

Confidential

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OUR COMMON RESPONSIBILITY FOR ECONOMIC BALANCE

In the past three years I have had to live pretty continuously with the problem of economic balance, with the problem of how to achieve and maintain full and continuous employment of the human and material resources of our nation. I have, as is natural, been chiefly concerned with the contribution the Federal Government in general and the Federal Reserve System in particular could make to the solution of the problem. As time has passed, however, I have become more and more impressed with the importance of securing favorable conditions for the effective use of monetary and fiscal controls, with the danger to our common goal presented by the conflicting and frequently unstabilizing policies of private groups. Before we can do away with business instability we will have to find some way of ensuring that the policies of private organizations, whether they be of business men, of farmers or of labor, are not in conflict with our common objectives. This, then, is the aspect of the general problem of economic balance that I propose to discuss at this time. I should like to show that there is no real conflict between the long-run interests of various groups and the public welfare.

I am afraid that the various groups in the community are engaging in a good deal of wishful thinking on the subject of economic stability. Perhaps I should say that they are behaving like ostriches. They know the problem is there but they refuse to face it. Although it may not be put

in so many words, there seems to be a hope that things will run along all right without anybody thinking too much about them. There is a feeling that the collapse after 1929 was attributable to certain special circumstances which will not occur again, a feeling that the government had for a time to operate as an emergency rescue squad, but that the emergency is now past and we ought to get back as soon as possible to the good old days when things supposedly ran themselves. This, I am convinced, is wishful thinking and will not stand up under analysis. I am as certain as I am of anything that if we now rest on our oars and drift with the current another bad breakdown will be inevitable.

There is, I think, a tendency on the part of all the different groups and classes in the community to dump common problems onto the Federal Government and its various agencies, and then forget about them, except as the attempts to improve the situation interfere with what they consider their own affairs. There is a tendency on the part of these groups to say "we have given you powers to cope with business instability and it is your job. Take care of that job but don't bother us. Let us concentrate on our own problems."

This, I need hardly tell you, is a most dangerous attitude. There is hardly an action taken by a business group or a labor group, or an agricultural group, that does not in some way affect business activity for better or for worse. All such actions have both their private and public aspects. In so far as they affect adversely the prospects of achieving economic balance they must necessarily be the concern of those

who are in some degree responsible for this. As long as I occupy my present position I shall continue to stress to the best of my ability the necessity for continued work and continued thought on what are really our common problems.

It would be easy for the Federal Reserve Board to take a similarly narrow view of its duties. I feel personally, however, that we would be derelict in our duty if we did so. There is no doubt in my mind that Congress expects the Board of Governors to make whatever contribution it can to the problem of achieving economic balance and that this imposes a responsibility not only to use our instruments of control as correctly as possible but also to point out disrupting developments beyond our control, to make recommendations for their handling, and, in default of recommendations, at least to call attention to the unstabilizing aspects of such developments.

In my official capacity I am not directly concerned with labor policies, price policies, monopoly practices, taxation, tariffs, and farm programs as such. In my official capacity I am not directly concerned with problems of justice or equity as between different groups, such as the rights or wrongs of labor in a dispute with capital. In a more general way, however, I am concerned with the relation of these developments to the broad problem of business stability. The community through its elected representatives may initiate or acquiesce in policies that will contribute to instability. The monetary authorities, of course,

cannot presume to set aside the dictates of the community. It is, however, their duty to point out to the best of their ability the relation of specific policies to the general problem of economic balance. The community may be perfectly prepared to pay the price in terms of instability for a specific policy. It should, however, know that it is paying such a price.

Stating the problem of securing full and continuous employment of our productive resources in the broadest terms, it is a problem of striking some sort of a balance between private initiative and freedom on the one hand and public responsibility for the economic health of the whole community on the other. This balance is continually being shifted by the course of events. In a small agricultural community which is largely self-sufficing a much larger scope can be left for completely unregulated private initiative than is possible in a large, highly-industrialized and urban community such as ours. The greater the division of labor and the degree of specialization, the larger the scale of operations, the more special groups and classes become organized to further their own immediate objectives, the more dependent does the long-run economic welfare of any group in the community become on the actions and policies of all the other groups. In this sense almost no policy is exclusively the private concern of the parties immediately involved. Bank failures affect not only the bankers

and depositors immediately concerned, but also the livelihood of people who may never have heard of the banks that failed.

