

Personal and Confidential

ROOM 9136, DU PONT BUILDING
WILMINGTON, DELAWARE
98

March 2, 1944

Hon. Marriner S. Eccles, Chairman,
Board of Governors,
Federal Reserve System,
Washington, D. C.

Dear Mr. Eccles:

Have noted with interest the account of your recent talk before the Tax Institute, of which I happen to be a member.

As you refer to the danger of "post-war inflation" resulting, as I understand, from accumulated purchasing power, I take the liberty to send along to you a memorandum analyzing this so-called "purchasing power" -- and I am frankly unable to see how much of it can be "validated". Hence, I doubt whether the post-war threat is as serious as some have believed.

Further, according to the papers, you stated that we would have to find employment for "at least 9,000,000 more people than were working in 1940".

However, a careful analysis of the Government figures, before they had been "doctored" for various propaganda purposes, indicates that more than 50,000,000 people, or practically the entire "labor force", as reported in the Census of March, 1940, were actually at work by the end of the year.

Of course, 1940 was a year of rapid increase in employment, and if those on Federal emergency work be included -- and they were all drawing pay -- then the average number of people employed in the year 1940 was about 51,000,000; while the Census reported total "labor force", as of the latter part of March, was 52,789,000, of whom 767,000 were young persons who had never before been employed!

The net annual increase in the number in the normal labor force¹ during the decade of the 30's, was less than 400,000 per annum. During the post-war decade, because of age distribution and earlier retirements, the net increase will probably be under 350,000 per annum. Furthermore, we will probably have 2,000,000 - 3,000,000 people in our armed forces over a period of several years following the war.

It is finally reasonable to suppose that most of the

10,000,000 who are now abnormally in the working force, because of war conditions, will pretty rapidly drift out again during a period of peace.

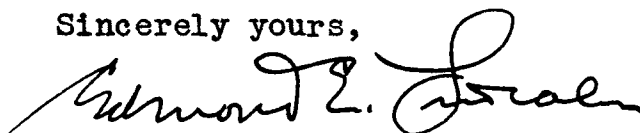
From very careful analyses, therefore, I assume that the average annual number who will normally be in the labor force in the 5 post-war years, will not much exceed 55,000,000 persons, of whom, as stated, from 2,000,000 to 3,000,000, on the average, will be in the armed forces; and it is normal to have from 2,000,000 to 3,000,000 unemployed, due to illness, shifting of jobs, etc., etc.

It would appear, therefore, that we will need non-military jobs for 50,000,000 - 52,500,000 people, on the average; yet even by the end of 1940 we were actually employing people at this rate, and in 1941 at a substantially higher rate.

I do not, therefore, see any insurmountable or unusual problem for post-war employment. The difficulty seems to be that, for some strange reason, spurious figures have been emanating from Washington for some time as to the number who were actually unemployed back in 1940. In my judgment, it would be a wholesome thing if these basic errors were corrected.

With kind regards,

Sincerely yours,

A handwritten signature in dark ink, appearing to read "Edmund E. Brown". The signature is fluid and cursive, with a large, stylized initial "E".

Enclosure

December 6, 1943

SOME CURRENT "SAVINGS" ILLUSIONS --
WITH PARTICULAR REFERENCE TO POST-WAR "PURCHASING POWER"

Until recently it has been continuously asserted, both in governmental quarters and by private bankers and many business men, that the American people are saving at an unprecedentedly high rate. Reference is made to "liquid savings" amounting to \$30,000,000,000 - \$40,000,000,000 per annum during the war period. The conclusion is then drawn that in the post-war period, because of these tremendous accumulated "liquid savings" we shall have such limitless "purchasing power" in the hands of individuals that serious "inflation" cannot be prevented, unless the so-called "inflationary gap" is now "closed" by progressively heavier taxation(1).

A. Perhaps a few facts will serve to illuminate this discussion:-

1. The only practical way to close the so-called inflationary gap, which is purely a theoretical concept, is for the Government to balance its budget through economy. So long as we have an unbalanced budget, the theoretical "gap" can never be closed, because what the Government receives with one hand through taxes from certain individuals and sources, it pays out with the other hand to other individuals for goods and services. Thus the deficit financing of the Government continually creates bank "credit" and paper currency, based not on productive transactions or the accumulation of wealth, but actually arising from the destruction or depletion of our assets -- and the "money" continues to go 'round and 'round.
2. All of our governments and agencies, federal, state and local, for the fiscal year 1943-1944, were originally proposing to spend an amount close to \$120,000,000,000, as compared with an estimated national income produced for the period which could not exceed \$145,000,000,000 - \$150,000,000,000. This expenditure figure has since been reduced, so that the total may not exceed \$105,000,000,000 - \$110,000,000,000; but, according to official estimates, our Federal Government alone will be expending an amount equal to about two-thirds of the national income as ordinarily computed.

