

May 21, 1936.

MEMORANDUM

Introduction:

I appreciate the opportunity of meeting with such a representative group of business and professional men who show by their presence here that they are seriously interested in public questions.

My experience in public life is of rather short duration. My background, I am sure, was a good deal like that of many of you. Up until the depression, I had given little or no thought to public questions. I had spent twenty-two years in the business of making money, in conducting banking and business enterprises in the competitive field. I have known what it was to employ thousands of men and I have known what it was to operate successfully banking and business enterprises. With the coming of the depression, I was required to confront problems which were entirely new to me, and as the depression deepened, the seriousness of these problems dawned upon me. When I was put in the position of cutting salaries and wages, and of discharging or laying off faithful and old-time employees, I recognized at the same time that there was need for the services of all the men that were laid off because there were millions of people who needed and wanted the goods and services that they were able to provide.

I am not necessarily an altruist. I think I am a realist. I think the system of capitalistic democracy is, of necessity, an individualistic system, where there must be competition and self-interest. But at the same time, I think it has been brought home to us that our activities and our interests are much more closely associated with public interest than we had ever thought they were.

Old order solved problem of production:

Conservative estimates are that 20% of plant capacity was unused in the peak years of the boom; the lack of a market for more goods was the limiting factor; that is another way of saying that buying power lagged behind productive capacity; as the Brookings Institution has pointed out in its study, "Income and Economic Progress" (page 57):

"The consumptive requirements or wants of the people were far from satisfied during the period of our highest economic achievement. The value of the total national production of goods and services in 1929, if divided equally among the entire population, would have given to each person approximately \$665. There were nearly 6 million families with incomes less than \$1,000; 12 million with incomes under \$1,500; over 16 million with incomes under \$2,000; and over 19 million, or 71 percent of the total, with incomes less than \$2,500. A family income of \$2,500, at 1929 prices, was a very moderate one, permitting few of the luxuries

of life. Hence it was clear that the consumptive requirements, and especially the wants, of the masses of the people were far from satisfied."

Speaking of what appears to be at least one of the reasons for some of our difficulties, the same report goes on to say:

"As to income distribution and its results, we found . . . the proceeds of the nation's productive efforts going in disproportionate and increasing measure to a small percentage of the population--in 1929 as much as 23 percent of the national income to 1 percent of the people. We found the unsatisfied wants--needs according to any good social standard--of the 92 percent of all families who are now below the level of \$5,000 annual income sufficient to absorb the product of all our unused capacity under present conditions of productivity and still demand much more from such unexplored potentialities as might thereafter be opened up. We found the incomes of the rich going in large proportion to savings and these savings strongly augmented by others impounded at the source by corporations through the practice of accumulating corporate surplus. These savings, after providing for such increase of capital goods as could be profitably employed, we found spilling over into less fruitful or positively harmful uses, ranging from foreign loans (bad as well as good) to the artificial bidding up of prices of domestic properties, notably corporate securities.

"Thus, we began to discern the answer to our question whether the basic defect in our economic system, not discovered in the technical processes of production, is to be found in the way in which we conduct the distribution of income. The answer is affirmative: This is the place at which we do find basic maladjustment."

New order must solve problem of distribution:

If our business-banking leaders will apply to this problem, and to the social-economic problems confronting government the same degree of vision, courage and enterprise they have applied to their ^{immediate} own problems, we would have little cause for worry about the future.

The record of opposition by business-banking leadership in the past is not enviable; too often they have resisted rather than assisted whenever remedies have been proposed; organized business-banking groups have repeatedly fought remedial legislation that has subsequently been recognized as desirable and necessary, such as the income tax, child labor regulation, the Federal Reserve Act, the Interstate Commerce Commission, the 8-hour day and numerous other steps in the march of progress.

Depression accentuated by failure to adjust to changing conditions:

Most of us were too prone to believe in the late '20's that we were in a New Era, that prosperity would proceed without serious interruption; we could not foresee the economic chaos which overtook us; is it not likely that the disaster would have been mitigated had we faced and solved earlier problems which arose to confound us in the depths of the depression?