While I think this would be agreed to by everyone, the conclusion does not follow, as many people believe, that the only alternatives are chaos on the one hand and minute regimentation on the other. If we are prepared to do what is necessary to ensure full and continuous utilization of our resources I am sure that the degree of conscious and deliberate planning and the degree of regulation required will not prove burdensome or constitute too great a sacrifice of individual initiative. Indeed, looking at it from one point of view, initiative would have far fuller scope, and freedom more real content, in a community free from economic cataclysms than in one that is cursed with them. Certainly initiative had little scope, and freedom little content, under the conditions prevailing in 1932. I may put my thought more specifically by saying that if various groups are prepared to subordinate immediate interests or objectives to the larger purpose they will fare much better in the long run.

All that I have been saying has been couched in very general terms. I find that when it is stated in such terms there is little opposition. The difficulty comes, however, in making the transition from the general case to the specific examples. Agreement on the general case, however, is of no use unless we are prepared to apply it in individual cases. Let me, therefore, illustrate my point by discussing the developments in one field that perhaps more than those

in any other threaten our prospects of achieving and maintaining a period of economic balance. I refer to the construction industry.

The interest of the public as a whole in the construction industry is, or at least should be, obvious to all. In the years 1925-29 the volume of construction averaged \$14 billion annually, or 40 percent of the output of all durable goods. By 1933 it had fallen to \$5½ billion. The drop was relatively more severe in residential building, which declined from a yearly average of over \$5 billion in the period 1923-28 to less than \$1 billion in 1933. The part played in our difficulties by residential housing developments has never been sufficiently stressed. It was the first important element in the economy that turned down, the slump in building becoming pronounced in 1928. The slowness with which building has got under way in more recent years has been one of the chief causes of continued unemployment.

The absorption of the unemployed, the continued growth in the national income, the possibility of providing decent housing accommodation which is a most important element in the standard of living, the possibility of avoiding a severe slump in the future -- all these are bound up with developments in the field of construction generally and the field of housing particularly. The situation in this industry today, and the prospective developments over the next decade, are of concern not only to the home buyer and those who build homes, but to each and every person in the whole community.

There are sure grounds for believing that an acute housing shortage is in the making. For nearly nine years now we have not provided housing accommodation for the normal growth in occupancies. The accumulated effect of this shortage is only becoming apparent with recent improvements in general conditions. During the depression it was concealed by the practice of doubling up, the postponement of marriages, and migration back to the farms. At the same time many existing houses were allowed to deteriorate. Now, with rising incomes, undoubling is taking place; the marriage rate and the birth rate have picked up, and people are moving again from the farms to the cities. In reflection of these developments, the National Industrial Conference Board Index of New Rents has risen 39 percent from its low. Despite this substantial rise in rents and the recovery of property values, building has continued to lag. Instead of eating into the backlog accumulated in the depression the construction industry is not even providing as yet for normal growth requirements. In order to provide adequate housing accommodation by 1942 we should build some 800,000 new housing units a year. Actually we built only between 250,000 and 300,000 units last year, and it is doubtful whether we will build more than 400,000 units this year.

Before I mention some of the causes for this lagging of residential building let me point out some of the consequences. I need only mention the obvious fact that this has been a leading factor in retarding the rate of recovery and has resulted in an increase in the recovery

and relief expenditures the Federal Government has had to make. What is equally true, though perhaps less obvious, is that existing conditions are laying the groundwork for one of the worst building booms in history, on the basis of the most exorbitant rents and costs that have ever been experienced in this country. The longer a substantial volume of building is delayed the greater will be the potential danger. I need hardly remind you that a boom on the basis of high rents and costs can have only one aftermath -- collapse. And in a field as important as this a collapse is likely to pull the whole economy down.

