

Address of
MARRINER S. ECCLES
before the
Executives' Club of Chicago
Hotel Sherman, Chicago, Illinois
Friday Noon--September 17, 1948.

Chairman Corbett, Distinguished Guests and Members of the Executives' Club of Chicago: this is, indeed, a privilege and a pleasure for me to meet with the business leadership of this great city. I never appear before a group to talk but that I am reminded of what happened to me one evening when I was invited to speak to the editors of the McGraw-Hill Publishing Company. There were about thirty or forty of them and as we were having dinner I turned to one of my associates, who was an assistant while I was Chairman, and said to him, "Elliott, as I look around I know a great many of these men and I am just wondering if I have spoken to this group before."

He said very seriously, "I am sure that you have not, because if you had you wouldn't be here tonight."

[Laughter]

So it is quite apparent that I have not spoken to this group before on the basis of that reputation!

Your chairman spoke of the rough ride that I had had on the Potomac. I rather feel that it was somewhat of, maybe, a fortunate ride. He spoke of the fact that my resignation had been in the President's desk. I think I need to clarify that statement to this extent. The members of the Federal Reserve Board are appointed by the President and confirmed by the Senate for terms of fourteen years. I had ten years of my term to run. One of the members is designated as the Chairman of the Board by the President to serve for a term of four years, and the same is true of the Vice Chairman.

Mr. Truman neither appointed me as a member of the Board nor did he designate me as Chairman. It always has been my belief--and I so argued before the committees of Congress during the hearings on the Banking Act of 1935-- that the Chairman should serve at the pleasure of the President because he is the liaison between the Federal Reserve System and any administration that may be in power at any given time. I did not succeed in getting that provision in the statute--that the Chairman serve at the pleasure of the President. However, as far as I was concerned, it seemed impractical that I, as Chairman, should undertake to be a liaison if I was ^{non} persona grata with the President.

So I said to Mr. Truman, "You did not designate me, and I want you to know that I will make available the chairmanship any time that you may desire." He assured me upon that occasion and others that he would not hear of it. But, when my term as Chairman--the four years--did expire, which was last January 31st, without any previous notice, except about two days, he had John Steelman advise me he was not going to redesignate me after I had served for so many years. Well, I didn't feel too happy about the way the matter was handled.

I have been away from Washington nearly a month, during which time I have been up in Canada—Banff, Lake Louise, and Jasper—and out to my home in Utah. Therefore, I did not have either the inclination or the opportunity to prepare a written speech, and I am going to have to ask that what I say today be off the record. I do feel that it is one thing to speak on the record before the committees of Congress when you have no choice as to whether or not you will go up there, but it is quite another thing to speak on the record under these circumstances and during these critical times, without preparing a statement. Accordingly, if the press will be good enough to treat what I may say off the record, I will be glad to meet them in a press conference after the meeting. I have nothing to say, but if they have some questions I can indicate whether or not I can answer them on the record.

Now, getting down to some of the serious problems I know you expect and you want me to discuss, that is, the development of the inflationary situation with which we all are confronted, and some of the causes and the effects of the situation, I am going to read just briefly from a statement I made before the Joint Committee on the Economic Report, which is known as the Taft Committee, on April 13th. This is the statement I made on behalf of the Board. I just want to give you this excerpt from it:

"Never in our memories has the world been pervaded by greater fears, confusion, and discouragement arising chiefly because of the disappointments of the past and the uncertainties of the future. The great hopes we had during the war for achieving a lasting peace in a prosperous world have been steadily diminished because a few ruthless and despotic men hold a sword of Damocles over the heads of a free peoples throughout the world. It is difficult, if

not impossible, to plan for a rational economic future either at home or abroad while that sword hangs over us. We think that the prospect of removing the threat by peaceful means will be immeasurably enhanced the sooner we assert our moral, and our physical power to establish the foundations for peace before we are engulfed by the economic and social problems which grow more menacing the longer the establishment of a firm basis for a permanent peace is delayed."

When the defense program was started in 1940, we had a great cushion of unemployment, of excess food, of idle productive facilities. It was not long, however, until the excess capacity of men, material, and plants had been utilized. That was brought about by war defense and soon thereafter by war financing. The war financing would not have brought about the inflationary situation had it all been financed currently out of taxes.

But that was not done. It possibly could not have been done. It never has been done in any country and we financed during the entire war only about 44 per cent of its cost, which was over \$400 billion, out of taxes. The balance of it was financed out of borrowing and the public debt went up from something around \$45 billion to \$270 billion in the short space of five years. A very substantial part of that public debt was financed by the banking system, which was the process of creating money. Money comes from bank credit—and I won't go into the mechanism of how that is brought about except that it is a fact.

