HUGH W. SANFORD,
FIDELITY BUILDING,
KNOXVILLE, TENN.

February 27, 1945

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

Mr. Henry W. Morgenthau
Secretary of the Treasury
Washington, D. C.

Gentlemen:

The recent suggestion by Mr. Eccles, which I understand has been approved by Mr. Morgenthau, that something should be done to stop people from making money on the rise in the selling price of stocks has filled me with dismay, and I think has had the same effect on a great many other people in the United States. The psychology of the investor is being hammered into pessimism, it would seem, on every occasion when the investor has some reason for being slightly optimistic.

I, and many others, purchased some first class securities in 1937 at a time when the Dow-Jones average of stocks was around $190 a share. In 1929 this same Dow-Jones average reached a price of $380 a share. But, since the value of the gold dollar has depreciated approximately 40% in the meanwhile, the value of stocks in present-day gold dollars in 1929 would have been approximately $630, because 60% of $630 equals approximately $380. At the very bottom of the depression, for a short time the Dow-Jones average fell as low as about 60. By the middle of 1933, after the panic was somewhat over, the Dow-Jones average reached approximately 105. We were then in very bad times indeed. By 1937, business got fairly going, but nothing exciting, and in 1937 the Dow-Jones average went as high as 192.

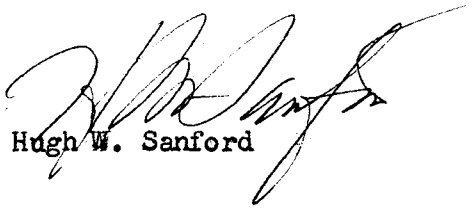
In 1937 a great many American investors thought we were on the way partially back to old levels, although we did not expect to receive the $630 a share value in gold dollars of 1929. However, we were all very much disappointed in what happened, and to-day the Dow-Jones average is approximately only 160. Now this average is not back to what it was even in the last half of 1936.

Just at the time when we had hopes that enough interest would be shown in the stock market to bring us back at least to the 1937 level, where we could get out without a loss and perhaps make a few pennies, we are informed that you two gentlemen are going to try to do something to prevent the stock market from going higher, and are ready to propose a measure by which the profit on increased values of stock will be very heavily taxed. This is quite contrary to what I regard as the wiser practice of England and Canada to place no tax whatever on capital gains, and it seems to be done with the idea of keeping people out of the stock market. To be sure, the in-and-out speculator did not buy his stocks in 1937 or in the higher years of the 20s, but the point is that if we do not have people willing to invest in the stock market in order to make a profit if the market goes up, the general market will almost inevitably go down, and the result will be that we holders of the securities that we bought at these higher values in previous years, if we attempt to sell our holdings, will incur a loss instead of a gain.

Personally, I think that all this is a great mistake, and I think that anything you gentlemen do to discourage the business man worse than he is already discouraged

by what has already been done is a mistake. I think that the things that are now proposed may cause the business man to draw into a hole and never come out again, and many things that have been done to date make him exceedingly pessimistic. Therefore, I hope that you gentlemen will reconsider the question of taxing capital gains, and instead of increasing the tax, I hope that you will follow the English and Canadian lead and cut out this tax altogether, which to my mind would be a far wiser course and would be for the benefit of the country in the long run. If the business man is not allowed to make money in any way by the use of his brains, he might as well commit suicide or else retire, and more and more I find that my friends are getting disposed to do this very thing - namely, to retire and quit. There is certainly no incentive left to go into any new business or expand an old one. I say this with some authority, because I am chairman of the board of two manufacturing companies and a director of others. Of course, if we are going to end up in national socialism, and turn over all of our savings and investments to the so-called "forgotten man" before the thing is done with, it makes no particular difference what is done at this stage, and to make the capitalistic class more pessimistic than ever may perhpas merely have the effect of reducing the shock when the ultimatum finally is delivered to the thrifty and to the industrious and to the creative people of this country.

Yours very truly,



Hugh W. Sanford

HWS:R

March 5, 1945.

Mr. Hugh W. Sanford,
Fidelity Building,
Knoxville, Tennessee.

Dear Mr. Sanford:

In reply to your letter of February 27, I am enclosing a copy of a statement which I have just issued to explain my proposals in regard to a capital gains tax. I gather from your letter that you have been misinformed as to the nature and purpose of my proposal and trust that this statement will clarify the matter.

