In my remarks today I shall confine myself mainly to a discussion of some of our domestic economic problems. I shall endeavor to lay before you a picture of conditions as they exist today and to describe some of the causes and events which have brought about these conditions, and before closing shall take occasion to discuss the inequalities in the readjustment which has taken place. By way of illustration, I was told recently by a gentleman from Oklahoma, whom I met in Kansas City, that he had just had a shave and a haircut. He said that a year ago when he was in Kansas City a shave and haircut cost him the equivalent of one bushel of corn and that yesterday his shave and haircut cost him the equivalent of three bushels of corn. I may have occasion also in the course of my remarks to say something about profiteers. For some years past and up to a few months ago we heard a great deal about profiteers and profiteering. Public officials generally have denounced profiteering. The public has winced under it. Sometimes the statement is made that the Federal Reserve System is open to the charge of profiteering. Such statements are based upon the earnings made by the Federal Reserve Banks in the year ending 1919 and more particularly in the year 1920 with respect to their paid in capital, but critics disregard the fact that there are other factors besides the capital of the Federal Reserve Banks which contribute to their earning power. The average paid in capital of the twelve Federal Reserve Banks combined during the year 1920 was about $94,000,000, or 3% of the capital and surplus of all banks which are members of the Federal Reserve System ; and their average surplus, accumulated as provided by law and accrued profits total $143,000,000. Figured against paid in capital alone the net earnings of the Federal Reserve Banks for the year 1920, $149,000,000, were 158.4%, but the ratio to combined average capital and surplus was but 62.9%. That, however, is not all. Every bank relies upon its deposits for its earning power. If banks had to depend upon their capital stock and surplus alone for their earnings, banking would not be very profitable and there would be very few banks. There would be no use for joint stock companies, for an individual could as well himself loan out his own capital. The Federal Reserve Banks during the year held reserve deposits of their member banks averaging daily $1,835,000,000. Every bank which is a member of the Federal Reserve System is required by law to carry its entire legal reserve with the Federal Reserve Bank of its District in the form of a collected balance, and must under the law, maintain its full reserve at all times or else be subject to penalties. If we consider the net earnings of the Federal Reserve Banks for the year 1920 as related to the total of capital, surplus and reserve deposits, we will find they amount to but 7 per cent.

There is, however, still another very important factor contributing to the earnings of the Federal Reserve Banks - the Federal Reserve notes, obligations of the Government of the United States, which the Federal Reserve Banks are permitted to have the use of under certain conditions. A Federal Reserve Bank can deposit with the Federal Reserve Agent of its District eligible paper which has been discounted for member banks or otherwise acquired and receive Federal Reserve notes and put them into circulation. The law provides that a gold reserve of not less than 40 per cent must be maintained by Federal Reserve Banks against their notes in actual circulation. This privilege, it will be seen, adds very greatly to the earning power of the Reserve Banks and has made it possible for them to extend to the member banks and through them to the public the very large credit accommodations which were granted during the year 1920;- the largest in the history of the System.

