

ADDRESS AT THE  
133rd ANNUAL DINNER  
OF  
THE ECONOMIC CLUB OF NEW YORK  
AT THE HOTEL ASTOR, NEW YORK CITY  
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BY  
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OF THE  
FEDERAL RESERVE SYSTEM

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Subject for Discussion:

"UNEMPLOYMENT - WHAT SHALL WE DO ABOUT IT?"

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Recently a colleague of mine on the Board closed his remarks with this statement:

"First and foremost, the counsel of sanity teaches us that we cannot help the world or ourselves by getting into this war, but that we may be able to help the world greatly, and ourselves with it in constructing a fair and enduring peace when the collapse of one side or the other or sheer exhaustion of both forces a truce. In the meantime plenty of man-sized problems here at home are challenging us.

"Let me close by mentioning one to which we must find the answer in spite of the fact that it hasn't been answered yet. It would be a healthy demonstration if the United States could show the world that here is one mature nation that doesn't have to go to war to lick its unemployment problem. If we feel we've got to fight, let's get together and fight that one."

I recognize that we do not live apart from the world, and that we are vitally and greatly influenced in what happens in other nations. I also recognize, however, that even with the world at peace we and other countries could have, in fact, have had, very great and serious internal problems of unemployment; and, as a matter of fact, one of the most important problems, it seems to me, that tends to bring about war is the internal economic difficulties of nations.

In accepting your invitation, I felt that I could come here tonight to speak to you as a business man among business men. I am interested above all, as you are, in understanding the economic difficulties that beset us and in trying to find the best answers consistent with our institutions.

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I have come more and more to distrust and dislike labels. However, if wanting to safeguard democracy in this warring world, if wanting to preserve private enterprise and the profit motive system, makes me a conservative, then that is what I am. But having a reasonably clear idea of what I want to conserve, I am prepared to favor measures that may be labeled liberal or even radical if they are at the same time a practical means to that end.

While we all agree that we want to preserve our institutions, political and economic, we are prone to indulge in words and to neglect or oppose action. That, of course, is not only because it is popular to echo fine sentiments and unpopular to propose specific action, but it arises from our confused thinking both about foreign and domestic affairs. We talk of the paradox of want in the midst of plenty. But the real paradox is that with all our boasted native genius, we do not end the dilemma. We speak of restoring confidence to business, as if that happy state of mind would come about spontaneously through some sort of benevolent attitude among public officials. We complain about excessively low interest rates--that is, we do if we are bankers and lenders--but we are reluctant to deal with the causes of this condition. We are greatly attracted to that catchy word "neutrality" as if we could hide behind it and be safe from the disasters overseas.

We sternly refuse to lend any more money to foreign debtors who have not paid us what they borrowed in the last war and its aftermath, but we take their gold and silver, which we do not need and cannot use at

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present, in exchange for our dollars, our goods and our services. The effect is to swell our bank deposits and our excess reserves in the banking system to record-breaking totals. That is the chief reason why interest rates are so low--not that I favor high rates while we still have millions of unemployed. We hear much about ending conflict between business and government, but the real conflicts are not between business--as if business were a personified unit--and government.

Those who say that what is needed is cooperation between government and business frequently fail to recognize the conflicting interests within, as well as between, business, labor and agriculture. For government to cooperate in the sense usually meant, it would have to support one group as against another. How can government cooperate with industrial groups who demand high tariffs and agricultural or other groups, dependent to a large extent upon the export market, who want tariffs lowered? How can it cooperate with unit bankers, on the one side, and with branch bankers, on the other, or with the independent retailers and jobbers who are fighting chain stores? Similarly, the automobile industry, railroads, water carriers, and trucking interests are continually coming to grips over their conflicting views as to legislation. The C.I.O., the A.F. of L., organized and unorganized labor, are engaged in frequent conflict, as are groups that favor and other groups that oppose wage-hour legislation. I need not elaborate. I think it is clear that the proper role of the government is to be an umpire, acting in the interest of the general welfare, not taking sides for or against the numberless conflicting private interests.

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Nor do I profess to any altruistic desire to spread some special doctrine. From a purely selfish standpoint, I want to safeguard what I have. I do not want to make a wrong analysis of conditions as they are and as they are likely to be as far as we can see at this time. The first necessity is to arrive at the analysis that seems indicated by all of the obtainable facts.