Is it not probable that if business-banking leadership had accepted and helped shape social-economic legislation which is only now being instituted, we would have better cushioned the collapse if, indeed, we could not have moderated the speculative extremes to which we were carried?

Orthodox remedies failed:

We tried them for more than two years; we clung to the gold standard; we tried to balance the budget, yet it steadily grew more unbalanced; Federal revenues steadily shrank at the very time when the burden thrust on the government became steadily heavier; we had the man power, the plant capacity and all the materials of prosperity; the processes of production did not collapse. I think it has become evident to all of us that it was largely the system of distribution that broke down; had we followed orthodox advice to curtail public expenditure while private expenditure was shrinking, the disease would only have been aggravated because that would have further restricted the very buying power essential to restoration.

National income, which is the most vital of our ^{economic} statistics, and out of which alone it is possible to collect the taxes to balance the budget, fell from \$83,000,000,000 in 1929 to \$39,400,000,000 in 1932, according to statistics of the National Industrial Conference Board, which in its volume, "Machinery, Employment and Purchasing Power," (page 83) computes the income per gainful worker (including unemployed) at \$793 in 1932, or less than at any time since pre-war days. The same authority computes, on the basis of the 1899 value of the dollar, that in 1932 per capita income for all of our people had fallen to \$176, the lowest on record since 1899--and their figures do not go back further than that. It seems to me incontrovertible that restoration of national income was the paramount problem to be met, compared to which all other problems were secondary. Although current direct estimates are not available, it would appear from other evidence that the national

income is running currently about 60 billions a year, which is about half-way back to 1928-1929 levels, and as a result of which, tax revenues in 1935, despite non-payment of part of the processing taxes, rose to \$3,857,000,000, a gain of \$2,000,000,000 above 1932.

Recovery would have been more rapid had we been prepared:

Odious though comparisons are, I cannot help contrasting our difficulties in the depths of the depression with those of Great Britain. As one magazine commentator has pointed out, the most reactionary party in Great Britain has been more liberal and receptive toward measures of government relief and recovery than either of our major parties; British business-banking leadership has, compared to our own, been less resistant to social-economic changes and more ready to help shape adaptation to changing conditions.

Or, as Professor Heaton of the University of Minnesota puts it in his informative book, "The British Way to Recovery,"

"The British Government had no such load to shoulder (as the United States) for many of the problems we are now tackling had emerged earlier and had been dealt with in a piecemeal fashion during the last hundred and thirty years. Much of the New Deal was part of Britain's Old Deal."

The Foreign Policy Association in its publication, Volume XI, Number 11, referring to Great Britain's acute difficulty due to her oppressive national debt and high rates of taxation, cites how much had been accomplished long ago by the British so that their problem of recovery was less complicated than ours, despite their huge debt:

"In spite of this vulnerable position, the economic life of the nation in the hour of crisis was not brought to the desperate standstill which confronted President Roosevelt in 1933. The lack of any spectacular boom in the 1920's saved Great Britain from collapses of stock exchange and real estate values such as accentuated the American crisis. Neither the trade depression nor the difficulties of the pound shook the centralized British banking system. Economic relationships did not require sudden compulsory reform, since the bargaining rights of trade unions had long been recognized by both government and employers, and numerous wage agreements provided for final appeals to government arbitration. Foresight in more normal times had provided widows' and old age pensions, unemployment insurance for the majority of industrial workers, and a national dole system and local poor re-

lief for the remainder; all of these constituted a bulwark against collapse of purchasing power and emergence of mass unrest far stronger than that of private charity or hastily organized relief of the United States. The government already possessed considerable regulative powers over industry. Railways were supervised under the Railways Act of 1921, which reorganized 120 companies into four great systems. The post-war depression in the coal industry had forced a licensing system of production for both foreign and domestic markets by the Coal Mines Act of 1930. The Electricity Supply Act of 1926 had inaugurated the generation of electricity according to a national 'grid' system under a Central Electricity Board appointed by the Minister of Transport. The Export Credits Guarantee Department of the government employed a revolving credit of 25 million pounds to aid the British exporter by guaranteeing the solvency of the overseas buyer in his own country up to 75 per cent of his contract. Moreover, Britain's unitary system of government and the supremacy of Parliament precluded voiding of legislation by the judiciary on the ground of unconstitutionality or interference with states' rights."

