

Mr. DOUGLAS. I may say to the Senator from South Dakota that I have here a tabulation of growth of bank credit to borrowers other than the Federal Government for the last half of 1950. The tabulation excludes United States Government securities. The increase in loans at all commercial banks amounted to $8,000,000,000 and holdings of corporate and municipal securities at all commercial banks grew by $1,100,000,000, or a total increase in commercial bank credit, excluding United States Government securities, of $9,100,000,000. That was private credit, including a few municipal securities, but excluding Federal Government securities. This compares with a gain of only $1,900,000,000 in the last half of 1949 and $2,600,000,000 in the latter half of 1948. Total bank loans at the end of January 1951, 3 weeks ago, stood at $52,800,000,000, or nearly $10,000,000,000 higher than a year previous.

Mr. President, the first victims of inflation are those least able to defend themselves. But even the shrewd speculators, who think they know how to profit from its ravages, can be engulfed in the final havoc. Surely after all these years of debate and of exhortation no one should be ignorant about the evils of inflation.

Yet the causes of inflation are still only little understood. This is perhaps because economists talk about it in terms which are only understood by other economists. Or perhaps it is because the words which we use, namely, money, credit, bank deposits, the general price level, and so forth, seem more mystifying than they really are.

MONEY SUPPLY AND PRODUCTION SHOULD BE BALANCED

If one pictures a pair of scales on which the amount of money available to buy goods is placed on one side and is balanced against the amount of goods available for sale on the other side, it is possible to get a picture of what is meant when we talk about monetary stability. This picture of what we mean by inflation becomes more clear if we imagine too much money demand on one side of the scales in relation to our capacity to produce goods available for sale on the other side. In that case the value of the money goes down while the price of the goods goes up. That is inflation.

Conversely, if the amount of money on one side of the scales is too small in relation to our capacity to produce the goods for sale on the other side, then the value of the money goes up and the price of the goods goes down. That is what we call deflation.

Let us use an arithmetical example to make this same point clear. If we have $100 to offer for 100 units of goods, it follows that the average price of each unit will be $1. Then, if we increase the quantity of money offered to $200, but the quantity of goods remains the same as before, the average price per unit will now rise to $2. This is inflation. If the supply of money is reduced to $50 but the quantity of goods is not changed, then the average price falls to 50 cents. That is deflation.

All this is simple enough. Obviously the purpose of Government should be to help promote as large a supply of goods as possible and to prevent an unbalance in money demand in either direction. What we face today, however, is too much money in relation to available goods.

What do we do about it? There is quite universal agreement that we should reduce the amount of money demand through taxation, for one thing, and make the greatest possible cuts in nondefense spending for another. That, of course, is vitally necessary. We should not let the budget show a deficit, because if we do so, the Government will probably be compelled to borrow from the banks, and the banks will lend by creating more "check book" money. That would increase inflation. As a matter of fact, up to date the Federal Government during the current fiscal year has taken in on cash operations almost $2,000,000,000 more than it has spent. To date our Government finances, therefore, have not fed the inflation.

SOURCES OF THE MONEY SUPPLY

What is not so well understood is that money demand is not limited to purchasing power arising from current income. Money demand can, in fact, come from three other sources. First, money in hand and cash and bank deposits which have been earned in the past but not spent. If these are too large, they will become active and will upset the balance. Second, past savings invested in liquid assets. If these are cashed—if there is a high rate of liquidity preference, as Mr. Keynes used to say—and the money spent, they can inaugurate an almost indefinite spiral of inflation. Third, and what I shall emphasize particularly in the present situation, new money created through bank-credit expansion. When these three additional sources of money demand run wild the stability of our whole society is endangered. All of them interact on each other and all of them affect the functioning of our banking system.

BANKING SYSTEM THE PRINCIPAL SOURCE

Basically, the source of our money supply is the banking system. Most of us who have not had time to go into the subject suppose that the banker later lends to other people the money that we deposit in his bank. This is true of so-called investment banking, but it is not true of commercial banking or the banking system as a whole. The real fact, which is so little understood even among bankers, is that the banking system creates money. It does not do it by having printing presses in the windows of banks where we can see $1, $5, and $10 bills turned out by the bale, but banks as a group do it just as effectively by making their loans to borrowers, for when they make these loans they credit the borrower with a deposit account against which the person or company which has borrowed can write checks. Indeed, nearly all the business of this Nation is carried on through bank checks, and the deposits in our banks constitute the overwhelming bulk of our money supply.

Still greater obscurity surrounds the subject of bank reserves and the relation of reserves to the creation of deposit money. I shall not try to go here into the full details of the bank reserves. It is important, however, to know that the main source of the banking system's ability to extend credit and thereby create money comes from these reserves.

Banks acquire their reserves in two ways: Either by borrowing from the Federal Reserve against commercial paper or paper collateraled by Government bonds or through the purchase of Government securities by the Federal Reserve in the open market—whether these securities are sold by banks themselves or by nonbank sellers. For various reasons, borrowing by member banks from Federal Reserve banks on commercial paper is not very important now, although that was thought to be the original purpose of the Federal Reserve System, and in recent years the rediscount of member bank paper by the Federal Reserve banks has never amounted to more than a few hundred million dollars at one time. Reserves within the Federal Reserve System today are, therefore, overwhelmingly created—indeed, about 99-percent created—by Federal Reserve purchases of Government securities in the open market.

Now, we come to a vital point: Upon each dollar of the reserves of the member banks of the Reserve System, the banks can make approximately $6 of loans, and hence can create that amount of credit.

RESERVE REQUIREMENTS NOW AT LEGAL MAXIMUMS

Mr. President, as is well known, the legal reserves of the member banks fall into three classes, depending upon the city in which the bank is located: the central reserve cities, where the reserves must be 24 percent; the reserve cities, where the rate is 20 percent; and the so-called country banks, where the reserve ratio is 14 percent. If we take all of them together, the average is approximately 16 percent; and I may say that the Federal Reserve System has now raised these requirements to their legal maximums except for the central reserve cities where the rate is 2 percent below the maximum which the Federal Reserve System could require. In any event if a bank has a dollar in reserves, it then can lend roughly $6, and thus can create $6 of bank deposits.

The more Government bonds the Federal Reserve buys, the greater will be the legal reserves of the banks. The more reserves the banks have to their credit, the more they can lend. Indeed, their lending capacity will increase by six times the rise in their reserves. The more money the banks lend, the higher—other things being equal—will be prices, for the ratio of money to goods will increase.

STATISTICS OF INFLATION SINCE KOREA

It is precisely this which has been happening since the start of the Korean War. Since June, wholesale prices have risen by about 17 percent and the cost of living by nearly 7 percent. During this time, the Federal Reserve have purchased about $3,500,000,000 of Government securities, and the reserves of the member banks have risen by $3,000,000,000, or from nearly $16,000,000,000 to $19,000,000,000. About $2,000,000,000 of this increase was needed to meet a rise in reserve requirements by the Federal Reserve Board in January, leaving just over $1,000,000,000 added to commercial bank reserves to support a loan and deposit expansion. Bank loans in this period increased by $8,000,000,000, and the total created demand deposits subject to check rose from $85,000,000,000 to about $93,000,000,000.

In this connection, I should like to emphasize that the Federal Reserve System has about reached the end of its rope under existing legislation, so far as bank reserves are concerned. It cannot increase that ratio except in the case of the central reserve cities, where it could send up the rate by about another 2 percent.

INCREASED MONEY TURN-OVER ADDS TO INFLATION

Mr. President, the increase of 10 percent in the supply of deposit money—namely, from $85,000,000,000 to $93,000,000,000—has been accompanied by an increase in the speed with which the average dollar of cash and credit changes hands. The turn-over of demand deposits has been more than 10-percent larger than a year ago. The combined effect of an increased supply of dollars and an increased velocity of dollars has permitted prices to increase despite a significant increase in total production since June.

We can make this point clearer by reference to some other figures. The total value of production of all goods and services—the gross national product—has increased by more than 10 percent since last June. Only half of this increase, or thereabouts, has reflected expanding production. The other half has reflected rising prices. Some elements of production have increased more rapidly than other elements. The total of all manufactures, for example, has increased by 10 percent.

Also, some prices have risen much more sharply than other prices. Basic raw materials have risen, for instance, by about 50 percent; but these rises have not yet been transmitted to all goods and services. However, they will be in time, if the bank credit continues to flow.

If most of the increase in bank loans had actually gone into expanding productive facilities, they would eventually have helped restore the money-goods balance. However, apparently they have not been used thus, but have been used, instead, to bid up the prices of existing goods. As I pointed out in response to a query from the eminent Senator from West Virginia [Mr. KILGORE] a recent survey showed that three-fifths of the expansion of business loans went to commodity dealers and processors. Loans to cotton dealers predominated. These dealers and processors used this additional money to bid for fixed amounts of agricultural goods, and the effects of this can be readily seen in an increase in the wholesale prices of all farm products of 22 percent since June 1950. Textile products were up 32 percent in the same period.

INVENTORIES BUILT UP

To point up my contention that bank credit expansion has fed rising prices, Federal Reserve figures show that the rise in bank loans to business since June has paralleled fairly closely the rise in business inventories. Building up stocks of basic materials, which have shown the sharpest price increases, has been the most important factor in the increase of business loans. Bank loans to finance purchases of consumer durable goods and houses have also increased considerably since June. These loans have been a factor not only in price increases in these buying areas but also in the prices of primary materials entering into the final consumer product.

Mr. President, the primary cause for the rise in prices since last June has been this tremendous increase in loan and checking accounts. These increased loans and checking accounts have been made possible by the increase in the reserves which the banks hold in the Reserve System; and these reserves available for increasing loans and deposits have been raised by more than one billion by the Federal Reserve practice of buying all the Government securities which have been presented to it, net purchases of which have totaled over $3,500,000,000 since June, with about $2,000,000,000 of that amount absorbed by the increase in the reserve ratio. The difference between the $3,500,000,000 of net purchases of Government securities and the $1,000,000,000 increase in effective bank reserves is accounted for, as I have said, by Federal Reserve action in January, raising by this amount the required reserves of member banks.

FEDERAL RESERVE BOND PURCHASES MAIN CAUSE OF INFLATION

It is this practice of unlimited bond purchase by the Federal Reserve System, therefore, which is the prime cause of inflation. It is not that these purchases of bonds would be wrong of themselves if they could be divorced from the credit of the country. But under present conditions, they cannot be divorced from the credit of the country, because the Government bonds and securities bought by the Federal Reserve have raised the bank reserves. This enabled banks to increase loans, which in turn has increased prices. It has been the Federal Reserve System, therefore, which for 8 months has fed the fires of inflation. Now, we all have good reason to believe that while the Federal Reserve has done this guilty thing, it has done so protestingly and unwillingly. It has wanted to lead a virtuous life.

But over the shoulder of the Federal Reserve System has stood the Treasury, making threatening passes and gestures and from time to time cracking its whip.

And what have been the Treasury's demands? They have insisted that the Reserve System hold its arms wide open and buy every Government security which is offered. They have insisted, moreover, that these securities shall be purchased above par—except in the case of some short-term issues—and shall be at low rates of interest—the actual coupon rate being 2½ percent on outstanding long-term bonds.

REASONS BEHIND TREASURY STAND

Now there are two assigned reasons why the Treasury insists upon this policy. The first is that they say the policy is necessary to prevent bonds from falling appreciably below par and hence bringing loss to those who hold them. The second reason is the saving to the Government in its interest payments. The total interest bill of the Government is now approximately $5,800,000,000 a year. A rise of one-half percent in the interest rate would, it is claimed, cost the Government a billion and a quarter dollars a year more in interest charges.

Since the Secretary of the Treasury is responsible for the management of the public debt, it is but natural, if he takes a somewhat restricted view, that he will want the Federal Reserve to do precisely what he has been urging—namely, to provide an unlimited market for the purchase of Government securities, so that anyone who sells them is assured of disposing them at a price above par, and so that the interest rate is kept at a low rate.

Mr. President, I want to make it clear that this attitude is not confined to the present Secretary of the Treasury, Mr. John Snyder. All of the recent Secretaries of the Treasury, Mr. Morgenthau, Judge Vinson, as well as Mr. Snyder, have adopted this same position. Whenever the Federal Reserve or its Open Market Committee, which carries out the purchases, has been reluctant to go along on this unlimited program of bond and security purchases, the Treasury has resorted to a strategy of mixed cajolery and threats. The Open Market Committee consists of seven members of the Federal Reserve Board and five presidents of the Reserve banks, with the Chairman of the Board of Governors as Chairman of the Committee and the President of the New York Federal Reserve Bank as Vice Chairman. The Reserve Board has been told that it should cooperate, that it should stand by the President and not rock the boat. It has been told that if the price of Government bonds falls or the interest rate rises, the Reserve Board will be held responsible. I thought I detected certain overtones of that position in the remarks by the senior Senator from Wyoming, before he was compelled to leave the Chamber.

It is intimated that if the Reserve Board is recalcitrant, the Reserve System will be nationalized, and all independence will be taken away. At times, a head or two has rolled. Three years ago, Mr. Eccles, the then Chairman of the Board, who had been protesting against the expansion of credit policy which was helping to boost prices, was not reappointed as Chairman.

Under this pressure the Federal Reserve System has gone along. The real responsibility has been that of the Treasury. The Treasury has pulled the strings, and the Federal Reserve has danced to its music. In the words of the Book of Genesis, "The voice is Jacob's voice, but the hands are the hands of Esau."

Mr. President, this is not a case of evil men, but of misguided men. Mr. Snyder is an honorable man. So were, and are, Mr. Morgenthau and Judge Vinson. So are they all honorable men. But in recent years, these gentlemen have been misguided men. For under the guise of keeping the interest rate down, they have forced the Reserve to action which has resulted in increased bank credits and hence created inflation.

The costs to the Government and to the people have been far greater than the gains which we have made from a lower interest rate. The increase in prices since Korea are probably already adding to the Federal Government costs at the approximate rate of six billion a year.

The cost of meeting the interest on the public debt is now roughly $5,800,000,000. The entire budget submitted by the President for fiscal year 1952 is approximately $71,600,000,000. This means that Government expenditures for purposes other than interest, that is for services and materials, will be approximately $66,000,000,000. It is a conservative estimate that there has been a general increase in prices of commodities and services of roughly 10 percent as a result of the inflation; so that this inflationary price increase, then is already costing the Government at least $6,000,000,000, and possibly more. That is in excess of the total amount which the Government now pays in interest.

Even if interest rates were doubled, which is at best a very remote possibility, the added cost of meeting the interest on the public debt would not equal the cost to the Government because of the rise in prices that has already taken place.

Furthermore, our whole society has been greatly disturbed and convulsed by the increase in the cost of living which has taken place; and no one knows what lies ahead. The responsibility for all this lies proximately and immediately with the Federal Reserve, but ultimately and really with the Treasury.

I am not interested in putting anyone in the pillory and holding him up to public scorn. I am not interested in castigating people or institutions for the fun of it. I am vitally concerned, however, as to what will happen to this country if this policy is not changed.

