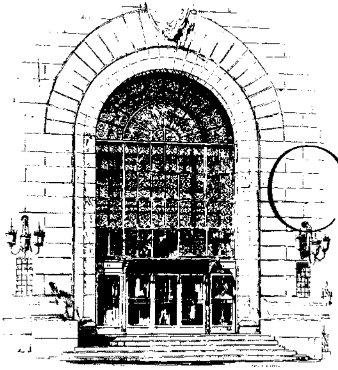

CONNECTICUT GENERAL
LIFE INSURANCE COMPANY

Established 1865

HARTFORD, CONNECTICUT

FRAZAR B. WILDE
PRESIDENT

February 26, 1946

Mr. Marriner S. Eccles
Chairman of the Board
of the Federal Reserve System
Federal Reserve Building
Washington, D. C.

Dear Mr. Eccles:

Your current discussion of the inflation problem and the general attitude of the Board on fiscal matters strikes me as constructive and in the right direction. I might take minor exception to your idea that higher taxes would restrain inflationary prices in the stock market, but that is not too important as I see it. Lower taxes and a longer waiting period might work better both to make more natural sales and to get more revenue for the government.

The two vital things are to move more of the government debt into the hands of the permanent investors and the other is to continue O.P.A. price control.

I am really thoroughly alarmed at the prices of fixed income securities. If the Treasury doesn't cooperate with the Federal Reserve and stop the downward trend in rates, I think we are headed for a disastrous crash in the market for fixed income obligation; i.e., bonds, preferred stocks, mortgages. Perhaps you will be interested in an imaginary letter which I did not send and do not intend to send to the Secretary of the Treasury. I attach a copy.

I hope I will have a chance to see you the next time I go to Washington. Kind regards!

Sincerely yours,

Frazar B. Wilde

Frazar B. Wilde

FBW:er
Enc.

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Federal Reserve Bank of St. Louis

January 18, 1946

The Honorable Fred M. Vinson

Secretary of the Treasury

Washington, D. C.

Dear Sir:

The problem of interest rates while of particular importance to the life insurance business is vital to our whole economy. The insurance point of view may properly claim to represent the interests of the country as a whole since policyholders and their families include the overwhelming majority of our total population. It is, therefore, not a purely selfish commercial approach.

The insurance companies are well aware of the responsibility and burdens imposed upon the Treasury Department. The Treasury among other things has to accomplish two major objectives: (1) to handle the national debt at a reasonable cost, and (2) to do it in a manner which will create the least disturbance and the least risk to the whole economy.

It seems to many of us in the life insurance business that the program of stabilized rates in accordance with the pattern announced in 1942 is best calculated to reach these ends; i.e., low cost and safety. It is, therefore, recommended that the Treasury reaffirm its policy of maintaining stabilized rates and that the stabilization be continued in the pattern of 1942.

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It is recognized that to stabilize the prices of anything, including money, is a difficult task. Historically, it has never been successfully accomplished. If it is to succeed, the probabilities are strong that maintenance of an established and announced program is a sounder policy than to depart from it in either direction. In other words, it is just as important to resist a further lowering of interest rates as it would be to avoid an increase.

Many students of monetary affairs are deeply concerned at present prices for fixed income obligations. By historical comparison or by any other test the present prices of bonds, preferred stocks and mortgages indicate that these securities are greatly inflated. In other words, the price of such securities is grotesque in comparison to their real value.

The direct evidence of this is the buying power of the interest received. Five years ago, for example, a good bond could be bought to yield 5%. Today, a bond of equal credit has a 3% coupon or less; i.e., the dollar income has been reduced 40%, but the buying power of the dollar has also been drastically reduced because the price of goods and services have gone up. Thirty per cent discount in buying power is a conservative figure to use. This means a total depreciation of nearly 60% in five years.

The arithmetic is illustrated below.