I am concerned particularly about capital values of farms, homes and businesses and not so much concerned about Dow-Jones averages. However, I question your use of the word "investor". I, for one, would not care to see another 1929 inflation which would inevitably be followed by another collapse. Your desire to get out at the top of the market is, of course, entirely understandable, but if you do and somebody else buys the securities you sell and those of others equally eager to get out at the top, then while you and they may gain, the purchasers stand to lose when the bubble bursts. I have spent a great many years in business and banking and I fail to see how that process contributes anything to production, employment and economic progress. I think one of the surest ways to end up in national socialism would be to let another inflation take place, with its inevitable aftermath of ruinous deflation.

Sincerely yours,

M. S. Eccles,
Chairman.

Enclosure

ET:b

HUGH W. SANFORD.
FIDELITY BUILDING.
KNOXVILLE, TENN.

March 8, 1945

Mr. M. S. Eccles, Chairman
Board of Governors of the Federal Reserve System
Washington 25, D. C.

Dear Mr. Eccles:

I have your letter of March 5 in reply to my letter of February 27.

I may have misunderstood your intention somewhat, but I think you have misunderstood my letter. You say, "Your desire to get out at the top of the market is, of course, quite understandable." If you can find any such suggestion in my letter, I am unable to do so myself. In the beginning of the fourth paragraph on page 1, I did write, however, "we had hopes that enough interest would be shown in the stock market to bring us back at least to the 1937 level, where we could get out without a loss and perhaps make a few pennies". As I also stated in my letter, the Dow-Jones average in 1937 of $190 a share in devalued dollars was the equivalent of approximately 32% of the high reached in the same value dollars in the year 1929. Therefore, what I suggested was desired by the investors was that they should receive about 33-1/3% of the price you have said I am anxious to obtain.

As to the question of the 1929 inflation, with your devalued dollars and with your national income running 160 billion dollars a year or more, your wage-scales and price-scales - if this continues after the war - may be inflated as much or more than they were in the late nineteen twenties. It seems rather strange, therefore, to peg wages and prices at a very inflated scale to maintain this national income, and at the same time let everybody get the benefit from the decrease in the purchasing power of the dollar except the people who own stocks.

However, the last remark is somewhat beside the point, because I have not intimated that anyone wanted to see a general inflation, followed by a collapse; but I think the business men are entitled to receive their share of the advance that is being given now to industrial workers and farmers. At present they certainly are not getting it; they are getting the hot end all the way through, as the figures show. For example, if you will take the profits of industry to-day after taxes, and then follow through to the individual owner and take what is left after he pays his taxes on the dividends, and calculate what his purchasing power will be of the total national production, you will find that it has slumped off terrifically, whereas the laboring classes and the farmers, as groups, are getting far larger percentages of the total income than they did before World War #2.

You perhaps do not realize how discouraged the business men to-day are on this situation. Since the corporations in which they own stock have to earn about three times as many dollars for them to obtain as much actual buying-power from the dividends as they used to be able to get from their dividends, and since they are not getting anything like this additional sum, and since it costs fifteen to twenty cents to get one's shoes shined, and since every time the business man tries to bring himself up to a parity with the rest of the population he is given a "swift kick", so to speak, it is obvious that the business man is very much discouraged to-day and very pessimistic about the future. But from what you say, I presume that you do not think that it makes any difference whatever to the future economic prosperity of the country as to how the business man feels, or what discouragement he may suffer that will prevent him from trying to develop progressive methods for producing goods. But, again, I am not talking about running an inflation bubble up to the top and then puncturing it. I am talking

about something far different, and something that is happening to-day; and if you will re-read my letter I think you will find you have misjudged entirely what I said in it.

This subject has many ramifications, and what you say could be discussed in a letter of a good many pages, which I shall not attempt to do. But I do wish to say that I have spent a good deal of time studying these matters, have written two volumes on economics and a good many pamphlets on this subject, and I would venture to say that I have spent more effort and time and burned more midnight oil in considering these things than any non-professional economist who is now in Washington, and if I do not have a grasp of the subject it must be that my mental capacity is below par.

By the way, if you would like a two-volume set of my book on economics, covering considerable ground, I shall be very glad to send this to you with my compliments, although I am not sure but what I sent you a set several years ago.

Yours very truly,

Hugh W. Sanford

HWS:R

Not in Cong Bd

March 14, 1945.

Mr. Hugh W. Sanford,
Fideltiy Building,
Knoxville, Tennessee.

