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Address of

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before the

Annual Convention of the Maryland Bankers Association

Atlantic City, New Jersey

May 28, 1921.

Mr. President and gentlemen of the Maryland Bankers Association, I am very happy to have an opportunity to meet you and discuss with you some of our common problems and troubles and perplexities.

I believe that you gentlemen constitute the State Section of your Association. Let me say, in order to relieve you of any doubt as to why I am here, that I am here neither to solicit membership of you in the Federal Reserve Bank of Richmond, nor to complain of such of you as are not members for not being members. The present, to my mind, is a time that invites us, whether as practical bankers or as men concerned with the administration of the nation's banking and financial affairs in a governmental way, to look a little beyond our own immediate precincts and try to take a broader and deeper view of the situation that is confronting the country at the present time. Whether you are National bankers or State bankers makes no difference; - whether merely business men or farmers, or even, for that matter, people who belong to the salaried or professional classes, or to the great body of consumers. The difficulties and perplexities surrounding the banker and the business man at the present time make no discrimination between national bankers and their customers and State bankers and their customers in the many different sections of the country, or in our many different classes of industry. If we have ever been confronted with an economic problem that concerns

all of us and from which there is no escape for any of us, except as it is an escape for all of us, it is the present situation.

I want to take occasion, therefore, this afternoon, in the time allotted to me, to draw attention to some of the outstanding factors that are involved in the existing economic and financial situation, whether you happen to be a banker in Maryland or in California; in Maine or in Texas. I mean to talk mainly about what we have come to describe by the term "postwar economic readjustment". But first I want to say a word by way of caution and correction.

A few months ago it was more common to describe what is in process as "deflation". Fortunately - fortunately for the truth, and fortunately for the truth that helps us toward a comprehension and a solution of our problem - we are latterly coming to talk less about deflation and more about readjustment. Many who did not see it last autumn now understand that it is not "deflation" from which we are suffering; that deflation, so-called, is merely a symptom of the regenerative or restorative process through which nature is putting us. What we are going through is, in fact, a readjustment or realignment of the distorted structure of industry and commerce throughout the length and breadth of our country to a normal basis. The readjustment, indeed, reaches beyond our own shores into world-commerce and into world-markets. We are not suffering alone, nor even most. We are suffering along with the rest of the world. There is no country, no matter how important nor how little important, in a commercial or financial way, that is not going through the throes of this terrible crisis of affairs from which we have been suffering. On the whole we have come through

most easily and safely. Much as we complain of our condition and much as we lament our individual sufferings and losses, we really have reason to be thankful that thus far we have come through so well and on the whole with so little damage to our economic and business morale.

Why do we call this mysterious movement or process through which we are passing "readjustment" rather than "deflation"? Foremost, and briefly, to my mind, for this reason: Deflation -- God protect the man who ever invented the word or ever undertook to naturalize it on American soil and apply it as a description of American conditions -- deflation to my mind always implies that somebody has got his hand on something and is trying to squeeze something out of it. It implies the intervention of a wilful and definite purpose on somebody's part to accomplish a result by means of forced pressure. More specifically it means forced liquidation and falling prices by restriction of credit and contraction of currency. In that sense there has been no deflation. The liquidation that swept over this country, in common with the rest of the world, in the year 1920 was not of anybody's making - least of all, of the Federal Reserve Board's. It came of itself. It was not the consequence of any policy of deflation. It was the result of an inevitable reaction in the course of economic affairs. So far as deflation has had anything at all to do with what has been going on in the last year, it has been a deflation of expectations: - a deflation of exaggerated expectations on the part of people generally throughout our country, north and south, east and west, and not only throughout the United States and the Western Hemisphere, but pretty generally throughout the world.

We went on a joy-ride soon after the Armistice. The sudden termination of the war in November, 1918, brought an immense relief to all of us. We had been tense, we had been nerved up to a terrific endeavor, the most heroic that people had ever been called upon to make in the public behalf. Suddenly, in the midst of this, came relief. All we had been told to do in the way of saving and self-denial suddenly seemed to have lost its meaning. Our pent-up emotions suddenly begot an orgy of recklessness and extravagance. People began to buy left and right, out of proportion to their means, in an endeavor to keep up with those who had become, by reason of the fortunes of war, the recipients of more than their ordinary incomes. Business, it seemed, had never been so "good". In a word, there followed close upon the Armistice a state of inflated expectation as to the future of business. Prices were rising. Speculation flourished. Everything looked good.

But in 1920 people began to doubt whether things could continue this way; they began to hesitate. In brief, their expectations began to deflate. It was they who deflated themselves in the process of getting themselves into a saner and more normal attitude as to the future of business in the country and the course of our foreign trade. So far as the Federal Reserve System was concerned, deflation never formed any part of its purpose. It went on expanding credit and currency throughout the larger part of the year 1920. It was not until crops were harvested, or until after the middle of October, that the volume of loans and discounts carried by Federal Reserve Banks showed any diminution. The great diminution has come with the year 1921 and has been a natural result of the economic reaction, intensified by reason of the fact that there

was a general let down of industry and commerce throughout the whole world as well as throughout our whole country.