I am, of course, well acquainted with the familiar diagnosis that is summed up in the phrases about restoring confidence, balancing the budget, removing restrictions and deterrents from business, and so forth. I am in complete sympathy with these objectives. I want to have confidence that I can make a profit when I return to my business. I do not like having the federal budget unbalanced year after year. I would do all I could to remove the deterrents, provided, of course, they are specified and provided their removal does not open up more difficulties and inequities than it overcomes.

I cannot overlook the fact, however, that we had a balanced budget and we had none of the deterrents usually enumerated--we certainly had magnificent confidence--in 1929, before the crash. We had a badly unbalanced budget and all of the specified deterrents, together with much talk about lack of confidence, when we had a large degree of recovery in 1935, 1936 and until the downturn of late 1937. Incidentally, during 1937 our budget was balanced on a cash basis, including social security collections, for a large part of the calendar year. Nor can I forget that after Congress practically did away with the undistributed profits tax and amended the tax structure more in accordance with business desires, we did not get a recovery until the

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budget was further unbalanced by pouring more government funds into the spending stream. Even if all of this be dismissed as a series of coincidences, it is, nevertheless, hard to escape the conclusion that the causes of maladjustment in the economy go far deeper than an analysis based only on the budget, confidence and so-called deterrents.

The available facts indicate that it is not lack of profits that has kept business from progressing further. The contention that high taxes and high costs have squeezed the profits out of business is not borne out by the facts. When business has had a market for its products, profits have been high, and when it didn't have the market, profits, of course, have dwindled or disappeared. No economic system has yet been devised which can provide large profits to business as a whole irrespective of its volume of operations, although business men seem to be demanding such a system when they assert that they must be given large profits before production and employment can recover. According to a tabulation published in the National City Bank letter for March, 1940, the net profits of all manufacturing corporations, after taxes, interest, and depreciation, amounted to 8.3 per cent of net worth in 1936 and 8.0 per cent in 1937, as compared with 8.2 per cent in 1928 and 9.1 per cent in 1929. These figures are taken from the corporate income tax returns filed with the Bureau of Internal Revenue and are not yet available for 1938 and 1939, but a compilation made by the National City Bank of the reported net earnings of about 1,000 leading manufacturing corporations showed that their profits declined from 10.5 per cent of net worth in 1937 to 4.2 per cent in the depression year 1938 and then re-

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covered to 8.4 per cent in 1939.

These averages do not reveal the huge profits in particular lines-- 19 per cent of net worth last year in drugs, 17 per cent in automobiles, 17 per cent in household equipment, 16 per cent in beverages, 16 per cent in aircraft, 14 per cent in chemicals, and 13 per cent in tobacco products. None of the 40 manufacturing lines shown in the National City Bank's compilation reported deficits in 1939, and in less than one-fourth of the manufacturing fields net profits were below 5 per cent.

Surely no one today would say that the stalemate is due to lack of man power or lack of capital. The National Industrial Conference Board estimates that, despite the relatively good last quarter of 1939, unemployment never fell below 8 millions during the year. This figure includes those employed on work relief. Various other estimates of unemployment are a million or more higher.

We should not forget, however, that large as even the most conservative estimates of unemployment are, and urgent as the need is to give employment to the millions of jobless, including the 500,000 new workers who are coming on the labor market each year, we have made great progress since the depths of the depression. At that time, according to estimates of the National Industrial Conference Board, 35,884,000 were privately employed in the United States. In January of this year, 45,475,000 were privately employed. This means that approximately 10,000,000 Americans have found jobs in private enterprise since 1933. In other words, since the bottom of the depression the number absorbed by private employment is equal to all of the

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new workers who are coming onto the labor market at the rate of nearly 50,000 a month--and this is a net figure--plus some 5 to 6 millions who were idle in 1933.

As for the abundance of capital available, one has only to look at the interest rate structure to find conclusive evidence. Notwithstanding the fact that the national debt is considered by most people excessively large, the competition for government securities is so great that bills are practically on a no-yield basis, other short-term securities are likewise close to the no-yield point, and the longer term bonds yield an average of 2-1/4 per cent.

