

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date April 5, 1938.To Chairman EcclesSubject: Comments on a MandateFrom Lauchlin Currie

Attached are some comments on a mandate prepared at the request of Governor Szymczak. I hope you will find time to glance over them, particularly the latter part.

COMMENTS ON MANDATE. DRAFT OF APRIL 4, 1938

1. I have already stated my objections on the grounds of advisability and propriety to the general idea of the first paragraph.
2. I should prefer to have Congress lay the mandate on the Board, rather than the System.
3. The actual mandate in the second paragraph makes no mention of "money" or "monetary" nor of "prices", both of which concepts the House group is keen on. I think it possible to work these ideas in without departing from our present implicit objective or "tieing" our hands.
4. Any justification we would have for ever adopting a restrictive policy rests solely on the word "sustainable". This is quite a load for this word to carry. I think the word "unstabilizing" in the 1936 draft is a valuable and perhaps indispensable means of strengthening our bonds in this respect.
5. Before the word "productive" should be inserted "other".
6. The last sentence raises the delicate question as to whether the recommendations for new banking legislation shall be made to the President or to Congress. I should let this sleeping dog lie.

COMMENTS ON A MANDATE

1. The Board is in a vulnerable position in exercising very important powers under the most vague terms of reference. As long as this condition persists the Board will be subject to attack and criticism. The vagueness of the present mandate lends a certain degree of plausibility to the "unconstitutional delegation of powers" argument. The attack has been beaten off a number of times, only to be continually renewed. I see no reason to believe that the attack will not gather momentum. If we should be purely obstructionist, there is danger not only of loss of goodwill but of having an objectionable mandate imposed on us. It would be a tactical blunder for the Board to let itself be maneuvered into a position wherein it appeared that it wasn't vitally interested in promoting conditions conducive to as full employment as can be sustained under generally stable conditions. It is on this ground that the strongest objection can be made to a stable price mandate.

2. The people who seek to impose a price mandate look upon the Board, and quite properly I think, as a monetary authority exercising monetary controls. Their arguments must, therefore, be met on monetary grounds, rather than on grounds of "sound banking and credit conditions", if they are to be opposed effectively.

3. The Board is in a weak tactical position in stressing its role as a bank supervisory agency rather than as a monetary authority. In the former role it has to compete with the political strength of the F. D. I. C. and the Comptroller's Office. In the latter role it could

acquire a great deal of support from the large number of Congressmen who are keenly interested in monetary control, in strengthening its position vis-a-vis other Government departments and agencies. Other bank supervisory authorities lack this element of strength.

4. I think that there is danger in being too fearful of the added degree of responsibility a carefully worded objective, containing the appropriate "escape clauses", would impose on the Board. The Board now feels that its objective is far wider than "accommodating" business in the narrow sense of the word, and has been concerned to promote as far as it can an orderly and sustainable recovery. When financial writers and others criticize our policy it is on the basis of such an implicit understanding. Hence we do not escape any criticism by not having an explicit statement of the objective we pursue, and expose ourselves to the unjust and unfair criticism that we do the wrong things because we haven't the proper objective. If we had an explicit mandate to which our political critics could not object, their criticisms would have to be based on specific actions, rather than on specific actions plus lack of a proper objective.

To take a somewhat analogous case. If the I. C. C. were given power to approve rate changes with only the vaguest and most ambiguous of terms of reference, it would be exposed to criticisms similar to those we are subjected to from Father Coughlin et al. Actually, the present mandate to the I. C. C. is fairly specific. It reads as follows:

"In the exercise of its power to prescribe just and reasonable rates the Commission shall give due consideration, among other factors, to the effect of rates on the movement of traffic; to the need, in the public interest, of adequate and efficient railway transportation service at the lowest cost consistent with the furnishing of such service; and to the need of revenues sufficient to enable the carriers, under honest, economical, and efficient management, to provide such service."

So far as I know, nobody has held the I. C. C. responsible for the present state of the roads. Actually, as recent events have demonstrated, rates cannot be set to serve adequately either of these objectives. However, nobody holds the I. C. C. responsible for this. It is generally held that it did give consideration to the various factors mentioned and that its recent decision was about the best possible compromise.

The mandate of the Bank of Canada is as follows:

"Whereas it is desirable to establish a central bank in Canada to regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit and to mitigate by its influence fluctuations in the general level of production, trade, prices and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of the Dominion: Therefore, His Majesty, by and with the advice and consent of the Senate and House of

Commons of Canada, enacts as follows: "

5. Many agencies of Government could with justice assert that in order fully to achieve their objectives they need the cooperation of other agencies. Thus the I. C. C. could say that in order to secure good and economical service and an adequate return to the roads, the volume of traffic should be stabilized at a high level and in this the cooperation of the Government is necessary. This, however, has never been proposed. It is recognized that its mandate merely says that it shall give "consideration" to various needs in determining rates, and that it is not responsible for developments beyond its control. The mandate we offered in 1935 was similar to the I. C. C.'s mandate and dissimilar to Representative Patman's proposed mandate, in that it did not say we must do so and so until such and such was accomplished but rather that we should use our powers to promote conditions conducive to business stability, and to mitigate by our influence unstabilizing fluctuations in the general level of production, trade, prices and employment, so far as may be possible within the scope of monetary action and credit administration. We could always defend our actions on these grounds, since they are the grounds on which we actually base our policy.

If the mandate is couched in such terms, I think it unnecessary to invoke the aid of all the government, since the mandate applies specifically to the use of our powers.