At the end of the war, the expansion of bank deposits and currency had increased about three times. In addition to that, the public held large quantities of government securities which were the equivalent of cash.

We wanted to prevent inflation during the war when 45 per cent of our entire productive capacity and goods were being devoted to the sustaining of the war and the balance was left for the civilian population. The money supply in the hands of the civilian population equaled 100 per cent because the goods available for war were not available for purchase by the civilian population who produced the goods, but they had the money which they got for the production. Therefore, you had a very large supply of money and a growing supply of money without a growing supply of goods available to the civilian population.

In order to prevent inflation during the war, the harness of controls was put into effect—price control, rationing, allocation of scarce materials, building permits, wage controls, export licenses, and excess profit taxes. It was perfectly natural that when the war ended there would not be a supply of goods and services available to meet the demand and available purchasing power.

Now, inflation is a condition where the means of payment in the hands of those who will spend it exceed the supply of goods and services available—^{had and still have} and you certainly ~~have~~ that condition. You had a terrific potential inflation. You had a backlog of demand that had accumulated for many goods and services over a period of five years. In addition to that, you had what was the normal current demand which you would have had had there been no war. So immediately there was what was the current demand plus everybody's desire to get what was the backlog of demand.

What we have had since the war ended is an attempt on the part of the American people and American business to not only satisfy their current demands, but to satisfy this backlog demand. It was not physically possible to produce

what would be the equivalent of seven years in housing, automobiles, and many goods in a period of two to three years. The miracle is that we have not had far more inflation. If it had not been for the great faith of the public in the government and the purchasing power of the dollar--in which they have been deceived, I think, in many instances--we certainly could have had far more inflation than we have had.

Now, to make this inflationary situation even worse, we have had recently an expanding military program without a terminal point. We have had an expanding European Aid Program, and there is no terminal point to that. A world aid program would be better. Right in the face of that, we cut taxes about \$5 billion. So the most important anti-inflationary weapon we had in the kit, which was a budgetary surplus, has practically disappeared.

The taking off of the controls was a tragic mistake--and that mistake was made, not last year, but in 1945. Practically every control was taken off before the end of 1945. Price control was left on, but price control was completely useless without rationing, without allocation, without wage control, and without the other harness of controls. All it did was to play into the black market--the racketeers, who were the strongest advocates for a continuation of price control. They were just like the bootleggers during prohibition--they wanted prohibition continued; and just so did the black market operators want price control continued. It was ineffective when you took the controls off.

Mr. Vincent and Mr. Snyder strongly advocated the taking off of the excess profits tax. Now, I am not saying that the Republicans who were not in control of Congress at that time raised any objection to taking off these controls.

[Laughter]

Neither am I saying American business and farmers and labor raised objection to it. Everybody wanted them off, except; labor wanted wage controls off, but wanted price controls left on; business wanted wage controls left on, but wanted excess profit taxes taken off; the farmer wanted the ceiling taken off of his farm products, but wanted a floor kept on them; the banker wanted higher interest rates as a means of controlling credit, but wanted no other means on the part of the Federal agencies to control his banking operations.

Well, you know the story. The Democratic Administration are largely responsible for the results. They were supported to a great extent by the Republicans and most of the American public.

The longer inflation goes, the more serious will be the adjustment. You have already created a terrific disequilibrium. Business as a whole, and the farmer and organized labor have not suffered by inflation. The income of business after taxes has more than doubled. I am speaking nationally. The income of the farmer has gone up more than two and a half times since 1941. The wages of organized labor--not taking into account their inefficiency, which in many cases is appalling--has likewise doubled.

On the other hand, you have the great mass of the unorganized groups, the pensioners, people living on annuities, the white collared groups, and the returned veterans--many of them were not members of unions. The union members are about 14 million out of about 60 million people employed. That group is hurt, and in order to keep up their standard along with the groups that have been benefited, they have used up some of their savings. They have cashed in their "E" bonds and they have gone into debt.

Consumer credit since the war ended has practically doubled. Installment consumer credit has more than doubled. Mortgage debt on housing has almost doubled in the past two years. We have been getting the little fellow in debt to purchase inflated houses in the last two years at the rate of around \$9 billion a year.