The abundance of funds is further evidenced by the record-breaking total of adjusted demand deposits and currency which are now more than \$36.5 billions, or \$17 billions more than at the bottom of the depression in 1933 and \$10 billions above the peak of 1929. Savings deposits have recovered from their depression low of \$20 billions to about the 1929 level of \$28 billions.

Accumulation of funds in life insurance companies has followed the same pattern. In the past seven years insurance companies have added more than \$4 billions of government securities to their portfolios, while at the same time commercial banks have added nearly \$9 billions, and the mutual savings banks, \$2.5 billions, making a total of more than \$15 billions of increased government debt absorbed by these institutions. Many of these fiduciary institutions would doubtless be in financial difficulties without the income from these government securities.



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It is estimated that during 1940 the life insurance companies will have about \$1,200,000,000 of funds available for investment. Last year they were able to place only about \$600,000,000 in securities other than governments, and even with a moderate increase in business, it does not seem likely that they can increase this amount substantially. In addition, the insurance companies entered the year with the largest amount of uninvested funds they have ever held. Since it does not appear that the government will issue any considerable amount of securities during the current year, the question arises of where the vast accumulations of bank and insurance funds are to find a field for investment. As one writer has put it, "One can't invest one's savings in lofty ideals about the inevitability of progress".

In the light of these facts, it is all too evident that the difficulty is a superabundance of funds seeking investment relative to the available investment opportunities. This means a lack of enough borrowers to absorb the accumulating funds seeking investment, notwithstanding the large volume of the government's borrowings. The fact is that business as a whole has not suffered for want of or inability to get capital. New industry has not been starved, as witness the airplane, brewing and distilling industries, shipping, munitions and chemicals, and gold mining.

Nor will the contention that industry is letting its plant run down stand up under examination. Certainly it cannot be said that in the steel industry, the automobile industry, the chemical and electrical industries, in transportation generally, including airplanes and railroads,

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there has been a failure to keep pace in taking advantage of new invention and technological improvement. The great industries of the country are highly efficient and up-to-date. I doubt if at any period in our history we have made greater technological advances or witnessed the introduction of more new products, especially in the chemical industry. The fact is that pioneering in new products and developments has been undertaken more and more by large industries, which operate great research departments staffed by the country's ablest technicians, rather than by numerous small ones. And one of the striking symptoms of the times has been the steady trend away from capital market financing and the ability of the larger corporations as a whole to finance their replacements and expansion out of retained profits, depreciation and depletion reserves.

In his writings and in his address tonight, Dr. Gideonse has ascribed our difficulties in large part to the maladjustments arising from various causes, including monopolistic practices both by business and by labor. If I understand him correctly, I am in general accord with him in the belief, which I have had occasion to express a number of times in the past, that restrictive practices and policies are incompatible with a free and progressive economy. In speaking of these factors toward the end of 1937, I said that "the resumption of an orderly recovery depends upon the adjustment downward of those monopolistic or controlled prices and wage rates which still remain too high in relation to consumer purchasing power and an adjustment upwards of such prices and wage rates as may be too low in relation to the cost of living". And I added that, "The policies of

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"government, agriculture, business and labor to be successful must be directed toward the objective of restoring and maintaining a better balanced economy that will make for a greater production and distribution of real wealth."

But we have been struggling with these internal maladjustments for a great many years. We have set up innumerable commissions and passed legislation and issued regulations in an attempt to deal with them, but without much success. We have tried to legislate monopoly out of existence, just as we solemnly outlawed war. Short of resorting to the very forms we want above all to avoid, that is, complete regimentation or government by decree, I see no practical way of enforcing and maintaining the needed adjustments. The ideal of a free economy which will automatically adjust itself is an admirable text book dream, but it is not the real world in which we have to live. Nor do I think the mere ironing out of the maladjustments is basic, serious as they are and desirable as it is that private groups see that their own long run interests require rational price and wage practices.

What, then, is the fundamental cause of the seemingly chronic unemployment condition of today? The difficulty, as I see it, arises from the way in which the national income is currently distributed. Too much idle money is piling up in the banks unused by individuals, corporations and other institutions owning the funds. Too little is going into the hands of potential consumers. Now, I am quite well aware that through most of our history as capital accumulated it flowed almost automatically into new

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production which, in turn, gave employment and enlarged national income. I do not for a moment minimize the great importance of this process of privately generated employment and progress. Nor do I subscribe to the doctrine that we are a matured economy incapable of further growth. But I do not believe that sufficient growth is going to come about, under prevailing conditions, by the same spontaneous processes that have been the dominant forces in the expansion of the past. Perhaps we will again reach a condition in which these forward surges of new investment will be adequate to absorb both idle funds and idle human and material resources.