In this connection, I may say that the Federal Reserve note has proved itself to be an elastic form of currency, expanding and contracting with the needs and requirements of the nation's business. The daily average of amount of Federal Reserve notes in circulation for all twelve Federal Reserve Banks during the year 1920 was $3,146,000,000. If the net earnings of $149,000,000 are considered in relation only to the average amount of circulation outstanding, it will be seen that they were but 4.7% of that amount. The Federal Reserve Board has the power under the law to impose an interest charge on that portion of the Federal Reserve note circulation which is not covered, dollar for dollar, by gold, the rate to be charged to be determined by the Federal Reserve Board. It is not mandatory, but optional with the Board whether or not it shall make such a charge and it has always been the Board's policy in order not to discourage the free circulation of needed currency to refrain from imposing such a charge. No injustice is done to the government because in the final analysis, the net earnings of the Reserve Banks after the payment of the 6% dividend required by law, go to the Government, for after the banks have accumulated a surplus of 100% of their subscribed capital they can retain only 10% of their net earnings and must pay the other 90% to the Government as a franchise tax. On the first day of last January, the Federal Reserve Banks paid more than $60,000,000 into the Treasury of the United States as a franchise tax. Had the Federal Reserve Board imposed an interest charge against the Federal Reserve Banks on the uncovered portion of their note circulation, the net earnings might very well have been reduced to the extent of 50 or 60 millions, but even in such an event the Government would not have been benefited because the amount which the banks would have had to pay under the imposition of such a charge would have been paid in to the Treasury month by month instead of being paid in as a franchise tax at the end of the year. The Federal Reserve Banks have accumulated a reserve for franchise tax for the current year of nearly $40,000,000, and the sum that they will pay to the Government as a franchise tax at the end of the year will no doubt be larger than the amount paid at the close of the year 1920,- not because of greater earnings, for the earnings will be less - but because of smaller deductions for account of surplus. The items I have enumerated as contributing to the earnings of the Federal Reserve Banks total $5,218,000,000, and if we consider $149,000,000 of net earnings in relation to that total, it will be seen that they are but 2.9 per cent. I ask you is that profiteering? When the Federal Reserve Act was framed care was taken that the stockholding member banks should not profiteer, for the Act provides that their dividends are limited to 6% no matter what the profits of the Reserve Bank may be. The charge has been made, however, that the Government itself is profiteering and the foregoing facts have been called to your attention in order to refute that charge.

Before discussing present conditions, I wish to point out some high lights in the financial history of this country as seen by the Federal Reserve Board from the first of January, 1919 up to last Wednesday night, May 18th.

When the United States entered the World War, our Government became the principal employer of labor, the chief borrower of money, and the greatest consumer of goods. All of our activities were readjusted with a view of furnishing the services, material, and the credits necessary for the winning of the war and our people willingly submitted to restrictions and regulations which would be plainly out of place in ordinary times of peace. With the signing of the Armistice on November 11, 1918, the war was ended from a military standpoint but not in a financial sense, because we had about two million men in France and an equal number in the training camps at home. The troops abroad had to be brought back demobilized and disbanded, and the men permitted to return to their accustomed avocations. The business and industry of the country had to readjust itself again - this time to a peace basis. The Government had large stocks of supplies on hand which had to be disposed of and also a large undetermined liability which had to be ascertained and arranged for. So in the early months of 1919 the Victory Loan was floated and even with the proceeds of that loan in hand the Government still had outstanding a large floating debt, represented by Treasury Certificates of Indebtedness, amounting to about $4,000,000,000 which amount, however, has been reduced from time to time and now stands at a considerably smaller figure.

During the year 1919 the impression prevailed that there was a world-wide shortage of goods. The people of the Old World and in America had deprived themselves during the War of most luxuries and of many of the necessities of life. They had subscribed heavily for bonds and were saving and paying for them. Our Government issued obligations amounting to over twenty-five billions of dollars within a period of eighteen months. The normal investment power of this country was estimated to be about six billion dollars a year and it had become necessary, therefore, to expand credit. People were encouraged to buy bonds, to make notes at the banks in order to carry them, the member banks discounting the notes with the Federal Reserve Banks, and this together with the burden which abnormal values placed upon our credit structure, caused great expansion of credit.

Wages advanced. Prices advanced and with raw materials advancing and wages advancing, the cost of production was greatly increased. But there was such an urgent world-wide demand for goods that even in Europe - war torn and debt ridden - a very active demand for American supplies of all kind sprang up. Our large exportations to Europe during the first half of the year 1919 were financed very largely out of the unused balance of the $10,000,000,000 fund which Congress authorized our Government to lend to those nations which were associated with us in the war. There remained over $2,500,000,000 still unexpended and available when the Armistice was signed, and our large exportations to Europe during most of the year of 1919 were paid for largely out of funds advanced by our own Treasury.

About the middle of September, 1919, various influences were at work, which all combined, gave a tremendous impetus to production and to commerce and business generally. This impetus at first was justified, but the situation was soon affected by speculation, and dangerous tendencies developed.