Dear Mr. Sanford:

This is to thank you for your letter of March 8 which I was interested to read. I trust we do not misunderstand each other. I had not intended to misread your previous letter.

The question you are raising about distribution of income is, of course, a very different and far-reaching one. Inasmuch as I spent considerably more than twenty years of my life not only in banking but in a widely diversified range of business interests, I am entirely conversant with the problems and discouragements to which you refer.

Because of your interest and studies in economics, I am venturing to enclose copies of some of the material expressing my own viewpoint, though I have not attempted to write a book.

You very kindly have offered to send me copies of the two-volume set of your book on economics with your compliments. I am very appreciative of your offer, but since we have an extensive library and arrangements to obtain published material from other governmental libraries, including the Library of Congress, I do not want to impose upon your kindness.

Sincerely yours,

M. S. Eccles,
Chairman.

Enclosures 5 (NICB speech; Tax Institute; Price Control Act statement; Chicago Investment Bankers speech; NICB of 1942.)

Er.

March 21, 1945

Mr. Gilbert H. Montague
67 Wall Street
New York 5, N. Y.

Dear Gilbert:

Your pamphlet entitled "A Proper Government Labor Policy" brings out what seems to be the true attitude of the Government in Washington towards labor, as compared to its very different attitude towards capital, but I do not know that there is anything that can be done about it. The people in charge all seem to be bent on disorganizing the capitalistic system, which has brought this country up to where it is, and are insisting on re-distributing wealth and taking away all incentive from the people who are thrifty, saving and enterprising - namely, from the people who have developed this country against the almost unceasing opposition of labor for the last fifty years or more to every improvement of method which would increase productivity and increase the standard of living of the masses. The labor unions even seem to think that they are responsible for the increased standard of living in the last fifty to seventy-five years, that has increased to the masses about 400% during this period, whereas the fact of the matter is that labor has constantly cut its own throat and has done everything, legal and illegal, to fight labor saving devices. And since labor has been organized, it is doing everything it can to reduce the output of the factories, with the fallacious idea in mind that this prolongs jobs, and therefore is for the benefit of the laboring classes.

I was talking yesterday to two men connected with a large structural steel plant who have about 900 men employed, and they were telling me the way they were being plagued to death by labor unions, and the unholy practices of the labor union gangs that res lted in their being able to operate only very inefficiently on their war contracts. To illustrate, they told me that if they had men working for them who would do the same sort of a day's job that they did before labor unions came into power, they could turn out just as much output with approximately 40% fewer employees. They state that the men are loafing on the job all the time and refusing to turn out a decent day's work. This is merely a commonplace, however, because the same thing is happening in my own factories, in knitting mills here in Knoxville, in the coal industries with which I am acquainted, and it is a general situation throughout the country.

In this plant, for example, they had a piece-work system on a certain job where men were turning out four or five pieces per day. The management estimated that a reasonable output was seven or eight pieces a day. It was an electric welding job, and they had about 300 electric welders employed. They finally got two men who were released from another plant and who did not know the union procedure of holding down output, and the first day these men turned out seven units and the second day eight units, and the third day they were told that would either have to get out of the plant or reduce their output. Another example of union practices was this: They had a breakdown job in the plant, and the foreman designated two electric welders to do the work necessary. This they did, each working about six hours. The next day they were waited upon by the union, which claimed that another welder in the plant had priority and should have been given the opportunity of doing this particular job instead of the men

selected by the foreman, and that therefore this man should be paid for six hours of overtime work that he did not do, because he had not been given the job originally. This money was paid out to prevent a shut-down of the plant by strike to enforce this unreasonable demand. This, of course, increased the cost to the Government on the Government work then being done, and illustrates that what organized labor is doing to-day is to run up costs as high as possible on Government contracts.

I was at a meeting of the board of directors of a company the other day that operates in steel, and whereas before the labor unions got hold of the plant about two years ago, the percentage of pay roll to sales was approximately 22%, it is now 37%. I have been told that the same thing is true in the large underwear factories and knitting mills here, and yet we are told that they are doing a good job, etc., etc., ad nauseam. If some of these persons in Washington who say these things, or believe these things, or pretend to believe these things, would go around the country and get a record of the way labor unions are slowing down production, increasing costs, and therefore reducing the standard of living of the average worker, they might possibly - if they were not too politically minded - try to improve the situation. However, it seems to be hopeless as it is. As far as the capitalist is concerned, it doesn't make any difference to him how inefficient his men are and how large the wage scale is, because he will add his measure of profit anyhow to the cost. The effect therefore of this constant struggle for higher dollar wages and less production per dollar of wages finally comes back on the masses of the people. The ones who suffer particularly are the white-collar class and the unorganized labor, and also the farmers would suffer except that they seem to be able to take care of themselves in these days and times by getting as much more unearned increment, perhaps, as some of the labor unions which control the transportation of the country, etc., and which therefore are able to hold up the country at large in their demands for more pay and less work.

