

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date July 16, 1938.To Chairman EcclesSubject: Notes on Industrial PolicyCc Lauchlin Currie
LBC

Mr. Sweezy and I met with some of the people, who
are on the Monopoly Investigation, the other evening,
and the attached notes by Mr. Sweezy were inspired
by the discussion.

*Voted with
interest* *LLC*

July 15, 1938

NOTES ON INDUSTRIAL POLICY

I. Objectives:

- (a) Reasonably full employment for the economy as a whole.
- (b) Decent wages and working conditions in each individual industry.
- (c) Scope for technical and operating improvements.
- (d) An adequate flow of new capital.
- (e) The lowest prices to consumers consistent with the above objectives.

To the extent that conflicts are involved in the pursuit of all these objectives at once, compromises must be worked out. This appears, in fact, to be the real core of the problem of formulating a satisfactory industrial policy.

II. Complexity of industrial structure:

The simple antithesis between competition and monopoly is of little use in analyzing most industries. They present instead a diversity of mixed forms. For this reason each industry must be studied as a special problem and measures suited to its peculiar circumstances worked out. (Of course, in some cases broad groupings may appear as the studies are carried out.)

The organization and functioning of each industry should be studied with specific reference to each of the objectives listed above. To what extent is the industry an unstabilizing factor? This would involve consideration of behavior with respect to sales, inventory and plant expansion, as well as price. (Particular attention should be given to periods of expansion since sustained expansion must be the primary aim of all national policy.) On this point no *a priori* conclusions can be drawn simply from an examination of the competitive or monopolistic character of the industry. Competition in sales pressure in automobiles last year, for instance, was as unstabilizing a factor as the monopolistic price policy of the steel industry. Inventories were increased excessively in industries conforming to a wide variety

of competitive and monopolistic patterns. In some cases, as, for instance, in a comparison of cement with lumber, the less organized industry, i.e., lumber, was much more of an unstabilizing factor in the rise of 1936-37 than the better organized industry, cement.

for what!

Likewise of great importance in judging the merits of a particular type of organization is the effect it has on the lives of the workers and the communities dependent upon it. Marked instability as to location is, for instance, generally recognized to be an evil. Types of organization which accentuate such instability must be judged inferior to those which moderate it. Certain forms of organization under certain circumstances likewise put a premium on the lowering of wages and working conditions on those employed in an industry. The garment and textile industries are familiar examples.

Another consideration is the adequacy of the long-run supply of capital which an industry will be able to command. Had the railroad rate wars of the '70s continued indefinitely, it is highly probable that, although shippers and travelers would have enjoyed very cheap transportation for a few years, eventually the railroad system of the country would have fallen into a dangerously bad technical condition. The railroad case is by no means an isolated example, moreover: The same type of destructive competition has broken out in other industries with large fixed plant and might easily break out again. In these industries some type of restrained competition or, putting it differently, some definitions of the limits within which competition can operate is essential to the long-run health of the industries. As long as private sources of capital are to be relied on, this consideration cannot possibly be neglected.

The above considerations frequently point to the necessity or desirability of various types of restraint on competition. They do not at all imply, however, that competition should be abandoned entirely. Competitive efforts to improve techniques and to secure customers by passing on the benefit of these improvements in the form of lower prices and better services are of the greatest importance. The problem, as already noted, is to define the limits within which competition should operate and to give it within those limits the greatest possible scope and freedom.

III. Instruments of policy:

- (a) Prosecution of unfair methods of competition of the type specified in the Federal Trade Commission and Clayton Acts.
- (b) Use of the anti-trust laws to inhibit combinations and agreements which tend unreasonably to limit output and raise prices. This does not mean that an attempt should be made

to break up all combinations and all agreements as was intended by some of the original sponsors of anti-trust legislation. Such a construction of the anti-trust laws has necessarily broken down in practice. As was pointed out above, competition where there is much fixed equipment can easily become ruinous in a very real sense.

Understandings, either explicit or implicit, on the part of producers to keep competition within the bounds of moderation are consequently inherent in the structure of modern industry if it is to function successfully. The railroad rate wars, it should be repeated, are merely the most striking illustration. The same thing can be seen in the steel industry where the U. S. Steel Corporation itself was the result of the threatened outbreak of a competitive war which would have been fully as disastrous as any of the earlier railroad conflicts.

- (c) In many cases Government competition, actual or potential, or the use of the Government's bargaining power derived from its large purchases of goods, would be better instruments for securing reasonable prices than the vigorous enforcement of the anti-trust laws. This applies particularly where there are marked advantages of large-scale organization or where the competition resulting from the breakup of existing organizations would be of a wasteful or sporadic type. In cigarettes, for instance, the advertising competition of the four big companies is a very doubtful advantage. In other industries the breakup of existing concerns might lead chiefly to an increase in excess capacity, combined with a policy of mutual tolerance in order to escape the dangers of price cutting.
- (d) Government regulation and Government ownership. Public utilities, railroads, shipping, and to some extent natural resources are already under Government regulation. The railroads have now reached a state where regulation itself can no longer be effective and Government ownership is the only possible way of overcoming existing difficulties. This may also be true of shipping. Natural resources, like coal, petroleum and perhaps copper (not now subject to regulation), cannot be left to the haphazard workings of competition. Regulation is here to stay and it is a question of how regulation can be made most effective. Where, as in the case of the railroads, it proves no longer feasible, Government ownership must be introduced.

(e) Cooperation under Government supervision. In an industry like textiles, more competition clearly is no remedy for obvious shortcomings. It appears that efforts to remove these defects will result rather in a trend toward increased cooperation on the part of those engaged in the industry. This cooperation should, of course, be under public supervision and subject to public approval.

A wide field in which cooperative action might be extremely useful from a broad point of view is as yet practically unexplored.

This comprises the whole range of problems in connection with the destabilizing effect of present competitive practices in a variety of industries. It is particularly serious at the present time with the economy suffering from a long period of depression, which has resulted in its weakening at many vital points. Building furnishes some of the most striking examples. It is very doubtful at the present time if the building industry could handle anything like a prosperity volume of activity even if such a volume were forthcoming. There seems to have been a permanent shrinkage in the regular supply and perhaps also in the capacity of the industry itself, which is going to be difficult to repair. An attempt to enforce stricter rules of competition will do little to remedy this situation. As the volume of building increases it would seem that a considerable measure of conscious planning with Government aid and supervision will be necessary.