1940 Price of bond $1000 Income 50

1945 Price of bond $1000 Income 30

Income reduction in dollars — $20 = 40%

1945 Price increase in cost of living approximately 30%

30 dollars less 30% = $21

$50 original dollar income at par buying power = only $21 in 1945; i.e., approximately 60% discount in real value of the bond

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We are talking about the same bond with the same credit standing. We assume the market price is the same. But the real value is 60% less. This is a concrete illustration of the extreme inflation concealed in bond prices. It is not fully appreciated by the public because the prices of the bonds themselves have not directly changed. That this situation is very real and is not a theoretical inflation is well understood because of its practical impact on all private owners of fixed income obligations.

The vital stake which the Treasury has in this matter arises from the danger of a collapse in bond prices. Most of us predict still further increases in the cost of living. It doesn't seem possible that an unbalanced condition can long continue in a free economy. The higher prices rise for goods and services the more the price of fixed income securities gets out of line. Nobody can predict with any certainty the time when a reaction will occur. One can surely predict that a reaction is inevitable when the price of anything is completely out of line with other elements in the economy. It is possible that present bond prices can go higher. They are, in fact, doing so. In other words, interest rates can for the moment be forced lower, but the conclusion seems crystal clear that, for the proper protection of the financial structure of the country and for the protection of the Treasury in its long term problem of financing the government debt, it is most important to try to avoid the increasing hazard of a major reaction in bond prices. It is certainly undisputable that the higher fixed income obligations go the greater the likelihood of trouble. Stabilization of rates at the present levels seems imperative.

Specific arguments secondary to this main issue can and should be mentioned. The statement often made that low interest rates are a stimulus to the economy

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is a theory which is wholly unproved if not disproved. The Treasury is not charged by the Congress with the duty of trying to demonstrate theories. If it were, it would observe that in the late Twenties higher and higher interest rates did not retard a dangerous boom which ultimately collapsed. It would further observe that in the Thirties easy money policies did not stimulate the economy. Those who have observed the practical workings of the country for many years can testify that the price of money is the least important consideration in the minds of those who wish to promote new enterprises or expand old ones. Availability of capital funds and the likelihood that tax laws would permit a net profit to the successful entrepreneur and investor are the real reasons why money is put to work.

The cost to the taxpayer in servicing the national debt seems important particularly from an uninformed political viewpoint. Actually from an economical standpoint it probably is unimportant. To a large extent, the people who pay the bulk of the national taxes are the same people who lose income when interest rates are reduced. If they pay less taxes because the government debt is financed at an all-over cost of 2% instead of 3%, they have less money to pay the taxes with because their securities and savings have been reduced in yield and their life insurance has cost more money. Under a program of stabilization with interest rates continued in the 1942 pattern total interest charges would be increased slightly. This is because of the necessity of placing a larger portion of the debt in the hands of permanent investors rather than leaving it in a temporary form in the banks. This is not, however, an upward revision of interest rates.

Long term permanent investors, both individuals and institutions, will probably be interested in the specific suggestions made below. Such a program would be

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distinctly good public policy because it would fund a portion of the present debt with the best type of investors and at only a fractional increase in the total interest requirements.

1. A long term bond, 40 to 50 years, 2 3/4 to a 2 5/8 rate. Such a bond could have restrictions against resale or pledge for a time, this to prevent its being used as a speculative vehicle.

2. The usual 22-27 year 2½ bond in the present form. These two types should be tap issues available at any time. It would also be desirable to permit larger purchases of F and G bonds. Trust funds, especially, would be served by this latter program.

Sincerely yours,

Frazar B. Wilde

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March 5, 1946.

Mr. Frazar B. Wilde, President,
Connecticut General Life
Insurance Company,
Hartford, Connecticut.

Dear Mr. Wilde:

This is to thank you for your letter of February 26 in regard to the general attitude of the Board on fiscal matters. Your favorable comment is very much appreciated. I was interested to read your unsent letter to Secretary Vinson and wondered why you had refrained from sending it.

While the problem of debt management is by no means unmanageable in my judgment, it is a complex and controversial subject which is easier to discuss in conversation than by letter. I hope I will have the pleasure of seeing you when you come to Washington. In the meantime, let me reciprocate most heartily your kind regards.

Sincerely yours,

M. S. Eccles,
Chairman.

ET:b

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