Reserve bank rates have had nothing to do with producing this reaction. In the winter of 1919-1920, and later when the further advance of rate was made in June, 1920, it did something to check the expansion which had been going on. It helped to retard the process and to prevent the eventual reaction from degenerating into a violent collapse. By moderating and steadying the reaction it helped to make the inevitable readjustment orderly by comparison with what it otherwise might, and probably would, have been.

What does readjustment mean? It means that when values and prices and volumes of production have gotten out of their natural relationships they have somehow or other got to be brought back before there can be a safe and stable basis for business activity. Ordinarily in the past when we have had a violent alteration of the course of industry the thing has culminated in a terrific panic and a short, sudden, and universal collapse. There are people who argue that on the whole the universal sudden collapse that comes with panic is preferable to the slow and moderated processes we have had during the last eight or ten months under the influence of the Federal Reserve System. They believe it is better to have a short and abrupt descent and be over with it and have everybody on the same level about the same time. What we have had in fact under the slow and relatively orderly readjustment during the last eight or ten months has been in the nature of a staggered process. The readjustment and liquidation have been uneven in their incidence, as between different lines of industry and as between different sections of the country.

Prices have gone down universally, but they have not gone down uniformly. The farmer has suffered the most, and even as amongst the farmers some have suffered more than others, depending on the conditions affecting the markets for their particular staples. The cotton planter has been worse hit than any other comparable group. He is most dependent on the foreign market. The live stock man has been in a very bad situation because his products also must find a considerable market overseas. The result is that there has been extreme inequality in the readjustment process. For the most part the South, especially the Gulf cotton states, felt the heavy blow of the readjustment first, and on the whole most severely.

Ordinarily in a healthy state of industry when things are in balance there is a parallelism between the prices of finished goods as they go into use and the basic cost prices of the raw materials that go into the manufacture of those goods. There is a close correspondence between the prices of muslin and calico and of raw cotton. There is a correspondence between variations of the price of boots and shoes and variations of the cost of hides and leather. There is a parallelism between the selling prices of all these goods and labor cost and fuel cost and transportation cost. That parallelism, however, does not exist at the present time. We have raw materials, particularly such raw materials as grow on the top of the soil, as distinguished from those taken from under the soil, down pretty near to bed rock. We have some a little below the 1913 level. But in many sections of the country there has been little reflection of the fall of raw material in the finished product prices. To illustrate the point, I offer an instance

though I do not offer it as typical. We know too little as a whole of the relationship between retail prices and prices of basic raw materials in the United States at the present time to make precise generalization possible. But the instance I give you will serve as a suggestion of one of the things bothering us at the present time. Wheat has fallen from the peak, 53 per cent; flour has fallen 47 per cent. Bread has fallen 10 per cent. This indicates a striking lack of correspondence between the movement of wholesale prices and retail prices.

Now, I am well aware that it takes more than wheat or more than flour to make bread. Bread is a product of a pretty highly organized manufacturing process. The manufacturer has his plant as well as his raw material. He has his fuel as well as his raw material bill. Beyond that he has his pay roll, concerning which he could doubtless tell some very disturbing things. He also has to market his product. But when allowance is made for all these factors I do not think anyone can doubt that the disparity between selling price and cost is abnormal. A drop of 53 per cent in wheat and a drop of 40 per cent in flour, as compared with 10 per cent in the case of the loaf of bread, indicates that something is out of joint. Before we can have anything like a normal economic situation the relationship between the prices of raw material and finished product must be reestablished.

We cannot expect extensive downward revisions in wages until we get considerable extensive downward revisions in the retail selling prices of those things that make up the bulk of the ordinary workman's family consumption.



We have got to get the parallelism more completely restored between the selling prices of basic raw materials and the finished consumable commodities before we can feel that we are reasonably through with the readjustment process and that industry and business in this country will again move on a reasonably steady keel. Until that is accomplished, we shall not be through with our economic difficulties. But we have a better understanding of the nature of those difficulties, and we have a better understanding of what we have got to do to hasten the solution or elimination of some of those difficulties.

If I were to venture a statement as to what is the most important immediate point upon which to concentrate attention in the process of furthering and hastening the readjustment process I should say it was the retail price situation.

The advice that Mr. Hoover gave before the United States Chamber of Commerce a few weeks ago, when he advised people who were purchasers at retail to shop around, was good advice. We need the retail price situation to be brought into closer touch with the wholesale price situation, with the manufacturing situation and with basic industry conditions before we can feel that we have got readjustment to a satisfactory point. