

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date June 25, 1940

To Chairman Eccles

Subject: _____

From Mr. Goldenweiser

I transmit herewith a proposed draft of a memorandum to the President which might be considered a report of progress.



June 25, 1940

Memorandum to the President

From Chairman Eccles

Referring to the assignment which you gave me the other day, namely, to find answers to the three questions: What to do about gold? About idle money? About price stability? I beg to submit the following observations which are in the nature of a report of progress.

I may say, at the outset, that answers to these three questions involve all important phases of our economy and that, in planning the answers, we propose to approach the problems in their bearing on the real objective of our Governmental policy, namely, the formulation of a long-time permanent program for the full utilization of our human and material resources with a view to assuring to our people secure employment and an income adequate to maintain an American standard of living. Ways of handling gold, of utilizing idle money, and of establishing a dollar of constant purchasing power are important only as pieces of machinery to facilitate the achievement of this objective.

The problem

The crisis in which American democracy has been for the past ten years has assumed a different aspect as the result of Hitler's successes in Europe. Until recently our real enemy -

unemployment - was viewed as a domestic problem and we as a people were content to fight this enemy in a half-hearted and tradition-bound manner. Now our potential enemy is a totalitarian world - and we as a people are prepared to fight this enemy in a wholehearted way with every means at our command.

For the moment - this simplifies our problem. We have popular support for a vigorous program of defense and armament which as an immediate consequence is certain to help alleviate, even though it may not cure, the disease of unemployment.

In going full steam ahead on this program, however, we must so plan our efforts as not only to achieve the maximum results in a minimum of time, but also to make the best use of the fact that traditional economic bogeys, such as an unbalanced budget and Government controls and participation in economic activity, have for the time being lost their terror to the people. We must so plan our efforts as to achieve adequate national defense without unduly distorting our economy and to be prepared, when the time comes to relax our efforts for defense, to do so without relapsing into a state of underactivity and large-scale unemployment.

Germany has demonstrated to the world that astounding results can be produced without money and with limited resources - provided these resources are effectively directed to the sole purpose of serving the desired end. In Germany these results were achieved by complete subordination of the individual to the state and by complete control of prices, wages, profits, enterprise, and materials, accompanied by the sacrifice of spiritual values. Notwithstanding Germany's success to date in reaching its goal, it remains to be seen how long the complex system of a totalitarian economy can withstand the strains to which it is bound to be subjected. Our problem is to achieve the results that we desire within the framework of our institutions. We must devise means for directing voluntary efforts into the necessary channels and limiting the intrusion of the state, through controls and participation in activity, to the minimum necessary for successfully carrying out our program. Less than that would sacrifice the success of the undertaking; more than that, would involve unnecessary loss of freedom.

Economically, our situation differs from that of Germany in that we start with an abundance, not a scarcity, of necessary raw materials. To be sure, we both start with a large volume of unemployment. Our immediate purpose is not, however, as in

Germany, to devote to armament all the national resources that can be spared from civilian consumption reduced to a minimum consistent with efficiency, but to increase both production and consumption until our material and human resources are fully utilized. Our defense program need not for some time to come impinge on civilian consumption; it can be carried forward out of resources now unutilized, and should be accompanied by an enlarged output not of defense material alone, but of consumption goods as well.

The plan

What we propose to do in carrying out your assignment is to survey the fields in which expansion must be made; to review the available labor force for this expansion; to analyze the actual and potential supplies of materials, and to attempt to formulate the policies that will be necessary to produce the results immediately desired and at the same time to lay the foundation for achieving longer-time objectives.

This will involve a review of public projects of all kinds, labor policies, and tax and fiscal policies. Finance by itself cannot produce a sound economy, but antiquated financial standards, so-called sound finance, can obstruct efforts to achieve and maintain a sound economy. Study of financial techniques that will serve rather than thwart the purpose will be part of our undertaking. Idle money is merely a symbol of the stalled economic machine which we must plan to set and keep in motion. This involves both a stimulus to lagging enterprise and adequate controls of speculative expansion.

We propose also to study the dangers of price maladjustments which may frustrate the efforts to achieve defense and fuller employment and to maintain employment at a high level. Situations in individual commodities and industries will be studied in cooperation with the Defense Committee and other agencies. We on our part will endeavor to study particularly the forces which might cause prices to rise on a wide front and to suggest policies to avoid such a rise. With heavy demand concentrated on certain basic commodities, like metals, prices of these commodities might advance sharply, bringing about higher prices for many finished goods and probably leading, indirectly, to a general cumulative advance. Action now to assure adequate supplies of materials and thereby to keep prices within bounds would help to avoid the necessity later for direct price fixing and restrictive credit policies. As a part of the whole program for maintaining stable economic conditions, improvements in our banking machinery will be proposed. The question of how to control the reserves created by the gold inflow is an essential part of this problem.

A third broad subdivision of our study will deal with our international trade position in a world where we shall have to compete with totalitarian states. Questions of trade policy on this hemisphere and in dealing with Europe and Asia have to be reviewed in the light of changed conditions. Individual Americans, who could

hold their own in competition with individual foreigners, cannot successfully compete with state-controlled foreign monopolies. Broad-gauge policies in the field of foreign trade must be worked out. Gold and silver policies, as well as problems of foreign exchange, must be determined in the light of the new situation. Even the most effective policies, however, may fail to prevent great shifts in the course of our foreign trade - shifts that may force adjustments in some domestic industries more sweeping than those brought about by the armament program. These must be taken into account in formulating domestic policy.

In preparation for doing our share of the work we are making full use of our staff and expanding and strengthening it where necessary. We expect, in cooperation with others in the Government, to develop the factual basis for recommending economic policies that will further the defense program and at the same time will help to promote a stable national wellbeing. I should like to have the privilege of submitting to you, in the course of a few weeks, a further report of progress, and such practical recommendations of immediate importance as we may be able to develop.

We realize that other Governmental agencies are working on many of the problems here outlined. We suggest that close cooperation between them and mutual assistance to avoid unnecessary duplication is essential. Machinery for assuring cooperation and coordination of effort should be adopted.