But this is not all. Let us look at the matter from the point of view of the standard of living of the community. Rent comprises a substantial portion of the wage earners' expenditures and any further increases can serve only to make still higher the proportion. What will it profit wage earners to secure hard-won advances in wages when they find that the advances are offset by increased rents for the same living quarters?

We are prone to take for granted a steadily rising standard of living without inquiring too closely into the basis for this belief. Actually there is only one way in which the general standard of living can rise and that is by an increase in the production and consumption of real goods and services per head of the population. This hard and stubborn fact, though incontrovertible, is too often ignored or forgotten. We think too much in terms of money incomes

and not enough in terms of what the incomes will buy. People have even been so fooled by this fact that they have often thought of war time as being a period of prosperity, despite the withdrawal of millions of men from production and the diversion of productive work into destructive channels. The impoverishment of the community in real terms, and these are the only terms that matter, is concealed by the rise of money incomes, and consideration is not given to the more than offsetting rise in prices.

Farmers have become keenly aware of the importance to their welfare of the prices of things they have to buy. Labor, also, though perhaps to a lesser degree, appreciates the importance of prices in translating money incomes into real incomes. The recent interest by labor organizations in rising rents is evidence of this fact. Many responsible labor leaders realize that the possibility of achieving a higher standard of living rests, in the final analysis, on an increase in productivity. They know that a manufacturer who is running his plant inefficiently cannot pay as high wages, or secure as large volume of business, as he might. He is hurting not only himself, but the entire community. A trade union that insists that skilled workers should do work that could just as easily be done by unskilled workers is likewise hurting the whole economy. A shortening of hours not counterbalanced by increases in efficiency results in fewer goods being produced per person. I would not depreciate the importance of leisure. All I

wish to point out is that if productivity suffers, a price is paid for increased leisure.

Let me now return to my main theme and relate the problem of increasing the standard of living to the conditions in the housing industry. Since so large a portion of expenditures goes for housing accommodation, and since so large an element in the standard of living is the size and quality of a family's living quarters, it is vitally necessary that efficiency in home building should increase. It cannot, I think, be denied that efficiency in this field has not kept pace with that in other sectors of the economy. Indeed, apart from improvements in materials and in design, I doubt if any substantial improvements have taken place. The present trend promises little increase in efficiency in the near future.

The whole community, therefore, has a vital concern in the residential building field on two main counts. In the first place this field has been in the past, and threatens to continue to be in the future, one of the chief unstabilizing influences in our economic life. In the second place, an increase in efficiency or, what is the same thing, a reduction in the cost of new buildings under a stable general price level, is vitally necessary in order to raise the standard of living of the great masses of the people.

This, then, is the broad picture. Here is an industry in which the public has a vital stake. It has been a major unstabilizing force in the past, it has delayed and is still delaying recovery, it threatens

to upset the whole economy in the future, it is not providing decent housing accommodation at low rates, and it has not provided adequate and stable returns to those engaged in the industry.

What is the explanation of this state of affairs? It is largely historical. The organization of the industry and the practices followed by the various groups in the industry were once either largely appropriate to the technical stage of the industry or began as appropriate reactions to specific situations. The trouble is that an organization appropriate for the building of a simple residential house in the 19th Century becomes inappropriate for a skyscraper apartment house. Collusion between unions and contractors may have started to meet chiselers and then have developed for the purpose of achieving other, and less socially desirable, objectives. Nobody in particular is to blame. The industry is a very old one and unfortunately has gotten itself into a straitjacket and has developed an organization and practices which prevent it from meeting the requirements of modern times. Instead of developing in the direction of large volume at low prices the industry is more and more tending toward low volume at high prices.

In a machine age the industry is still in a handicraft stage. This is put aptly by Mr. Shire, technical editor of the Architectural Forum. "If we examine", he writes, "an ordinary house in process of construction we find there are delivered to the site on which this house is being built, twenty thousand to forty thousand parts or pieces of material, to be handled, assorted, rehandled, fitted, and fastened together. We find that

there are over a thousand items -- kinds of material -- to be ordered, received, checked, invoiced, and paid for; that there may be a hundred men working directly on the design and construction of that house; that these hundred men represent twenty different kinds of skills and specialized work; that as many as one hundred different firms studied the plans and prepared estimates of the cost of certain parts of the work; and that about fifteen different contracts were drawn up with the fifteen successful bidders.*

As long as the provision of housing accommodation is made along such lines it is going to be difficult to effect much increase in efficiency.