CHANGE IN FEDERAL RESERVE PRACTICE PENDING

In recent days, the Federal Reserve Board has shown signs of restiveness, signs of an awareness of sin, and of a desire to turn over a new leaf. Judging from press reports, it has apparently indicated a desire to change its policy. Then the whole Board was called to the White House, and an appeal was apparently made to them to support the Treasury. There is some dispute as to what the reply of the Board actually was. The President and the Secretary of the Treasury apparently thought the Board had acquiesced. Most members of the Board thought this was not the case. But I pass over this, for misunderstanding is not unusual in such conferences. Then, according to the press, the Board 9 days later addressed a letter to the President. It is understood that no action has yet been taken on the policy issues involved.

We are therefore at the very hour of decision, and that is the only reason why I have risen to discuss the matter.

PROBABLE EFFECTS OF ENDING FEDERAL BOND PURCHASES

Let us now go into this matter a little more deeply, and let us ask ourselves what would happen if the Federal Reserve quit buying Government bonds. I should like to explain here that I am talking about the so-called marketable bonds; that is, the kind of securities which are bought and sold in the open market. The E, F, and G savings, or Defense bonds, are not sold in the open market. These can be cashed at values written into the contract at any time one may wish, but, unless the owner keeps them until they are due and payable, he will take less in interest than if he held them until maturity.

The E bonds are the ones which are held by the great bulk of small investors throughout the land. They are very different from the Liberty bonds of World War I, which were bought and sold in the open market. We should not forget that fact.

MINOR FLUCTUATIONS DO NOT DISTURB LARGER INVESTORS

To return to my question, what would happen if the Federal Reserve were to stop buying Government bonds? Frankly, I do not think very much would happen in the Government-bond market. The outstanding marketable bonds are held by the very large and, for the most part, sophisticated investors. They have invested for income and are not concerned with temporary fluctuations in price. If they could not sell their marketable bonds at prices well above par, or at what bond brokers call a premium, they would be less inclined to sell them; and if they could sell them only at prices below the level at which they were originally bought—that is, at a penalty—they would still be less disposed to sell them, because it would show up on their books as a loss; and insurance companies and other institutional investors do not want to show losses on their dealings.

One thing is certain; the yields on other and riskier investments, which these sophisticated investors have been selling Government bonds to purchase, would have less attractiveness than they have at present.

Ours is a high-saving economy. A substantial volume of savings normally flows into fixed income securities when confidence exists in those securities. It is not normal or natural for the investor to seek risky investments.

THREE PERCENT CONSIDERED FAIR RETURN

Now I happen to think that there are innumerable investors, insurance companies, churches, universities, and other institutions that would think that 3 percent or perhaps a little less was a fair return, a living wage which would enable them to carry on and pay their way and keep on hiring their ministers and their professors. But when the return on their money is a good deal less when prices are rising, and the cost of their operation is increasing, it is natural for them to sell some of their Government securities in order to put their money into higher-yielding investments that will give then a living wage. With somewhat higher yields, and a more stabale level of prices, these investors would be buyers rather than sellers of Government bonds.

Government bonds are, for the most part owned outright. They are not bought on credit, and a fluctuating Government bond market is no more likely to discourage investors than an artificially pegged market. A fluctuating market, responsive to the laws of supply and demand, does not cause loss of confidence in State and municipal, or in corporate securities which are not supported. I am confident that a more realistic return on Government securities will enable them to stand on their own feet. And a more realistic rate means one that is more nearly in accord with the income needs of the large institutional investors, such as life insurance companies and pension funds, most of which are geared to an actuarial rate of 2¾ to 3 percent. These institutional investors are the natural buyers of the marketable Government securities with which we are concerned in this matter of supporting and pegging of the market.

AWARENESS OF REALITIES WILL REVEAL GOVERNMENT CREDIT IS STRONG

It is said that nobody knows at what prices Government bond prices will settle if the Federal Reserve withdraws support from the market. Exaggerated predictions are sometimes made that it will be at some very low figure which would cause serious financial troubles for present holders of outstanding securities.

That seems to me to be entirely unwarranted lack of faith in the real values of Government bonds. I think that the Government bond market may well adjust at a level very little below its present levels and that genuine investors would be drawn into the market as eager buyers if the returns offered were more nearly in line with a realistic appraisal of investor needs and prospects for income.

I can see no sound reason for failure to test out the true market by open-market operations, and if that is done I believe that sellers will soon be outnumbered by willing buyers.

If the market does not stabilize through normal supply and demand forces, if the investors' appraisal is, in fact, at lower levels than I would expect, then it would still be the part of wisdom to know it and to face the truth of the the matter. We would be concealing, instead of dealing with the cause of a disease that needs to be treated boldly.

It seems to me that bold, not timid, grappling with this fundamental matter of the true worth of the obligations of this Government may well reveal that the credit of the United States is far stronger than the pessimists think—and, indeed, the best way to put pessimism and lack of faith to rout is to strip all camouflage from the problem so that we may deal with it in its true light, and adopt the fiscal, monetary, and other measures that are required to convince even the most skeptical that the American dollar and American Government securities are intrinsically sound and worthy of universal confidence.

Mr. President, I think that prophecies of any serious decline in Government bond prices following withdrawal of Federal Reserve support are hysterical and wholly unrealistic. We have had inflation—too much inflation—since the end of the war. But the credit of the United States is still the best on earth. It is not so enfeebled as to require constant artificial stimulants. As a citizen, I find intolerable the idea that the bonds of my Government have to be artificially bolstered up.

SEC ACT FORBIDS PRICE PEGGING IN STOCKS

The Securities and Exchange Commission Act contained a proviso that no one should, by rigging the market, maintain the price of corporate bonds sold in the open market; that an investment house should not maintain prices artificially on the market in order to dispose of the securities which it issues. There were too many instances of that kind in the 1920's. I do not want to see my Government adopt a similar policy in the maintenance of prices of Federal securities.

I dislike intensely the idea that the bonds of my Government are not intrinsically sound and deserving of the support of real investors. I recoil from the notion that the central bank must constantly administer artificial respiration to the securities of the United States. The credit of the United States does not need a pulmotor. I believe our securities are able to stand on their own feet. I think they merit the support and confidence of the public. I am not willing to accept the defeatist conclusion that, as a nation, we lack the intelligence, the will, and the courage to protect our dollars and our securities against progressive debasement. We are, perhaps, slow to act, late in doing what needs to be done to protect the dollar. But I deny that the battle is lost. It has just begun. And once the fight is launched in earnest, it will reinspire faith and confidence in the dollar and in the Government credit. It will not be necessary to provide an unreal—an artificial—market, which in the end will deceive no one, least of all the experienced investors in the country.

SALES OF SECURITIES RESULT FROM FEAR OF INFLATION

Mr. President, during recent weeks and months there has been a considerable sale of bonds, both governmental and private. Why have these sales been conducted? It has been largely because people have been fearing inflation. They know that in the case of Government bonds they will get 100 cents on the dollar, but they are afraid that those 100 cents will in the future not buy very much. They are not afraid of a depreciation of their capital in money terms, but that their money itself will depreciate. Hence they sell bonds, in order to purchase either stocks, which have residual claims upon earnings, farms, other equities, or commodities. A large part of the sales of Government bonds has been because of the fear of inflation.

If we can stabilize prices and remove this fear, or greatly reduce the fear, then the temptation to sell Government bonds will be diminished, and the need to maintain the bond market by an artificial pegging on the part of the Federal Reserve System will be removed.

Mr. President, let me again ask the question: What would happen if the Federal Reserve System were to cease buying Government bonds? One result would be that the continued flow of reserves into the hands of member banks would stop, and the ability of the banks to make future loans to speculators and others would be diminished. The danger of a further substantial increase in the price level would be reduced. We would dampen, if not perhaps completely check, the increase in prices which would otherwise surely result.

Unless the Federal Reserve System sharply curtails its rate of purchase, it will be constantly pumping, pumping, pumping more monetary purchasing power into the economic system and sending prices up. If it curtails its purchases, the rate of flow of new money purchasing power will be checked and the rise in prices will be slowed down.

So, Mr. President, I would not say that a complete cessation of purchasing by the Federal Reserve System would necessarily bring with it any catastrophe. Quite the contrary, it might be extremely valuable.

MAINTENANCE OF ORDERLY BOND MARKET ESSENTIAL

Confident as I am that the Government bond market's natural level is by no means to be found at such low levels as would bring financial embarrassment to present holders, I am not advocating the complete abandonment of open-market operations by the Federal Reserve. I am proposing that the Federal Reserve continue its policy of maintaining an orderly market.

I am not advocating an abandonment of all operations and the dumping of the open-market portfolio on a chaotic market. I suggest simply that the Federal Reserve, which has had many years of practical, day-to-day experience in its open-market operations, permit the Government securities market to reflect the underlying factors of supply and demand—that it permit the market to adjust, without disruption, and avoiding sharp price fluctuations to a point at which the true investor will buy and hold Government securities.

It is not possible to fool the public long by artificiality. Confidence in the dollar and in Government securities is founded on public willingness to buy and hold such securities. It can only be undermined by central bank financing that eats away the value of the dollar.

I have heard it said that all of this is old-world economics, and that, in time, as there are fewer and fewer civilian goods available, people will not know what to do with their money, and will have to invest it in Government securities at present, or even lower levels.

Mr. President, that is a weak reed to lean upon when bank credit is growing daily and adding more and more dollars to the money supply. Moreover, we are facing a defense period of indefinite length. We are facing rapidly mounting defense expenditures. Unless further taxes are enacted to cover these costs—and we have done well thus far—we may be in for another period of deficit financing before long, we will be faced again, as we were after Pearl Harbor, with the problem of how to manage the deficits. We must be in a position to avoid the financing mistakes of World War II, which left us with a heritage of inflationary fuel in the form of an excessive money supply.

No system of Government price controls can permanently or greatly reduce the pressure toward high prices if there is an ever-increasing amount of bank credit in the hands of private banks ready to be siphoned out to business.

Even before new Government deficits develop, however, we shall continue to face the potentially much greater threat of inflation that could result from private credit expansion based upon unrestrained purchases of Government securities by the Federal Reserve.

REAL ISSUE IS SUPPLY OF "HIGH-POWERED" RESERVE DOLLARS

Mr. President, I want to restate briefly what I think is the real issue here. The real issue is the high and still rising cost of living. We have to meet this problem in various ways. Curbing the creation of more credit dollars and particularly high power Federal Reserve dollars, is probably the most important way of meeting it. If we let the creation of these dollars go on, there is no question what will happen, no matter what else we may do, and all of the other sacrifices which we are asking of the American citizen—in the form of heavy taxes, price and wage controls, and consumer credit restrictions—are likely to be of little avail. We will have more inflation and a higher and higher cost of living.

STEADY PRICES MORE IMPORTANT THAN STEADY INTEREST RATE

Mr. President, this country stands to gain much more from steadiness in the price level, even if it may mean a slightly higher rate of interest, than it does from steadiness in the interest rate and a constantly increasing level of prices.

That is the issue, Mr. President. The Federal Treasury is trying to peg the interest rate, and by so doing force the Federal Reserve System to pump into business billions upon billions of additional bank credit, the only sure result of which would be to send up prices and possibly bring ruin upon both the Government and the people.

Mr. President, one of the advantages of our system of representative government is that in the legislative chambers a humble representative of the people can arise and state the issue, so that he who runs may read, as those who will read the CONGRESSIONAL RECORD tomorrow morning will, I hope, understand what the conflict is about.

I hope very much that the Treasury will not persist in the attitude which it has taken to date. I hope very much that it will lessen its resistance to the Federal Reserve System's proposal to turn off the spigot. I hope it will not insist that the Federal Reserve System be committed to an unlimited purchasing of Government bonds from everyone who presents them. I may say that the volume of purchases which the Federal Reserve System has had to make in the past 2 weeks, if I can judge from their reports issued to date, is very high.

Mr. President, Rome is still burning. But there is time for the fire company to put out the fire. There is time to do so if the Treasury will cease its obdurate attitude and acquiesce to the Federal Reserve System, which, in my judgment, should return to the paths of virtue and use its clear legal authority to slow down or stop the open-market purchase of securities.

I know it is said that we must keep down interest charges to the Government. But I should like to point out again that the Federal Government itself is losing far more from an increase in prices than it could possibly lose from an increase in interest rates. Therefore the Treasury has a very restricted point of view of the Government's interests when it sees only interest charges.

Mr. MILLIKIN. Mr. President, will the Senator yield?

Mr. DOUGLAS. Yes.

Mr. MILLIKIN Has the distinguished Senator from Illinois put into the RECORD during the course of his address the number of bonds held by institutions and those held by the public?

Mr. DOUGLAS. I do not know about institutions, but I shall ask unanimous consent to include a number of documents in the RECORD, including a statistical record of bond purchases, bank reserves, bank loans, and price increases, I shall try to classify the Government bonds according to their type and how they are held.

Mr. MILLIKIN. Can the Senator tell us roughly how the bonds are divided as between institutions and the public?

Mr. DOUGLAS. I shall submit for the RECORD a table showing figures as to how they are held.

Mr. MILLIKIN. Mr. President, will the Senator yield further?

Mr. DOUGLAS. I yield.

Mr. MILLIKIN. Can the Senator give us an approximation out of his head?

Mr. DOUGLAS. As the Senator from Wyoming has stated, of a total of $257,000,000,000 outstanding, approximately $58,000,000,000 are in series E and F bonds. Forty-one billion dollars are held by public and quasi-public institutions. About $152,000,000,000 of marketable securities are in private hands.

Mr. MILLIKIN. Mr. President, will the Senator yield further?

Mr. DOUGLAS. Yes.

Mr. MILLIKIN. Does the Senator have any table showing the maturities of the bonds in the hands of the public?

Mr. DOUGLAS. I shall include such a table in the statistical material.

Mr. MILLIKIN. The Senator is not contending is he, that in the long run the savings bonds would not reflect the rate of interest payable on the other bonds?

Mr. DOUGLAS. It would depend on how much interest rates on marketable securities rose. If the general interest rates should move upward moderately, it would not be necessary to adjust the interest on savings bonds. The Government might be compelled eventually to lift the savings-bond rate to a higher figure, a figure high enough to keep savings bonds competitive with other forms of savings.

Mr. MILLIKIN. If the Government refunds savings bonds, it would have to be done at a higher rate.

Mr. DOUGLAS. Savings bonds run 10 or 12 years to maturity. They are redeemable only at a sacrifice of interest return or on one type at a discount. It would not be necessary to refund outstanding savings bonds unless other forms of savings available to small savers became so attractive that they redeemed their bonds to hold their savings in these other forms.

Mr. MILLIKIN. I do not make any argument as to that point. I mention it because earlier in the Senator's address I understood that the interest problem in connection with savings bonds was not particularly covered.

Mr. DOUGLAS. Not so much the interest problem as the problem of the depreciation of the face value. Savings bonds are different from the Liberty bonds of the First World War, which could be sold in the open market. Series E, F, and G bonds can only be redeemed; then cannot be sold, as the Senator knows.

Mr. MILLIKIN. I was merely making an observation. There is no way of stabilizing, except for a short term, any Government rate of interest. It flows over into all Government issues, and it flows over into private finance.

Mr. DOUGLAS. That is correct.

Mr. MILLIKIN. The Senator from Illinois raised the question as to what extent we should increase the interest rate, with the incidental risks which he has mentioned. If we withdrew support from the bonds—and I am listening with great interest, and do not argue the point—there would at least be a temporary increase in the interest rate.

