2002 W. Lake of the Isles Blvd.
Minneapolis 5, Minnesota

December 20, 1947

Mr. Merriner S. Eccles, Chairman
Board of Governors of the Federal Reserve System
Washington, D.C.

Dear Mr. Eccles:

I am disturbed by many of the suggested "cures" for inflation. One of them is the suggestion of the National Association of Manufacturers of "Permitting interest rates to seek their own levels free of government domination". I have reacted to this one by writing two letters to the Wall Street Journal. Both of these letters are herewith enclosed. I am sending these letters to you because I feel that the subject discussed is highly important to the economic health of our country. My presentation is, I think, somewhat different from others that I have read and I therefore hope you will find them of some interest.

Without any intention of flattery, I wish to state that in my opinion you deserve public gratitude for the fine, public-spirited work you have been doing during this very difficult period.

Yours very truly,

Stanley K Platt

Stanley K. Platt

P.S. As an aid to you in appraising the letters enclosed: my background has largely been in the investment end of banking, but I have been in a position over many years to appraise a wide variety of the aspects of the financial operation of our economy; I am a student of government-business relationships; I have acted as an instructor of a university course in "Money and Banking". At present I am engaged in investment and research work, for myself and on my own initiative.

December 30, 1947.

Mr. Stanley K. Platt,
2002 W. Lake of the Isles Boulevard,
Minneapolis 5, Minnesota.

Dear Mr. Platt:

As Chairman Eccles is spending the holidays in Utah, I wish to acknowledge and thank you for your letter of December 20 enclosing copies of your letters to the editor of the Wall Street Journal. I think your letters should be very helpful. They reflect a grasp of the problem that unfortunately is all too rare. How closely your views coincide with those of the Chairman may be seen from the text of the statement he presented before the Joint Committee on the Economic Report, copy of which I enclose in case you may not have seen it.

I know the Chairman will appreciate your courtesy and your generous personal references and on his behalf let me thank you.

Sincerely yours,

Elliott Thurston,
Assistant to the Chairman.

Enclosure

ET:b

2002 W. Lake of the Isles Blvd.
Minneapolis 5, Minn.

December 12, 1947

Editor, The Wall Street Journal
44 Broad Street
New York 4, N.Y.

To-day's acute monetary dilemma cast its shadow before it. It is important that the misconceptions of yesterday should not be transmitted into the faulty actions of to-day.

The New Deal thought to usher in "reflation" of prices by devaluing the dollar. The immdiate effect on prices and on business stimulation was a great disappointment. Prices did not respond to the added dollar amount of reserve money. Low interest rates failed to stimulate business recovery. It seems that interest costs were not a determining factor promoting business stimulation when weighed against all the other costs and risks. Consumer purchasing also needed other supports.

In spite of this recent experience the thought is being advanced that we are faced with a dilemma: (1) to keep interest rates low and run the risk of greater inflation, or (2) to allow rates to increase, and thus add to the burden of servicing the federal debt. The stated conclusion is that it would be better to pay an added debt-servicing cost than to keep rates low and thus cause more inflation.

Fortunately, the neat statement of a dilemma does not prove that it exists, or that the premises, conditions and conclusions are well founded.

In the first place, it may be a false premise to emphasize low interest rates as an important cause of the current inflation. This appears more evident when we consider the great increase in the flow of money relative to the flow of goods. Devaluation of the dollar attracted the accumulation of a huge monetary gold stock that has served as a base for the piling up thru deficit financing of a fabulous supply of credit-money in the form of bank deposits. Production of civilian goods has been disrupted by the war, by strikes, and by the political difficulties of reconversion on an international scale.

Secondly, it is not clear or conclusive that even a sharp rise in interest rates would have the desired effect of checking inflation. Domestic and world-wide shortages of goods are too great. Just as low interest rates did not bring an immediate revival in the 1930's, so now high rates might again prove unreliable in checking inflation.

Thirdly, any non-selective attempts to roll back credit, by increasing interest rates or otherwise, might prove to be destructive rather than constructive. The inflation that comes from an extention of credit for purposes of production might well be considered to be a reasonable price to pay for the assurance that shortages and inflation will not become permanent. Consumer purchases might be controlled to better advantage by methods other than encouraging an advance in interest rates.

Fourthly, higher interest rates may be too high a price to pay for a doubtful solution. Not only would increased rates increase the burden of servicing the federal debt; the cost of money for purposes of production would also be increased. So long as the demand for goods exceeds the supply, higher costs of financing will be added to the selling price of goods. Such an addition to costs can hardly be considered to be an effective instrument for fighting inflation.

We thus return to the conclusion that the only sound ways of overcoming at the source the forces of inflation are to increase production or to decrease spending.

Yours very truly,

Stanley K. Platt

2002 W. Lake of the Isles Blvd.
Minneapolis 5, Minnesota

December 20, 1947

Mr. W. H. Grimes, Editor
The Wall Street Journal
44 Broad Street
New York 4, N.Y.

Dear Mr. Grimes:

In reply to your letter of December 15th, I wish to state that my letter of December 12th was not written specifically as a reply to editorials in the Wall Street Journal. It was limited to a consideration of the effects of interest rates on the extention of member bank credit, combined with the general effect of high interest rates as a cost factor of inflation.