No amount of taxation within the power of a democratic government to levy could possibly be sufficient to cover such a volume of expenditure. Even under a totalitarian regime, citizens would have to be reduced to a status of virtually complete slavery in order to accomplish such an end.

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- (1) Briefly and broadly, the newly devised concept of the "inflationary gap" means the difference between our national income and the total amount spent by individuals for goods and services plus all personal taxes. For example, if the national income should turn out to be \$140,000,000,000 in 1943, if all personal expenditures for goods and services should be \$90,000,000,000, and if all personal taxes should

3. Accumulated Federal Government deficits from 1931 to 1941 (fiscal years) inclusive, amounted to about \$31,500,000,000. Between the middle of 1941 and the middle of 1943 the accumulated deficits increased by approximately \$77,000,000,000 additional, while the forecasted deficit for the current fiscal year, barring drastic economies, would add about \$71,000,000,000 further to the Federal Government debt. During the past 12 months ending November 30th, the debt has already actually increased by \$70,000,000,000 to a total of \$170,000,000,000. By the end of 1944 it will be well over \$200,000,000,000.

To be sure, the country may have gained or developed a few assets, relatively small in value or of questionable further use. Upon the whole, however, this debt does not represent real economic values, but is evidence of the fact that labor and materials have either been destroyed or given away, or in general applied to uses which are non-productive in the economic sense.

4. As mentioned above, it is commonly alleged that, despite the diversion of well over half our productive effort into the channels of war and destruction, yet the American people are now accumulating "liquid savings" at a rate infinitely higher than anything known in prosperous times of peace. In fact, many would have us believe that within another year we may have accumulated, since the outbreak of the war, at least \$100,000,000,000, which can be realized as "purchasing power" in the immediate post-war period.

We may well ask, How can this be? How can a country become more and more indebted as a result of war, while its citizens become richer and richer -- if such is in fact the case?

Footnote (Cont.)

amount to \$15,000,000,000 - \$20,000,000,000, then the potential "gap" would be regarded as \$30,000,000,000 to \$35,000,000,000 -- an amount which might theoretically be used in "bidding up" the price of goods and services.

However, as a matter of fact, the goods and services are not available, and prices generally are controlled. There are also many additional unrecorded personal expenditures. Further, many billions are being spent in buying Government bonds and some new private securities, in reducing private debts, for personal insurance, and for new home construction.

Personal "reserves" now need to be far larger than before the war, because of heavy taxes, lack of use of bank facilities in new war plant locations, etc., etc. For many years, also, the "turnover" of demand deposits -- far more important in affecting prices than the mere amount of money and credit -- has been scarcely half the rate which we used to regard as "normal".

Finally, when the war is over and the national budget is balanced, there will be no "gap". For practical purposes, therefore, this concept is little more than mental imagery, although it has been used with almost tragic effect in "softening" people to bear confiscatory taxes, while colossal Government wastes have gone virtually unchallenged.

Perhaps if we examine the alleged "savings" more closely, some light will be thrown on the problem. According to computations made by the S.E.C. and the U.S. Department of Commerce, "liquid savings" of "individuals" for the third quarter of 1943 amounted to almost \$10,000,000,000. Roughly, the chief items adding up to this remarkable total were, first of all, \$5,500,000,000 "invested" in Government bonds; next, \$1,700,000,000 in insurance and pension reserves, \$1,000,000,000 of which was in Government insurance! Finally, there was a big item approaching \$3,000,000,000 in "currency and bank deposits".

However, a more careful examination of the records of representative banks, which has recently been made in various districts under the auspices of the Federal Reserve Board, indicates that these so-called "individual" deposits actually include the deposits of all unincorporated businesses. After a good deal of analysis, the Federal Reserve Board has been unable to show that more than a very small percentage of the increase in demand deposits during the war period has actually belonged to private individuals. The same qualification would undoubtedly apply also to the apparently great increase in money in circulation, as well as to the alleged increase in private Government bondholdings.