In the Fall of 1919 there was manifest a great wave of speculation. It was not confined to any particular section, but it swept over the country everywhere and over all countries. People who had commodities of all kinds to sell were in no hurry to place them on the market. They saw week by week prices rise and rise again, and they saw that as they took this as a guarantee of the stability of prices, prices rose/and costs of production advanced also. Merchants thought it advisable to lay in large stocks of goods in anticipation of future requirements, and many of them were in no hurry to dispose of their goods at a reasonable profit, because it seemed that the longer they held their stocks the more valuable they would become. But there were dangers in the situation and not a few were alive to those dangers. Many, however, failed to sense them. There were signs all over the world that a reaction was coming. After frequent warning, to which little heed was given, the Federal Reserve System took action. The discount rates of the Federal Reserve Banks which had been advanced first to $4\frac{1}{2}\%$ and $4\frac{3}{4}\%$ were during the latter part of January advanced to 6%. The final advance to 7% did not come until about the 1st of June, 1920. These rates were less, however, than current market rates, and the banks having the 7% rate have recently reduced it, some to 6% and others to 6½%.

On the 19th of September, 1919, the earning assets of the Federal Reserve Banks amounted to about $2,350,000,000. By January 23, 1920, during a period of four months, they had increased by nearly one billion dollars. What would have been the result if those who had charge of the administration of the Federal Reserve Banks had sat supinely by and permitted this rate of expansion to continue? If no restraining measures had been taken, if no warning signals had been given, it is probable that this rapid and reckless pace might have continued for perhaps two or three months longer, when a collapse would have been inevitable. It was highly desirable that nothing should be done of a sensational nature but that the unavoidable reaction should be controlled and made as gradual and orderly as possible. The effect of advanced discount rates of the Federal Reserve Banks was merely to slow down the rate of expansion. There was no curtailment of credit on the part of the Federal Reserve Banks, nor was there any contraction of the currency. As a matter of fact the loans and invested assets of the Federal Reserve Banks increased from the middle of January, 1920 until the 5th of November 1920, a steady and gradual increase all the way along by about $400,000,000. The volume of Federal Reserve notes in circulation increased during the same period, from January 16, 1920 to December 24, 1920, from $2,800,000,000 to $3,400,000,000, so that during the most acute period of readjustment, when the sharpest reactions were taking place, there was going on all the time a steady and gradual expansion both in Federal Reserve note issues and loans - $400,000,000 in loans and $600,000,000 in currency. A great many people have been deceived into thinking that the drastic reactions which took place last summer and fall resulted directly from some decree of some arbitrary power.

I want you to know that the reaction which took place was not decreed by any Governmental Board or by any group of banks. It was decreed by the people themselves, by the greatest of all forces - popular sentiment. People began to reduce the volume of their purchases, became more economical and discriminating, and there resulted a condition which is sometimes called the "buyers strike". Wholesale prices began to decline about the middle of May 1920. The wholesale price index number on January 1, 1919 was 203 as compared with the wholesale price index number of 100 for 1913. By the middle of May, 1920, the wholesale price index number reached 272 and stands now at about 150. It is interesting in this connection to note again that during 1920 when wholesale prices were falling there was practically a steady increase in the volume of Federal reserve notes in circulation, and in the loans and invested assets of the Federal Reserve Banks.

The first manifestation of the changing condition was the break in the silk market in March 1920. This precipitated a financial crisis in Japan, involving the suspension of many banks in that empire. Next we had the break in the wool market about the middle of May, 1920, caused primarily by an excessive supply of raw wool. The War Department had large amounts of wool on hand, accumulated for war purposes for which it had no need. It undertook to sell at public auction in the great wool market of Boston. The sales were not satisfactory. The British Government brought in wool from Australia and other dependencies and attempted to sell it in the same way. Regular importations of wool were coming in from the Argentine. About the same time the Western wool clip was ready for market.

Meanwhile it was evident that public opinion all over the world had undergone a change. For a while back, people did not seem to care particularly what prices they paid. The main idea was to get deliveries, and you will remember we had what is known as a sellers' market. It was experienced in all business. Purchasers had an idea that there was a real shortage of almost everything and in some cases there were actual shortages. But after all this question of surplus and shortage is merely a relative one.

