

May 18, 1938.

Dear Mr. Swope:

Because of your interest in the subject matter, I am venturing to send you the full text of a talk I gave last week before the New Jersey Bankers Association, which was an effort to appraise what seem to me to be the leading causes of the present economic situation and my own views as to how it could best be met.

As press reports are necessarily fragmentary, I felt you might be interested in seeing the full text.

Sincerely yours,

M. S. Eccles,
Chairman.

Mr. Gerard Swope,
570 Lexington Avenue,
New York City.

 ET:b

GENERAL  ELECTRIC
COMPANY

GENERAL ELECTRIC BUILDING
370 LEXINGTON AVE. AT 51ST ST., NEW YORK

GERARD SWOPE
PRESIDENT

May 23, 1938

Honorable M. S. Eccles
Chairman, Board of Governors
Federal Reserve System
Washington, D. C.

Dear Mr. Eccles:

Thank you for your letter of May 18, enclosing your address before the New Jersey Bankers Association in Atlantic City on May 13. I had read the portions of your speech printed in the papers, but was glad to have a copy of the complete address, which I took home with me and read over the weekend.

There are so many things in this that I should like to comment on that I do not want to include them in a letter, as it would make it too long. However, I am going to touch on a few of them, and then I hope sometime when you are in New York you will come and take luncheon with me, when we can discuss them, or if I come to Washington and it is convenient for you, maybe we can sit down and discuss these and other matters.

Starting right out in the beginning, where you say, at the end of the second paragraph, "Such a policy of maintaining a large volume of government expenditures, on the basis of a balanced budget and through a broad tax base, has been successfully pursued in England and some of the other democratic countries;" to this I say, very heartily, "Amen." I have discussed this question of a broader tax base with a number of people in high places in Washington but, like Mark Twain used to say about the weather, "We all talk about it but nothing is done about it," which is true even in the latest tax bill.

On page 6, you say, "the collection of \$1 billion of social security taxes in 1937 diminished buying power" etc. I suppose you refer to the collection of social security taxes for old-age pensions from individuals, and not from corporations. As a matter of fact, according to the figures I have, the total amount collected by the United States Government under the Social Security Act for the fiscal year 1937 was \$252,000,000, of which by far the larger portion was collected from the employers. And secondly, this went into the United States Treasury and was immediately put into circulation. Of course I admit that the individuals were not able to spend the money as they wished,

but it was deflationary only to the same extent that the payment of income taxes, etc. is deflationary. In situations like ours, where money collected by governmental agencies is immediately put back into circulation, in addition to borrowed funds, is it really deflationary?

On page 8, in your paragraph on public utilities, I think you have stated it truly, and very modestly.

In your opening sentence on page 14, you say, "As for the budget, the only road to a balance is through restoration of national income." Of course I interpret this to mean restoration of national income by increase in production and not increase in national income by increase in prices. And of course I heartily agree with you - which we discussed last fall in your office - in the desirability of a comprehensive program in the housing, public utility and railroad fields. Although the housing activity is going forward, it seems to me it is going very slowly, and I think one reason for it is the high price of labor and the failure to have made any progress on the suggested guaranteed wage over a period. Is this still to be regarded as hopeless?

In passing, may I call your attention to what I think is a typographical error in the fourth line of page 16, where you speak of the "first quarter in 1937." I suppose this means the first quarter in 1938.

Then also on that page, you say that with more abundant crops the outlook is for lower prices and hence lower incomes. The latter need not necessarily be true; with more abundant crops and lower prices you can still have increased income, and this will surely be true this year for a number of the farmers, although of course not for all. I think this is the trend to which we should look forward, both in industry and agriculture, that of lower prices for food, shelter, clothing and the conveniences of life, which will come about by increased production, and therefore be in position to supply to a much larger portion of our people.

On page 19, I think your position in regard to wage costs imposed on the railroads in 1937 is also sound, but unfortunately there does not seem much likelihood of accomplishing this just now.