Furthermore, because of changed conditions resulting from the war, extraordinarily heavy taxes, new taxes in the lower income brackets, etc., etc., probably comparatively little of the currency and demand deposits reputedly in the hands of individuals other than unincorporated businesses, can be used directly, either presently or in the post-war period, for the purchase of goods. In recent years, also, the rate of "turnover" of deposits -- their effectiveness in use -- has been at record low levels, due primarily, no doubt, to fear and uncertainty.

Again, the amount which is deducted from the payroll for Federal Social Security insurance certainly cannot be so used. Nor can private insurance premiums be siphoned through current purchasing channels except by a very dubious credit operation.

But this is by no means the whole story. The biggest part of the alleged "liquid savings" is now being "invested" in Government bonds. Let us, therefore, examine briefly the nature of the Government debt, and the prospects of validating this debt as post-war "purchasing power", from a national point of view.

B. Does the Government war-time debt create or store up future purchasing power?

Let us note first that, in the economic sense, "saving" is merely refraining from current consumption with a view to future production; while "investment" is the application of such "savings" to productive ends. True "savings" must be backed up by useful goods, or by securities which represent productive assets. The mere accumulation of promissory notes does not constitute savings or investment. A country or its people can become "richer" only if the available quantity of economically useful goods and services is increased.

When we buy a bond or a stock of a well-run business, we "invest". When we buy a Government bond, we acquire a first lien on the productive assets and

manpower of the United States, which, however, does not create the means for its own "servicing" or "liquidation", but which can be validated only by the Government's power to tax the people who own the productive resources of the country, i.e., by decreasing their purchasing power. This is not "investment" in the true economic sense.

As implied above, our war-time Federal debt arises primarily from the economically unprofitable use, destruction, or loss of our physical resources and our labor, which under the circumstances are not devoted to further production and to the accumulation of valuable physical things for the future. From the very nature of the case, most of these war-time Government debts result from the actual destruction of the means of their validation, whereas a prudently created private debt actually produces the means of its own servicing and ultimate liquidation.

How, then, can a Government war-incurred debt be validated in the hands of the individual during the post-war period? Obviously, from a broad national point of view it cannot be done; but even from the individual's point of view it can be done only by taxing away money from a non-bondholding group in order to give it to the bondholding group. Temporarily an illusion of validation might be created by shifting the terms of payment, by trading new pieces of paper for old, or by issuing irredeemable paper money in exchange for outstanding Government bonds.

But let us go back to the important question, "How, if at all, can war-created Government bonds be used to increase post-war purchasing power, from a national point of view?" Obviously, the bonds must be converted into something which is exchangeable for goods and services, i.e., "money" or bank credit. How can this be done?

1. Can the bonds be sold back to the Government? No --
 - (a) because the Government could buy them back only by the imposition of an equivalent amount in taxes, which would merely "shift" a certain amount of purchasing power without any aggregate increase, but probably with an aggregate loss; or
 - (b) the Government would have to issue in return "phony" money, which in itself would cause loss of confidence in the credit of the Government, and rising prices which in turn would reduce the national purchasing power; or, finally
 - (c) the Government would have to sell new and more attractive bonds to others in order to raise the "money" to "redeem" the old bonds -- but the new bondholders would have their immediate purchasing power curtailed commensurately.
2. Can the bonds be sold to other persons? Hardly -- because virtually everyone will be a bondholder at the end of the war, and probably even more may wish to sell than to buy. But even though there should be a willing buyer for every bond that was offered, yet to the extent that new people invested in Government bonds, to that same extent their purchasing power for goods would be reduced. Former holders might have increased their purchasing power, while the new holders would have decreased their purchasing power by a corresponding amount. There would be no net national gain.

However, if there were a greater eagerness to sell than to buy, the market price, if unsupported -- and it probably could not be supported -- would fall to such an extent that total purchasing power would be decreased, and we would be threatened with drastic deflation.

3. Could the bonds be sold to the banks? Hardly, for several reasons:-

- (a) Most of the bonds now held by individuals are not legally purchasable by banks.
- (b) The banks will already be loaded to the danger point with Government bonds, and in the post-war period they will find themselves so "frozen" with the Government debt that they will undoubtedly prefer to be on the selling rather than on the buying side.
- (c) Furthermore, they will need liquid resources in order to enable them to make normal business loans, which should yield a substantially higher rate than the return on Government bonds.