Speaking only of the prospects of the next few years, I do not see, even if all the deterrents of which business complains were removed, a sufficient volume of new investment to take up the slack we have today. It is imperative to meet now the needs of those who, through no fault of their own, have no jobs, no security, no tangible stake in the society we wish to preserve. As a democracy we can't afford to take the position that because economic conditions are satisfactory for many of us, others who are less fortunate can be shunted aside, or merely kept alive by hand-outs, until economic revival develops at some unpredictable future time. Aside from humane considerations, it is not good government, good democracy, or good economics to lose the productivity of millions of workers. Those of us fortunate enough to have property sometimes forget that for millions of our people their only possession is a job. When that is gone, they have but slight reason to remain loyal to our institutions and our economic system. You and I know very well that fine phrases about the inalienable right to

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work are a meaningless mockery to a man who cannot find a job.

Then, why shouldn't we declare as a national policy that we will, collectively, through government, offer the security of a job to all who are able and willing to work but are unable to find private employment? Why not provide assurance of employment, not merely insurance for unemployment? Is this a radical idea in a democracy? Is it in any way inconsistent with our professed ideals and aspirations? Is there any better way to make democracy work? Can't we afford it?

I think we cannot afford to adopt any other course. I see no other road to a balanced budget. I cannot see any other way at present to sustain the profitability of existing investment and to open the way for new investment. If business expects to have the freedom it has always enjoyed of hiring and firing, should it not recognize that government has an obligation to society as a whole to provide the stand-by service of public employment to take up the slack when business cannot do so? Government should not be a competitor with private business, but could and should provide those useful public works in times of slack business that private enterprise cannot be expected to provide.

At the present time with the huge volume of unemployment we could well have a long range public improvement program, since there is not a prospect that all of the unemployed can be reabsorbed into private activity within a few years, short of war. There is a vast need for super dual-highway systems, bridges, tunnels, as well as for housing, hospitalization, parks, schools, rural electrification, and many other public improvements.

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In addition to the longer range program of public works, we should have a flexible program of relief employment so planned as to be quickly susceptible of expansion and contraction in response to decreases and increases in the current demand for labor by private enterprise. This flexible program should undertake to provide jobs at wages somewhat below those prevailing in private industry for all those whose unemployment insurance benefits have been exhausted and who are willing and able to work.

To the extent, of course, that our man power and productive facilities are needed for an expanded military and naval defense program which is of vital importance in the world of today, other public work could be reduced or deferred accordingly.

However, with the large volume of unemployment today and the great need for public improvements and military preparedness, there is no excuse or justification in freezing the army of unemployed at 8 or 10 millions by reducing public employment as fast as private employment increases. For example, if public employment is reduced by, say, 500,000 whenever private employment increases by 500,000, we have made no net gain in reducing the number of unemployed. The reason for the failure up to date to get full recovery is that we have never carried through with a program of public employment to the point at which the stimulation it gives to private activity has resulted in approaching a condition of full employment.

A government policy such as I have in mind must be flexible, for the time might come, as it has under war conditions in England today, as we hope it may come under peace conditions in our country, when the govern-

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ment, instead of stimulating private consumption further, might need to withdraw all stimulus in order to avoid inflationary results as we approach full employment. We cannot have inflation on a dangerous scale so long as we have millions of unemployed. The danger would only arise when we had reached the limits of our ability to produce.

It seems to me we could move far along the road to full recovery by establishing the principle of assurance of employment and, to this end, using only the broad functional powers of the government, avoiding the endless complications that arise from attempting by legislation to regulate the complicated activities of commerce, industry, agriculture and labor. The latter approach, if carried too far, creates more problems than it solves and cannot possibly be carried out successfully in a democracy because such a political system does not provide the mechanism to do it.