On page 20, where you speak of output of electric power, and compare the percentage increases from 1929 to 1937, this is not an altogether fair basis, as I am sure you will admit, to take the point of starting as 1929, because of the low output in some of these countries in 1929, which is now just developing, for instance in Great Britain. In 1929 their output was 13 billion kilowatt hours, while ours was over 90 billions. Today our per capita use is 909 kilowatt hours, while in Great Britain it is still only 541. The only countries in Europe that had a greater per capita output than ours in 1937 were Norway, Sweden and Switzerland, where it is so largely a question of utilization of their water power in small and closely integrated countries. The per capita output in all

Honorable M. S. Eccles

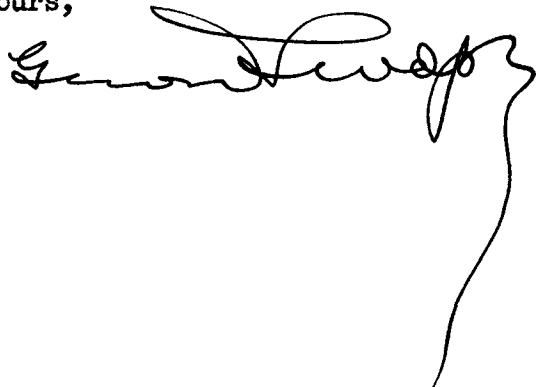
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other countries in Europe, including Great Britain, in Germany, Italy and France, is far below that of the United States. In this connection, my article in the March Atlantic - copy of which I enclose for your ready convenience - shows the price of electric energy stated in terms of the time a man would have to work to procure it in various countries.

You see from these few points I have made how much room there is for discussion, and I am sure you will wonder at my temerity in being willing to discuss such matters with you, who have made so much more of a study of these matters and know so much more about them than I do.

Cordially yours,

A handwritten signature in cursive script, appearing to read "George Dyer", with a long, sweeping tail extending downwards and to the right.

GS:H

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The citation for the original is:

Swope, Gerard. "Standards of Living." *Atlantic Monthly*, March 1938, Vol. 161, No. 3.

May 27, 1938.

Mr. Gerard Swope, President,
General Electric Company,
570 Lexington Avenue,
New York City.

Dear Mr. Swope:

Your letter of May 23d is particularly gratifying, reflecting as it does your penetrating consideration of my observations, even to catching a typographical error which eluded all of us here. I would welcome the opportunity, as you suggest, either here or in New York to carry on the discussion with you because letters are such unsatisfactory mediums for dealing with problems of the magnitude and importance of those which I know concern you as they do me.

This particular speech was by no means brief, yet could not cover these problems in adequate detail which is perhaps necessary to a more complete understanding. I could only touch on the more important aspects of the present situation and the outlook as I see it. The introductory paragraphs to which you refer had to be so much shortened that they may have failed altogether to convey what I had in mind. Possibly you might not say "amen" had I been more explicit. I have been driven inevitably to the conclusion that for social, political, as well as economic reasons there is no alternative, certainly for one who wishes to see capitalistic democracy preserved, other than the maintenance of a far larger volume of public expenditures for socially beneficial purposes than has been called for under past conditions.

The broader tax base to which I referred is merely incidental to this necessity as I see it. The point is that there must be an adequate flow of funds in order to keep up consumption and thus production and in order not only to discourage speculation, but primarily to protect both existing investment and furnish an outlet for new investment.

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I shall not attempt to pursue this very large theme here, but I should like to talk to you about it sometime, for it seems to me that where so many of my business and banking friends are deluding themselves is in clinging to the hope that mere "freedom of the capital markets" and "confidence", which so many identify with a balanced budget, would be sufficient under present day conditions to assure an adequate productive use of capital sufficient to be politically and socially tolerable and also to protect existing as well as to encourage potential investment. It is not necessary for me to tell you that I recognize the importance of the capital markets and that I am as desirous as anybody could be of seeing a balanced budget.

But where I part company with so many of my business friends, and hope I do not part company with you, is in thinking that these desirable things are sufficient of themselves to make this economic machine produce and distribute as it must be made to do if we are to continue to have the system which we want to keep. Nor am I one of those who supposes we have reached stagnation. It is because I am so firmly convinced that we can achieve and, I hope, maintain a far greater degree of prosperity than has ever existed before that I am so much concerned with the importance of taxation as one and only one factor in the maintenance of a more balanced flow of funds as between consumption and production on the one hand and capital formation on the other.

This is overlong, yet it is an inadequate treatment of the subject, but I felt I should mention it in case you had been misled by my references to a broader tax base.

Where your figures and mine apparently do not coincide with reference to social security taxes is that you are using figures for the fiscal year and I was using them for the calendar year. I was referring to the collections of taxes for old-age pensions under the Social Security Act and deposits by states of taxes collected for unemployment compensation during the calendar year 1937. The taxes for old-age pensions did not go into effect until January, 1937.