4. Can the bonds be discounted at the Federal Reserve Banks at par?

This is very doubtful, particularly if many holders should wish to discount them. Federal Reserve Banks are already very much overloaded with Government bonds, as is the entire banking system. If large quantities were to be "discounted" after the war, the operation would be equivalent to unlimited paper money issues.

As a result there would be the gravest danger of loss of confidence in the Government credit, followed by uncontrolled inflation which in itself destroys and does not increase purchasing power. The probabilities are that definite restrictions would have to be put on the re-discounting of Government bonds during the post-war period, provided the holders of large quantities should wish to "cash them in" by this method.

5. Even if the war should be entirely over by the end of 1944, the Federal debt will be approximately twice as great as the highest aggregate long-time private debt that we have ever known in this country. Most of the resources of our commercial banks will be invested in Government bonds. The insurance companies and the savings banks will also be top-heavy with Government bonds. Those who have been increasing their insurance and their savings deposits, have really been buying Government bonds.

For many years there has been no net increase, but rather some decrease in the amount of bonds and stocks representing the assets of private enterprise. However, the Government having issued upwards of \$200,000,000,000 in bonds, will have acquired a first mortgage up to fully 100% of the reasonable value of all the economically productive assets of the United States. Virtually all the marketable private property of the United States will be in "hock" up to 100% of its peace-time value. By no stretch of the imagination can such a condition in itself be transformed into increased post-war purchasing power.

6. Finally, even though we should be wrong in any or all of the foregoing analyses, and even though some sound method could be discovered

whereby the holders of Government bonds could, in the aggregate, increase the national purchasing power as a result of their ownership of bonds; yet, even so, why should anyone assume that such "potential" purchasing power would be exercised in any big way in the immediate post-war period?

This period will be full of great national and international uncertainties. Some 10,000,000 people not normally in the labor force will be in process of demobilization; the longer working hours will be curtailed, and over-time penalties will be abolished. Actual and potential supplies of goods will be over-hanging both national and international markets.

Why, under such conditions, should people in great masses rush to sacrifice their Government securities and to lose their small amount of interest income, even though it should be economically possible to follow such a course -- which, in the light of known facts and principles, we deny?

- C. The conclusion of the matter -- "Purchasing power" can be increased only through increased production of goods and services, and through the accumulation of productive property.

The question is asked, "Will not the average citizen be better off in the post-war period, and in a position to buy relatively more, because of his comparative freedom from private debt and because he is the holder of Government bonds which yield some income?"

It is undoubtedly true that many individuals will be better off in this sense, and will be able in the post-war period to increase their "consumer credit", as well as their mortgage indebtedness, each by several billions of dollars. It is also true that those who receive a small amount of interest from Government bonds and are not subject to any substantial tax, may be in a relatively better position than in earlier times.

However, there is only one way to maintain the value of Government bonds, and that is through taxing somebody in order to provide the interest and a reasonable amount of amortization. Since the bonds in themselves do not represent any economically productive resources, as is the case with prudently issued private securities, somebody's purchasing power will have to be reduced through taxes in order to increase by a very slight amount the purchasing power of bondholders, to be realized in the form of interest received on the Government debt. The larger owners of Government bonds will themselves be heavily taxed to furnish their own interest payments!

There is no conceivable national gain in the process. On the contrary, it is all a national handicap, which will tend to hold the standard of living down to a lower point than would have been realized had there been no war, and had our energies and resources gone into the production of economically useful goods and services over the past several years.

In this game of Federal deficit financing, from a national economic point of view one hand merely washes the other, and usually becomes a bit dirty in the process!

The total amount of interest to be received on all Government bonds held by individuals at the close of the war will probably not be much in excess of \$1,000,000,000 per annum. The total prudent increase in consumer credit, made possible because of the war-time liquidation of personal debts, will not be more than a few billion dollars. Likewise, a few billions in new home mortgages may be loaned. All these things together, however, can scarcely account for more than \$10,000,000,000 - \$15,000,000,000, or only 10% - 15% of the post-war normal annual income of the country.

Perhaps some people may for a time spend more freely because they are totally or relatively free from personal debts. Yet we are sobered by the fact that when the war is over the aggregate public and private debt will be from two to three times as great as pre-war, and the average Federal debt per family will be at least \$6,000! Those who must pay the taxes are likely to be more cautious, rather than less cautious.