Mr. DOUGLAS. I should like to state it this way: If the Federal Reserve Board does as the Senator from Illinois recommends, namely, greatly reduce its volume of purchases of Government securities, it is obvious that bank reserves would not increase by the degree to which they otherwise would. Bank loans, consequently, would not increase to the extent they otherwise would. The supply of credit would largely be contracted below what it otherwise would be. If the supply of loans is reduced in relation to the demand, the inevitable result will be an increase in the price of credit. Since the price of loans is the rate of interest, a consequence of such a restrictive policy on credit would, therefore, be a rise in the interest rate. I emphasize that this rise in the interest rate is, however, a consequence of an attempt to stabilize prices of Government securities and the general price limit. It is not the primary issue which is at stake. The primary issue at stake is whether we should continue to issue unlimited quantities of bank credit. If we stop it, probably the interest rate would rise. However, that would be a lesser evil than a continued expansion of credit and a rise in prices.

Mr. MILLIKIN. That is the whole burden of the Senator's argument.

Mr. DOUGLAS. Yes.

Mr. MILLIKIN. At this time I am not taking any issue with his stand.

Mr. DOUGLAS. It is always a pleasure when a high-powered intellect agrees with me.

Mr. MILLIKIN. I asked the questions so that I could be accurately informed.

Mr. DOUGLAS. As accurately as I can inform the Senator.

Mr. MILLIKIN. Usually the Senator's infirmities are not such as to preclude him from giving an accurate answer.

Mr. DOUGLAS. I hope the Senator will carry over his tribute to me when we come to a discussion of the protective tariff.

Mr. MILLIKIN. I wish to have the RECORD show how these bonds are held, what their maturities are, and what the impact of a higher rate of interest might be, not only in its immediate relationship to the problem of inflation but also on the holders of our so-called savings bonds.

I should like to make one further suggestion, if I may. When the economy is stinking with inflation, as it is at the present time, there are also some psychological factors, which may not reflect completely the type of argument which the Senator is making. They sometimes lead to explosive inflation, regardless of the fundamental factors which are operating one way or the other. In other words, the psychology in the explosive inflation phase can override many sound measures.

Mr. DOUGLAS. That is true; but I think the psychology becomes sounder and sounder, if I may use that expression, as it is to a greater and greater degree based upon awareness of the facts.

Mr. MILLIKIN. If the medicine is not administered too long after the patient has become ill.

Mr. DOUGLAS. I can think of nothing worse for the American psychology than to have a constantly mounting cost of living and a constantly increasing scale of prices. That will lead to the sale of Government bonds. It will lead to the purchase of stocks and commodities, which will send prices still higher. It will lead to labor unrest and to strikes. It will undermine confidence in government. There is nothing economically worse than an appreciable increase in the cost of living. Though I am not in favor of an increase as such in the interest rate, I am ready to take it as a necessary evil as compared to the much greater evil of suffering a large price increase.

Mr. MILLIKIN. With much of what the Senator has said I would not disagree. I am merely making the point that perhaps we are oversimplifying the remedies. Assuming that the Senator is correct in every particular, there are a number of things which have led to the present state of inflation which might or might not be overcome by the corrections which the Senator has mentioned. However, that is no reason for not administering a good remedy if one is available to us, if it does not, in turn, stimulate other illnesses which would be bad.

Mr. DOUGLAS. Dealing with the question of complexity, let me point out this fact: The increase in the total supply of bank credit has been about 10 percent. The increase in the total quantity of physical production has been apparently about 10 percent. The increase in the velocity of circulation of money and credit has been about 10 percent. The increase in prices has been about 10 percent, if we include wholesale and retail prices together.

It is interesting to note that if we divide the relative increase in the total amount of money plus the increase in velocity of circulation by the increase in the quanity of goods produced, we get an increase of about 10 percent in prices, which is precisely what has occurred.

While these things are interrelated, what I am trying to say is that probably the chief cause for the increase has been the increase in the quantity of credit which has resulted in an increased money supply. Once prices start going up, the velocity of circulation increases, because the people know that with every day their money is worth less, so they hasten to spend it as quickly as possible. Therefore we have a cumulative force at work. An increase in money relative to goods leads to an increase in the velocity of circulation as well.

Mr. MILLIKIN. That has direct relation to my last suggestion, that if we do not use the remedies which are available to us, or if they should not work, there may come a time when certain psychologies will have greater force than all the academics of the situation.

Mr. DOUGLAS. If the Senator from Colorado is implying that I am merely influenced by academics, let me say to him that since I do not have the emoluments of academic life, I should not have the opprobrium. [Laughter.]

Mr. MILLIKIN. I imply nothing adverse to the distinguished Senator.

Mr. DOUGLAS. I thought there was a certain tone in the Senator's voice.

Mr. MILLIKIN. That shows that the Senator has a bad ear for music.

Mr. DOUGLAS. The sound of the Senator's voice is very sweet.

Mr. MILLIKIN. The Senator should get in tune with the music and it would register more sensitively. I do not like to be judged on the tone of my voice, because the good reporter here is not writing music. He is writing symbols representing words.

Mr. DOUGLAS. If we may turn from music to harsh realities——

Mr. MILLIKIN. Let us not be harsh.

Mr. DOUGLAS. Is the Senator saying that the Federal Reserve System should continue buying Government bonds?

Mr. MILLIKIN. No. I am a humble student; I am a sophomore, listening to the Senator's academics.

Mr. DOUGLAS. They are not academic issues at all.

Mr. MILLIKIN. Under such circumstances the teacher always has a victory.

Mr. DOUGLAS. The Senator from Colorado is quite able to answer back, and he does so on many occasions with great skill.

Mr. CASE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. CASE. It has been my impression that the Government itself is the loser on the alternatives which the Senator has suggested. That is, the Government today is a large procurer. It is buying many things. If it is a choice between having a higher price——

Mr. DOUGLAS. I would not like to say that the Government is a procurer, but it procures large quantities of goods.

Mr. CASE. I will accept that modification or clarification.

Mr. DOUGLAS. Whatever may have been the record of the Federal Government from 1920 to 1933, it is certainly not true under the present administration.

Mr. MILLIKIN. If the Government is a procurer, it is under the present administration. [Laughter.]

Mr. CASE. In any event, the Government is in the market today buying a vast quantity of goods, military and otherwise. I agree pretty largely with the thesis of the Senator from Illinois with respect to the probable cost of an increase in the interest rate and the lack of desirability of such an increase per se. But if it is a choice between paying a higher price for what the Government has to buy and paying a higher interest rate at a lesser price, what is the picture for us?

INFLATION OF PRICES COSTS GOVERNMENT MORE THAN HIGHER INTEREST RATE

Mr. DOUGLAS. There can be no question about that matter. The interest payments of the Federal Government amount to five and eight-tenths billion, out of a total projected budget of $71,000,000,000, leaving $66,000,000,000 for goods and services. The Government stands to lose much more from an increase in prices than it does from an increase in interest rates.

Mr. CASE. That is, the Government can buy money at a higher rate and still have economy, as against paying higher prices for goods.

Mr. DOUGLAS. Provided it can keep the price level down. Of course, if both interest rates and prices rise, it is caught both ways. But if we could shut off the supply of bank credit or greatly reduce the supply of bank credit and stabilize prices, then we could take the slight increase in the interest rate which would be needed as a cheap price with which to purchase both fiscal and general social stability.

Mr. CASE. Has the Senator made any computation of the additional cost to the Government by reason of the increase in prices since the 27th of June?

Mr. DOUGLAS. I have made a rough computation that when the effects are fully evident, they will amount to at least $6,000,000,000 a year, and probably more, because the increase in wholesale prices has been 17 percent; the increase in the cost of living has been about 7 percent. If we take an average of the two, and perhaps of services, the average would be between 10 and 12 percent. Apply that as an average and it works out from $6,000,000,000 to $7,000,000,000. Even if the interest rate on long-term securities should rise from 2½ to 3 percent, and the rate on other Government securities should go up correspondingly, that would represent an increase in the total interest bill of only $1,250,000,000.

Mr. CASE. I have seen the observation made that since the 27th of June we have lost 100 times more planes by reasons of the increased cost of planes than we have lost in conflict.

Mr. DOUGLAS. That is quite possible.

Mr. MILLIKIN. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MILLIKIN. I think it has been said—I have not checked it—that we have really lost the value of our recent tax increases.

Mr. DOUGLAS. We have lost very close to it.

Mr. MILLIKIN. May I ask one further question?

Mr. DOUGLAS. Certainly.

Mr. MILLIKIN. Has the Senator made an estimate during the course of his remarks as to what he would call the amount of legitimate bank credit which should flow at the present time, in order to measure the amount of inflationary bank credit?

Mr. DOUGLAS. It is quite difficult to secure an accurate figure.

Mr. MILLIKIN. Oh, yes.

Mr. DOUGLAS. But I should say that at the very least we should not let the total supply of bank credit increase.

Mr. MILLIKIN. Let me put it another way, please. Obviously, with an economy of the size of ours there must be a legitimate base of bank credit.

Mr. DOUGLAS. Yes.

Mr. MILLIKIN. I am trying to figure whether the Senator has measured what that base should be to support legitimately an economy of the present size of ours.

Mr. DOUGLAS. I should say that probably it would have been desirable not to have increased the total amount of demand deposits above $85,000,000,000 and to depend upon a philosophy of increase in the velocity of circulation to match the increase in production. The increase from $85,000,000,000 to $93,000,000,000 has been a misfortune. I would not like to see an increase above $93,000,000,000.

Mr. MILLIKIN. Is it the Senator's idea that in the main that increase is inflationary?

Mr. DOUGLAS. Yes.

Mr. TAFT. Mr. President, will the Senator yield?

Mr. DOUGLAS. Yes.

Mr. TAFT. As I understand—and I agree with the Senator—the effect today of the policy of the Federal Reserve Board in supporting the Government market at par is practically to monetize the public debt at the request of any bank that chooses to make the request.

Mr. DOUGLAS. It makes it possible for anyone who wants to present Government bonds to the bond market committee of the Federal Reserve Bank to have the bonds purchased. The effect will be to increase the bank reserves by that amount.

Mr. TAFT. I agree with the general thesis of the Senator. I have one or two questions. Does not the Senator think it is possible that the 2½ percent rate, which is the basic Government rate on long-term bonds, may be a sound rate, so that if the Board stops buying bonds, at least the bonds will not fall very far below par?

Mr. DOUGLAS. That was my argument.

Mr. TAFT. So under those circumstances, does the Senator think the banks would be very much discouraged from disposing of such bonds? Would there not in effect, so to speak, be a general public market for the bonds even if the Federal Reserve Board should stop buying them?

Mr. DOUGLAS. I regret that the distinguished Senator from Ohio was not on the floor when I made that point, because I tried to develop it in some detail. What the Senator from Ohio suggests is quite true. Insurance companies and financial institutions will not want to show losses on their books, and if and when the bonds fall below par, if they sell them, that means that the institutions will have to admit that they have taken losses, and they do not like to do that. Secondly, as the price of bonds with fixed interest rates falls, of course the yield rises proportionately, so that they become more and more attractive and hence they will less and less be sold. Therefore, I do not think we need fear that the bottom will fall out of the bond market.

Mr. TAFT. I agree fully with the Senator from Illinois. I question whether the price is going to fall at all, and therefore whether the bond situation will have much effect on inflation. I agree with the Senator that we ought to abandon the present policy. I raised the question as to whether such abandonment actually will have the effect of preventing inflation, as the Senator desires. It may do so. I think it will not.

Mr. DOUGLAS. If I may say so, I think the Senator from Ohio is now falling into the same fallacy the Senator from Wyoming [Mr. O'MAHONEY] fell into earlier in the day. The Senator from Ohio is assuming that those of us who want to check inflation hope to do so by raising the interest rate. That is not the point. I certainly do not argue that a rise in the interest rate will appreciably reduce the amounts which borrowers will want to borrow from banks. Interest payments are such a small fraction of the total cost of business operations that a rise in the rate would not represent much of an increase in total cost. Therefore, I do not think it would appreciably reduce the demands for loans. I think that economists and bank authorities have in the past erred in overstressing this point.

What I am saying is that we should try to control credit not by raising the price but by helping to shut off the supply.

Mr. TAFT. But my point is that the banks, after all, will be able to cash their bonds. The basic difficulty lies in the fact that the bonds are so liquid that ordinary methods of credit control are not going to be extremely effective. I am inclined to agree with the Senator from Illinois. I think the abandonment of the policy will cause bonds to drop a little, though not a great deal, below par, and that may discourage the banks from cashing their bonds and increasing their reserves and other loans.

Mr. DOUGLAS. The significance of correct Federal Reserve action lies not in increasing the interest rate, but in reducing the amount of purchases, so that the banks will not be able to get reserves by selling their bonds. That is the essence of it.

Mr. TAFT. That is true unless they can sell their bonds to the general public and later on say, "A 2½-percent bond or the short-term bond is pretty good, even at present interest rates."

Mr. DOUGLAS. Yes; but if bank loans do not increase the total amount of money does not increase, and we do not have inflation.

Mr. TAFT. I agree it will have less effect if the bonds are sold to the public than to the Reserve banks.

What does the Senator from Illinois propose that Congress do about it?

Mr. DOUGLAS. I do not know what the Congress can do about it, but I hope that the present admonition from this side of the aisle to the Treasury may make the Treasury a little less hidebound, and strengthen the will of the Federal Reserve Board to take the action which the law authorizes. I think the Treasury and its advisers have been engaged in a wrong policy for a considerable time. I should like to see them yield their position. If they do not yield, I am ready to propose a resolution at an appropriate time, similar to that which our subcommittee proposed a year ago, providing that the control over the total supply of credit be put into the hands of the Federal Reserve Board, and that the issue of servicing the debt be subordinate to that, rather than be made, as now, the primary consideration.

Mr. TAFT. I agree with the Senator from Illinois that the admonition from the other side of the aisle is going to be much more effective than a similar admonition given from this side of the aisle.

Mr. DOUGLAS. I agree.

Mr. TAFT. I am quite delighted to join with the Senator from Illinois in that admonition. I should be interested to see the resolution which the Senator from Illinois may ultimately have to propose if the Treasury remains obdurate in spite of the admonition from the other side of the aisle.

Mr. MILLIKIN. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MILLIKIN. I think the distinguished Senator from Illinois is working in a very hopeful atmosphere. The Senator from Arkansas [Mr. FULBRIGHT] won one battle the other day.

Mr. DOUGLAS. May I say in all modesty that I helped him.

Mr. MILLIKIN. That victory will help to feed the Senator's furnace.

Mr. DOUGLAS. It is a great tribute to the power of truth in a democracy.

Mr. MILLIKIN. It is a great tribute to the powers of the Senator from Arkansas and the Senator from Illinois, without undue disparagement so far as the significance of the word "truth" is concerned.

I should like to ask the Senator from Illinois a question. What was the call-money rate when everything went to pot in the late 1920's?

Mr. DOUGLAS. I do not recall exactly; but, as I remember, call money in New York was very high, say about 10 percent. That was a rate paid by stock market speculators on their loans.

Mr. MILLIKIN. Interest rates have profound significance with relation to, let us call it, inflation.