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Taxes collected from employers, especially when, as is usually the case, they are passed along in added costs (unlike income taxes), are as deflationary as the taxes collected from employees in the immediate effects upon the flow of purchasing power. While it is true, of course, that the expenditures of the Treasury add to buying power just as the collection of taxes diminishes buying power, the point, however, is, that the borrowings of the Treasury do not in general diminish buying power because they draw upon idle funds of investors or, as is the case when the Treasury sells bills, notes or other securities to the commercial banks, new deposits are created. If the social security taxes had not been in effect and the Treasury had borrowed an equivalent amount or drawn upon its cash resources for that amount, the buying power of the community would have been over a billion dollars higher than it actually was in 1937. In other words, the point I was trying to make was that in 1938 the government on balance spent approximately \$3,700,000,000 more than it took in, while in 1937 it spent only \$400,000,000 more; the net difference being more than \$3,000,000,000, accounted for largely by the bonus and the social security taxes. This was a very important deflationary influence by comparison with the inflationary trend from 1936.

As to budget-balancing, of course I agree that the national income should be increased through production on a reasonably balanced price level. It would be possible to get a balance through extraordinarily high prices but that would be as undesirable as abnormally low prices, which would have the opposite effect. In this connection I regret to say that as far as the annual wage question is concerned, it appears to be hopeless at present.

As to lower farm prices, I think that would be all right if it were balanced off by lower prices on the other side of the economy. As a practical matter, if the farmer's income declines rapidly, as it is now threatening to do, you get defaulted taxes and mortgages, the farmer doesn't buy automobiles, housing, etc., at the same rate, and while it is true that the

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industrial worker gets cheaper food, the farm standard of living goes down. While the farmer's gross income may be the same, if he gets less net income he has less to spend after meeting his fixed charges, and the result is an unbalanced condition, however it may be justified from a technical economic standpoint. However, this is assuming that if the farmer goes on producing more for less he can always find a market, which, of course, is not the case. Nor does industry operate on that basis. Either agriculture must be subsidized to make up the difference between domestic and world prices, or industry will be forced to give up tariff protection, because regardless of any technical arguments, as a practical matter agriculture will not long tolerate a free market for its products along side a protected market and rigid prices for organized labor and industry.

According to current estimates of the Department of Agriculture, farm income for 1938, counting in benefit payments, will aggregate about \$7,000,000,000 as compared with \$8,521,000,000 for 1937. Here is a drop of \$1,500,000,000 that, in my judgment, cannot help but have an extremely adverse effect.

I recognize that the figures on output of electric power are not altogether fair, as you correctly point out. I, of course, did not expect that we would equal countries that were far behind us in development, but the point I meant to make was that our expansion was less than we had reason to expect if it had not been for the uncertain legal status of the utilities and the government competition with them. With our capital and resources our power industry should and could be developed far beyond what it is now. We have natural water power, gas and oil, all of which are largely lacking in many of the European countries. Our population has increased a good deal since 1929. I see no reason why we should not have an output per capita much larger than that of other countries. Certainly our use of telephones, automobiles, radios and other modern conveniences is ahead of other nations.

Mr. Gerard Swope - (5)

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Your figures in the Atlantic article, which you thoughtfully enclosed, were very striking and are all the more reason for believing that we can continue to maintain and improve living standards above and beyond those of other countries. No one envisages the potentialities any more clearly than you have, I am sure.

At least it is just these considerations which have led me to the conclusion that we cannot rely wholly upon once valid theories of capital formation, investment, expansion, etc., under present day conditions, and that it is to the real interest of owners of capital to advocate governmental functioning like that in England, whereby a fairly steady and continuous flow of buying power is kept up to take off industrial production, protect existing investment and provide outlet for new investment. This buying power cannot be kept up by the continual expansion of installment credit, which should not increase relatively faster than national income. Otherwise we run into the very same things that have happened in the automobile field and other lines where consumer credit rapidly ran ahead of income in 1936 and 1937, but could not continue to expand or be sustained.

It was not my intention to burden you with so long a reply, but your own careful commentary both flatters and tempts me into it. I shall look forward to seeing you in Washington or New York, I trust at some early date, when we may discuss these questions more satisfactorily than is possible by correspondence. Let me add that I am genuinely indebted to you for your letter.

Sincerely yours,

M. S. Eccles,
Chairman.



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