When we turn to some of the particular factors making for high building costs and high rents the vicious circle of high costs and low volume becomes even more apparent. Take, for instance, financing costs. Because of the small scale, highly-individualized nature of the industry, the risk of deterioration of a neighborhood, the high cost of servicing a small loan, and various legal restrictions, financing costs remain high. In addition, there may be a reluctance to endanger existing loans by making new loans for new construction at a low rate. This reluctance, while understandable, is nevertheless bad from a social point of view. I am, however, not blaming anybody. I am merely pointing out that this is but part of the vicious circle that the housing industry has gotten itself into. The erratic and unstable nature of the industry makes for high financing costs and high financing costs contribute to the instability of the industry.

The same picture is presented in an acute form in the skilled building trades end of the industry. The highly skilled nature of the work has favored organization. The highly unstable nature of the work has encouraged the organizations to maximize incomes by an attempt to get as much out of the few good seasons and few good years as possible. The result has been high pay for short working periods but over a period of years a low average rate of annual earnings.

The trade unions have not stopped with high hourly wage rates. The skilled trades have in many instances attempted to spread the work for themselves by instituting a short work week and by requirements relating to the use of unskilled labor. They have sought to spread the work over time by stringent requirements relating to apprentices and admissions to unions. The shortage of skilled labor, in conjunction with these various requirements, will probably prevent us from getting an adequate amount of building in the next couple of years. The same struggle for a limited amount of work and the development of a more complex type of structure have led to bitter jurisdictional disputes and to jurisdictional limitations which have increased the cost of building. I have heard of one instance where an electrician had to be employed all night at time and a half in order simply to push the switches that turned the electric lights on and off for a group of painters.

The same struggle to make hay while the sun shines, to get all you can while the going is good, has been true in lesser degree of material

and equipment makers and supply dealers. I have heard of cases, as doubtless you have also, where the supply dealers make arrangements with local unions whereby the latter would refuse to handle material bought from out of town. Building codes have been so worded as to necessitate the purchase of certain expensive materials when cheaper materials would have done just as well. Building codes have been used to further monopolistic practices.

Property taxes have been boosted in order to pay for building sewers and roads past vacant lots held for speculative gains. It is expensive to get clear titles to land. I could go on right through all the items making up the cost of the finished home, but it is not necessary. The general picture is one of loaded costs at every turn.

We are prone to think of monopolies in terms of very large business units. Monopolies and monopoly practices, however, are no less serious and are no more to be condoned if they are on a small scale and yet pervasive, as in the field of residential building. The result in both cases is restriction of output and excessive prices.

It would be easy to damn the whole industry by saying that it was shot through with rackets, monopolies and inefficiency. It would be easy, but it would be superficial and misleading. There is no reason to think that people in the building industry are any less honest or any less efficient than people in any other industry. Monopolistic practices engaged in by the skilled building trades, for example,

are on all fours with monopolistic practices engaged in by business men when the opportunity offers. The problem will not be solved by recrimination and abuse. It will not be solved by pointing out how actions of each group in the industry can be justified in terms of the situation concerning that group or by comparison with like actions of other groups. It will not be solved by the Federal Government putting up the money to build a few thousand housing units along traditional lines to be rented below cost to a few thousand fortunate individuals. It will be solved only by a broad attack on the problem participated in by all the groups concerned with residential construction.

This broad attack must be directed at two objectives, -- lower costs and higher average rates of return over a period of years for the building industry. Somehow, in some way, the industry must be converted into a large-scale mechanized industry, ensuring continuous employment and large volume at low cost.