Mr. DOUGLAS. I have never maintained that high interest rates—and I think this is the fourth time I am making this statement today—I have never maintained that high interest rates greatly diminish the demand for loans. Economists have been wrong about that. Bank authorities have been wrong about it. The important point is the question of supply. If the supply is shut off, the money simply is not there to loan. I am sorry to see that the Senator from Wyoming [Mr. O'MAHONEY], the Senator from Ohio [Mr. TAFT], and the Senator from Colorado [Mr. MILLIKIN] have all fallen into this fallacy.

Mr. MILLIKIN. The Senator from from Colorado has not disclosed his position.

Mr. DOUGLAS. The Senator from Colorado always hides behind the thicket and has a machine gun concealed there which is ready for action.

Mr. MILLIKIN. I have not as yet unmasked the machine gun. I am in process of attending the Senator's seminar and trying to learn something. Maybe some day I shall submit a paper for a master's degree, or for one of the lesser degrees.

Mr. DOUGLAS. As I said, since I do not have the emoluments of the teaching professor, I ought not to be reproached with conducting a seminar. But I can learn from the Senator's legal stance and I am anxious to do so.

Mr. MILLIKIN. I am not asserting that the Senator is receiving any such emoluments. I should like to receive some of the emoluments myself. I suggest that the Senator place in the RECORD, not that the Senator thinks it would be of any significance, but someone else in considering the Senator's thesis might think so, what the interest rate was on call money when the collapse came in 1929.

Mr. DOUGLAS. In October 1929.

Mr. MILLIKIN. Yes.

Mr. DOUGLAS. Would the Senator like some figures for December 1907?

Mr. MILLIKIN. Yes.

Mr. DOUGLAS. And for January 1897?

Mr. MILLIKIN. It would not be a bad idea, if the Senator from Illinois related them in some kind of a pattern.

Mr. DOUGLAS. And the price of rubber in Brazil in 1907?

Mr. MILLIKIN. Before the Senator concludes putting in the RECORD his charts and other material I expect to see all those figures exposed, and I also expect that the Senator from Illinois will give some kind of a reason for exposing them.

However, let us confine ourselves to 1929 or whenever it was when interest on call money and interest rates reached their peak, just before the flood came.

Mr. DOUGLAS. Earlier in the day the Senator asked for information as to who held various types of Government securities, and in what quantities. For the sake of the RECORD, let me say that the total volume of outstanding Government securities as of December was approximately $257,000,000,000; that $152,500,000,000 were marketable; that the Reserve banks held $19,000,000,000; commercial banks, $62,000,000,000; mutual savings banks, $11,000,000,000; insurance companies, $19,500,000,000; other corporations, just short of $20,000,000,000; State and local governments, $8,100,000,000. Individuals held savings bonds amounting to just under $50,000,000,000; other securities, $17,600,000,000; miscellaneous investments, $11,000,000,000.

Mr. MILLIKIN. I thank the Senator.

Mr. DOUGLAS. I will also put in a table of maturity dates and amounts.

Mr. MILLIKIN. For the benefit of those who might believe there is some relationship between the problem we are considering and the rate of interest, will the Senator include in his remarks or in the annexes to his remarks the call money interest rate before the collapse came in the late twenties?

Mr. DOUGLAS. I shall be very glad to do so just as soon as I am able to obtain this information. I think it was around 10 percent.

Mr. President, I have wished to conclude before now, but have been on my feet longer than I intended to be, only because of the very alert questioning of certain of my colleagues.

TREASURY SHOULD YIELD AND FEDERAL RESERVE SHOULD DIMINISH BUYING

I conclude with the plea that the Treasury abate its policies and yield on this issue. May I also enter a plea that the Federal Reserve Board gird its legal loins and fulfill the responsibilities which I believe Congress intended it to have?

I ask unanimous consent to have included at this point in the RECORD, as a part of my remarks or as an appendix to them, certain statistical material and other statements which I should like to have included.

There being no objection, the statistics and statements were ordered to be printed in the RECORD, as follows:

APPENDIX I

INCREASE IN BANK CREDIT AND THE MONEY SUPPLY SINCE KOREA

Table 1, which follows, shows the unprecedented increase in bank credit to private borrowers and State and municipal governments in the period from Korea to the end of 1950. It also lists the totals of loans at all commercial banks at the end of January 1949, 1950, and 1951.

Table 2 shows the equally unprecedented increase in the money supply for the same period. The second part of table 2 shows the absolute totals of the private money supply on four dates, from January 1949 to January 1951.

Bank credit to these borrowers in the first 6 weeks of 1951 reflects a continuation of strong inflationary pressures. Loans to business increased over this period by the largest amount ever recorded in the entire 14-year history of the weekly commercial, industrial, and agricultural loan series. Total loans increased by a smaller amount than business loans because of a decline in high year-end borrowing for purely financial purposes such as security loans.

The privately held money supply declined in the first 6 weeks of 1951, as it ordinarily does in this period, from purely seasonal forces. Currency in the hands of the public was reduced as a result of the usual post-holiday inflow of currency to the banks. Tax payments, as usual, had the effect of transferring deposits from individuals, partnerships, and corporations to United States Government accounts at commercial banks and the Federal Reserve banks. Other factors which account for the reduction in the privately held money supply include an outflow of gold and some purchases of United States Government's by nonbank investors from the banking system. Ordinarily, a reduction in bank loans accounts, in part, for the seasonal reduction of the money supply in this period, but, as mentioned above, bank loans increased this year.

TABLE 1

A. Growth in bank credit to borrowers other than the Federal Government, last half of 1950

[In billions of dollars]

Loans at all commercial banks	+8.0
Corporate and municipal securities at all commercial banks	+1.1
Total increase in commercial bank credit excluding United States Government securities	+9.1

B. Total of loans at all commercial banks

[In billions of dollars]

End of January 1951	52.8
End of January 1950	42.9
End of January 1949	42.5

TABLE 2

A. Growth of the privately held money supply, last half of 1950

[In billions of dollars]

Total deposits adjusted and currency outside banks [1]	+7.2
Demand deposits adjusted	+8.2
Time deposits adjusted [2]	−0.7
Currency outside banks	−0.2

[1] Adjusted to exclude U. S. Government and interbank deposits and items in process of collection.

[2] Includes deposits in commercial and mutual savings banks and the Postal Savings System.

B. Total private money supply (total deposits adjusted and currency)

[In billions of dollars]

End of January 1951	175.7
End of June 1950	168.5
End of January 1950	169.7
End of January 1949	168.2

APPENDIX II

ADVANCES IN COMMODITY PRICES SINCE KOREA

Commodity prices have shown marked widespread advances since last summer to new record levels. Following an initial wave in buying last July, demand showed some abatement during the autumn as Korean developments were temporarily favorable, and the rise in prices slowed down. Following Chinese intervention and declaration of a national emergency, buying and prices showed a renewed upturn until the general freeze was imposed on January 26. Since that time, average wholesale prices of farm products and foods, controlled only in part, have risen further by 3½ percent. The general level of wholesale commodity prices is now 17 percent higher than last June and 20 percent higher than a year ago, as shown in table 4. Average prices of consumer goods and services in mid-December were reported to be 5 percent higher than in June. It is likely that the consumers' price index will show a further rise of 2 percent in February to a level 9 percent higher than a year ago. As shown in table 3, wholesale prices of a number of major materials have risen by 50 percent or more. Farm products are 28 percent above a year ago after rising 5 percent in January. Wool prices rose 35 percent in January. Cotton prices are 50 percent above the Federal support level.

TABLE 3.—*Advances in prices of major commodities*

Commodity	Percentage increase to Feb. 16, 1951, from—	
	June 23, 1950	Feb. 16, 1950
INDUSTRIAL MATERIALS		
Rubber	281	168
Tallow	279	184
Waste paper	203	255
Tin	140	146
Silk	113	113
Burlap	107	81
Apparel-type wool	97	123
Alcohol	70	121
Print cloth	51	43
Hides	47	60
Cotton	32	39
Steel scrap	21	68
Zinc	16	73
Pig iron	14	14
Copper	9	33
FOODSTUFFS		
Corn	25	43
Steers	25	25
Cocoa	18	52
Hogs	18	34
Butter	16	11
Wheat	15	15
Coffee	14	14
Sugar	2	7

TABLE 4.—*Advance in wholesale and retail prices*

Series	Percentage increase to Feb. 16, 1951, from—	
	June 23, 1950	Feb. 16, 1950
WHOLESALE PRICES		
All commodities	17	20
Farm products	22	28
Grains	16	21
Livestock	21	34
Foods	17	22
Other commodities	15	17
Textile products	32	31
Chemicals	29	27
Building materials	12	18
Metals and metal products	10	12
Fuels and lighting materials	3	5
CONSUMER PRICES		
All items	5	7
Foods	5	11
Apparel	6	6
Rent	2	2

NOTE.—Compiled from BLS data. Changes in consumers' prices are to mid-December.

TABLE 5

A. Changes in member bank reserves, reserve bank credit and principal related items, selected dates

[In millions of dollars]

	Aug. 16 to Oct. 4	Oct. 4 to Nov. 22	Nov. 22 to Jan. 3	Jan. 3 to Feb. 14
Reserve bank credit, total	+1,083	+190	+1,717	+1,451
U. S. Government securities	+1,041	−79	+1,275	+1,237
Other Reserve bank credit	+42	+269	+443	+214
Gold stock	−472	−385	−391	−446
Money in circulation	+212	+262	+235	−526
Treasury deposits with Federal Reserve banks	+131	−307	+5	+318
Nonmember and other Federal Reserve accounts	−50	−114	+10	−36

TABLE 5.—Continued

[In millions of dollars]

	Aug. 16 to Oct. 4	Oct. 4 to Nov. 22	Nov. 22 to Jan. 3	Jan. 3 to Feb. 14
Member bank reserves: Total	+328	−4	+1,069	+1,261
Required reserves	+235	+226	+399	[1]+1,747
Excess Reserves (estimated)	+93	−240	+670	−486

[1] Increase entirely due to increase in reserve requirements.

B. Member bank reserves, reserve bank credit, and principal related items

[As of Feb. 14, 1951, in millions of dollars]

Member bank reserves, total	18,952
Required reserves	18,226
Excess reserves	726
Reserve bank credit, total	23,330
U. S. Government securities	21,808
Loans, discounts, advances	298
Other reserve bank credit	1,225
Gold stock	22,260
Treasury currency outstanding	4,637
Money in circulation	27,159
Treasury cash holdings	1,292
Treasury deposits with Federal Reserve banks	864
Foreign bank deposits with Federal Reserve	916
Other deposits with Federal Reserve	310
Other Federal Reserve accounts	734

TABLE 6

A. Changes in Federal Reserve holdings of Government securities, selected periods

[In millions of dollars]

Issue	Aug. 16 to Oct. 4	Oct. 4 to Nov. 22	Nov. 22 to Jan. 3	Jan. 3 to Feb. 14
Bills	−2,915	−382	+190	+534
Certificates and notes	+4,822	−141	+723	+125
Bonds	−866	+444	+335	+579
Total	+1,041	−79	+1,275	+1,237
Net purchases of marketable securities for Treasury account estimated)				+125

LEGEND

Aug. 16 to Oct. 4: Treasury refunding at 1¼ percent for 13 months.

Oct. 4 to Nov. 22: Rising short-term rates.

Nov. 22 to Jan. 3: Treasury refunding at 1¾ percent for 5 years.

Jan. 3 to Feb. 14: Increase in reserve requirements.

B. Federal Reserve holdings in Government securities

[Close of business Feb. 14, in millions of dollars]

Total holdings	21,808
Treasury bills	1,700
Certificates and notes	15,905
Treasury bonds, total	5,202
Bank eligibles (short-terms)	1,562
Restricted (long-term 2½ percent pegged)	3,640

APPENDIX III

CHANGES IN PRODUCTION COMPARED WITH BANK CREDIT EXPANSION SINCE OUTBREAK OF KOREAN CONFLICT

The effects of bank credit expansion in present circumstances: It seems reasonable to believe that, even without any expansion of bank credit, the outbreak of hostilities in Korea and subsequent developments would have created demands for goods and services which would have strained this country's productive capacity and pressed hard against the prevailing price level. Most business firms and consumers were in a position to increase their purchases of goods and services without increasing their indebtedness. Nevertheless, fears of shortages of goods and price rises have encouraged many businesses and consumers to borrow additional funds in order to obtain a larger share of the total output of goods and materials than their existing financial resources would permit. Banks have been able to accommodate these swollen demands for credit by disposing of part of their large holdings of Government securities, which bear a much lower rate of interest than do business loans. This switch from Government securities to loans was made possible by the Government's rigid policy of having the Federal Reserve support the price of Government securities above par.

The recent increases in bank credit have operated to expand the private money supply (the amount of deposits and currency held by individuals and businesses), which was $7,200,000,000 higher at the end of December than at the end of June. This increase was much larger than the usual seasonal expansion in the money supply. Businesses and individuals also hold large amounts of Government securities which they can convert into cash at will. Thus, the total volume of liquid assets which can be drawn upon at any time to finance purchases of goods and services is very large, not only absolutely but, even more important, relative to the level of output.

The growth in the size of liquid asset holdings (including Government securities as well as currency and deposits) has been accompanied by an increase in their use. The turn-over of demand deposits has become greater. Turn-over is still low as compared with some periods in the past, however, and could easily become the basis for a substantial further increase in spending without additional deposit creation.

In these circumstances the additional demands for goods made possible by the ready availability of bank credit have been superimposed upon already great demands arising out of large and growing incomes and previously accumulated liquid asset holdings. These additional, bank-financed demands have not been necessary to evoke greater output. Their principal effect has been to contribute to the chain of price increases which has been set in motion and which is proving difficult to check, notwithstanding the fiscal and monetary actions that have already been taken.

The statistical evidence: It is estimated that the gross national product in physical terms increased by 5 or 6 percent from the second quarter of 1950 to the last quarter of the year. If the index of industrial production is used as a measure, there was a small decline in production immediately following the Korean crisis. Recovery was very rapid, however. By October output was 10 percent higher than in June. Production then sagged in November and has remained relatively unchanged since then. The expansion of production was accompanied at first by an almost equivalent proportionate rise in prices, but prices continued to rise, whereas production did not. The higher prices may be attributed in no small part to the tremendous increase in total bank loans, which were over 17 percent, or $8,000,000,000, greater at the end of December than at the end of June. This additional bank credit intensified the competition for resources, for which demand at existing prices had already exceeded supply.

A sample survey by the Federal Reserve System of the nature of the increases in business loans from the end of June 1950 to the beginning of November of banks in leading cities strengthens the belief that the recent sharp expansion in bank credit has not, for the most part, facilitated greater production, but has merely contributed to the rise in prices. The purpose of the Board's survey was to obtain information on the types of businesses responsible for the recent increase in business loans of banks and the purposes for which such businesses borrowed. Replies were received from member banks accounting for about half of the recent increase in business loans of all commercial banks.

The most striking finding of the survey was that increased loans to commodity dealers and processors of agricultural commodities accounted for approximately three-fifths of the total reported expansion of business loans. Loans to cotton dealers predominated. The stated purposes of these loans were almost exclusively for inventories and other working capital. Inasmuch as the available supply of these agricultural commodities was fixed, it may be concluded that bank loans to commodity dealers and processors of agricultural commodities did not contribute to the rise in industrial or agricultural production. What they did do was to provide the funds which led to increased bidding for a fixed supply of goods, and to encourage the accumulation of stocks in anticipation of rising prices. These actions were important contributing factors to the recent sharp advance in commodity prices. Another notable finding of the survey was that increases in loans for defense contracts and to durable goods industries were negligible, notwithstanding the importance of these industries in a defense economy.