except in this period O.P.A. kills the idea that it is wholesale merely in reducing profits from leaving money

Mr. Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System, has recently sent me some of his addresses, and I think that you might be interested in reading them, and I also suggest that you send him a copy of your pamphlet. Mr. Eccles is a fair-minded man, no doubt, and he has also had business and banking experience, but this does not mean at all that he is a trained economist, to my mind. In fact, I have talked to many bankers and business men, and I don't think one out of a thousand knows the first principle of political economy. I have yet to ask a banker what the significance of the gold standard is as a regulator of the average wage scale that can be paid without unemployment, and find even one who could give me a logical answer. As you know, I outlined the meaning of the gold standard in the first chapter of my book on economics, "The Business of Life".

For instance, in Mr. Eccles' address of November 25, 1941, on page 2, he seems to agree with The London Economist that the gold standard has come to an end, whereas the truth of the matter is that we are clinging to the gold standard so tightly that we have been unwilling to allow gold to leave the country when foreign balances can only be paid in gold or its equivalent, and when we still require a certain minimum percentage of gold reserve for the paper currency that is issued. How can it be said, then, that the country has gone off the gold standard? He also refers to the "departed gold standard" on page 5 of the same address.

On page 7 he refers to the desire of the American people to have a "free world". In the United States to-day a man is not even free to take the kind of job he wants unless he pays for it. Nor is a thrifty saver of his income permitted to turn over what he saves to his own children without paying a large part of it to the tax authorities.

Moreover, we have doubled and tripled the tax on a single amount of income which would otherwise go to a thrifty saver. In fact, about the only freedom left in this country is the freedom of the individual to think how rottenly he is being treated by the Government, and this kind of thinking is being done to a large extent these days by the people who have been the cause of this country's development.

The socialistic attitude of taking away from one class and giving to another class is expressed in the paragraph beginning on the bottom of page 9 of Mr. Eccles' address. His idea of appropriate taxation to promote "public morale" is stated on page 12 - namely, "It is essential that the long purses be tapped first and heaviest in accordance with the equitable principle of capacity to pay." In other words, to soak the wealthy and to take the money away from those who have developed this country industrially and have raised the standard of living of the masses, is not only for the public morale but it is also the equitable form of taxation. He then refers to the lowest income groups "whose standard of living is already down to or under reasonable subsistence levels". I do not know of any such except the bums and the defectives and the he'er-do-wells that we always have with us, and always shall.

In an address given November 16, 1944, Mr. Eccles says, "The Government should underwrite and guarantee a national minimum of income, education, health and old-age security for all citizens. By so doing, the Government can place a floor of purchasing power under the economy. This in turn will place a floor under the market for the goods and services of business, industry, and agriculture. Decent minimum levels of income will themselves help to achieve and maintain full employment." This paragraph illustrates the fallacious ideas that some of our well-intentioned leaders now hold. In the first place, they assume that if a man can only produce $10 worth of gold value a day, the employer can afford to pay him a minimum wage of $15 per day. A minimum wage scale has the effect of putting a large percentage of the inefficient on charity when, otherwise, they could earn at least part of their living. He does not mention the minimum wage scale here, but I understand this is what he means. Then he speaks of the fact that high income - and I presume he means high dollar income - would have the effect of promoting employment because it prevents the purchasing power of the people from sinking. Everybody in Washington seems to think that the more money people get, the better off they are and the more things they can purchase, when the reverse in many situations is true. The people of the United States theoretically could be just as prosperous if the wage of the average worker were 10¢ a day and the prices of goods were pegged in correspondence. The principle of the gold standard sets the minimum wage that can be paid without unemployment appearing sooner or later; but this is all forgot, or is not realized, or is unknown.

