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LOOKING FORWARD

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What I have to say on looking ahead in this general field of banking and war finance can, like Caesar's Gaul, be divided into three parts. The first deals briefly with some basic principles underlying the whole problem of financing such an all-out war as this must be if we are to come out victorious. The second relates more specifically to the questions surrounding banks and their place in relation to wartime Government borrowing. And the third attempts to peer ahead further through the foggy future to some of the post-war implications of present developments to which bankers may do well to give some advance thought and action.

I.

In discussing the general problem of inflation there is one general point I want to emphasize strongly at the outset. This is to stress again the importance of thinking in terms of real goods and services as contrasted to financial terms. Given such real limits as there are on the volume of goods which can be produced, there is only some given amount of real goods available for distribution to the armed services, to our fighting allies, and to civilians.

The President estimated in his budget message that only around 65 billion dollars of goods (at January 1943 prices) would be available in 1943 for civilian use, or only \$500 worth for each American civilian man, woman and child. Figure out what this means for you! We will have only this drastically reduced amount available to consume out of what we produce. What financial means we use to raise the money will change only

the distribution of these scarce goods among us. Ultimately, the question is--how shall our sacrifices be divided?

The basic facts of inflation are simple and clear. As a people we have tremendously more money to spend than there are civilian goods and services to buy. There will be an average of only around 500 dollars worth of goods and services available to each civilian in 1943. If it is more, it will only mean that we are paying higher prices for the same amount of goods, not that there are more goods. Inflation thus is merely one means of dividing up the goods available--one way to decide who gets more and who gets less than his 500 dollars-per-capita share. Inflation means letting people bid up prices until the poorest are squeezed out.

Many of us, ostrich-like, still refuse to face the facts, but recent evidence demonstrates all too plainly that direct controls can not hold prices down when buying power vastly exceeds goods available. If price ceilings are steadily revised upwards, or growing subsidies are paid to producer groups, the effect is inflationary. And outside the legally controlled realm, black markets and price evasions inevitably flourish.

It has become commonplace to assert that the inflation problem lies in the huge pressure groups each relentlessly intent on forcing up its own incomes. The number and power of huge economic pressure groups is perhaps the most alarming domestic aspect of the war. But we must recognize that these pressure groups--laborers, farmers, big business, or whomot--can exert their pressures and obtain their demands only because of the demand situation. If all excess purchasing power were removed from consumers' hands and transferred to the Government for war spending, upward pressure

on civilian prices would vanish. Producer pressure groups would find themselves in no position either to get rich quick out of the war or to demand arbitrarily that price ceilings be pierced.

The President in January suggested 16 billion dollars of new taxes or savings. This figure should be a minimum, rather than a maximum goal to shoot at. This means far heavier taxes on those able to bear them than we have yet experienced. Such taxes would really cut into consumer buying power--and nothing less will do. Let us not be deluded by the "gradual" price increases shown by the indexes thus far. Inflation begins this way, and in such periods indexes of official prices always lag far behind actual prices paid. Furthermore quality depreciation has already increased the real price of many products.

Is this alarmist talk? Is it painting the picture too black? Perhaps it is, but we must not underestimate the dangers. The American people must be roused to wage war against inflation as relentlessly as we wage it against any common enemy. It is essential that all of us see why we must urge vastly higher taxes for our own protection--not fight them or sit back and do nothing. The greatest service you, as influential leaders in your communities, could do to yourselves and your communities would be to fight hard for much higher taxes.

II.

What relation does all this bear to banks and their place in the war financing program? What does it mean to you as bankers?

Ideally, almost no new securities should be sold to the banks throughout the rest of the war. This is a central fact. If the Government

obtained by taxes and borrowing all the excess consumer purchasing power that cannot be spent without bidding up prices, this would be roughly just the right amount to finance the entire volume of expected Government expenditures. People receive incomes for producing all types of goods and services--war and non-war. It has been often emphasized that only about one-half of all our production this year will be for civilians. Thus if we should spend only one-half of our incomes in these goods, prices would stay roughly constant. The other half of our incomes could be given to the Government in taxes and loans. This would be roughly just the right amount for the Government to buy the war goods part of 1943 output. No recourse to the banks for new money would be necessary. Inflation would be beaten!

Yet I need not tell you that taxes are far lower than this amount. And purchases of war bonds by individuals, though still growing under the Treasury drives and the pay roll deduction plan, are as yet too small relative to the total deficit. The big financing drives in December and April raised lots of money for the Treasury--but not enough was raised from individual savings out of current income, which is what counts most in fighting inflation. In the April drive less than one dollar out of every twelve raised came from Series E bonds, which represent the purchases of most people in the middle and lower income groups. Moreover about two-thirds of the 1.5 billion of Series E bonds sold in the April drive presumably came in more or less automatically, since that was the average monthly rate of sales before the drive. We have done well in raising huge amounts smoothly. But we have not done well enough so far in raising them from the really anti-inflationary sources, namely the current incomes of the upper-middle, middle

and lower income groups. And we should sell proportionately less to banks.