It seems to me that we are inclined to approach the problem from the wrong end. We have had our eyes, with growing alarm, on the budget, rather than on the problem that has resulted in the unbalanced condition of the budget. We have proceeded on an emergency basis. We have talked about pump priming, but this is a poor simile based on a false analysis. When our economy suddenly stalled in the early '30's, we were slow in analyzing the situation and believed that the machine was just at dead center and only required a push to resume its former progress. We know better now. What we are confronted with is not an unprimed pump or a machine at dead center. We are confronted with a large volume of idle resources which are not being called into operation because of a lack of demand for their products due to

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the lack of purchasing power by the consumers, and the consumers to a large extent are working people, or people who would like to work. Give them jobs and they will consume--let them consume and the demand for goods would be sufficient to keep the economic plant in full operation.

The core of the problem is not social or humanitarian, but economic. I am convinced that there is only one way in which our essential purposes can be served, and that is by assuring an adequate income for consumers with which to buy the products of industry. Alfred P. Sloan recognized this dilemma when he was quoted as saying recently, "The real question that arises is whether the current rate of productivity can be maintained from the standpoint of the ability to consume." Those who have many unfilled needs and would satisfy these needs if they had the purchasing power, simply do not have it. One-third of the families in the United States are able to spend for food only \$20 a month, for shelter only \$10, and for clothing only \$4. We must influence the flow of income in such a way as to increase the buying power of the mass of our people. This is the only way in a democracy to provide a market for the goods and services which industry can produce, and to give industry a real incentive for expanding its productive machine.

I do not want you to think that I am just proposing another dash of "pump priming". It is high time we stopped talking as if we were in a temporary emergency. We've got to face the realities of our present distribution of income, consumption and saving, and work out a permanent program.



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The most direct and simplest way to approach the problem is to recognize that we must provide jobs for all those who are willing and able to work. If we make full employment the touchstone and principal objective, then a further important conclusion emerges: workers must not only be employed but must receive compensation at a rate sufficient in the aggregate to give them the buying power necessary to purchase the product of their labor, aside from savings necessary to provide new investment required to take care of an increasing population and an increasing standard of living. If they do not have that, then the shortage of effective demand for goods currently produced will result in the curtailment of operations and of the working force. This, in turn, will necessitate more employment by the government. In either case, ultimately we will have to bear the cost in accordance with ability to pay, either indirectly by taxes or directly by wages.

The one thing that a capitalistic democracy cannot afford--is unemployment. Prevent it--and the machine can never slow down to the point where a serious recession will develop.

Can we honestly say that we have faced the underlying question frankly and summoned our genius, our organizing ability, to provide the assurance of employment? We should recognize that we can do little individually. The problem is a national one and must be solved through collective action.

We have at last established the principle of unemployment insurance and old age pensions. It is a notable advance. Necessarily, it has been

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largely experimental because it is new. Nevertheless, we have had enough experience to see that it needs thorough revision.

In connection with this subject, I said in a speech last fall in St. Louis:

"As part of a national policy of encouraging consumption, I have, over a long period, urged revision of our system of old-age and unemployment insurance, which at the present time is increasing rather than diminishing the volume of funds that must find investment outlets. If we are to accumulate reserves for old-age pensions, they should be built up in good times when their collection through taxes will tend to moderate unsound boom tendencies and will not have an adverse effect upon consumption. We have made the mistake, in my judgment, of accumulating a vast reserve in times of large unemployment, taxing it not out of those best able to pay or those whose savings are idle, but out of payrolls mainly of those who otherwise doubtless would have kept the funds moving in the income stream. The more we have taken out of consumption by this process at the time when we need above all to increase consumption, the greater the need has been to unbalance the budget still further in order to increase consumption. Other countries have built up social security programs and have adjusted their taxing and financing methods to the countries' economic needs by paying out in social security benefits sums much larger than they currently take in from contributors."

A pension plan to be adequate to the country's needs should be broadened to apply to all those reaching a fixed age of retirement at such

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time as they retire. It should be adequate to provide minimum requirements in relation to what our economy can afford.

At the same time, we should do away with the so-called means test, both in its application to unemployment as well as to pensions. I feel that it tends to put a stigma on our unemployed and old people to require them to proclaim themselves paupers before they can get a job or, in case they are not covered by the contributory system, before they can get a modest pension.