We may learn what the supply of a commodity is; that can be ascertained or estimated with approximate accuracy, but no man can state in advance just what the demand for consumption is going to be, because that is a matter which depends largely upon sentiment. It is almost impossible to say what things and how much people are going to require or what they need, for while actual human needs are very simple, there are a great many things people have become accustomed to which they regard as absolutely necessary. Many a man, I presume, has more clothing than he really needs, and the depression in the textile trade was due to the fact that people realized that they could do without new clothes and that in large measure brought about the demoralization of the wool market. The retailers found that they had little or no demand for woolen goods, and the tailors were not doing the usual business. They did not order goods from the mills or they cancelled orders already placed. The mills found, in the new circumstances, that they had ample supplies of raw wool and the wool merchants called in their buyers from the West and the price of wool dropped from about 72 cents a pound down to 15 or 20 cents.

Two or three months later the same experience was undergone in the cotton market. Of all American products, cotton is probably the one most dependent upon foreign markets and is most quickly affected by conditions abroad. People who were engaged in the sugar trade imagined that there was a great shortage in sugar. You will remember how sugar sky-rocketed up to 25 or 26 cents a pound. There seemed to be a shortage of sugar, but there was much held off the market in order to be sold out gradually at high prices, and then a situation developed, which seems perfectly natural now when we look backward. In view of the depreciation of foreign exchange, all other nations which produced sugar, attracted by the high price at which sugar could be sold in our market, shipped sugar here and a great many nations which were not producers of sugar but merely consumers, shipped sugar to us in order to get dollar exchange - - in other words, they were perfectly willing to deprive themselves of sugar in order to get things they needed or desired more. Consequently along in September there was a collapse in the sugar market.

During all this time the Federal Reserve Banks maintained their legal reserves but they did it by means of inter-bank rediscounting. There were 8 Federal Reserve Banks at one time which were borrowing $267,000,000 from four Federal Reserve Banks. We had no financial panic, the reserves of the Federal Reserve Banks were maintained in accordance with the law, and there never was a time when the Federal Reserve note was not redeemable in gold as required by law.

However, since the first of January of this year there has been a gradual change for the better in the position of the Federal Reserve System. The loans and earning assets of the 12 Federal Reserve Banks last Wednesday night were $2,314,000,000, a decline from the high point on October 15, 1920 of $1,108,000,000; Federal Reserve notes in circulation were $2,767,000,000, a decline since Christmas of $637,000,000, total cash reserves have increased from $2,249,000,000 on December 30 to $2,549,000,000. The Federal Reserve Banks are strong; they hold today a gold reserve larger than that ever held by any central banking institution in any country, an amount equal to more than one-fourth the entire known gold supply of the world.

The invested assets and loans of the Federal Reserve Banks have now declined to a point where they stood in September, 1919. They are about $300,000,000 less than their cash reserves; and Federal Reserve notes outstanding have declined to an amount only about $200,000,000 greater than the total cash reserves. Now, when any bank has more cash on hand than it has loans, it is in a pretty strong position.

The Federal Reserve Banks, which are the ultimate financial bulwark of all member banks and through them of the public are now in a position better than ever before to extend to all legitimate business the assistance needed and in addition to having the ability, have the disposition to do so. There are now no credit restrictions whatever. We must meet changed conditions. We have a strong reserve. We have had experience and business is readjusting itself to the new levels.

There has been no change in principle in the policy of the Federal Reserve System. There has never been any change in the underlying principles of the Federal Reserve System and I hope there never will be, because the broad policies of the Federal Reserve System are based upon the fundamental principles of sound finance and legitimate banking. While there has been no change in the principles of the Federal Reserve System, varying conditions from time to time, however, necessarily bring about changes in measures and methods of applying policies.

One thing that is holding back a revival of business is the disproportion and lack of uniformity in the readjustment process which is taking place. There are some things, certain basic raw materials for instance, prices for which are very low, below the pre-war levels and below cost of production, but there are other elements which figure in production and distribution which are still high, which have not been readjusted, so that somewhere in the process of distribution between the primary producer and the ultimate consumer, there is a hold-back. The ultimate consumer is not getting prices in proportion to what the primary producer is paid. One problem of the business and industrial world today is to iron out all these inconsistencies and let the proper relationship between one class of goods and another class of goods and between goods and services be restored.