In short, there is very little evidence to support the view that the recent increases in bank credit have been responsible or necessary for the increase in industrial production that has occurred since June. What they have done is to facilitate inventory accumulations and to drive up prices.

TABLE 7.—*Ownership of United States Government securities, direct and fully guaranteed*

[Par value in millions of dollars]

End of month	Total gross debt (including guaranteed securities)	Held by U. S. Government agencies and trust funds [1]		Held by the public									
		Special issues	Public issues	Total	Federal Reserve banks	Commercial banks [2]	Mutual savings banks	Insurance companies	Other corporations	State and local governments	Individuals		Miscellaneous investors [3]
											Savings bonds	Other securities	
1940—June	48,496	4,775	2,305	41,416	2,466	16,100	3,100	6,500	2,100	400	2,600	7,500	700
1941—June	55,332	6,120	2,375	46,837	2,184	19,700	3,400	7,100	2,000	600	3,600	7,600	700
1942—June	76,991	7,885	2,737	66,369	2,645	26,000	3,900	9,200	4,900	900	9,100	8,700	1,100
1943—June	140,796	10,871	3,451	126,474	7,202	52,200	5,300	13,100	12,900	1,500	19,200	11,700	3,400
1944—June	202,626	14,287	4,810	183,529	14,901	68,400	7,300	17,300	20,000	3,200	31,200	14,800	6,400
1945—June	259,115	18,812	6,128	234,175	21,792	84,200	9,600	22,700	22,900	5,300	40,700	18,300	8,900
1946—June	269,898	22,332	6,798	240,768	23,783	84,400	11,500	25,100	17,700	6,500	43,500	19,500	8,800
1947—June	258,376	27,366	5,445	225,565	21,872	70,000	12,100	24,800	13,900	7,100	45,500	20,500	9,800
December	256,981	28,955	5,404	222,622	22,559	68,700	12,000	24,100	14,100	7,300	46,200	19,100	8,600
1948—June	252,366	30,211	5,549	216,606	21,366	64,600	12,000	23,100	13,500	7,800	47,100	18,100	9,100
December	252,854	31,714	5,614	215,526	23,333	62,500	11,500	21,500	14,300	7,900	47,800	17,500	9,300
1949—June	252,798	32,776	5,512	214,510	19,343	63,000	11,600	20,800	15,100	8,000	48,800	17,800	10,000
December	257,160	33,896	5,464	217,800	18,885	66,800	11,400	20,500	16,300	8,000	49,300	16,900	9,800
1950—June	257,377	32,356	5,474	219,547	18,331	[4] 65,600	11,600	20,100	18,300	8,200	49,900	[4] 17,300	10,200
July	257,557	32,518	5,465	219,574	17,969	[4] 64,600	11,500	20,100	18,800	8,200	50,000	[4] 17,500	10,900
August	257,891	32,705	5,430	219,755	18,356	[4] 64,000	11,400	20,000	19,500	8,200	49,900	[4] 17,600	10,800
September	257,236	33,396	5,490	218,350	19,572	[4] 62,100	11,200	19,700	19,400	8,100	49,900	[4] 17,600	10,700
October	256,959	33,539	5,475	217,945	19,252	62,100	11,100	19,500	19,800	8,100	49,800	17,600	10,800

[1] Includes the Postal Savings System.
[2] Includes holdings by banks in Territories and insular possessions, which amounted to $300,000,000 on June 30, 1950.
[3] Includes savings and loan associations, dealers and brokers, foreign accounts, corporate pension funds, and nonprofit institutions.
[4] Revised.

NOTE.—Holdings of Federal Reserve banks and U. S. Government agencies and trust funds are reported figures; holdings of other investor groups are estimated by the Treasury Department.

Source: Federal Reserve Bulletin, January 1951.

TABLE 8.—*U. S. Government marketable public securities outstanding Dec. 31, 1950*

[On basis of daily statements of U. S. Treasury. In millions of dollars]

Issue and coupon rate:	Amount
Treasury bills [1]:	
Jan. 4, 1951	1,003
Jan. 11, 1951	1,002
Jan. 18, 1951	1,000
Jan. 25, 1951	1,001
Feb. 1, 1951	1,100
Feb. 8, 1951	1,102
Feb. 15, 1951	1,101
Feb. 23, 1951	1,105
Mar. 1, 1951	1,102
Mar. 8, 1951	1,103
Mar. 15, 1951	1,001
Mar. 22, 1951	1,001
Mar. 29, 1951	1,005
Certificate of indebtedness: Jan. 1, 1951, 1⅛	5,373
Treasury notes:	
July 1, 1951-B, 1¼	2,741
July 1, 1951-C, 1¼	886
July 1, 1951-D, 1¼	4,818
Aug. 1, 1951, 1¼	5,351
Oct. 1, 1951, 1¼	1,918
Oct. 15, 1951, 1¼	5,941
Nov. 1, 1951, 1¼	5,253
Mar. 15, 1954, 1⅜	4,675
Mar. 15, 1955, 1½	5,365
Dec. 15, 1955, 1¾	2,309
Treasury bonds:	
June 15, 1951-54,[2] 2¾	1,627
Sept. 15, 1951-53, 2	7,986
Sept. 15, 1951-55,[2] 3	755
Dec. 15, 1951-53,[2] 2¼	1,118
Dec. 15, 1951-55, 2	510

Footnotes at end of table.

Issue and coupon rate—Continued	Amount
Treasury bonds:	
Mar. 15, 1952-54, 2½	1,024
June 15, 1952-54, 2	5,825
June 15, 1952-55, 2¼	1,501
Dec. 15, 1952-54, 2	8,662
June 15, 1953-55,[2] 2	725
June 15, 1954-56,[2] 2¼	681
Mar. 15, 1955-60,[2] 2⅞	2,611
Mar. 15, 1956-58, 2½	1,449
Sept. 15, 1956-59,[2] 2¾	982
Sept. 15, 1956-59, 2¼	3,823
June 15, 1958-63,[2] 2¾	919
June 15, 1959-62,[3] 2¼	5,284
Dec. 15, 1959-62,[3] 2¼	3,470
Dec. 15, 1960-65,[2] 2¾	1,485
June 15, 1962-67,[3] 2½	2,118
Dec. 15, 1963-68,[3] 2½	2,831
June 15, 1964-69,[3] 2½	3,761
Dec. 15, 1964-69,[3] 2½	3,838
Mar. 15, 1965-70,[3] 2½	5,197
Mar. 15, 1966-71,[3] 2½	3,481
June 15, 1967-72,[3] 2½	7,967
Sept. 15, 1967-72, 2½	2,716
Dec. 15, 1967-72,[3] 2½	11,689
Postal-savings bonds, 2½	109
Panama Canal loan, 3	50
Total direct issues	152,450
Guaranteed securities: Federal Housing Administration, various	21

[1] Sold on discount basis.
[2] Partially tax exempt.
[3] Restricted.

Source: Federal Reserve Bulletin, January 1951.

APPENDIX IV

STATEMENT OF MILTON FRIEDMAN, LLOYD A. METZLER, FREDERICK H. HARBISON, LLOYD W. MINTS, D. GALE JOHNSON, THEODORE W. SCHULTZ, AND H. G. LEWIS, OF THE DEPARTMENT OF ECONOMICS, UNIVERSITY OF CHICAGO

THE FAILURE OF THE PRESENT MONETARY POLICY

Our purpose in preparing this statement is to show that the present monetary policy of the Federal Reserve is highly inflationary, that the monetary actions of the Federal Reserve since Korea have permitted the marked price rise which has already occurred, and that the Federal Reserve, presumably under the influence of the Treasury, is pursuing an ill-conceived policy that will interfere with effective mobilization of our economic strength even though taxes are increased enough to keep the Federal budget in balance.

Prices are rising at an alarming rate. This rise is widely attributed to the armament effort, to the efforts of business firms as they get ready for military contracts, and to speculative purchases by businessmen and consumers in anticipation of further price rises. This explanation neglects the critical role being played by a misconceived monetary policy in permitting these armament and private efforts to produce a price rise. As a result of the monetary failure, the Government is now committed to drastic measures in its attempt to control prices and wages which do not strike at the root causes of inflation and which impair the general efficiency of the economy and, also, affect adversely the armament effort.

Actually the production of armament is as yet a mere trickle. The recent price rises cannot, therefore, be attributed to expenditures on these. Neither can they be attributed to other expenditures by the Federal Government. During the second 6 months of 1950, the Federal Government took in substantially more than it paid out. The Federal budget was, therefore, if anything, a deflationary rather than an inflationary force during this period. True, as armament expenditures rise, this situation will change unless new taxes are levied to meet the increased expenditures. Such additional taxes should be levied. But the recent price rises cannot be attributed to failure by Congress to enact adequate taxes. On the contrary, the willingness of Congress to impose new taxes has been the brightest spot in our economic policy during the last 6 months.

The expectation has been that there would be substantial armament expenditures in the future, that a wide variety of goods would be unavailable, and that there would occur future rises in prices. The expectation has given a strong incentive to businesses and individuals to buy now. The repeated threats by Government of wage and price ceilings have further promoted price rises by serving notice on any groups that can exercise control over prices or wages to increase them before it is too late. But neither force could have produced a price rise together with full employment and a high level of output unless businesses and individuals had been able to get funds with which to finance additional purchases. Anticipations of future price rises could have been prevented from producing a price rise by a vigorous monetary policy designed to make credit tight, to prevent an increase in the quantity of money, or if necessary, to decrease the quantity of money in order to offset a rise in the rate of use of money.

Instead of following such a policy, our monetary authorities have done nearly the reverse. They have provided additional reserves to the banking system, thereby making it possible for banks to expand both their loans and their deposits at an extraordinary rapid rate. The loans have provided the financial means for speculative purchases; the deposits have provided the circulating medium for the larger money volume of transactions.

The consequences are written clearly and dramatically in the statistical record since Korea. From May 31 to the end of 1950, bank loans rose by nearly $10,000,000,000 or nearly 20 percent. Adjusted demand deposits, the most active component of the money supply, rose by over $7,000,000,000, or over 8 percent. Currency outside banks rose only slightly, by about $500,000,000, so that the total circulating medium rose by 7 percent. This increase in the money supply was made possible primarily by Federal Reserve purchases of Government securities. Federal Reserve holdings of Government securities rose by also $3,500,000,000, or 20 percent. Almost half of this increase was offset by a gold outflow, but nearly two billion was added to member bank reserve balances by the security purchases and other Federal Reserve operations. The resultant 12-percent increase in reserves was more than enough to support the 8-percent increase in demand deposits, so that excess reserves were actually more than twice as large at the end of 1950 as they had been 7 months earlier.

With a rise of over 8 percent in demand deposits, it is little wonder that personal income rose about 10 percent, wholesale prices about 11 percent, cost of living by nearly 6 percent. It is no accident that these figures are so nearly of the same magnitude. This is about as clear a case of purely monetary inflation as one can find.

These are admittedly highly technical matters, which is one of the main reasons why, as professional economists, we feel it incumbent on us to call them to the attention of the public. They clearly are technical matters of the gravest importance. The price rise of the last 6 months could almost certainly have been largely or wholly avoided by effective monetary action. Indeed, prices would probably today be little above their level in May if the Federal Reserve System had kept its holdings of Government securities unchanged instead of adding to them by $3,500,000,000.

The Federal Reserve System has had ample legal power to prevent the recent inflation. Its Board of Governors are an able and public-spirited body of men. Their failure to stop the inflation can be charged neither to impotence nor to ignorance nor to malice. Why, then, have they failed to use the means at their disposal?

The failure to tighten bank reserves since Korea is a consistent part of the financial history of the last decade. One cost of effective use of monetary measures to stem inflation is a rise in the interest rate on the Government debt. The major weapon available to the Federal Reserve System is control over its holdings of Government securities. Sales of securities produce a flow of money into the Federal Reserve System and out of currency in circulation and out of bank reserves. This action reduces the availability of credit to the public. This weapon has not been used effectively throughout the last 10 years because the Treasury and the Federal Reserve System between them have been unwilling to let one particular price, the interest yield on Government bonds, rise more than fractionally. They have preferred to hold this one price down even at the cost of facilitating a rise in all other prices. It is long past time that this short-sighted policy was abandoned.

These remarks are clearly of more than historical interest. The problems we have been facing during the last 6 months are unfortunately likely to plague us for a long time. A sound economic policy for this period should rest on two pillars: monetary policy and fiscal policy. It should use monetary policy to prevent the civilian sphere from adding fuel to inflation; it should use fiscal policies to offset the inflationary pressure of Government spending. The need for fiscal policy, specifically, heavier taxation to match heavier expenditures, is fortunately by now widely recognized. The need for, or even the possibility of, using monetary policy is hardly recognized at all. Nor can we accept the dictum of the Council of Economic Advisers that "because of the needs of debt management, * * * general credit policy cannot be expected to be a major anti-inflationary instrument during the coming period of intensive mobilization." The prices at which the citizens of this country can buy goods and services are much more important than the price at which the Government can borrow money.

The so-called needs of debt management have been magnified out of all proportion to their actual importance in economic policy. A determined policy to stop inflation will have numerous consequences, one of the least important of which would be a rise in the interest rate on Government debt, a rise that would probably be moderate. But even from the narrow point of view of debt management, the policy being followed by the Treasury is, to say the least, short-sighted. The nearly $35,000,000,000 of series E bonds outstanding can be redeemed at the will of their holders. Further price rises that continue to reduce the real value of these bonds are almost certain to produce sooner or later a flood of redemptions of outstanding bonds, to say nothing about the effect of further price rises on the willingness of the public to purchase additional savings bonds. This outcome would raise far greater difficulties for debt management than a rise in interest rates.

Monetary measures to keep down the supply of money have the great advantage that they operate impersonally and generally, affecting all alike. They do not interfere with the details of day-to-day operation, require no great administrative staff to enforce them, do not interfere with, but rather add to, the incentives to produce efficiently and economically. By preventing an expansion of credit, they assure that credit obtained to finance armament production is at the expense of credit for other purposes instead of in addition to such credit. In this way, they make the financial operations consistent with the physical operations. The physical resources for armament production must largely be obtained by diversion from other uses; they can more easily be so obtained if the financial resources are diverted as well.

Monetary policy cannot serve two masters at once. It cannot at one and the same time buttress a strong fiscal policy in preventing inflation and be dominated by the present misconceived cheap money policy of the Treasury. The necessity of making a clean-cut choice between these two objectives has been obscured by brave talk and rear-guard actions by the Federal Reserve—the raising of reserve requirements, moral suasion of the banking fraternity, selective controls on installments and stock market credit, and the like. These are all doomed to failure so long as the Federal Reserve System stands ready to buy unlimited amounts of Government bonds at essentially fixed prices.

Our national security demands a major armament effort. This armament effort is bound to create inflationary pressure. We cannot afford to add to this inflationary pressure by an inflationary monetary policy. The Federal Reserve System should at once announce that it will conduct its operations with an eye single to their effects on the supply of money and credit and on the level of prices. It should at once begin to sell Government securities to whatever amount is necessary to bring about a contraction in the currently swollen credit base. And it should persevere in this policy to the point that the inflation is checked even though one of its incidental effects is a rise in the interest rate on Government securities.