6. If we propose a mandate I think it would be a mistake to lay too much stress on the limitations of monetary control and the necessity of invoking the aid of all the Government. The mandate should be constructive sounding, appear to mean something, and not give the appearance of being offered grudgingly as a sop. There would be far less objection to an "escape clause" than to explicit belittling of the effectiveness of monetary control, and an "escape clause" would serve our purpose just as well. The important thing, it seems to me, is that the mandate should state an objective in general terms, and should direct us to use our powers towards contributing, promoting or furthering this objective, so far as possible within the scope of monetary action and credit administration.

7. Extracts from the President's Statement on the Administration's Price Policy

"This Administration has from the beginning pursued a policy designed to promote full employment of our human and material resources. That continues to be our policy. The productive power of our workers and our resources, if fully utilized, can provide and maintain a national income far above any levels we have yet reached."

"Our program seeks a balanced system of prices such as will promote a balanced expansion in production. Our goal is a constantly increasing national income through increasing production and employment. This is the way to increase the real income of consumers."

"This is not a policy of restriction; it is a policy of abundance."

"Our agricultural, industrial, housing and monetary programs have been and will be directed toward this end."

8. I do not think it advisable nor appropriate for the Board to suggest that "all agencies of the Executive branch of the Government shall use the powers entrusted to them with a view to economic stability and the greatest sustainable employment of labor and of the productive resources of the nation." Various agencies operate under specific mandates and if the general mandate were taken seriously possible conflicts might arise. For instance, a proposal to consolidate various railroads might involve economy in the use of railroad labor and hence less full employment.

By applying to all of government it states, in effect, the purpose of government, which is surely much broader than this particular mandate. In any case it is hardly appropriate for the Federal Reserve Board to appear to state the purpose of government."

9. I think it important to avoid the unqualified phases "full employment". "Full"employment is never attained except in boom times when it is accompanied by night work, rising prices and inefficiency -- highly unstable conditions. Enduring stability requires some slack in the labor as well as the physical resources of the nation. Even in

1929 it is estimated that there was 4 or 5 per cent unemployment. It would be a mistake to suggest something as an objective which is both undesirable and which would never give us any justification for a restrictive policy.

10. In the light of the above considerations I suggest something along the following lines:

"In the exercise of its powers the Board shall seek to promote conditions conducive to as full employment of the labor and other productive resources of the nation as can be continuously sustained, and shall seek, by its influence, to mitigate destabilizing fluctuations in the general level of trade, prices, production and employment, so far as may be possible within the scope of monetary action and credit administration. To further the coordination of monetary policy with other policies of the Government affecting business activity, the Board of Governors shall, whenever it deems the occasion warrants, convey to the President, through its Chairman, its views and recommendations on policies and developments relating to the attainment of the objective stated in the preceding sentence which lie outside the Board's authority."

In support of this proposed mandate I would urge the following considerations:

(a) We are perfectly prepared to seek to promote conditions conducive to as full employment of the labor and other productive resources of the nation as can be continuously sustained, so far as lies within our power.

(b) As full employment of the labor and other productive resources of the nation as can be continuously sustained, is a desirable objective and one which has been approximated in the past.

(c) The mandate that the Board "shall seek, by its influence, to mitigate unstabilizing fluctuations in the general level of trade, prices, production and employment, " is likewise one that the Board can accept. We only seek to "mitigate", which is a milder word than "prevent". The word "unstabilizing" is important as it permits of wide discretion and judgment on our part. The word "prices", which so many people are intent upon incorporating in the mandate, is introduced, but in such a way as not to tie our hands. Instead of seeking to secure "stable prices" we shall seek to mitigate "unstabilizing fluctuations in prices". This permits us to disregard fluctuations which we do not feel to be unstabilizing and so removes the theoretical objections to stable prices as a desirable objective. At the same time it is difficult for Congressmen to object to the desirability of attempting to mitigate unstabilizing fluctuations. Finally, the word "unstabilizing" introduces by implication the concept of stability which gives further content to the earlier words "as can be continuously sustained". It constitutes an additional justification for the adoption of a restrictive policy when and if we feel the occasion warrants it.

(d) The second sentence on coordination of monetary with other policies and the granting of the right to the Board to state such views and make such recommendations as it wishes to the President, is designed to accomplish the following ends:

1. It constitutes a recognition of the limitations of monetary control and the importance of other policies of the Government affecting business activity.

2. It emphasizes the fact that the Board is the main agency devoting its time, study and attention to the problem of business stability. In this way it enhances the importance and prestige of the Board and hence of the System and to this extent is an additional safeguard of the independence of the system. If we assume no responsibility for general planning we shall find ourselves one day "coordinated" with some agency that does. The Treasury has just created a Division of Monetary Research.

3. By providing an official avenue of approach directly to the President much of the force will be taken out of the contention that we occupy an anomalous position of determining policy which can be quite at variance with the aims and policies of the Government. It lessens the need for further "coordination" or "centralization" without in any way sacrificing the Board's independence.

4. It acknowledges our status as an independent agency. Such instructions would never be suggested for a Department.

5. Whereas, now, the Board might hesitate to make some recommendation with reference, say, to fiscal policy, on which it has strong convictions, on the ground that since it lies outside its authority it would appear presumptuous and "meddling" to make such a recommendation direct to the President, under the proposed mandate it would be its legal duty and would be recognized as such by other agencies.