

WADDILL CATCHINGS
CHRYSLER BUILDING
NEW YORK

One East 54th Street

February 23, 1945

Mr. Marriner S. Eccles, Chairman
Federal Reserve System
Washington, D. C.

Dear Mr. Eccles:

I have been greatly interested in the reports of your suggestion of a tax on the profits of speculation. I am quite sure that you will find it interesting to read the enclosed memorandum on that subject which expresses the views that I have formed as a result of long and wide experience in mining, manufacturing, merchandising and in the investment and banking business.

May I say to you that I think the Federal Reserve Bulletin is possibly the most valuable and informative economic publication of the day. I congratulate you most heartily upon the manner in which you have developed its form and substance in recent years.

Yours faithfully,

A handwritten signature in black ink, reading "Waddill Catchings". The signature is written in a cursive style with a large, prominent initial "W".

February 27, 1945.

Mr. Waddill Catchings,
One East 54th Street,
New York City.

Dear Mr. Catchings:

This is to thank you for your letter of February 23 enclosing the copy of your memorandum, which I was particularly interested to read not only because of your apt use of words, but because I recognize the keenness and accuracy of your observation. I had not previously seen the capital gains tax discussed from this illuminating standpoint. I was especially impressed by the way in which you draw the distinction between productive investment and speculation.

I was likewise pleased to have your favorable comment on the Federal Reserve Bulletin. For a good many years I have sought to have it a medium for informative and, I hope, challenging discussion.

Sincerely yours,

M. S. Eccles,
Chairman.

ET:b

A WAY TO GET RID OF GREAT DEPRESSIONS

By a simple Act of Congress, the American people can make certain that never again will a great depression occur in the United States.

We know what causes depressions. Any doubt about that was settled a few years ago when Carl Snyder published "Capitalism the Creator". Snyder during more than eighteen years was engaged in factual research and exploration as head of the statistical work and the economic investigations of the Federal Reserve Bank of New York.

Booms and depressions are the result of speculation - wild speculation in securities, land and commodities. Speculation has turned every period of prosperity into a boom followed by a depression. There are excellent records which go back more than a hundred years, and cover the great booms which burst in 1837, 1857, 1873, 1893, 1907 and 1929, and the smaller ones in between. What happened in 1929 is fresh in our minds.

In free enterprise there are two separate and distinct ways of making money. One is to engage in the production and distribution of goods and services either as a worker or as an investor. The other is to speculate: to seek a profit merely by buying at one price and selling at a higher price - the way commonly known as "playing the market."

In speculation no merchandising, no transporting to market, no fabrication, no cultivation, no improvements take place. Money is made or lost merely by a change in price between the time of purchase and the time of sale - just that and no more. Wild speculation occurs in stocks and bonds, real estate

and in such commodities as wheat, corn, cotton and metals for which there are public markets and storage facilities.

Speculation is not to be confused with speculative enterprise. That is something quite different. The United States has grown great by speculative enterprise.

To engage in commerce, industry and agriculture under conditions involving great risk of loss as well as great possibility of profit - that is speculative enterprise. Exploring for metals or oil, developing a new product, a new process or a new invention - these long chances in business are called speculative. Such activities are part of productive enterprise, and may readily be distinguished from speculation, which is no more than "taking a ride" on prices whatever the risk may be.

When we speculate we just look for something with a price which we believe will either go up or go down. On the "long" side of the market we seek something of which there is less than buyers will want at current prices. In real estate we try to acquire land that will be needed for residential, industrial, agricultural or other use. In metals we look for one which will be scarce in relation to the needs of manufacturers. In the field of agriculture we look for crop failures, or anything else which will put up prices because supply is less than demand. And in a "bull" market on the stock exchange we just look for prices which will go up.

When we play the "short" side of the market, we seek something of which there will be more for sale than buyers will purchase at current prices: bumper crops; overproduction of metals; stocks or bonds which are selling "too high". As "bulls" - we buy, we hold, we sell. As "bears" - we sell, we wait, we buy.

For fifty years or more the stock market has been the favorite field for speculators. However there is speculation a plenty in land and commodities. The following is a list published recently by the largest organization furnishing services throughout the United States for playing the market on rising and falling commodity prices: barley, butter, cocoa beans, coffee, copper, corn, cotton, cottonseed meal, cottonseed oil, eggs, flaxseed, hides, lard, lead, oats, onions, pepper, potatoes, ribs and bellies, rubber, rye, silk, soy beans, soy bean oil, soy bean meal, sugar, tin, wheat, wool and zinc.