It is not my purpose here to indicate how this might be done. I can only state it as my conviction that we now possess the technical knowledge to do it. If we fail to get low cost housing and in its place get a high cost boom it will be because we have failed to deal with the human and organizational side of the problem. We will have failed as a community to think the problem through. We will have allowed fear and suspicion, mistaken self-interest and monopoly to stand in the

way of a general rise in the standard of living, to delay the period of full employment, and eventually land us in a collapse that will cost the community billions of dollars in loss of income. And here again there is no real incompatibility between the public interest and the true interests of those whose fortunes are more directly bound up with the industry. Both would be served by the achievement of large and stable volume at low cost.

I have singled out the building industry for special comment, as the problems of common interest and concern in connection with that industry are so pressing. I do not wish, however, to give the impression that the problems in that industry are unique. The necessity of identifying private interests with the general welfare, and the necessity of ensuring that the precious forces of freedom and initiative will be directed into channels that will contribute to a rising standard of living for all, is present in every industry throughout our entire economy. We are all in the same boat and we will all rise or fall together.

The public aspects of every private action must be recognized and kept in mind. The provision of productive capacity, for instance, is generally held to be the concern only of ownership and management. Yet, when an industry in a strategic position fails to provide enough capacity to handle the volume of business that comes to it, the resulting retardation of general production and the advance in

prices affects the whole community. When business men combine for the purpose of diminishing fair competition, their action has wide repercussions on the public welfare. Similarly, when a labor union is successful in securing such an advance in wage rates or such a decrease in hours as to raise unit prices beyond a point that allows an adequate return to capital -- adequate, that is, to induce a continued investment in that industry -- the resulting advance in prices affects the rest of the community adversely.

Everywhere we turn we can find actual or potential clashes between private interests and the public welfare due to a failure to recognize our common goal and our common responsibility. This conflict of interests must be resolved if our system is to survive. One way out, and I for one sincerely regret its necessity, is public regulation. The other way, the way I hope will develop, lies in the assumption by private groups of responsibility to the general public and the adoption of far-sighted private policies to that end. This is not merely a pious hope. I think the trend of events can be directed in that direction. Let me illustrate my point by developments in the field of labor.

It is unreasonable to expect a small organization or group to be particularly concerned with the public interest. It would, for example, be expecting too much of human nature to expect a

particular labor union to forego a twenty percent advance in wages because such an advance would result in a one-half of one percent rise in the cost of living. Each union in the building field can point out that its wages make up but a very small portion of the total cost of a building. The same is true of all the other separate factors that contribute to the total cost. The public interest, in other words, will not be adequately represented as long as the disparity between the gains of the private group and the loss to the general public is so great.

This line of thought leads inevitably to the conclusion that the larger the organization and the more completely it covers the entire field, the more closely will it perceive the identity of its interests with the general public interest. I for one do not fear the consequences of general unionization of labor, provided it can be achieved as a disciplined movement, under responsible leadership, and without the use of intimidation or coercion in any form. I am hopeful that the more labor is organized under national leaders, the more the leadership will be compelled by the force of circumstances to adopt wider views and assume a larger measure of public responsibility. This appears to be the truly democratic way to the reconciliation of private interests and the general welfare, to the substitution of an

amicable way of solving difficulties for friction and disturbances. Such a situation will come to exist, however, only when labor generally is so organized that its leaders will realize that after a certain point the gains of labor are dependent upon increased productivity. Such leadership will recognize that a general shortening of hours not offset by increases in efficiency can only mean a lower standard of living for workers generally. It is not too much to hope that it will exercise its influence toward increasing the efficiency of management in general. It will, in other words, become keenly aware of and assume a greater measure of responsibility for movements in the general price level, for the standard of living and for the problem of securing as full and as continuous employment as possible of the human and material productive resources of the nation.

I am, as I have said, hopeful that the progress of unionization will have this result. At the same time I should like to utter a warning that if it does not, that if labor should regard any gain on any front and at any cost to the public as legitimate and desirable, our system will not work. The same is true of short-sightedness on the part of any important economic group in the community. If, for example, present trends in the building field are allowed to persist and if they are duplicated in many other fields, I am sure that the results eventually will be disastrous. There is one thing

our system will not tolerate and that is a series of disastrous breakdowns. If this occurs I am sure that the demand for increased public regulation all along the line will arise and that freedom and initiative will suffer.