Now, true, you can have inflation as long as you keep up the process of getting the public living beyond their incomes by the process of consumer credit, mortgage credit, or bank credit that is not tied directly to the production that would not be produced without the bank credit. On top of all of this inflationary effect, as I say, you have had the Federal Government and the states and municipalities carrying out public works and public projects. So what you should be holding today for a cushion for a deflationary period in public works and public roads, not only on the part of the Federal government but on the part of all the municipalities and states, is being spent. ^{that,} In addition to state and local governments have been passing soldier bonuses and increasing the public's purchasing power. These measures have been financed through debt, and this creation of debt has helped to sustain inflation.

You have had the Federal government stimulate this housing program on the one hand, particularly through the mortgage which is known as Title 6, while they are talking about controlling inflation on the other. We have had the veterans' housing program which has been another stimulation. We have had the RFC to provide credit where banks did not.

So we have been perfectly inconsistent. At one and the same time, the Government talks about controlling inflation through various means while ~~is doing~~ the very thing that tends to create and sustain it.

You have got what we call parity payment in the case of the farmer. The Department of Agriculture talks about the reduction of production so

as to be able to sustain prices. It appears now that we are going to get some surpluses and, with the Government bound to maintain parity, they are going to have to buy up the surpluses and therefore there is a feeling that production should be restricted so Government will not have to buy up the surpluses.

You see, we are not dealing with the economic facts of life-- neither the government, nor business, nor the farmers, nor labor. It is unfortunate that we did not keep controls on. It is too late to put them on now. First of all, the public would not accept them. It is like humpty-dumpty on the wall. You just cannot put it together again, and one control without all of the others would be quite useless.

You must have the entire harness, and I don't think any such a regimentation in peacetime is practicable or possible without a greater degree of education and understanding than the public now has.

There are some things that could be done. I am going to just give you what I said off the cuff the other day before the Committee of Congress, if I have it here. I am not sure that I do. This was before the Committee, and it read fairly well, so I possibly could not say it any better.

"What we are interested in this time, of course, is not so much re- crimination. What we are interested in is what can be done, at this late date, to overcome as far as possible the mistakes of the past. I do not believe it practical to put back a complete harness of wartime inflationary controls."

The press can get this because this is what I said before the Committee of Congress.

"I do not believe that to put back some and leave off others would do the job. I do believe that it is too late to avoid a serious deflationary adjustment at some point. The disequilibrium and the distortions have already been created and the public are in debt. I do believe that the inflation can

go further if nothing is done and if budgetary deficits develop," that is, if we don't have the budgetary surplus, "it can be long postponed, and can be catastrophic in its ultimate effect the longer it is postponed. I do believe that the sooner inflationary development is stopped the less serious the adjustment, or the deflationary development, will be.

"I do believe it essential that credit controls, sufficiently broad in power and authority, both in consumer credit and bank reserves field, be made available. That can be, at the present, the most useful, the most practical and the most effective."

Of course, budgetary surpluses would be more effective than anything, but that is not something that you can get quickly.

"I do believe that everything within the power of the administration and the Congress should be done to maintain or to secure a budgetary surplus. I do believe that the Federal Government should do everything within its power to encourage the States and cities to postpone every expenditure that it is possible to postpone, and to set an example to the states by doing likewise. I do believe that the Federal Government should not, for what seems to me political reasons, encourage a housing program in excess of the capacity of labor and material available, and encourage further inflation thereby. I do believe that the Federal Government should do everything in its power to bring down food prices, to take off floors if necessary, and to encourage more and not less production"--at least at this time.

"I do believe that we should...and I may sound naive in this regard--adjourn political considerations, and I say that for both parties, and to consider honestly and openly in the interest of all the people ⁱⁿ the economic facts of life."

In the beginning of my statement, I quoted from a statement that I had read on the 13th of April, which you will observe, recognized that our domestic inflationary situation could not be dealt with, no matter what we did, adequately as long as we did not have a basis for peace in the world. So long as we have a burden of world aid to prevent communism from engulfing the world, and so long as we feel it necessary and urgent to spend the billions we are for a preparedness program, it is pretty difficult to deal with these economic problems on the domestic front. We cannot and do not operate in a vacuum.

Therefore, I think that we must be realistic in dealing with this foreign situation, and I cannot help but feel that the results of the past three years have not been very fruitful. It is apparent to all of us that the world situation has been rapidly deteriorating. We have not kept pace with the developments, at least sufficiently, to even maintain a status quo which was entirely unsatisfactory. But it seems that we may have lost ground.

We must have a basis for world peace, and we must have it soon. If we must risk war while we have the atom bomb and the enemy does not have it, then we had better risk it now rather than be forced into it at a time when, with all of our preparation—and preparation is relative—we may be less well prepared than the enemy.