Without the prospect of profit there is no purpose in speculating. So Congress by a tax can take away the incentive and end the practice - a tax say of 90 per cent on the profits of speculation.

The people have always taken speculation as a matter of course, for they like the idea that anyone may "get rich quick" by a fortunate turn of the market. The hope of some day "hitting the jack-pot" is deep rooted in the adventurous American spirit. But the people do not realize that depressions are the result of speculation.

Other forms of gambling affect only those who participate. No more than the transfer of money from one person to another is involved in lotteries, slot machines or betting on horse races. Playing the market, however, is the buying and selling of things which people use, or of securities which represent

their investments. These activities interfere with the operation of the law of supply and demand, and with the circulation of money in the production and distribution of goods and services.

There is no trouble about enforcing the tax. Even now speculators are required to report their profits. And the Bureau of Internal Revenue and the Department of Justice have ample power to take care of tax dodgers.

Today the tax laws are more favorable to speculators than to those who engage in production and distribution. The so-called "capital gains" tax is supposed to stimulate investment, but it applies only to the profits of speculators and to those of investors who sell their investments. Speculators who wait for six months need pay a tax of only 25 per cent of their profits however large these may be. All workers and those investors who receive capital gains in the form of interest, dividends, salaries and profits other than from the sale of investments, are now subject to taxes which reach as high as 90 per cent.

In the proposed tax law speculation would be so defined as to exclude any activity which is part of the process of production and distribution. The tax therefore would not apply to "hedging", which is really not speculating but protecting a profit in production or commerce; nor to "making a market", which is acting as a dealer or trader engaged in distribution.

To restrain speculation and still not interfere with investment is easily accomplished. With respect to the sale of real estate the statute would provide that the tax not apply to any part of a profit that arose from improvements made upon the property. Thus a distinction would be drawn between gains due solely to enhancement in price and those due to capital invested in improvements.

With respect to securities a similar method would be used. From the profit realized upon the sale of a security there would be deducted so much of the profit as might be attributable to a corporation's earnings between the time of purchase and the time of sale. Thus if a share of stock were sold at a profit of ten dollars, and meanwhile the corporation had earned but not distributed six dollars a share, the tax would apply to only four dollars of profit.

If the tax on the profits of speculation should restrain somewhat the investment of capital the harm would be small in comparison with our present income and profit taxes. The growth of industry and agriculture in the United States has been the result mainly of plowing back the earnings of successful enterprise. More than four-fifths of our capital today was accumulated in this manner. Taxes today take away most of the opportunity for such capital accumulation, particularly for the small businessman.

There will be much opposition to the proposed tax. Some can be met and disposed of by argument. But antagonism to the bitter end may be expected from many persons who will do all they can to force us to go on with our planned economy.

The opposition of the New York Stock Exchange will not be as vigorous as you might expect. Many members will see from the outset that they will gain by conducting only a great market place for investors, and not also an arena for speculators. Their business will be better without rising to the heights of 1929 and falling to the depths of 1932.

The main fight against the tax will be waged by believers in communism. They want the United States to have another great depression. They are sure that capitalism will not survive another experience like 1929 and the years that followed.

They see a real opportunity in the present ownership by the Government of vast plants throughout the United States - what Mr. Jesse Jones has called "Uncle Sam's Industrial Empire". In the construction of these plants businessmen have put their utmost in the all-out effort to win the war. The factories are built to make use of the latest processes of manufacture; they are equipped with the most recent design of machine tools, driven by power in the most efficient form; and they are skilfully laid out for mass-production. In another depression the Government will not put the unemployed to work raking leaves and digging ditches - not with these plants ready to produce what the people need.

In a communist state there is no wild speculation, and there are no depressions. Last summer at his meeting with Eric Johnston, president of the United States Chamber of Commerce, Stalin made the challenging statement "depressions come to capitalist countries."*

Later in the same meeting Stalin said "the greatest problem that will confront the American people after this war is to avoid unemployment and thereby prevent another depression." That is the planned economy method. The free enterprise method is to prevent another depression and thereby avoid unemployment.

* Reader's Digest, October, 1944.