What is the "end of the whole matter"? The science of economics shows us clearly that "purchasing power" is only another aspect of "production", in the economic sense. We can have high post-war purchasing power only by producing more goods for civilian peace-time use, either currently or for the future. The power to produce is the power to consume, i.e., to purchase.

In the post-war period we will have the essential conditions for the greatest scale of economic production that this country has ever known. We will have the plant capacity, the trained man-power, the natural resources and many substitutes therefor, the managerial "know-how", the compelling desire for "better things for better living"; and, we hope and fervently believe, there will be a sound Government which will not try to convince the public that blowing on the financial thermometer will raise the economic temperature.

Under these conditions we can, in the post-war years, through our own efforts and efficiency, realize the highest level of purchasing power that this country has ever known, despite the handicaps of our colossal Government debt -- but not because of those handicaps.

March 13, 1944.

Mr. Edmond E. Lincoln,
Room 9136, Du Pont Building,
Wilmington 98, Delaware.

Dear Mr. Lincoln:

Your letter of March 2 commenting on my speech before the Tax Institute and your memorandum, "Some Current 'Savings' Illusions", have been read with interest.

With reference to your memorandum, I certainly agree that our war financing would be more satisfactory if we approached more closely a balanced budget. However, it seems to me wholly unrealistic to contend that "colossal" wastes could be eliminated during the war, making heavier taxes unnecessary. Except for relatively small amounts, government expenditures are dictated by military imperatives and while there may be some waste involved, I think the amount is remarkably small in view of the urgency and magnitude of the problems faced.

I, of course, agree that there is no necessary reason why the huge accumulation of liquid assets will lead to inflation after the war. The point I made in my speech was that the existence of this accumulation increases the danger that inflation may occur and I think that sound statesmanship requires serious attention to this problem. Moreover, the danger arises from the point you mention, namely, that more people may want to sell than buy government bonds, that pressure will be exerted to reduce instead of raise taxes, and as a result the banking system will have to absorb bonds in large volume, thus creating additional funds available for spending in a period in which the supply of goods is still restricted. I think, however, your concern about the ability of the banking system to absorb the bonds offered or to maintain them at par is unnecessary.

As you point out, the Federal Reserve deposit surveys have indicated that a comparatively small volume of demand deposits are held by individuals. Your assertion that the same is true of currency and government securities does not, however, appear to be supported by available evidence. More important, it seems to me, is the fact that inflation can result from business spending as well as individual

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March 13, 1944

spending. Indeed I am inclined to think that business spending to rebuild inventories, especially if prices are tending upward, is as likely to lead to an inflationary situation after the war as consumer over-buying.

You emphasize that wartime accumulation of liquid assets does not represent an accumulation of real wealth or result in production of useful goods and hence cannot contribute to higher standards of living. While during the war our productive effort must obviously be directed at supplying war materials, these savings if spent at a later date may well lead to increased production of goods for civilian use. If the economy is operating with large areas of unemployment, spending of accumulated savings may not be merely a transfer from one group to another but can actually increase the total volume of consumption and investment. If taxes are drawn from funds which otherwise would remain idle and funds placed in the hands of businesses or individuals that invest or spend them, a net increase in total output does result.

With reference to the statements in your letter about the labor force and employment, I recall that in 1940 you presented similar data which were carefully considered by many technical experts in this field. I think it is most unfortunate that anyone in a position of influence in industry such as you occupy should impute to these experts a bias or willingness to "doctor" statistics for "propaganda purposes". I know personally a number of the younger men who work in this special field and I am very much impressed with their technical competence and their high standards of professional integrity. It is unthinkable that these experts in the various agencies would lend themselves to any such deceit or misrepresentation as you ascribe to them. Conceivably one or two might be corrupted, but in order to "doctor" statistics, as you allege, it would be necessary to corrupt a very large group--men of scientific mind and approach, men who are remote from and incapable of thinking in terms of politics and propaganda. They may be in error, but if so I am sure it is honest error, and that their failure to agree with you can not justly be attributed to any such mean or partisan smallmindedness as your letter ascribes to them. I feel compelled to say this in replying to your letter, for I can not, by silence, give assent to such an accusation.

Sincerely yours,

M. S. Eccles,
Chairman.

ET:bjd

FILE COPY

Mr. Thurston:

I see no point in continuing the argument. The production index situation has been explained to him already by Gov. Draper. Neither Woody nor Garfield are inclined to go into that with him again.

Kendall.