Statistics and sources

1. FEDERAL GOVERNMENT CASH BUDGET

1950, second half:	*Billions of dollars*
Cash receipts	21.9
Cash payments	19.95
Difference	1.95

Source: ½ the annual rates given in table 9, Annual Economic Review by the Council of Economic Advisers in the Economic Report of the President, January 1951, p. 160 (hereafter referred to as Annual Economic Review).

2. MONEY AND CREDIT DATA, BANKS OTHER THAN FEDERAL RESERVE BANKS

[In billions of dollars]

	End of—	
	May 1950	December 1950
Demand deposits adjusted	85.0	92.1
Currency outside banks	24.7	25.2
Total circulating medium	109.7	117.3
Time deposits	59.5	58.9
Total privately held money supply	169.2	176.2
Loans (all banks)	51.2	60.8

Source: Annual Economic Review, table A-28, p. 198, for all items except loans. May loans, Federal Reserve Bulletin, December 1950, p. 1641; December loans, increase to Nov. 29, from Federal Reserve Bulletin, January 1951, p. 55; increase from Nov. 29 to Dec. 31 estimated on basis of increase for commercial banks shown in Annual Economic Review, p. 197.

3. OPERATIONS OF FEDERAL RESERVE SYSTEM

[In millions of dollars]

	May 31, 1950	Dec. 31, 1950
U. S. Government securities	17,389	20,778
Total credit outstanding	17,935	22,216
Gold stock	24,231	22,706
Member bank reserve balances:		
Total	15,814	17,681
Excess reserves	526	1,174

Source: Federal Reserve Bulletin, January 1951, pp. 43-44.

APPENDIX V

AN ECONOMIST'S STATEMENT ON ANTIINFLATIONARY MEASURES

The undersigned economists believe that prevention of inflation in the situation created by the expanding defense program requires, as the principal line of defense, a substantial increase in taxation, reductions in expenditures at all governmental levels wherever this can be done without impairing national defense or other essential public services, and a more restrictive credit policy. The basic cause of inflation, an excess of money demand relative to available goods, must be attacked. Only adequate fiscal and monetary measures can remove this basic cause.

With the economy already operating at very high levels, further increases in spending cannot fail to enhance inflationary pressures. Under the influence of the expected increase in defense spending following the Korean outbreak, business and consumer spending has already risen markedly, and price and wage increases are augmenting business and consumer incomes. Yet most of the planned rise of defense spending is still to come, and this further rise will generate additional increases in private money incomes. Large expenditures on military programs and foreign aid, with their inflationary impact, may be needed for a decade or more. Faced with this long-run inflationary prospect, we recommend that the increase in total spending be continuously curbed in three principal ways, and that these constitute the first line of defense against inflation:

1. Scrutinize carefully all Government expenditures and postpone or eliminate those that are not urgent and essential. Substantial reductions can be achieved only if some programs are cut.

2. Raise tax revenues even faster than defense spending grows so as to achieve and maintain a cash surplus. Merely to balance the budget is not enough. If the inflationary pressure is to be removed, taxes must take out of private money incomes not only as much as Government spending contributes to them but also a part of the increase of private incomes resulting from increased private spending of idle balances and newly borrowed money. Larger taxes must be paid by all of us. Reliance should be placed primarily on increases of personal income taxes on all income in excess of present exemptions. Higher corporate profits taxes, in one form or another, are also imperative. In addition, loopholes in our tax laws should be closed.

3. Restrict the amount of credit available to businesses and individuals for purposes not essential to the defense program. An expanding supply of low-cost credit which swells private spending cannot fail to stimulate inflation when the supply of goods available for private use will be difficult to expand and may even decline.

Selective controls over consumer credit, real-estate credit, and loans on securities are useful for this purpose and should be employed. But we believe that general restriction of the total supply of credit is also necessary. This can be accomplished only by measures that will involve some rise of interest rates.

If general inflationary pressure is not removed by fiscal and credit measures, we face two alternatives: (1) continued price inflation, or (2) a harness of direct controls over the entire economy which, even if successful in holding down prices and wages for a while, would build up a huge inflationary potential in the form of idle cash balances, Government bonds, and other additions to liquidity. Such accumulated savings would undermine the effectiveness of direct controls and produce open inflation when the direct controls are lifted. Everyone remembers vividly the sharp inflation of 1946-48 when the wartime accumulation of liquid assets went to work on prices after the removal of direct price and wage controls. Either of these alternatives is extremely dangerous. A prolonged decline in the purchasing power of the dollar would undermine the very foundations of our society, and an ever-spreading system of direct controls could jeopardize our system of free enterprise and free collective bargaining. For these reasons we urge that fiscal and credit policies constitute our primary defense against inflation.

The best possible fiscal and credit policies, however, will not eliminate altogether the need for other types of restraints. The first impacts of a defense program are felt especially in particular commodities. Effective allocation programs and orders limiting the consumption of short materials to essential uses, and an expansion of supplies can help stabilization of prices and wages in such specific lines; but they cannot of themselves insure price and wage stability. Moreover, it is obvious that stability of the general level of prices in the economy would be impossible in the face of general wage increases that substantially raise costs and private spendable incomes. For the above reasons, voluntary restraints by business and labor are an important ingredient of a successful antiinflation program, and if business and labor cannot or will not exercise such restraint some mandatory Government ceilings may be necessary.

In sum, fiscal and credit measures are the only adequate primary defense against inflation, and can minimize the extent of direct Government controls over wages, prices, production, and distribution. If adequate fiscal and credit measures are not employed, the country will face the ominous choice between continuous inflation and a prolonged application of widespread Government price and wage controls.

NOVEMBER 30, 1950.

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APPENDIX VI

STATEMENT ON MONETARY AND CREDIT POLICY TAKEN FROM REPORT AND RECOMMENDATIONS OF THE COMMITTEE ON ECONOMIC STABILIZATION OF THE TWENTIETH CENTURY FUND

(John Maurice Clark, chairman, professor of economics, Columbia University; Theodore W. Schultz, chairman, Department of Economics, University of Chicago; Arthur Smithies, chairman, Department of Economics, Harvard University; Donald H. Wallace, director of graduate program, Woodrow Wilson School of Public and International Affairs, Princeton University.)

MONETARY AND CREDIT POLICY

Federal Reserve measures in recent months to tighten credit for the purchase of durable goods, houses, and securities, have reduced particular inflationary pressures where buyers of certain assets outspend their incomes. Further tightening of some of these controls as production of new cars and houses shrinks can further check the growth of excess demand in these fields. Combined with excises, it may enable us to avoid some difficult rationing problems, unless shortages become so severe as to create acute inequities.

To permit effective limitation of credit, the Federal Reserve System must be enabled to tighten bank reserves. Actually, since Korea (end of May to end of December 1950), the net effect of monetary actions was to add $1,700,000,000 (11 percent) to commercial bank reserve balances. (A rise of $3,400,000,000 in Federal Reserve holdings of Government securities was partly offset by gold losses.) This reserve expansion supported a rise of roughly $7,000,000,000 in bank earning assets and the public's cash assets. A restrictive Federal Reserve policy since Korea, given the Treasury's cash surplus during these months, could have blocked this monetary expansion and prevented much of the inflation.

The failure to tighten bank reserves since Korea is a consistent part of the financial history of the last decade. The cost of effective use of monetary measures is a rise in the interest rate on the Government debt. The major weapon available to the Federal Reserve is the sale of Government bonds. Payment for the bonds produces a flow of money into the Federal Reserve System and out of currency in circulation and bank reserves, thus reducing the availability of credit to the public. Throughout the past 10 years, the Treasury and the Federal Reserve between them have been unwilling to let the interest yield on Government bonds rise. They have preferred to hold this one price down even at the cost of facilitating a rise in all other prices. This policy deprives the Federal Reserve of the major weapon just referred to. It commits the Federal Reserve to buying bonds with one hand, for the sake of maintaining the market price, as fast as it sells bonds with the other hand for the purpose of tightening bank reserves. Thus, in the end, bank reserves remain uncontrolled. It is long past time that this shortsighted policy be abandoned.

To revive the effective open market power would doubtless involve some increase in Treasury interest payments. But the resulting increase in the anti-inflationary effectiveness of monetary policy would be an ample return. Even in the narrowest financial calculation, reduction of subsidies and of inflation-caused increases in procurement outlays and pay of Government employees would be likely to outweigh interest costs. Similarly, any reduction in the nominal price of Government securities would be far outweighed (from the standpoint of Government creditors) by strengthening safeguards on the purchasing power of the dollars in which those securities will be repaid.

APPENDIX VII

STATEMENT OF THE RESEARCH AND POLICY COMMITTEE, COMMITTEE FOR ECONOMIC DEVELOPMENT

CONDITIONS NECESSARY FOR EFFECTIVE PRICE-WAGE CONTROLS

For the past 7 months the American economy has been under strong inflationary pressure. The psychological factors have been very powerful; individuals and businesses have stepped up their buying in an effort to protect themselves against expected higher prices and shortages. Advance buying and the growing requirements of the defense program, added to the normal needs of our economy, have increased the demand for goods and services beyond the supply immediately available. Prices have been pulled up by the excess of demand and pushed up by rising costs, including wage costs, and by the anticipation of price and wage controls. The resulting spiral of increasing prices and wage rates seriously threatens the stability of the economy.

In order to check the price-wage spiral, our Government has adopted a set of direct controls designed to stabilize prices and wages. This decision having been taken, it is now imperative that we do everything within our power to make these price and wage controls work as effectively as possible. Price and wage controls will not by themselves stem the tide of inflation. They deal with symptoms rather than with underlying causes. They can be helpful provided other steps are taken to reduce the real causes of inflation. They will be harmful if we are lulled into a false sense of security and fail to take the other steps that are necessary.

So long as the total demand for goods and services is greater than the supply the evil effects of inflation will operate throughout the economy. If not expressed immediately in terms of higher prices and higher wages, they will be expressed in other forms no less damaging. There will be black markets. The quality of goods will deteriorate. The pattern of production and distribution will be distorted; the economy will be less adapted to producing what consumers want. The force of competition for greater efficiency will be weakened; incentives will be reduced.

The point we wish to make is a simple one. The stability and productivity of the economy is dependent on our ability to bring total demand into a reasonable relationship to the total supply.

The problem is twofold. We must increase production in every way possible and we must find ways to restrain demand. There are substantial possibilities for increasing production. We should bring women and older men into the working force. The workweek can be lengthened, productive capacity can be expanded, productive techniques can be improved. We can increase our imports from other countries.

It is obvious that the solution which would be most palatable would be a substantial increase in production, but an increase in production is not enough. Strong measures will be necessary to hold down demand. The program will affect the activities of government, business, and of private individuals.

1. Drastic steps should be taken to reduce all Government expenditures not clearly essential to the defense effort. The Federal budget for 1951–52 contains large sums for which the immediate need has not been demonstrated. We are confident that substantial sums can be eliminated from the proposed budget if every expenditure is required to pass the test of necessity in the present emergency. The defense program, as well as other parts of the budget, should be rigorously screened to hold down the waste of materials, manpower, and money that so often develops in a large rearmament drive.

The expenditures of State and local governments are about as large as the nonmilitary expenditures of the Federal Government. Maximum economy is now a matter of national concern and necessity. Many State and local expenditures can and should be postponed.

2. Taxes should be raised sharply and promptly, to restrain consumers' expenditures as well as to increase revenues. The goal should be a substantial cash surplus in the early part of calendar 1951 and at least a balanced cash budget in the latter part.[1] The inflationary pressure of 1950 arose in spite of a Federal cash budget surplus. If we now move into deficits we shall add a new powerful inflationary force to the forces that have been at work since last summer. With the military programs now in sight there can be no excuse for a deficit in calendar 1951.

Inasmuch as the spending of individuals is one of the powerful elements in the inflationary movement, a tax program designed to combat inflation must have the effect of restraining consumer expenditures by reducing spendable income wherever it is. For this reason the tax on individual incomes must be raised for lower and middle-income groups as well as for the upper level and higher-income groups. In addition, higher and more extensive excise taxes should be imposed.

3. The expansion of bank credit should be checked. The $9,000,000,000 increase in bank credit to private and local government borrowers in the second half of 1950 was certainly a major factor in the inflation of that period. There can be no reasonable basis for confidence in the control of inflationary pressure if the expansion of bank credit and the resulting increase in the amount of money is not brought under control.

The Federal Reserve System, using its powers over the availability and supply of the banking system's reserves, can control the expansion of bank credit. It is of the utmost importance that this power to check credit expansion be used to reduce inflationary pressure. This will require a modification of the present policy of using the Government's monetary powers to maintain a stable market for Federal Government securities at low interest rates. The contribution that an anti-inflationary monetary policy can make to preserving the stability of our whole economy and the holding down of the cost of the defense program is more important than the preservation of an existing pattern of interest rates in the security markets. The costs of an anti-inflationary monetary policy in the form of higher interest burden on the Federal debt are commonly exaggerated and in any case would be small by comparison with the costs of greater inflation.

The management of the Federal debt should be adapted to conditions consistent with an anti-inflationary monetary policy. Federal securities whether issued for refunding or for new money should be offered at rates, maturities, and other terms that will make them attractive as a permanent investment to willing savers.

In view of the present differences of opinion about monetary policy and debt management and the need for greater public un-

[1] Footnote by Fred Lazarus, Jr.: "I disagree with the proposal that a substantial surplus be raised in the early part of 1951 and that the budget be balanced in the later part. The tax program for calendar 1951 should raise an amount sufficient to meet governmental cash expenditures for calendar 1951. The pay-as-you-go principle does not call for achieving a large surplus by dangerously high tax rates."

derstanding of the issues involved, Congress should without delay establish a National Monetary Commission to make recommendations on the policies to be followed in the control of money and credit during the defense emergency.

4. A national program to encourage savings should be inaugurated. Anti-inflationary policy requires an effort to keep the community as a whole from trying to buy more goods and services than are available. In this effort the Government has certain clear responsibilities—to economize in its own expenditures, to raise taxes, to tighten credit. But the action of private individuals can be decisive in the success or failure of this effort. As members of a free society engaged in a struggle for survival each of us has a responsibility to assist—by saving.

A national program of education is needed to bring home to our people their individual responsibility to save. As part of such a program we should enlist the cooperation of the leadership that exists in our communities. The Government should cooperate by instituting an aggressive campaign for the sale of savings bonds. The program should be more than a drive for savings bonds—all forms of savings should be encouraged.

In the final analysis the burden of defense falls upon the great mass of individuals. Some groups may seek to achieve a more favorable position than others, but in the main the burden must fall on all the people. In a country which enjoys the highest standard of living in the world, the burden of the projected defense program can be borne without serious hardship. But by our efforts to escape from the common responsibility we add to the force of inflation and aggravate its burdens.

Our educational, religious, social, and economic institutions can do much to bring to the American people a greater sense of individual responsibility for preventing inflation. From government we need more than price and wage controls. We need a clear and consistent national policy. We need a policy that will convince our people that our Government is facing the realities of the situation—that all of the available means will be used to deal with the basic forces of inflation, so that direct price and wage controls will have a reasonable chance of success. We can then proceed first to live with controls and later, as production rises and demand is stabilized, to live without them.