Recovery must be continued and preserved:

Much depends upon enlightened business-banking leadership and willingness to face public problems with open-mindedness and readiness to help find the solutions, much as British conservatism has, in its own interest and for its own preservation, been prepared not only to accept, but to shape, rather than to resist altogether, social-economic modifications and adaptations to changed conditions.

Outlook one of great promise:

Granted enlightened leadership, prepared to face and find practicable, workable solutions, particularly solutions for the vital problem of distribution, there is every reason for believing that we can move on as a nation to a far greater and a more stable, orderly economic progress than we have heretofore experienced; we must not be deluded into supposing that we can move onward by the let-nature-take-its-course attitude prevailing in the post-war years, nor, at the other extreme, is there the slightest justification for the fatalistic, defeatist spirit growing out of our late disillusionments.

vergent as those that characterize our debtor and creditor areas, our South, East, and Middle West. There were no groups quite comparable in their influence to the veterans, the silver bloc, or the embattled farmers, though some are gathering strength now that the country has embarked on a policy of tariffs, quotas, and subsidies.

"More important still, there was little lingering faith in any doctrine of economic individualism or in the sanctity of inalienable natural rights where economic matters are concerned. The theory of natural rights went overboard early in the nineteenth century; in fact, it never got its feet so firmly planted on the political deck in England as in France and the United States. Experience with the new economic order of industrial capitalism soon showed that the rights of all individuals were not best fostered by a policy of laissez faire. As society grew more complicated and interdependent, the need for control at vital points made state action inevitable. Hence both the old political parties have long lists of social legislation to their credit, and while the Labor party accuses them of being 'tools of the capitalist class' its practical program, as distinct from its ultimate objectives, differs only in degree from those of its opponents. In the eyes of all, rugged individualism is an ideal unsuited to a world in which men live and work close together."

As for British taxation, the same author, referring to the reduction in British taxes which was finally achieved, points out (page 52):

"This first installment of reward for patience in suffering still leaves the British tax burden heavy beyond North American comprehension. Suppose you were a married man with one child. If you were a university head, your income tax on a salary of \$10,000 in 1931 was \$1,765; it is now reduced to \$1,585, which is 15.8 per cent of your salary. If you were a university professor earning \$5,000, you would have paid \$640, but will now pay only \$575, or 11.5 per cent of your salary. If you were a lecturer getting \$2,500, you would now pay \$125 (5 per cent) instead of \$140. If you were a 'big business executive', earning \$50,000 a year, your income tax and surtax combined would now be a mere \$17,425, or 35 per cent of your salary, instead of \$19,360. If you were unmarried, your payments would be somewhat higher. Even a single artisan earning \$1,000 a year pays \$34 in income tax."

Opportunities for business and banking enterprise:

Especially in housing; with vast unused human and material resources and a poorly housed nation; the opportunities in this field alone are a direct challenge to business-banking leadership as well as a refutation of the notion that we must always have a "dole" and a permanent army of unemployed; stagnation in the building field during the depression years has resulted in an enormous shortage; millions of our people lack electric lights, modern plumbing and other improvements; millions live under conditions of unhealthy overcrowding.

A downward trend of residential construction began in this country in 1928 and continued at a steadily accelerating pace until 1934; in 1933 it reached the lowest level since the end of the World War; for the three years 1932, 1933, and 1934, it represented only about 10 per cent of the average of 1926; it began to rise in 1934, and during the past year has steadily increased, but it is even now going on only at the rate of about 20 per cent of the pre-depression figure; variety of computations have been made and published, some of them placing the estimated requirements over the next decade up to 14 or 15 million units. If we put aside what appear to be the more extreme estimates, and take those which have the virtue of moderation, we find that even if we assume a surplus of 700,000 dwelling units to have existed at the end of 1929, we now have a deficit of not less than 2 million units resulting from the discrepancy between the small number of replacements and additions during the depression in relation to an average yearly increase of some 475,000 to 500,000 in the number of families; if we project the requirements over the next 10 years, say to the end of 1945 or the middle of 1946, the total provision of new housing called for, in order to take up the accumulated deficit, meet the net increase in number of families, and replace, say, but 75,000 houses a year that may certainly expect to burn down, or be torn down, or be otherwise withdrawn from use, we shall have to average approximately 760,000 new dwelling units per year, or a total for the 10 years of more than 7-1/2 million.

