(Dr. Currie)

(Original sent to Cong. Murdock on 8/5/39 Incl.) #UC 70

August 4, 1939

DEBT AND INFLATION

We are treated to a steady flow of oratory these days about the dangers lurking in our public debt, which, we are told, has reached a point where inflation and repudiation are inevitable. Most of this oratory sounds very impressive. The only trouble with it is that it never gets anywhere near the lowly level of facts. This is only natural, for if our orators would interrupt their resounding periods long enough to look at some pertinent facts, they would run the danger of suffering drastic deflation themselves.

Take, for instance, the glib statement that "rise in the public debt is inflation". What can this possibly mean? Inflation, according to ordinary common sense language, is a drastic rise in prices. The only possible relation between debt and inflation is through the effect of debt on prices. Let us look at the facts: The total public debt in this country today is almost twice what it was in 1929, and the debt of the Federal Government alone is about 2 1/2 times as great. And yet, the wholesale price index which stood at 95 in 1929, 1926 being 100, is only 75 at the present time. Obviously there must be something wrong with the idea that a rise in debt in itself constitutes inflation.

But this apparently isn't what the prophets of doom really mean. They don't actually try to prove that we already have inflation--

that would be too nonsensical for anyone to believe--but rather they warn us that "Some set of circumstances will set it off--don't ask me when." We have heard this precise warning for at least six years now. Perhaps the time has come when it is up to the orators to tell us "when". The same old warning repeated year after year gradually begins to lose its force when nothing ever happens.

But you will say six years is a short time. Maybe just a little while more and the inflation will be here. It is easy enough to check up on this notion by looking at the facts for another country where they have had a much longer experience of a high public debt than we have here. In England--a country incidentally much praised by critics of Administration policies in this country--the total public debt, including local units as well as the National Government, amounts to $1,050 per capita as compared with $450 in this country. In other words, the per capita in England is almost 2 1/2 times what it is here. Surely if there is anything in the theory that our debt is rapidly becoming so large that inflation and repudiation are just around the corner, England must already be engulfed in a disastrous inflation accompanied by the repudiation of her public obligations.

The actual facts are quite different. In the last five years England has been enjoying one of the most extraordinary periods of prosperity in her history. Prices have been steady; production has been at an all-time high; and employment is above the 1929 level. Government bonds are selling at remarkably low yields. And all this has taken place with a public debt almost 2 1/2 times as large as ours. In other words, when we have a public debt of $125 billions we'll still be short of the "crushing burden" under which England has enjoyed such extraordinary prosperity.

If inflation and repudiation are just around the corner, it is strange that the bankers, insurance company executives, and wealthy capitalists of this country are so stupid that they are willing to pay continually higher prices for Government bonds. Yield on the average long-term Government bonds recently got down to 2.07 percent, an all-time low, which means that the Government is selling its obligations on the most favorable terms in its history. And yet, we are told that the policies of this same Government are leading us to financial ruin.

What we are suffering from at the present time is a deficiency, not an excess, of demand for goods. As long as we have a deficiency of demand, or, in other words, a "surplus of commodities", prices instead of soaring to inflationary levels are going to lag in their present depressed condition. The distribution of purchasing power by the Government, through its borrowing and spending operations, tends to sustain demand at something like a tolerable level. But with the tremendous productive power that both industry and agriculture in this country have developed, the amount of purchasing power necessary to raise prices even by a small amount would have to be much greater than at present. As the money consumers have to spend increases, the flow of goods industry and agriculture will put on the market will also increase. Only when we have absorbed all of our idle men and resources and the factories and the farms of the nation are producing at full blast can there even begin to be talk of inflation.

But consider for a moment what would happen to the Federal Government's finances if we reached that happy condition of full employment and full productive activity: Tax yields, without any increase in tax rates, would increase so tremendously that the necessity for further borrowing to finance expenditures would automatically cease. If there be any doubt as to the accuracy of this statement I need only call attention to studies of the Treasury which show that the budget will be balanced with an $80 billion national income. This level of income, according to the estimates of experts, will still be somewhat short of the amount necessary to employ our men and our resources fully.

Putting the whole thing in a nutshell: Any increase in the total spending of the nation that would tend to make prices rise would call forth a tremendous increase in industrial and agricultural production. Slightly higher prices, together with increased production and increased employment, would mean larger incomes and hence larger revenues for the Treasury. The necessity for further borrowing would cease and the danger of inflation through further increases in the public debt would automatically disappear.