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APPENDIX VIII

EDITORIAL COMMENT

A. EDITORIAL FROM THE NEW YORK TIMES, FEBRUARY 7, 1951

Reserve versus Treasury

The Federal Reserve System was conceived 37 years ago in the administration of Woodrow Wilson as an American adaptation of the traditional central bank. Above everything else the idea of independence was stressed by the framers of the Federal Reserve Act. The System must be able to act in the interest of economic stability, even though its policies at any given time might run counter to the prevailing interests of the banking community or the stock market, on the one side, or the Treasury, with its natural easy money bias, as the country's No. 1 borrower, on the other.

As time went on, Congress acted to strengthen further the original protections provided against the undue influence on Federal Reserve policy of such vested interests. During the thirties, Congress revised the law in such a way as to shift the balance of power to the Board in Washington. But Congress showed that it was equally conscious of the danger that the Board might fall under the political domination of the administration in power, as represented by the Secretary of the Treasury. With this in mind, it amended the law and eliminated the provision in the original act which had made the Secretary of the Treasury an ex officio member of the Board.

Stripped of technical details, the function of the Federal Reserve is to maintain stability of the money supply, which is the basic force behind inflation and deflation. It seeks to do this by putting a brake on credit when supply is excessive and by releasing the brake (and even using the accelerator) when the problem is one of excessive credit contraction, or deflation. This means that it must be prepared to move freely in the direction of "tightening" money or "easing" money as the situation may demand. Prior to World War II the Reserve had been employing an easy-money policy for several years because of the depressed state of the national economy. When the Treasury found itself faced with the task of financing deficits in amounts of unprecedented magnitude, the Reserve deferred to the latter's convenience and continued its easy-money policy at a cost in terms of price inflation during and after the war which, whether necessary or not, was incalculable.

With the war and demobilization over, the Reserve has maintained that the time had come for the Treasury to stand on its own feet. It should, said the Board, sell securities bearing interest rates that were related to market conditions, rather than be dependent upon the Reserve to step in and take the surplus off the market. There are two reasons behind this position of the Reserve, reasons which are inassailable, in our opinion, if the Reserve is to maintain its usefulness to the economy, a usefulness which was never more obvious. One is that, released from its commitment to support the Government market, regardless of whether interest rates on Government securities are realistic or not, it can resume its original, and much more important, responsibility of combating inflation (or deflation, as the case may be). The other is that to support the Government security market it must buy Government bonds, and for every million dollars it buys it creates a million dollars of commercial bank reserves, and for every million of such reserves the commercial banks can expand their credit by six millions.

This is the central issue between the Reserve and the Treasury—the issue of whether the convenience of the Treasury or the general interest of the Nation is to be paramount in determining money policy. Closely tied to this issue is the question whether policy in this respect is to be determined by Presidential intervention, or whether it is to be determined by Congress, which created the Federal Reserve System and to which the System is alone directly answerable.

B. EDITORIAL FROM THE ST. LOUIS POST-DISPATCH, FEBRUARY 13, 1951

Stabilizing bank credit

While everybody is choosing up sides in the Treasury-Federal Reserve controversy over credit policy, we hope the smoke of battle does not obscure the need for curtailment of bank credit somehow.

Federal Reserve open-market operations in Government bonds are one way of controlling bank credit, but not the only way. The Treasury's policy of cheap money and a pegged market in Government bonds interferes with this method of credit control. Instead of assuming that there will be no control unless Treasury policy is changed, Congress ought to be considering alternative methods.

Prices and wages are being stabilized as of January 25. Why should not the Government undertake to stabilize bank credit in the same way? Why should not banks be required to put up special reserves for all loans granted beyond the level in force on a certain stabilization date?

Bank credit is a major factor in the money supply, and it goes without saying that an inadequately controlled money supply must increase inflationary pressures. Credit might be curtailed by offering banks a higher interest rate on Government securities, thus inducing them to hold more of these instead of commercial loans, but it can also be curtailed by a direct increase in reserve requirements. The objection to this has been that all banks would be hit alike, whether they contributed to credit inflation or not. That objection might be overcome if the new requirements were related to a particular stabilization level and applied only to loans above that level.

C. BUSINESS TIDES, NEWSWEEK MAGAZINE, FEBRUARY 19, 1951

Inflation plus usurpation

(By Henry Hazlitt)

On January 31, at a meeting that should never have been called, President Truman presumed to lecture the Open Market Committee of the Federal Reserve System on what its policies ought to be in the present crisis. The next day the White House press secretary announced: "The Federal Reserve Board has pledged its support to President Truman to maintain the stability of Government securities as long as the emergency lasts." Then Mr. Truman made public a "Dear Tom" letter to Chairman McCabe of the Federal Reserve Board in which he thanked him for "your assurance that the market on Government securities will be stabilized and maintained at present levels."

Governor Eccles, of the Federal Reserve Board, was astonished by the President's version, denied flatly that the agency had given any such pledge, and made public the Board's own memorandum covering what took place. The memorandum failed to support Mr. Truman's version.

We need not be diverted by any attempt to appraise the comparative accuracy of these conflicting versions. If we keep our eye on the legal and economic issues involved, it is clear that Mr. Truman is wrong on both.

The President has no more legal right to tell the Federal Reserve Board what to decide than he has to tell the Supreme Court what to decide. To minimize Presidential influence, Congress deliberately made the board an independent body, with 14-year terms for each of the seven members, overlapping so that no President should have the appointment of more than one member in any 2-year period. The late Senator Glass long ago quoted President Wilson as saying: "The very moment that I should attempt to establish close relations with the [Federal Reserve] Board, that moment I would be accused of trying to bring political pressure to bear." The pressure that Mr. Truman is now bringing to bear on the Board is a clear usurpation of power.

President Truman and Secretary Snyder are patriotic and sincere. They simply do not understand the economic consequences of what they are proposing. They wish to force the Federal Reserve banks to keep buying as many Government bonds as necessary to hold them above par, and so keep down the long-term yield to the arbitrary maximum of 2½ percent. Now when the Reserve banks buy such Government bonds, they pay for them simply by creating deposit credits or printing money in exchange. These in turn become the reserve bases for member banks to create still more money and bank deposits. This creation of more money and bank credit without more goods is not merely the cause of inflation; it is the inflation. Mr. Truman and Secretary Snyder might just as well tell the Federal Reserve Board point blank: "We demand more inflation."

None of the reasons that either Mr. Truman or Mr. Snyder gives for wanting Federal bonds pegged at par or over will stand examination. Mr. Truman recalled before the Open Market Committee "his wartime experience when he bought Liberty bonds out of his soldier's pay. When he returned from France and had to sell his bonds to buy clothes and other civilian things, he got only $80 or a little more for his hundred-dollar bonds. * * * He did not want the people who hold our bonds now to have done to them what was done to him."

Now, none of the Liberty bonds ever fell quite as low as 80. Some issues did fall within a few points of that price, but only for a few months in 1920. And the decline affected only those people who were forced to sell in those months. The maximum loss even of these people was only about 18 percent. Today, on the other hand, mainly as a result of the very bond-pegging and low-interest policies on which Mr. Truman has insisted, a Government bond bought in 1942 has a purchasing power in terms of consumer prices of only 70 percent of what it had then. This is a real depreciation of 30 percent. Which policy—that of the First or the Second World War—was worse for the bondholders?

D. EDITORIAL FROM CHICAGO DAILY SUN-TIMES, FEBRUARY 16, 1951

Hole in the dike

President Truman has been busy plugging up cracks in the Nation's wall against the great tidal wave of inflation that is rolling up. But he has been curiously blind to the greatest hole of all—one that could bring the whole structure tumbling down and wash out great portions of the value of savings, insurance policies, and our paper money.

If this happens, there may be no limit to the price of food and other items in the household budget. The cost of rearming America would boom like an atom bomb mushroom. In short, the Nation could face the disastrous inflation that wrecked other nations after World War I when money was measured by the wheelbarrow load.

Mr. Truman understands that high prices are the result of too much money in circulation as compared with what's available to spend it on.

So he has been busy trying to mop up the extra money—or purchasing power—by higher taxes, stricter controls on housing, installment credit, and wage and price controls.

But through the hole that he is overlooking a torrent of "check-book money" is pouring. It is coming from the Nation's banks, which have more money to lend than they should have. It is coming faster than it is being mopped up.

The Federal Reserve Board can stop the flow or slow it down. It is, in fact, a duty of the Board to do so when prices are rising. But the Board has delayed action because of a stand taken by President Truman's crony, Secretary of the Treasury Snyder.

The Reserve Board can cut down on the amount of money banks have available to loan by abandoning its policy of buying Government securities from banks at par or better. Allowing banks to cash in securities at a pegged price gives the banks more money for loans. In fact, because of the workings of our banking system, a $10,000 Government bond cash cashed by a bank could add $50,000 worth of bank credit, or check-book money, to a community.

By supplying purchasing power not previously existing, banks have contributed to the bidding up of wholesale prices which are quickly reflected in retail prices.

The Reserve Board can cut that artificial purchasing power by changing its policy of buying up Government bonds at par. Lower bond prices would discourage banks from cashing in Government securities. They would hold them to maturity to collect the full price.

If the Federal Reserve removed the guaranteed prematurity price, or pegged it lower, the effect would be to increase interest rates on Government securities. When the Treasury offered a new issue it would have to pay higher interest. The cost of interest on the Nation's debt—now about $6,000,000,000—would be increased. So Snyder is dead set against any change in Reserve Board policy.

Snyder can't see the woods for the trees. Even a billion or so increase in the cost of servicing the Nation's debt would be a drop in the bucket compared to the cost to the Nation as inflation sweeps in. The cost of armaments alone can go up several billion because of the impending inflation that might be prevented by a change in policy, a change now blocked by Truman's Mr. Snyder.

E. ARTICLE IN THE WASHINGTON POST, FEBRUARY 11, 1951

Top agencies split on credit control

(By Alfred Friendly)

Last week's crop of news stories about the White House-Federal Reserve Board misunderstanding reflects only one episode—a current manifestation—of a deep, long-standing conflict.

It is a conflict between the FRB and the Treasury, centering on the ways and means of Federal debt financing. It is important because it concerns a fundamental cause of inflation. It is complicated because the subject matter is among the blackest of the black arts—Government finance, the operation of bank lending and the creation of money.

Would-be explanations in terms of rival groups making a power grab, or [illegible] bankers trying to fill their coffer[illegible] simple—and simply inaccurate.

One approach to an understanding is to pose a question: How, in the present defense program, do you prevent the creation of more money in the economy than there are goods to buy? Or, if you prefer it this way: How do you prevent monetary inflation?

There is a three-fold answer:

First, you increase production as much as possible, so there will be more goods to buy for both military and civilian use.

Second, you balance the budget through pay-as-you-go taxation, so that the Government does not have to create, through borrowing, additional money to pay for the defense program.

Third, you prevent the creation by private hands of additional money in excess of the volume of available goods.

These are arguments on methods even for the first two goals. But those are as nothing compared to the deep cleavage in basic thinking of economists and Government agencies on the third point. It boils down to an argument on how to curtail the private extension of credit.

When a bank makes a loan, its effect is to create new purchasing power. In some periods of history, when the total of loans keeps expanding, and faster than the resultant increase in the supply of goods, the effect can be to create excess money—too much money compared to the supply of things in the market to be bought.

The Federal Reserve Board contends that just exactly that has been happening. It further contends that, because of Treasury policy, the Board is powerless to stop it. In fact, it has been forced to facilitate or encourage the process.

It has become, itself, an "engine of inflation" instead of fulfilling the function Congress assigned it, which is to regulate the supply, availability and cost of credit.

Here is the way the FRB feels that comes about:

When a bank makes a loan, it increases its deposits—or at least total deposits in the whole banking system—usually by the same amount as the loan. The borrower simply gets a credit of the loan amount set up in his drawing account, or he may take a check and deposit it in another bank, or pay off a second person who, in turn, deposits it.

But whenever a bank that is a member of the Federal Reserve System obtains increased deposits, it is required by law to place about one-sixth of the amount of increase into a statutory reserve on deposit with a Federal Reserve bank.

This means, for practical purposes, that whenever a bank wants to extend additional credit—thus creating additional deposits—it must scratch around for about one-sixth the amount of the loan to deposit in its statutory reserve.

It obtains that money these days by selling a security from its holdings. What it sells, it turns out, is a Government obligation

During the war, banks acquired some $60,000,000,000 worth of Treasury issues. This means they have a virtually inexhaustible supply of bonds to turn into the statutory reserves whenever they want to make new loans. Whenever a prospective loan appears more desirable than holding onto a Government bond for its income, the bank can sell a bond to make the loan—six times as large as the bond it sells.

This process has been going on at a frenzied rate. Since the Korean War began, commercial banks have increased their loans outstanding by about $8,000,000,000. They have reduced their holdings of Government securities by about $5,500,000,000. The total money supply increased in 1950 by more than $7,000,000,000.

More money produces higher prices. Or a lower value of the dollar. Or inflation. They all mean the same thing.

This conclusion, which is fundamental to the FRB argument, is disputed fore and aft by the Treasury experts and many other economists. They assert that the inflation since Korea has simply not been caused, in any fundamental way, by monetary factors. They argue that the expansion of the money supply has been less, not more, than the expansion in goods that were produced.

They assert that the skyrocketing prices of imported raw materials, plus intensified buying by individuals and businesses who anticipated shortages and higher prices in a war or semiwar situation, are far more responsible for the inflation.

When banks and other holders of Government bonds sold them, all creating more bank deposits, more reserves and more loans, it was the FRB that bought them, because it had to. Its holdings of Federal securities have increased by more than $3,000,000,000 since Korea.

Why was it so easy for the holders of Government bonds to dump them on the FRB?

At the outset of World War II, when it was obvious that the Government was going to do a huge volume of deficit financing, there was no option for the Board. It had to stand ready to buy Treasury securities at the price they were offered and at a low interest rate. It was necessary publicly to guarantee the market so that private buyers would be assured against a loss and would therefore be willing to absorb the billions of Government securities that were issued.

In this process the FRB was, of course, stopped from controlling or influencing the supply of money and credit by effecting changes in the interest rate.

But after the war, it wanted to get back into the business Congress gave it, of regulating the supply, availability and cost of credit. Its main useful tool for doing this is to sell Government bonds vigorously on the open market when it wants to blot up bank reserves and curtail lending, or to buy bonds when it wants to reverse the process.

Now, however, it has no choice and no initiative. The Treasury wants it to keep on pegging the price of Government obligations at a fixed level, and, so far, the FRB has complied, more or less. This means it buys whenever someone wants to sell and can find no private buyer.

The result, the FRB argues, is that any bank wanting to make a new loan can be sure of obtaining the statutory reserves it will need. It simply sells Federal securities from its portfolio. It knows that the FRB will buy them, if no one else wants them, at a fixed price, so there is no risk of capital loss to the bank when it sells its Federal bonds.

Indeed, its holdings of those securities have become, in effect, interest-bearing cash; they can be converted instantly to cash without any capital loss.

The FRB feels that if it were relieved of the obligation to peg the prices of Government obligations, and if the free market were allowed to find the price at which individuals and institutions would willingly buy and hold Government bonds, then the opportunity and the invitation to banks to create additional reserves would be sharply reduced.