In my judgment, our experience with unemployment insurance has already demonstrated that the relationship between taxes and benefits is seriously out of line. The unemployment trust fund, which was also built up through taxes on payrolls, was at the beginning of this year four times as large as estimated 1940 unemployment benefits, and these benefits will return to jobless workers this year probably less than half of the fund's current receipts. This continuing drain on consumer incomes can best be corrected by making the benefits larger, starting them earlier and continuing them longer.

A greatly modified tax structure is an essential part of any program designed to bring about elimination of unemployment, to provide an adequate old age pension and ultimately to balance the budget. As I have previously stated with reference to this subject:

"The volume of taxes on consumption, including social security taxes as well as sales taxes, excise taxes and tariffs, is at present much higher than at any previous time. We should undertake a far-reaching revision

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"of our Federal and State tax structures so as to cut down these consumption taxes and to increase taxes on funds which would otherwise remain idle.

"Also as a part of the general program, I would favor applying taxes that will have the effect of discouraging over-accumulation of so-called rainy day reserves which are being set aside in excessively large amounts, particularly by the larger corporations. These sums come out of the income stream and unless put back into the stream through being paid out in dividends to stockholders or spent for plant modernization or expansion are bound to diminish consumption, then employment and finally production. It would be preferable if these excessive accumulations were avoided in the first instance by reducing prices to consumers or by increasing the wages of the lower income groups of workers. If this is not done, then it is not logical to oppose taxation that will keep these funds that are unused for plant or for dividend purposes moving in the income stream. They cannot be taken out of the income stream without reducing it and thus reducing employment and production.

"I opposed at the time and would continue to oppose application of corporate surplus taxes to the small businesses which do not constitute the heart of this problem of idle funds. But we should also consider increasing the normal income tax of corporations and revision of the inheritance tax, particularly a reduction of the present exemptions."

With reference to individual income taxes, I said further:

"Our income tax rates applying to these groups with incomes of from \$3,000 to \$50,000 are much lower than the rates, even before the war,

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"in England, France and most other countries. Moreover, our income tax structure has a much narrower base than that in other nations. I am in favor of spreading it out. The time has arrived, I think, when this should no longer be delayed, when additional revenue should be derived from the intermediate income groups that I have mentioned. The effect will be to offset continued over-accumulation of idle funds, to add less to bank deposits through the process of deficit financing, and to help close the gap between Government receipts and expenditures."

I attach great importance to the psychological effects of a public program that assures employment and provides an adequate pension system for those beyond working age. By giving people a sense of security, there would be released into consumption channels funds that are now being set aside, often at great personal sacrifice, in the vain effort of individuals to provide their own security. Individual thrift and savings, of course, are admirable. But we must ask ourselves frankly whether at a time of underconsumption due to lack of purchasing power, it is wise for countless individuals to deny themselves needed food, clothing, shelter and other necessities of life in order to save against a rainy day or old age, when the effect of their efforts is to diminish the consumption and business activity we so much need today and to increase the volume of funds striving to find profitable investment.

This brief analysis of a program brings us up to the question: Where does this leave us with regard to the national budget? Shall it remain permanently unbalanced? My answer is that the way to balance the budget is

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by the restoration of full production and distribution through assurance of full employment. To attack the budget directly by cutting expenses at the wrong time means to reduce activity, and to attack it by raising taxes in the wrong way at the wrong time has the same effect. If we can restore the national income and keep it firmly on a rising basis, if we can adopt more equitable and rational taxation, we can balance the budget because we will have corrected the underlying causes of its unbalance. If the national income increases, revenues will increase and many types of public expenditure will automatically go down.

I cannot give you a precise balance sheet to show just what the budget picture would be if we were to inaugurate a pension system such as I have indicated and a program of public employment sufficient to assure jobs to most of those unable to find private employment, revising our tax system to place all expenditures gradually upon a pay-as-you-go basis. However, I am confident that by this general approach we would be assured, far beyond any other course open to us, of a sustained and rising national income, increased private profits and outlets for new investment, and increased revenues to close the present gap in federal income and outgo.

I have tried to outline what appeals to me as a constructive program for the preservation of capitalism and democracy. It is intended to construct within the existing economic and political framework a mechanism that will meet the essential needs of the people and consequently will keep them content with their economic organization and their system of government.

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Democracy cannot survive half free and half slave--with millions of people enslaved to poverty, unemployed, and in misery, on the one side, and great wealth and affluence, with idle money and idle resources, on the other side.