A program of preparedness is all right if it is preparedness for offense. But a preparedness program for defense does not seem to me to make too much logic. If a preparedness program of defense means anything in the present situation, it means an armament race and an armament race ultimately leads to war—and in this instance it would be an atomic war.

We may not be the ones to choose the time. Democracies seldom, if ever, do. The British and the French were sufficiently prepared to stop the Germans and enforce the conditions of the Versailles Treaty in 1934 and '35 and '36,

even though they were less prepared than they were in '39 when they were entirely unprepared to deal with Hitler.

We were well prepared to stop the Japs from going into Manchukuo when they broke the Nine-Power Pact. But even though we were possibly much better prepared at the time of Pearl Harbor, relatively we were less prepared.

It seems to me that we are confronted with these very difficult alternatives. We carry on a preparedness program of an expanding amount of money—\$15 billion this year, eleven last and eighteen or twenty next. Who knows? The more inflation you get, the more money it takes. A world aid program to hold our position! All of that means that we are getting weaker in a sense. We are getting weaker in an economic sense on the home front while our enemy is getting stronger.

It seems to me, then, that we are confronted with either wrecking ourselves ultimately on the rocks of inflation, or destroying the very system that we are preparing to save by the adoption of such rigid controls that we would be, in essence, a totalitarian economy ourselves to control the domestic situation, or the third alternative is to find ways and means very shortly of forcing a basis of peace in order that we can avoid the catastrophe that we will be ultimately confronted with if we do not face up to these very unpleasant alternatives.

In that connection, I would like to give you some quotation from a book written by none other than Major General Dean who headed the United States Military Mission in Moscow throughout the Period of Our War Alliance with the Soviets. Nobody could know better than he the situation.

What does he say? *If the record up until the end of the war was not sufficient to clarify Soviet intentions, certainly all doubts should have been dispelled by February 9, 1946, when Stalin reaffirmed the doctrine of Marx and Lenin in exhorting his people to extraordinary efforts in the preparation for the inevitable wars which must be expected so long as the capitalistic system exists.

*In a sense, we are fortunate that the issue is so clearly drawn. Never before in our history have we had so much advance warning of the peril which confronts us. Never has it been more important to take preventive measures to avoid the dangers which lie ahead and to prepare to overcome them if they prove to be unavoidable. This is going to require American leadership which is crystal clear as to our own objectives and which is supported in pursuit of them by a unified public opinion. Most important, we must adopt a program which is designed not to defend our American way of life passively, but offensively, to counteract constructively those forces which threaten it.

*Again, Soviet leaders would probably have used the threat of the Red Army with much greater abandon were it not that they know that we still have a strategic air force whereas they have none that is comparable to it, that we still have naval supremacy despite the number of our ships that are inactive and above all that we alone have the atom bomb. Until the Soviet Union has atom bombs of her own, she will be restrained from crossing swords with those who have and the chances of obtaining our objective by peaceful means will be enhanced immeasurably if we are prepared to defend our position by force at any point where it is threatened.

"Nothing induces greater restraint on the part of the Soviet leaders than a display of strength by their adversaries".

I have just one more quotation--Winston Churchill, that great British wartime leader, in an address before the Parliament on February 23rd of this year said: "The best chance of preventing war is to bring matters to a head, to come to a settlement with the Soviet government before it is too late. This would imply that the western democracies would take the initiative in asking the Soviet for a settlement. It is idle to reason or to argue with the communists. It is, however, possible to deal with them on a realistic basis and in my experience they will keep their bargains only as long as it is in their interest to do so, which might, in this grave matter, be a long time once things are settled.

"I said that the possession of the atom bomb would give three or four years' breathing space, perhaps it may be more than that. But more than two years of these years have already gone. I cannot think that any serious discussion which it may be necessary to have with the Soviet government would be more likely to reach a favorable conclusion if we wait until they have got it, too. We may be absolutely sure that the present favorable situation cannot last."

What I have said on this last subject is entirely out of my field of monetary banking and credit control. But I cannot think in terms of a domestic economic social problem when every problem you look at, whether it is taxes, whether it is appropriations for the military or foreign aid, or whether it is inflation, goes back to Russia. That is the controlling factor at the present time, not only of the foreign situation, but of our domestic situation.

You have been very patient and I possibly have talked too long.
What I have said has been off the record, and I appreciate very much your
attention.

I thank you! (The audience arose and applauded)