It further believes that this happy state would come to pass, with the market supporting Government issues without an FRB guarantee, if yields were allowed to rise by about one-half of 1 percent. Would-be sellers, the FRB thinks, would then find buyers outside the FRB; the FRB itself would be able to avoid purchasing Government bonds and thereby expanding bank reserves willy-nilly.

Holders of Government bonds would not then have "interest-bearing cash." Banks would have to run the test of the market in selling their Federal holdings. Accordingly, the FRB argues, they would be deterred from extending credit so freely because they would not be able to obtain reserves so easily and without risk of capital loss.

It is probable that a majority of American economists go along with the FRB argument, as did a subcommittee of the Joint Congressional Economic Committee which studied the subject last year.

The Treasury disagrees most vehemently, and has many prominent economists on its side, for example, the President's three-man Council of Economic Advisers.

The classic statement of opposition to the FRB position was expressed by Treasury Secretary Snyder in a speech January 18. He said in part:

"The Treasury is convinced that there is no tangible evidence that a policy of credit rationing by means of small increases in the interest rates on Government-borrowed funds has had a real or genuine effect in cutting down the volume of private borrowing and in retarding inflationary pressures. The delusion that fractional changes in interest rates can be effective in fighting inflation must be dispelled from our minds.

"The 2½ percent rate of interest on long-term Government securities is an integral part of the financial structure of our country. It dominates the bond markets—Government, corporate, and municipal.

"Any increase in the 2½ percent rate would, I am firmly convinced, seriously upset the existing security markets—Government, corporate, and municipal."

Part of the problem that the FRB complains of, according to proponents of the Treasury view, will solve itself as the defense program progresses. They say that the opportunities to make loans will dry up, just as they did during World War II. Even though the banks had enormous Federal security holdings with which they could have obtained reserves, they did not expand loans.

Furthermore, some lending should be stimulated for the time being to increase production facilities, this group argues. Let lending for nonessential purposes, causing inflation, be curbed by selective controls. But don't burn down the house to obtain a few roast pigs.

Here are some expansions of the Treasury arguments, with the FRB counterarguments:

1. Very high interest rates in the past—5 percent on short-term Government issues and 20 percent on call money in 1929, and 6 and 33, respectively, in 1919-20—had no effect in stopping inflation, Snyder has declared.

The idea that banks would be willing to hold onto Government securities at 3 percent, but not at 2½ percent, when a glowing opportunity to make a 4, 5, or 6 percent loan presented itself, is sheer nonsense. Nor would banks hesitate to take a small capital loss (as bond prices dropped when the yield increased) in order to make such an attractive loan.

As one expert put it, the idea that a fractional change in the interest rate is a consequential matter to a would-be borrower or lender is "academic fiction."

To all of which the FRB would reply that anyone who doesn't believe a change in interest rates—even a small one—has the most profound effect on credit extension is flying in the face of economic history, and is an economic idiot to boot.

2. Raising the interest rates on Government obligations by one-half of 1 percent would cost the Treasury an additional $1,500,000,000 a year in carrying charges on the public debt, Snyder declared in a recent interview. This would be about the most inflationary measure one could conceive of.

The FRB experts challenge the calculation. In the first place, the proposed increase would not apply to savings bonds. Second, it would make no difference with respect to those Federal bonds already held by Government trust funds—just paying out of one Federal pocket into another.

This leaves about $145,000,000,000 of marketable securities to be considered. If all of them were refunded at an interest rate one-half percent higher, the added cost would be between seven hundred and eight hundred million dollars a year. But of this one-third to two-fifths would return to the Treasury through higher income-tax receipts.

The last word, for the present, on this argument was said in a recent staff study of the Joint Congressional Economic Committee: "If you could only be sure that this mild increase of Federal security interest rates would actually curb credit and combat inflation, the resulting increased cost of carrying the Federal debt would be a small price to pay."

3. Unpegging the rates and prices on Federal securities might cause a real panic, the Treasury group has argued. That might be just the way to destroy all public confidence in Federal obligations.

On the contrary, says the FRB, the real danger to the future acceptance of Treasury issues is that the public will not buy them because it fears what inflation will do to their value.

Furthermore, says the Board, it has no intention of moving out of the open market entirely; it will and must continue to participate in the buying and selling of the issues to maintain an orderly market and prevent any panic. Its point is, however, that it does not want to participate at pegged rates; nor always maintain its position on one side of the market—the buying side.

4. The Federal debt has assumed overwhelming importance in the last 10 years in its effect on all financial developments. Previous theory on the effect of changes in the cost of credit no longer are valid.

The Government debt is now half of the whole debt of the Nation. As a result, interest rates on private transactions are closely tied in with those on Government issues. An increase of one-half of 1 percent on Government issues would be quickly reflected by an equivalent rise elsewhere.

If banks received another one-half of 1 percent interest on the Government holdings, they would have the prospect of at least that much of an increase on future commercial loans, so there would be no more incentive than before to hold on to the Federal securities—in fact, probably less.

You are likely to hear a great deal more about the issue in the months to come. The fight will probably get worse before it gets better.

F. EDITORIAL FROM THE WALL STREET JOURNAL, FEBRUARY 2, 1951

A dangerous maneuver

There took place in Washington Wednesday afternoon a meeting which should never have happened. That was the meeting between Federal Reserve officials and President Truman, which the latter called at the White House.

The President was taking sides with the Treasury in its firm stand to maintain low interest rates, and he wanted to impress the Reserve people with the importance of this. In other words, they ought to conduct themselves and their operations in a manner to support a low-rate policy.

Now, the reason that this meeting should not have happened is that the President has no authority to dictate to the Federal Reserve. He appoints the members of the Reserve Board, as vacancies occur, and he names the Chairman. But the Federal Reserve Act which gave birth to this central banking system specifically says that the Board shall report annually "to the Speaker of the House of Representatives, who shall cause the same to be printed for the information of Congress."

So the Reserve Board is responsible to Congress, not to the President. And when the President steps in to tell Reserve officials what they ought to do, or ought not do, he is assuming power which he does not have.

The Federal Reserve System was founded 37 years ago with a specific aim in mind. That aim was to provide flexibility for the banking and credit operations of the country. The aim was to set up an independent body which could regulate credit and money—in a way to combat excesses either of inflation or deflation.

If the supply of credit becomes too tight and interest rates are too high, the Reserve System, under the theory of its founding, can take steps to make more credit available. Resultant borrowing can expand business activity. If, on the other hand, too much credit is available and borrowing leads to inflationary excesses, then the Reserve System can take actions designed to curb credit.

That is the theory of Reserve operations, but in recent years its practice has been curbed—to put it mildly—by political considerations. The Federal Government has become by far the biggest borrower. Not unnaturally, Treasury Secretary Synder is concerned at the interest cost of the Government's huge debt, which may become even larger. So he is putting all the power of his office behind maintenance of low interest rates. And the Federal Reserve has reluctantly cooperated by supporting the prices at which Government securities sell.

The danger of that supporting practice is that it all but eliminates the Reserve's power to control credit. Just why that is so is discussed elsewhere on this page by Dr. E. A. Goldenweiser, for many years economist of the Reserve Board. In recent months the Reserve officials have become more than reluctant to continue their practice. They see the further inflation threatening; they believe they should be free to do their part in combating it. Otherwise the aim originally given this central banking system is gone.

But there is a much greater danger in this than appears on the surface. The power to inflate currency and credit is the power to destroy an economy. This can be done by printing currency or it can be done by limitless expansion of credit.

The Federal Reserve System was set up as a check on this power. But if its banks are to become ever-expansible stuffing boxes for Government securities, then the check on inflation of Government and private credit is gone.

The Congress in 1913 had this in mind when it passed the Federal Reserve Act. It saw the dangers, we're sure, of administrators who might lose all fiscal conscience.

We believe the Reserve officials, despite White House pressure, should stick by their view—to be free to fight inflation. We hope, too, that Congress will recognize the dangerous maneuver which the President has made.

PROPOSED TAXATION OF INCOME FROM MUNICIPAL BONDS

Mr. HENDRICKSON. Mr. President, there is pending before the Ways and Means Committee of the House of Representatives an extremely controversial measure which is designed to tax the income from municipal bonds. I now hold in my hand a number of telegrams, resolutions, and other forms of communication which indicate that this proposal should be studied with great care by both Houses of Congress before it is enacted into law.

To the end that the Senate may have before it the expressions of many New Jersey municipalities, I ask unanimous consent that these telegrams, resolutions, and other communications may be printed at this point in the RECORD, as a part of my remarks, and may be appropriately referred.

There being no objection, the telegrams, letters, and resolutions were referred to the Committee on Finance, and ordered to be printed in the RECORD, as follows:

CAPE MAY, N. J., *February 21, 1951.*
Senator ROBERT C. HENDRICKSON,
Senate Office Building,
Washington, D. C.:

Commissioners City of Cape May strongly opposed to taxation of income from municipal bonds greatly increased interest on future issue of local bonds will cause further real estate tax increase.

SAMUEL ELDREDGE.
SOL NEEDLES, Jr.
CARL YOUNGBERG.

SAYREVILLE, N. J., *February 21, 1951.*
Hon. ROBERT C. HENDRICKSON:

Respectfully urge your strong opposition to taxing income from municipal bonds since it will add greatly to already heavy burden of municipal financing.

BOROUGH OF SAYERVILLE,
By FRANK P. KOLB,
Borough Clerk.

NEPTUNE CITY, N. J., *February 21, 1951.*
Hon. ROBERT C. HENDRICKSON,
Senate Office Building,
Washington, D. C.:

Unalterably opposed to taxation of income from municipal bonds. Urge best efforts to block passage of pending bill before House Ways and Means Committee.

BOROUGH OF NEPTUNE CITY,
GEORGE E. AMBROSE, *Mayor.*

DUMONT, N. J., *February 21, 1951.*
Senator ROBERT C. HENDRICKSON,
Washington, D. C.:

Mayor and Council of Dumont, Bergen County, N. J., oppose proposal now before House Ways and Means Committee to tax income from municipal bonds. Such action would result in increasing interest paid by our tax income from municipal bonds; such action would result in increasing interest paid by our taxpayers on bonds sold for municipal improvements. We ask you to exert all efforts to defeat proposal.

JOHN R. ZELLWEGER,
Borough Clerk.

THE CITY OF EAST ORANGE, N. J.,
February 20, 1951.
Hon. ROBERT C. HENDRICKSON,
Senate Office Building,
Washington, D. C.

MY DEAR SENATOR HENDRICKSON: The following resolution was adopted by the City Council of the City of East Orange on February 19, 1951, and approved by the mayor on February 20, 1951:

"Whereas it appears from the public press that the Congress of the United States has under consideration the Federal taxation of State and municipal securities; and

"Whereas it is self-evident that the removal of the present tax exemption from future issues of municipal securities would greatly increase the interest rates municipalities would have to pay on future borrowing: Be it

"*Resolved,* That the mayor and members of the City Council of the City of East Orange do hereby record their opposition to any amendment to the law exempting the taxation of municipal securities, and do respectfully urge that the Members of Congress from New Jersey oppose any legislation tending to remove such tax exemption or to otherwise exercise Federal control over municipal finances; and be it further

"*Resolved,* That a copy of this resolution be forwarded to Senators H. ALEXANDER SMITH and ROBERT C. HENDRICKSON, to Congressmen ROBERT W. KEAN and HUGH J. ADDONIZIO, and to the executive director of the United States Conference of Mayors."

Very truly yours,

ALICE I. WEBSTER,
City Clerk.

RIVERSIDE, N. J., *February 21, 1951.*
Hon. ROBERT C. HENDRICKSON,
Senate Office Building,
Washington, D. C.

DEAR SIR: The members of the Township Committee of the Township of Riverside wish to register protest against the proposed legislature which would tax municipal bonds, and have asked that I urge you to oppose this measure. If enacted it would add at least 1 percent to the interest rates of any future municipal issues and add directly to the cost of government at the local level, which is at the present time a very expensive proposition.

Thanking you for your interest in this matter, we remain,

Very truly yours,

TOWNSHIP COMMITTEE OF THE
TOWNSHIP OF RIVERSIDE,
ELMER T. DECHANT,
Township Clerk.

CITY OF CAMDEN,
February 21, 1951.
Hon. ROBERT C. HENDRICKSON,
Senate Office Building,
Washington, D. C.

DEAR SENATOR HENDRICKSON: Enclosed find certified copy of resolution adopted by the Board of Commissioners of the City of Camden regarding its disapproval of the proposition of the Secretary of the Treasury to subject future issues of State and municipal bonds and securities to Federal taxation.

We strongly urge you to vote against such proposition if the same ever comes before the Congress.

Very truly yours,

GEORGE E. BRUNNER, *Mayor.*

Whereas the Secretary of the Treasury has proposed to the Ways and Means Committee of the House of Representatives that future issues of State and municipal bonds and securities be subject to Federal taxation; and

Whereas such proposition would materially affect the borrowing ability of municipalities and would result in a substantial increase in the interest rates which municipalities would have to pay on their future borrowings, which in many instances would be double the rate they are paying at the present time; and

Whereas we believe such proposition would result in increasing the cost of local government and that such increased cost would necessarily be transmitted directly to the local taxpayers; and

Whereas such proposition strikes at the very foundations of our system of government which has preserved the immunities from taxation between Federal and State Governments, which immunities have been defended repeatedly by the courts and Congress heretofore: Now, therefore, be it

Resolved by the Board of Commissioners of the City of Camden, N. J., That it hereby records its disapproval of such proposition and strongly urges Congress to reject said proposal; and be it further

Resolved, That certified copies of this resolution be forwarded to the Members of Congress from this State.

Dated February 21, 1951.

Mr. TOBEY. Mr. President, will the Senator yield?

Mr. HENDRICKSON. I am very glad to yield to the distinguished Senator from New Hampshire.

Mr. TOBEY. I think the Senator from New Jersey will find that he has a great many powerful allies throughout the country on the thesis to which he is now addressing himself. I speak for the New England cities. I know that all over the country there will be a feeling of very righteous indignation in regard to any proposal to tax the income from municipal securities. As the Senator knows, the burden already is becoming very heavy. The States certainly still have some rights as to their taxing powers, rather than to have them taken over entirely by the Federal Government.

Mr. HENDRICKSON. I thank the Senator. I know the Congress will zealously guard the principle of States' rights as it involves itself in this issue.

LEGISLATIVE PROGRAM

Mr. McFARLAND. Mr. President, if there is no further business to be transacted at the session today——

Mr. CASE. Mr. President, will the majority leader yield for a question?

Mr. McFARLAND. I yield.

Mr. CASE. Will the Senator from Arizona tell us about the program for Monday? I understand that the first order of business for Monday will be the consideration of House bill 1 or the substitute therefor.

Mr. McFARLAND. Yes; that will come first.

Mr. CASE. Following that, will we consider certain proposed legislation coming from the Committee on Armed Services?

Mr. McFARLAND. Yes; first we shall dispose of House bill 1, the so-called Servicemen's Indemnity Act of 1951; and there is a possibility that following that we shall take up Senate bill 1, the so-called universal military-training bill.

Mr. CASE. I thank the Senator.

RECESS TO MONDAY

Mr. McFARLAND. Mr. President, I now move that the Senate stand in recess until Monday next at 12 o'clock noon.

The motion was agreed to; and (at 3 o'clock and 35 minutes p. m.) the Senate took a recess until Monday, February 26, 1951, at 12 o'clock meridian.