Where we get the money is the core of the inflation problem! Therefore, we must move much farther toward tapping these inflationary funds in the hands of those whose incomes have greatly increased, and we must move far faster toward that goal than we have thus far. You as bankers know well the amazing way your individual and business deposits are growing. In fact, this growth has been faster than the growth in war bonds in almost every Federal Reserve district. And strikingly, it is the districts which have had the most rapid deposit growth where sales of war bonds have been relatively least. This is a disquieting fact, indicating again the urgent need for people to use their accumulating funds for financing the war. In so far as we do not do the job through taxes, we must do it so far as possible by savings whether voluntary, compulsory, or some of both, with a minimum of reliance upon bank financing.

You bankers have done your job well, and are doing better every day. You are using your excess reserves more fully, rather than holding such large volumes of idle funds--a step advantageous to your own profits and to the Government. You are relying more on Treasury bills and rediscounting to adjust your reserve positions in times of temporary tightness. You are advancing funds to private industry where needed for expanding war production, as well as to the Government.

The Reserve System, on its part, is attempting to do everything possible to smooth and assure your way. It has posted a bill buying rate of three-eighths, always available to you with a repurchase option if you want it. It has undertaken to stabilize the Government security market against any substantial fluctuations so as to remove any fear that you will

lose by buying now instead of waiting for better returns. It has given its pledge that the banking system will be given all the reserves necessary to perform its part in financing the war.

Looking forward, then, for the duration your responsibilities to the nation are fundamentally two: First, you must help assure a stronger non-inflationary financing program based on non-bank funds. Lead the effort to sell securities to the public. Second, in so far as you do extend new credit to the Government or war industries, use your funds as fully and effectively as possible, bearing in mind the need for maintaining both a balanced investment portfolio and a flexible reserve position. These are the core of sound wartime bank management.

You as bankers are also performing many other special services for the nation. There is more to come, as the scope of rationing widens and as tax collection at the source begins to operate. You have the satisfaction of playing your role in our country's fight for survival. The Government needs and wants your whole-hearted cooperation. For our part, we of the Reserve System assure you that you have our fullest cooperation.

III.

Of post-war implications of war developments I want to say only a little. The subject is so big, so vast, that it would provide many evenings' discussions by itself.

One of President Roosevelt's four freedoms is freedom from want. This has been generally interpreted to mean that those who want to work should be given a real chance to do so at a decent living wage. I doubt that any government will very long stay in power again in this

country which fails on this basic issue. If private business and industry does not run at full enough capacity after the war to provide reasonably full employment, it is my opinion that, whatever party is in power, the Government will be forced by popular demand to take action. It will either give direct public employment or provide otherwise for at least subsistence living for those out of work. Many alternatives are open--some have been discussed in connection with broad social security programs; a variety of others were suggested through the last depression. I doubt that any government will need to be forced to take such action. The maintenance of reasonable social security and employment conditions is more and more recognized as a Governmental responsibility.

From this fact stems an important lesson for bankers. An important opportunity for service lies open to the banking industry after the war.

A huge problem of reconversion to peacetime operations will lie before us. In many cases reconversion is not the proper term--opportunities for essentially new products and new industries will be manifold. If private industry seizes these opportunities firmly and aggressively, yet not speculatively, the job of reconversion and that of putting men back to peacetime work will solve each other mutually.

Where do you as bankers fit in? How should you plan ahead? The question almost answers itself. The need of business and industry for reconversion and operating funds after the war will be vast. Such funds will play a critical part in enabling a smooth, efficient transformation process. Swelling business reserves will provide many dollars, but where more are needed the banker must step in. Rest assured that

the lack of such funds will not be permitted to hobble the reconversion and reemployment process. It should not and it will not. If private industry and banking cannot handle the job themselves, Government will inevitably provide the financing or possibly provide the employment itself as it did in the thirties. But I know of no responsible Government official who prefers that the Government should finance the reconversion process and peacetime business operations. It is clear that the country wants private enterprise to shoulder the job of production and distribution on the basis of private capital. Yet we cannot ever again stand by and watch growing unemployment rolls and sharply falling national income.

It behooves you as bankers, in looking to the future, to encourage your customers to plan ahead, and to work with them on tentative financing and production plans. For your own part, you can gauge something of your post-war prospects by analyzing carefully your own accounts and the status of your customers. Many bankers are now getting real benefits from studying carefully their deposits--classifying various types of business funds and separating large from small accounts. In this way it is often possible to estimate roughly which funds are likely to "stay put" after the war and which are likely to be withdrawn and spent elsewhere. In business accounts often the prospects may vary substantially for different industries, and careful study will reveal this fact. Without such real knowledge of his deposit accounts, I find it hard to see how any banker can feel he is adequately informed on his own prospects and on the basis for his investment policy.

The day of victory will mark the opening of a glorious new era of opportunity for American business and finance. I for one want you to seize it aggressively. I for one want the flow of investment funds to continue to be primarily privately directed. I believe in private enterprise and financing. Look forward and plan ahead. We must take these steps today if we do not want chaos in the early post-war period.