Sears, Roebuck and Co.

Executive Offices

Chicago

R. E. Wood
President

October 19, 1937.

Honorable M. S. Eccles,
Chairman, Board of Governors
of the Federal Reserve System,
Washington, D. C.

Dear Governor Eccles:

I thought you might be interested in the attached bulletin put out by Lionel D. Edie. Dr. Edie has quite a following in New York. While I do not agree with him on all points, he is a brilliant man, and I do agree with what he says in paragraph 5 of this particular bulletin.

In the light of subsequent events, I feel that the Federal Reserve Board did make a mistake last spring. I think that if it does not start and start speedily to try to remedy this mistake, we are in for quite a serious time. I do not think the Federal Reserve Board should continue to sit by idly, and I want to put myself on record personally as giving you this opinion. Either the remainder of the gold ought to be desterilized or the last 50% increase in reserves eliminated or both steps taken and in the very near future. If the state of near-panic in the securities market is allowed to continue, it is bound to have very serious repercussions on business, on employment, on the tax problem, and on the relief problem this winter.

Very truly yours,

R E Wood

CONFIDENTIAL

October 15, 1937

MONTHLY ANALYSIS

COMMODITY PRICE SITUATION

1. The year started out on a keynote of inflation, with nearly every one making commitments on the inflation premise. That premise has turned out to be wrong. The error of calculation has been costly to most corporations and a considerable recession in business is necessary to correct it. The pendulum has swung sharply from extreme forward commitments to extreme hand-to-mouth buying and, in this swing, new demand suffers severely.

2. These sharp changes are not reflected in the broad index (Bureau of Labor Statistics) of wholesale prices which continues to hang around the 86-87 level. Nor is much change in this sluggish index expected over the balance of the year. But this is such a broad average that it conceals some very striking developments within the price structure. Fifteen principal raw materials reached a peak in late March and early April at a time when everybody was talking about shortages, inability to get deliveries, armament boom and inflation. Since that peak, there has been a decline in spot prices of about 25 per cent. Futures prices have also come down sharply. The peak of futures was reached at about the same time as spot, but the decline has been greater, amounting to over 30 per cent. This special weakness in futures is mainly traceable to farm commodities which reflect bumper crops. If the proposed AAA legislation goes through Congress this coming winter, and right now the prospect is all in that direction, it seems inevitable that the curve of futures prices will turn upward, perhaps rather sharply. Spot prices would logically be delayed for some time in responding sympathetically to the influence of futures. These futures prices are now about 44 per cent below the average of 1924-1926 and the stage is set for an upturn when crop control on 1938 acreage becomes assured. Since a special session of Congress has been called for November, futures on some farm commodities are quite likely to strengthen.

3. A general scramble is now under way in the merchandise field to reduce inventory. Just as the tide six months ago was toward big forward commitments, so now the struggle is toward empty shelves. In retail trade this objective will be reached by most companies by December or January. A longer period would be required in some manufacturing lines. What happens when empty shelves are reached? Probably another inflation scare and another wave of forward commitments some time in 1938.

4. The universal attempt to pass higher costs on to the consumer has come at an unfortunate time. Consumer resistance is more apparent now than was anticipated by most merchants. Dollar value sales show fair percentage gains over a year ago but the gains are mainly absorbed by price advances. Automobile sales have not yet met the test of price advances,

but it would be surprising if they do not have the effect of dropping unit sales below the year ago level by a figure in the neighborhood of 10 per cent. In retail trade generally the next few months are likely to witness many special sales, anniversary sales, price-slashing sales. It is difficult to say how much these will amount to on the average but the peak prices of autumn are on the defensive. Some kind of new equilibrium will doubtless be found for the retail price structure during the coming winter.

5. These matters cannot be adequately explained without reference to monetary policy. No two people seem to agree on money questions and the view here entertained is open to all kinds of dispute. However, the view will be stated without reservation. The view is that the Federal Reserve stepped on the brake too hard last spring and started a deflationary spiral of the same sort as prevailed under the Hoover Administration. The high price of gold has failed to avert these consequences. The year to date has been marked by contraction of total deposits of commercial banks. Officials seem still to be nursing the illusion that the credit contraction is not significant because the bulk of the decline is in the form of inter-bank deposits rather than of individual deposits. Before the winter is over one cannot help wondering if the Federal Reserve will not be compelled to admit the error and to reverse the influence of monetary policy. They have already taken initial steps in that direction but bigger steps are necessary if monetary policy is to be a factor in turning this situation around. If and when such action is taken, the logical accompaniment would be another violent inflation scare. Everyone has to be on the watch for this possibility, indeed probability. One great supporting factor all this year has been that British monetary policy has definitely refused to adopt the deflationary character which has been true of Washington policy. For the year 1937, supposedly inflationary Washington has actually pursued a deflationary policy and conservative London has held the fort of the world price structure. The New Deal experiment in managed currency has made a serious error and probably, after undue delay, will seek to correct it before the winter is over.