TO

Ken Williams

FROM _____

REMARKS:

I doubt if we need
to say any more to him.
What do you think?
Perhaps Woody should
see the references to the
Production Index.



CHAIRMAN'S OFFICE

ROOM 9136, DU PONT BUILDING
WILMINGTON, DELAWARE

March 15, 1944

98

Hon. Marriner S. Eccles, Chairman,
Board of Governors,
Federal Reserve System,
Washington, D. C.

Dear Mr. Eccles:

Many thanks for your thoughtful letter of March 13th.
In reply, I would try to make only two major points:-

1. My memorandum tried to indicate that the alleged accumulation of individual savings during the war period, does not in any practical sense represent post-war purchasing power of the same nominal amount. On the contrary, it has seemed to me that pieces of paper representing the destruction of economic goods and services, do not in any true sense constitute "liquid assets". The matter seems to me a very fundamental one, which I fear many have overlooked or misunderstood.
2. With respect to the employment and unemployment situation, I am considerably surprised by the last paragraph of your letter, inasmuch as we are trying to arrive at a common ground of understanding, based on the facts as originally presented by certain Government agencies, such as the Census Bureau.

The point I was trying to make in my letter to you, was that in reality the employment situation by the end of 1940 was far better than is popularly supposed and than was indicated by the press account of your statement, which was apparently based on the first part of the year, although employment by the end of the year was several millions higher. Also, in the past decade the net growth in the all-year-round labor force has been much lower than is commonly asserted. For these reasons, among others, I have been encouraged to feel that the post-war unemployment situation should be less serious and more readily "managed" than many have feared.

In my letter to you I did not suggest that the original figures had been "doctored" by Government agencies or individuals. I do know, however, that they have been carelessly and almost hopelessly misused by many people outside the Government service.

In addition, both I and many other people are aware that in

recent years in many Government departments there have been many bright young men who have dealt in "subjective" rather than "objective" statistical analyses. There is always a rather wide range of judgment in the interpretation of most economic data; hence, even with the best intentions in the world, many of the enthusiastic young "experts" tend to read their own pre-conceived notions into data which are not too exact, and to make out a "case" accordingly.

If you have at any time carefully gone into the matter, I should expect you would be very much surprised, as some of us have been, at the different ^{employment and unemployment} estimates presented over a period of years by the Department of Agriculture, the Department of Commerce, the Department of Labor, the Social Security Board, the W.P.A., the A. F. of L., and the C.I.O. -- not to mention the National Industrial Conference Board, the Hoffman Committee, and others.

On so important a matter as employment statistics, it would seem that there should be carefully worked out some official nomenclature, together with basic figures showing the number employed under the various important categories, together with definite figures on the bona fide number unemployed, so that all students of the question and all administrators could refer to the same official compilation, which would stand up under expert analysis. It seems to me that such data would be extremely useful in the work of the Federal Reserve Board.

Further, you are undoubtedly aware that a good many of the careful students outside of Washington find the latest "edition" of the Federal Reserve Board Index of Industrial Production baffling and, if I may say so, misleading, so far as concerns any historical comparisons.

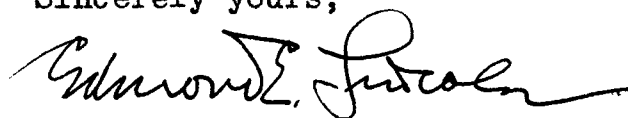
The farther away such an index gets from the physical quantities of basic materials, the more involved it becomes. And the heavy inclusion of "man hours", as well as of temporary war-time manufacturing activities, of a wealth-consuming rather than of a wealth-producing nature, certainly tends to confuse or invalidate peace-time comparisons and forecasts. I have often wondered whether it would not be more helpful to carry two indices, perhaps the present one, and a second one which would be confined only to those basic commodities and operations which can be measured in physical units of output.

Maybe some time there will be a chance for us to discuss

these very interesting and important matters further. My sole aim is to stick as close to the facts as I know how, in order to help work out a sound post-war condition in this country -- and I am sure that you have in mind exactly the same objectives.

With kind regards,

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Edmund E. Fitch". The signature is fluid and extends to the right with a long, sweeping tail.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

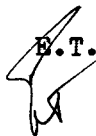
May 3, 1944.

To - Mr. Williams
From - Mr. Thurston

Here's that man again! The Chairman would like to answer him in a way that will silence him, if possible. You will recall that we didn't answer the last one.

