Ans. 8/1 W.R.Burgess

International Labour Office,

GENEVA.

31.7.23.

Dear Mr. Strong,

I am taking the liberty of writing to you to ask your assistance in a matter on which any suggestions you might give me would be particularly valuable. It is in connection with a study I am making for the International Labour Office on "The regulation of credit and currency as a means of stabilising production and employment." Having been appointed to make a report on this question, I am very anxious to gain as complete an understanding as possible of informed economic opinion on the business cycle and of the latest ideas for monetary reform, and any assistance which you might be willing to give me would therefore be most appreciated.

In examining the recent literature on the relation of money to unemployment, I find one point of almost general agreement; the need for restricting the rate of rise or fall of the price level. A further generally agreed point is that the most efficient means for controlling price movements is provided by the rate of discount. Assuming these hypotheses, there are various practical issues which arise. Perhaps the most important for the United States is that of determining the most suitable means by which the discount policy of the Federal Reserve Board can be made effective in controlling the market rate of discount. This, at all events, is the point on which I should like most to solicit your assistance.

Various ideas have been suggested for enabling the Federal Reserve Board to secure complete control. For instance, it might be effected by raising the legal reserve requirements of banks. A suggestion is also made that State and country banks might be compelled by law to make their discount rates conform within certain limits to movements in the federal reserve bank rate. Another proposal is that the federal reserve banks should themselves borrow in the market after the manner of the Bank of England when they wish to make money scarce, and that they ought not to discount bills for clients other than member banks except at times when they wish to make money very cheap. (A suggestion which Mr. Keynes tells me he intends to develop). It is shown also as a further possible solution that if prices are allowed from now onwards to rise slowly to a point at which the legal reserve limit is almost reached and then a serious attempt is made to stabilise or at least to prevent serious deflation from that point, the country and State banks would at all times require to keep strong reserves at the federal banks, which would thus be permanently in command of the situation.

Then there are methods suggested either for creating an artificial scarcity of gold, or for ensuring that a rise in prices is more rapidly reflected in the reserve situation. With regard to the former, I am thinking more particularly of the proposal of Messrs. Foster and Catchings that a
2 certain reserve of gold should be set aside for possible future export. Mr. Miller's suggestion for assimilating the federal reserve system and policy to that of the Bank of England would seem of interest in the latter connection.

Again, there are methods which would entail the alteration of the gold content of the monetary unit: the Fisher scheme, or modified forms of it, which by artificially affecting the volume of bank reserves would oblige banks to use the discount rate in the required manner. Other suggestions of a similar character would entail the modification of the gold content as prices rise or fall according to a progressive or degressive scale, to make the scheme either more or less immediate in its effect. Finally, the gold content of the unit might be modified according to the requirements of the moment rather than according to a fixed plan or system. This would presumably be done by the Federal Reserve Board on its own initiative whenever it became necessary to make money cheap or dear; and since loss would be incurred in the process it would be necessary for the State to indemnify the federal reserve banks.

I feel considerably out of my depth in discussing these methods, since my knowledge of the working of the federal reserve system is somewhat elementary; but most of the ideas contained have been passed on from persons who should understand the question. There seems every reason to think that if all the alternative methods proposed for enabling the Federal Reserve Board to secure permanent control were thoroughly thrashed out, there would surely be one which might prove acceptable. It would be of the greatest assistance to me to know whether you yourself are of the opinion that any of the above methods would be practicable.

In addition to learning in what ways the entire banking system of the United States of America might be compelled to follow a common discount policy, it would be of the greatest value to know if there is any movement towards voluntary co-operation. If, as seems probable, the control of the trade cycle will entail, amongst other things, the adoption of a credit policy which would aim at discriminating between or "rationing" different classes of the producing community at different stages of the cycle, such a policy could only be made effective through voluntary co-operation between banks on a national scale. Any "credit" policy, as opposed to a mere "discount" policy, would seem impossible without definite mutual agreement between banking institutions. One of the most important questions, therefore, seems to be whether there is any movement in America for closer collaboration between banks and whether complete co-operation is an unattainable ideal in the future. I should be most interested to learn whether you consider any tendency in this direction is indicated in current banking methods and practice in America.

It was Professor Seligman who, when in Geneva, suggested that if I found myself in difficulties in appreciating the situation in America, I should be well advised to appeal to yourself for an opinion and assistance. My knowledge of economics is only such as I could gather together in a hurried post war course, and I am consequently having to educate myself to the problem as I go along. One method I have adopted in order to secure a more complete appreciation of international opinion with regard to the monetary solution, has been to write a short essay on trade cycles and circulate it for criticism. I am taking the liberty of sending you a copy under separate cover. This essay has of course no connection with the official work of the Office; and I hope, when you read it, you will not imagine that I myself am of the opinion that the methods proposed for the application of the "remedy" are of more than theoretical value in present times. If I were to venture an opinion as far as practical policy in America is concerned, I should be inclined to recommend the adoption of a combination of the two methods I have marked on page 2, the second as an immediate measure until the first, the final aim, were reached.

I should be very grateful indeed for any assistance you might be willing to give me either in gaining an appreciation of the practical difficulties involved in the stabilisation of prices by means of the discount rate or in propagating the idea for which I am working. From my side, the only return which I shall be able to give will be to make the best use of any ideas and suggestions you may be kind enough to give me. Incidentally, the official work I am doing at the Office is limited to an expression of the opinions of other persons not my own.

Thanking you in anticipation for any trouble to which I may be putting you,

I remain

Yours very sincerely

J. R. Bellerby.