Your letter raises an additional question. You state: "What we tried to say was that only by offering higher interest rates that appealed to savers can we stop the process of the Treasury continuing to dump its securities into the central bank". The thesis upon which you based that statement is, I presume, somewhat as follows: The acquisition of government securities by the central bank adds to the reserves of member banks, making possible a multiple expansion of credit to their customers, the effect being that the monetary demand thus created exerts an upward thrust on prices.

It is not my wish to question the credibility of this thesis that is accepted so widely by monetary theorists. However, because actions based upon it could be very important to the financial health of our country, and because experience has shown us that plausible arguments do not always correlate with practical results, I wish to mention several considerations that trouble me into less than full acceptance of the implications of that thesis. Specifically, I do not agree with the implications of that thesis, as stated by the National Association of Manufacturers: "Discourage inflationary expansion of bank credit by permitting interest rates to seek their own levels free of government domination". While I am in favor of discouraging "inflationary expansion of bank credit", I do not believe it is desirable to effect this objective by "permitting interest rates to seek their own levels free of government domination".

My reasons are as follows:

1) War-time financing has eliminated the excess reserves of the majority of the banks. Under present conditions, either a voluntary or an involuntary reduction of government bond holdings by the banks would, in the absence of support by the central bank, result in a sharp break in the bond market. Neither the public nor business corporations are in a position to support the market for even a small part of the total government debt. Such a break would tend to go too far; the central bank would be forced again to reverse its policy and buy. The whole process could prove to be a very expensive way of combating inflation.

2) Inflation has already reached a point at which the forces that caused it appear to be in equilibrium. I will borrow a few figures from a letter by Philip L. Warren addressed to your paper under date of December 16th., by way of evidence. The money supply is 300% of 1939. Production is 160% of 1939. Money supply of 300 over production of 160 gives a price level of 187%. This correlates with the actual advance in prices that has developed since 1939, roughly 87%. The chief factor causing the money supply to increase, namely deficit-financing, has ceased to expand. Loans to business appear to be reaching a peak, accounted for largely by the building back of inventories at the higher prices and by new plant investment at the higher prices. On the other hand, production has and is increasing. Total deposits of member banks have declined since 1945. Reserve Bank credit is lower. Money in circulation is about unchanged. From these observations it would not be unreasonable to conclude that inflation has largely run its course in the United States, based on the supply of money and the volume of production. This appears to reduce the necessity at this time for money-managing activities to combat inflation, an inflation that has already integrated itself into the economy. The proper time for such action appears to have been in the past, but not now.

3) A sudden reversal of central bank and Treasury policies might be very disturbing, bringing about an unhealthy shake-out of prices rather than the gradual development of a lowering price trend such as can be expected in view of the tremendous investment in plant and inventories that has taken place over the past two years. Instead of a gradual falling off of prices, reversal of interest rate policy could result in a precipitate decline, accompanied by a business depression induced by the pressure on established loans now tied

up in inventory, plant and equipment.

4) While bank credit is part of the money supply, not all bank credit should be stifled because of its inflationary implications. A distinction should be made between loans for production and loans for consumption. Such a distinction is not made by an overall reduction in bank reserves. While it is true that initially both loans for production and loans for consumption are inflationary, loans for production have the ultimate effect of increasing the flow of goods at the same time that credit is being reduced thru the repayment of the loans. While discretion is needed as to how fast productive capacity should be built up with the aid of loans, it is open to question whether blanket operations from Washington would provide a more intelligent answer than the individual appraisals of the bankers in the field. The purchasing power added by loans to consumers is in a different class when it comes to control of inflation during a period of shortages of consumer goods. Even here, however, it would be better to effect any program of restriction thru the individual bankers rather than by means of artificial controls imposed on an overall basis. Often consumer loans are essential to the equalization of individual opportunities and to the avoidance of hardships; such cases cannot be judged from Washington.

5) From the viewpoint of strengthening privately-owned and operated enterprise in the United States, a course other than shifting the debt from the banks to individuals or of placing the bond market "on its own" is preferable. That would be to encourage equity financing by the elimination of "double taxation" of corporations and their individual owners, by ending tax-exemption for municipal securities, and by equalizing the ability of corporations to finance with equities with their ability to borrow from banks by allowing the stock market the same credit support as industry itself gets thru bank loans, i.e. by lowering margin requirements for carrying equities, whether new issues or old. Continued low interest rates on government securities would help to point up the attractiveness of equities.

This program would promote sounder financial structures for industry and trade. In addition, it would have the effect of reducing borrowing from the banks to strictly bank paper. Money raised by sale of corporate issues to the public and used to retire debts at the banks reduces bank credit as effectively as sale of government bonds to the public and use of the proceeds to retire government debt held by the banks. Moreover, the effects on the economy would be more constructive and less upsetting to established relationships.

6) The above points do not imply that at no time in the future should the government bond market be placed "on its own". Instead, the possibility is suggested that the shift may be effected at a later date with less strain on the economy. Then the shortage of goods will have been met and the credit need for productive purposes will have subsided. At that time a strong point can be made not only for shifting government bonds from the banks to individuals, but also for outright retirement of the debt on a carefully designed but flexible schedule.

I would appreciate any comments you care to make on the above.

Yours very truly,

SKP

Stanley K. Platt

P.S. This letter is not for publication in its present ~~form~~ form. However, ~~you~~ you may use all or any part of it for editorial comment, without using my name.

Because of the general significance of the subject to our national economy, I am forwarding a copy to the Board of Governors of the Federal Reserve System and to the Secretary of the Treasury. I am also forwarding to them copies of my letter of December 12th.