If it is correct, I would like to emphasize that experts or economists in various departments concerned with employment or unemployment figures have carefully considered his analysis and found it faulty for the following reasons -- whatever the reasons may be.

Would greatly appreciate your help again.

E.T.


Attachments

Confidential

ROOM 9136, DU PONT BUILDING
WILMINGTON, DELAWARE

98

April 29, 1944

Hon. Marriner S. Eccles, Chairman,
Federal Reserve Board,
Constitution Avenue,
Washington 25, D. C.

Dear Mr. Eccles:

Although I don't like to keep "needling" you on your public utterances, yet I feel badly when a man in your position uses figures which seem to me inconsistent with the known facts.

I refer particularly to certain statements which, according to the Wall Street Journal of March 25th, you made to the Senate Banking and Currency Committee.

According to the report you stated that "if the volume of national production in this country is reduced to the 1939 level, it will mean unemployment for 19,000,000 workers."

I am aware that certain minor Government officials and advisors have made such statements, and some of them may have supplied you with the figures. May I, however, call the following facts to your attention:-

1. For the year 1939 there were, on the average, probably not more than 2,500,000 people in the normal working force unemployed, if we consider that those engaged in Federal Emergency work were employed (averaging close to 3,000,000 for the year). With the most liberal interpretation of the figures derived from the various Government sources, therefore, the average number of the normal labor force unemployed in 1939 could not have exceeded 5,500,000, of whom almost 3,000,000 were doing emergency work for the Government, and being paid therefor.

2. The average annual net increase in the normal labor force was around 400,000 in the decade ending 1940, judging by the population statistics, the annual increase will certainly be no greater during the present decade. Hence, there might presumptively be ^{scarcely} 2,500,000 additional members of the normal and permanent labor force available by the middle 1940's.

3. If the general efficiency in manufacturing of labor continued at about the same point as in 1939, and if there were no Government relief work, and if the physical volume of production were the same as in 1939, then there would be indicated an average unemployment in the post-war period of approximately 8,000,000, assuming the war should end in 1945, as contrasted with the estimate of 19,000,000 which the press attributes to you.

4. The analyses of both public and private figures show that the average factory output per man-hour has been declining sharply since the peak was reached around the middle of 1940, and that for the year 1943 it was scarcely as high as in 1939. Some of the experts of the Department of Commerce have seriously misled the public by assuming,

(a) that the efficiency of labor would continue to increase in the future as rapidly as during the period 1919 - 1939, and

(b) that the increase in efficiency hitherto observed in manufacturing would be applicable to those employed in all kinds of work.

This careless use of the data has led to some very fantastic post-war conclusions.

For your information, some of our very careful post-war analyses and projections indicate that in the average year 1945 - 1950 the physical volume of manufacturing production, given reasonable governmental conditions, should probably be at least one-third higher than in 1939. This, when translated into units of man-power required, and when related to the general increase in demand for labor in all collateral pursuits, seems to indicate that there should be plenty of jobs available, even at the high efficiency rates of 1940, for all of those who constitute what may be termed the "normal" working force, i.e., those people who, in times of peace, are ordinarily available for steady work throughout the year.

Personally, I believe it is a major mistake to assume that the 8,000,000 or 10,000,000 ^{additional} people who have been driven or "induced" into the armed forces and the labor forces during war-time, will continue to be generally available for employment, or will, after a brief period of transition, constitute any significant "unemployment" problem. On the contrary, the experience both of Britain and of the United States following the last war showed that most of such people, or their equivalent in numbers, drift rapidly out of the employment stream.

Also, if we are to regain our earlier standard of living,

no larger proportion of our population can be working in the future than in normal good years in the past, i.e., somewhat less than 40%.

I hope you will understand that my sole purpose in calling these matters to your attention is because I realize the gravity of the problems which we must face in the post-war period, and believe that the known facts will be sufficiently difficult to handle, without any previous exaggeration in the public mind. I think we need to be very cautious on some of these matters.

With kind regards,

Sincerely yours,



Edmund E. Lincoln

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

May 18, 1944

Mr. Edmond E. Lincoln,
Room 9136, Du Pont Building,
Wilmington 98, Delaware.

Dear Mr. Lincoln:

In reply to your letter of April 29, I wish to call your attention to some of the specific statistical errors in your analysis and to explain the assumptions underlying my statement before the Senate Banking and Currency Committee.