What this means in the way of further industrial recovery and employment can be judged from the British experience of recent years. The relative prosperity that Great Britain has enjoyed during a corresponding period of depression in this country has been attributed in the main to the country's extensive program of small-house construction.

During the past 5 years the number of houses built in England and Wales totaled 1,179,294. The number built in the United States during the same period is estimated at about 700,000. Had we built at the British rate in proportion to our larger population we should have produced during the same 5 years 5 times as many houses as we actually produced, or 3,500,000.

Where are the funds to come from to finance the home-building that will be required for these three-quarters of a million or more houses that we shall need to build each year on the average over the next 10 years? The answer is that the funds are to come in the main from the banks, unless the banks are to relinquish to other agencies a large proportion of the savings now held by the banks. It would appear that at the present time the national banks, the State member banks of the Federal Reserve System, and the non-member insured banks have the authority, under existing law, to make real estate loans up to a total of approximately \$9,100,000,000. Their outstanding loans on real estate are approximately \$3,300,000,000. Thus there is legally available from this source an additional \$5,800,000,000.

In addition it is estimated that life insurance companies and mutual savings banks hold something like 4 billion dollars in cash or United States Government securities over and above the proportion of their total assets held in these forms from 1925 to 1931. From this it may be estimated that, if the portfolios of these institutions were to return to more normal distributions, they would be able to absorb with their present resources, given appropriate conditions, something like \$2,900,000,000 of non-farm mortgages. An additional \$100,000,000 may be estimated to be currently available in the idle funds of building and loan associations. This might be increased to some \$400,000,000 if the potential borrowing power of these associations were availed of through membership in the Federal Home Loan Bank System.

New frontier is at home:

Let's have world trade, but let's have a bigger market at home, which can be developed by solving the distributional problem as exemplified by various studies of income, all reflecting the concentration of individual and corporate income in relatively few hands.

Taxation is necessary not only to balance the budget and to pay down the depression-incurred debt as recovery proceeds, but to prevent accumulations of idle funds from spilling over again, as they did in the late '20's, into speculative excesses; hence the principle of taxing corporate surplus that is diverted into speculative and unproductive channels deserves to be seriously considered by business leadership; this is an integral part of the mechanism necessary to produce a more orderly economic progress in the future, in conjunction with banking and monetary policies.

Conclusion:

Broadly speaking, the effect of government intervention on a comprehensive scale in the past three years has been to meet the problem of distribution so that production could be revived; that intervention served to stop the process of forced liquidation caused by deflation, to restore purchasing power, to replenish bank deposits, and to bring down long-term interest rates in order to encourage and make profitable the use of capital for new enterprise and to adjust, through refunding, a substantial portion of the existing debt structure on a supportable basis; national income has been restored by some 50 per cent; industry and finance have been enabled to improve greatly their position through increased earnings, adjustment and reduction of debts and refunding on more favorable terms; favorable long-term interest rates are available for financing in practically every field; rents have risen, hence real estate values have increased; the index of commodity prices has remained steady for more than a year. The cost of intervention has been small compared with restored values. The point has been reached where the budget can be balanced, with increasing taxes, out of restored incomes, and the outlook is altogether very encouraging.

It remains for business and banking leadership to take full advantage of the opportunities that the restoration has once more presented to private initiative; as rapidly as private enterprise takes over the task, government can withdraw from the picture; looking ahead, the fundamental problem which bankers and business men must, in their own interest, solve is the problem of distribution; it will be solved by the same spirit, ingenuity and courage that triumphed over the problems of pioneer days, that demonstrated to the world the potentialities of the country's productive genius. These great potentialities of raising the standards of living of all of our people to steadily greater heights can be fully realized only when our business-banking leaders face fairly and squarely the problem of distribution--which, it seems to me, is the great challenge to the modern world.