When one states that when wages go up, prices go up proportionately, and that the circulation of money that then obtains will pay the wages of fewer people and if the wage scale is carried up too high it will inevitably cause the unemployment of a large percentage of the population, one usually receives the answer that pay rolls are a small percentage of the cost of production. I received such an argument a day or two ago from Mr. Stanley Lebergott, who is in the Bureau of Labor Statistics. He actually wrote me that "For most industries wages do not constitute .... anything near 100% of the cost of production. Reductions in wages by and large will therefore tend to decrease buying power--and the market for goods-- more proportionately than they enable the manufacturer to cut prices." Mr. Lebergott apparently does not properly interpret the statistics, and he argues from the fact that because, for example, the pay roll in one factory is only 35% of the sales, only 35% of the sales goes to labor. This is a childish fallacy. The truth is that the raw materials of my own factory represent

the wage payments made by another producer, and if you add up all the labor that goes into the final sales, you see that it represents around 90% of the total cost of production. The rest goes to profits, interest and rents. Moreover, since the statistics prove that from 1926 to 1937 inclusive the total profits of capital, after taxation, averaged less than 3.65% of the total national income, it is quite obvious that capital is not getting very much of the national income. Furthermore, this figure was before losses by bankruptcy were charged off, or the losses of companies reporting losses. If the whole situation is considered, it is probable that in the average capital receives no profit whatsoever, and the only profits derived by capital are due to the superior skill of certain individuals, and the earnings of capital are themselves disguised wages. These figures are taken from Government records as quoted in Business Week of November 2, 1940, page 64. Or, if you refer to the Statistical Abstract of the United States for 1920, page 725, you will find that persons receiving less than $5,000 per annum received 85.1% of the total national income, and that persons receiving more than $25,000 per annum received only 2.9% of the total national income, but paid 53.2% of the total personal income taxes. Moreover, things are worse now than they were then so far as soaking the rich is concerned. And whereas Mr. Eccles thinks that we should pay largely for our war effort out of taxation, he still seems to advocate getting most of this tax money from the people with incomes of more than $5,000 a year, and a very small percentage from those who really receive the bulk of the national income - namely, about 85%. If this does not establish the most perfect legalized communism in the world, I don't know where you would find one which is more perfect. Certainly things are not as bad for the thrifty and saving and enterprising persons in Russia as they are in the United States to-day.

Mr. Eccles, in his address of November 16, 1944, page 5, also makes these statements which I regard as highly fallacious: "A high level of consumers' expenditures is not possible without a large volume of wage and salary income. If our economy is to operate at full capacity, average wage and salary incomes must be high enough at normal hours of work to give the people sufficient purchasing power to take the product off the market." This, as I have stated before, is one of the worst forms of economic fallacy that burdens the Administration in Washington to-day.

If these gentlemen in Washington would spend some midnight oil studying their John Stuart Mill and David Ricardo, or perusing the works of Professor F. W. Taussig or Ex-President Hadley of Yale, they would find these fallacies completely exposed. However, this is the situation as it stands to-day, and Mr. Eccles honestly thinks he knows his political economy and, as stated, I think he is one of the fairest-minded men we have in Washington.

I worked under Mr. Bernard Baruch and visited him in his home in Washington during World War I, and found that he was a wonderful chap and very likeable and earnest and honest, but I also discovered that, like the average business man, he is not a political economist. Mr. Baruch has recently announced that he does not believe that Germany or Italy should be allowed to export any commodities after the war because it might hurt the economy of the United States and the other Allies. In other words, it is a wonderful thing for a man in Tennessee to get his automobiles at less cost by swapping cotton grown in Tennessee for automobiles produced in Michigan. This trade is admittedly advantageous both to Michigan and Tennessee. It would not be carried on unless it was. But if you hang another type of flag on the flag pole of the factory and call it a Canadian factory, then it is supposed to be utterly disastrous for the American people to swap the goods in which they have an advantage in production for the cheaper goods of some foreign country. In the fundamental sense, all this is

ridiculous and is based on insufficient reasoning and thinking. The cheaper we can get our goods from Japan or China or Germany, and the fewer goods we have to export in exchange, the better off we are. Everyone should know this. No trade will be carried on unless it is mutually advantageous, and it is advantageous for each country to swap the goods it can produce cheapest for the goods that the other country can produce the cheapest. In this way the average standard of living is increased - provided, at least, that the population does not quickly increase according to the Malthusian Law to take up the improved standard of living.

Well, I am not going to write you any longer about such economic matters, but I am going to send a copy of this letter to Mr. Eccles anyhow, because I think it is my duty to do so whether it will do any good or not, and I hope that you will send him a copy of your pamphlet.

Yours very truly,

Hugh W. Sanford

HWS:R

CC: Mr. M. S. Eccles