Two recent publications of the Bureau of the Census should clear up most of your statistical errors. These publications are:

- (1) Monthly Report on the Labor Force, No. 22, April 26, 1944.
- (2) Summary of Estimates of Labor Force, Employment, and Unemployment in the United States; 1940 and 1930. Series P-44, No. 6, March 25, 1944.

Note that for the last week of March 1940, when the Census was taken, unemployment is shown as being nearly 8 million, including 3 million on emergency work programs and 787,000 inexperienced persons. There are no official figures for total employment, unemployment, or labor force for 1939, but statistics available for major segments of employment indicate that total employment was moderately lower, and unemployment higher in 1939 than in March 1940.

Your contention that workers on emergency projects should be counted as employed has merit for some purposes. However, since I do not believe that a permanent work program of that size is necessary or desirable, I prefer to count these

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people as unemployed. My preference in this respect focuses attention on the problem of providing them jobs within the enterprise system which seems to me to be the proper goal.

The net increase in the normal labor force from 1930 to 1940 was 5.9 million when proper adjustments are made for comparability of definitions and classifications. Your figure of 400,000 a year is thus substantially too low. A further increase of 5.9 million is estimated by the Bureau of the Census for the decade 1940 to 1950. A report containing this estimate is scheduled for publication by the Bureau.

The number of "war-induced" entrants to the civilian labor force or the armed force is calculated to be approximately 6.5 million for December 1943, not 8 to 10 million you suggest. A breakdown of the total by age and sex shows that about 3.5 million are men and 3.0 million are women. Of the men 1.5 million are under 20 and of the women 1.0 million are under 20.

You are incorrect in saying that the Department of Commerce confuses the increase in output per manhour in manufacturing alone with that for total employment. Actually, the Department's calculations show an average rate of increase per manhour in physical output of all goods and services of 2.5 per cent a year for the period from 1929 to 1941. For manufacturing alone the rate is even higher in this period.

These are the essential facts. In my statement about the volume of unemployment which might be expected after the war I made several assumptions. I think they are reasonable but anyone is entitled to make other assumptions. First, as a base for my calculation I used 1947 as the postwar year to be compared with 1939. I gather you were thinking in terms of 1945. Second, I allowed for an increase in output per manhour for all employment of 10 per cent, or about half the increase which might be expected from a straight projection of past trends. Third, I allowed for 2.5 million men in the armed forces. This is merely a guess. Fourth, I assumed a net increase in the labor force above the normal amount for 1947 of 2 million after allowing for casualties and withdrawal from the labor force of those believed likely to want to return to housework, school, or retirement. Included in my estimate of total unemployment is the normal amount of unemployment which would exist for frictional reasons even in a condition of full employment. If you wish to deduct 2 or 3 million for such unemployment, I have no objection, although some of the people affected will be entitled to unemployment compensation and cannot be ignored in that connection.

I have the highest regard for the competence and integrity of the experts in the Census Bureau and in the numerous other agencies whose combined statistical judgments are expressed in the official figures. I know something of the care and earnestness with which these men work. Many of them have spent years of full time effort in the fields of population, employment, and labor market analysis. Not all of them are young men by any means and several have national reputations in their profession. The cross-checking of their results among themselves and with experts in private organizations leaves little opportunity for major errors to prevail. Moreover, these men have access to clerical and mechanical assistance in quantities available to few outside of government and to unpublished records, studies, and statistics not available outside of Washington.

I have no illusions about the conceptual and statistical difficulties involved in measuring and defining labor force, employment, and unemployment nor of the gaps still remaining in the series. I am aware that phenomenal strides have been made in this field in the last few years and I assume that later studies and additional data may throw new light on current measurements. Yet it seems to me wholly unlikely that anyone, however brilliant, working alone or part-time without access to the records, cross-checking, and technical assistance available in the government agencies could approach the accuracy of results which is reflected in the official statistics. Frankly, it is difficult for me to take seriously the loose undocumented statistics and estimates you present as "proof" that the scores of trained experts in the governmental agencies are either incompetent or engaged in a large-scale conspiracy to deceive.

On the questions of judgment, it seems imperative to me that we accept and attempt to appreciate the significance of the fact that our economic capacity as demonstrated by the war is far greater than any of us realized before the war. I am convinced that if we permit ourselves to return to our prewar habits of thought and prewar concepts of our productive capacity we are in for serious trouble.

Sincerely yours,

M. S. Eccles,
Chairman.