

October 1, 1934

Secretary Morgenthau

Mr. Eccles

Re: Comments on unemployment insurance.

At a time like the present when there is a large volume of unemployment it is to be expected that various schemes involving some form of so-called unemployment insurance should be urged for enactment by the Government and should gain considerable support in some quarters.

It is true that unemployment insurance has some merit, and an inauguration of it would have certain desirable effects. If the funds were handled capably we might expect that benefit payments in periods of depression would maintain consumption in the lines of industry producing basic necessities and favorable repercussions would be felt throughout all industries. Also, a premium schedule might be set up so as to encourage employers to regularize production, thus tending to decrease the seasonal peaks of certain industries and to cut down the labor surplus attached to such industries and employed only in peak seasonal periods. Finally, unemployment exchanges if included in the unemployment insurance scheme would increase the fluidity of labor, provide a more efficient organization for relief and increase our knowledge about the unemployment problem.

However, in spite of these beneficial results unemployment insurance schemes entail difficulties, and we must not be misled by the glib claims which their proponents make for them.

If unemployment insurance were set up on a national ^{scale} ~~scheme~~ large funds would be involved. How these funds are invested in periods of prosperity and liquidated in periods of depression would have a considerable effect upon the volume of business activity and the level of national income. If they are handled in a haphazard manner we might well expect that unhealthy booms would be furthered and depression periods increased in intensity. I have a memorandum analysing the difficulties that are involved that I will be glad to have you read. Strangely enough in most discussions of unemployment insurance this very important question of how the reserve funds shall be handled is almost entirely ignored.

A much more important objection to unemployment insurance is that it only treats a symptom of the industrial maladjustments without any attempt to get at the basic factors which create them. Thus if a comprehensive unemployment insurance program were inaugurated it might lead to complacency on the part of leaders in Government and a feeling that we have solved the problem of unemployment.

My general position upon unemployment insurance is that it might be all right to introduce some form of it into our economic system in the future for the reasons mentioned earlier but by all means we must remember that this is not going to introduce any "cure all" into the system and that much more important measures must be taken and greater controls introduced over basic factors in our economic life if we are to obtain stability.

Such a program for increasing security and introducing stability should concentrate it seems to me upon the operation of our money system because money factors are of the greatest importance

in permitting both boom periods and depression periods to go to great lengths and to get out of control with disastrous effects upon business activity and national income. Unemployment arises in largest volume at times when we are having a severe contraction of bank credit and hence a destruction of bank money which is the most important type which we now use. Under such circumstances we also find that deposits are hoarded by corporations and individuals and this places a further depressing factor upon business activity and leads to further curtailment of employment. Thus at the present we find that bank deposits have shrunk something like 50% from the prosperous days of 1928 and 1929, while the velocity of circulation of these deposits has declined by 50%. If the President expects to increase the price level to anything nearly approximating the 1926 level and to increase industrial production and hence employment, it is essential that the available money supply and its velocity of circulation be increased by very appreciable amounts or his program will be doomed to failure. Of course, we have gotten ourselves into a very severely depressed condition and therefore much more drastic action will have to be taken to work ourselves out of it, hence it may be necessary for very large Government expenditures before they will take hold and private industries will come back into the picture, but as the President answered critics in his speech the other night, "No country however large can afford to waste its human resources". Nor should we worry about an unbalanced budget in carrying out such a program because if we have a large increase in national income there will be no difficulty at all in balancing the budget from normal tax revenue. It is only when we have a very much

shrunk national income that the tax burden becomes onerous. We must get the people of the country thinking in terms of a balanced budget over a period of years instead of a balanced budget within any one given fiscal year.

As a long run proposition we should provide for more direct and forceful action by the body which is entrusted with the responsibility for monetary control. It seems to me that if this body would take action immediately after a decline has started much of the cumulative effects of deflation could be averted. Also, if the Government were willing to start out immediately with a spending program which was designed to fill the gap which private enterprise had left by its curtailment of new capital construction the monetary policy would be desirably supplemented.

We might obtain a better control over the velocity with which funds are spent if we had a tax system which was more ^{flexible} ~~adaptable~~ and which was designed to effect a more even flow of funds. However, this question of velocity, while extremely significant, is one which is difficult to analyze and one to which ~~the~~ Governmental policy is not ^{readily adaptable} adapted to controlling.

In other words, we must concentrate upon decreasing the volume of unemployment and to adopt and carry out policies designed to keep employment at a maximum, and if as the President said in his speech Sunday night "I stand or fall by my refusal to accept as a necessary condition of our future a permanent army of unemployed", it will be well to take such measures promptly. In my opinion, no scheme of unemployment insurance offers the prospect of doing this to any really significant extent. It is unemployment engendered in the depression phase of the

business cycle, when all industry and business is curtailing operations and turning men out, that calls for immediate and sustained attention for here is the great waste of our material and human resources. At best unemployment insurance can but slightly improve the level of production over the period of a business cycle. Although it might decrease seasonal and technological unemployment these after all are of minor significance. Moreover, its benefits in providing a better organized labor market and a more efficient organization that might be used to administer relief while desirable are not of prime importance in solving the real problems of the economic system which apparently works so badly in certain periods.

In conclusion, I suggest that we attempt to put through an insurance of income upon a national basis for the unemployables through the introduction of old age and incapacity pensions of some type. Unemployment insurance on the other hand would be deflationary if introduced at the present time even though there were a delay of say one or two years before the system were actually inaugurated and I believe that this might wait until a later date, inasmuch as unemployment insurance is not of fundamental significance in solving the employment problem for the country as a whole.