It seems to me that this is one of the most important of our present domestic economic problems. I take it that one problem of any manufacturer or producer is to get his costs down in order that he may be able to offer his products at figures attractive to buyers, for the sellers' market has now been replaced by the buyers' market. The farmer is in hard lines, and the farmer, as we know, is a most important element. He constitutes a large percentage of our population. He is the principal producer of the necessities of life, upon which the industrial world depends for sustenance, and he is also the principal consumer of manufactured goods of every kind. Whenever any circumstances arise which impair the purchasing power of the farmer, the effect is felt in commercial and industrial centers everywhere.

The reduction of over a billion dollars during the last four or five months in loans and investments of the Federal Reserve Banks has resulted from liquidation in the larger cities, in the financial centers and in the manufacturing centers. In no appreciable degree has liquidation taken place in the agricultural districts. The Federal Reserve Act provides that all paper discounted with the Federal Reserve Banks must have a maturity of not longer than 90 days, except agricultural paper or paper based on livestock, which may have a maturity as long as six months. The Federal Reserve Banks were carrying the first of May of this year $230,000,000 of agricultural and livestock paper, of maturities from three to six months. On the first of May, 1920, they were carrying $106,000,000 of such paper and on the first of May, 1919 they were carrying only $66,000,000.

The Federal Reserve Banks have done a great deal to sustain our basic industry upon which so many other industries depend. Through rediscounts for member banks they extended credits to farmers and livestock men during the year 1920 aggregating three times the amount extended in 1919. The idea that some people have that the Federal Reserve Banks have been pressing the farmer is entirely erroneous. The Federal Reserve System is not operated with the view of coercing, pressing or oppressing anybody. It is designed to be the great safety valve of business. It is the final reservoir of credit to be resorted to in time of need and as such must be neither clogged nor depleted. The System has stood the tests of war and of the readjustment period following and it finds itself now in a stronger position than it has occupied since the flotation of the Third Liberty Loan.

The cash reserves of the twelve Federal Reserve Banks last Wednesday night, May 18th, were $2,549,000,000 as against $2,080,000,000 a year ago. There is nothing as far as the banking position of the country is concerned, as reflected by the Federal Reserve Bank statements that causes any other feeling than one of confidence.

I stand before you today as a conservative and constructive optimist. The pessimist is with us and he has his uses, but the main fault I have to find with the pessimist is that he operates at the wrong time. The present is no time for the pessimist,- the time for him to have gotten in his work was in the Fall of 1919.

I look for better conditions in the not distant future. We have still an evening up process to go through with. Things that are too low must either rise to the level of those things that are higher, or those things that are too high must come down to a lower level, or perhaps there will be an average and we will reach some level half way between.

I think that we have passed through the most trying and dangerous part of the readjustment period. If we can all get together and aid the orderly processes of production and distribution and get the public out of the idea that things will go lower and lower indefinitely, then we will get some stability into the situation. The public has a great deal of buying power left and buying power begets buying power. When one important industry resumes, others automatically revive.

In the changed conditions resulting from the war we occupy a new relationship to the world. We are no longer a debtor nation as we were in 1914 when we owed the rest of the world about $4,000,000,000. We are the world's great creditor nation today. The world owes us $10,000,000,000 on account of advances made by our Government and owes us perhaps two billion (it is impossible to ascertain the exact amount) on private account.

It is certain, however, that the United States today is a great creditor nation. In order to maintain our rate of production, we must push our foreign trade. We produce more cotton, more foodstuffs, more of a great many things than we need for our own use. We must reach out and do business with the world. We must buy things from other nations which they can produce better and more cheaply than we can, and exchange commodities with them. If we determine to do business with and for ourselves alone, it seems to me inevitable that we must then reduce our production to meet merely American requirements.

I know of no royal road back to business revival. Working back to normal will test our patience and energy, but the process will be expedited if we observe these sound principles which have stood the tests of the ages - Let us give and take, live and let live; give good value or service for what we receive and be content with moderate profits.

Let us be sane and reasonable - let us cast aside those speculative and get rich quick ideas which were so prevalent eighteen months ago and get down to hard work and solid business - then in due course we shall return to more orderly and normal conditions, and can develop not a false and hectic prosperity such as was recently experienced, but a sounder and more enduring era of good times than we have ever had before.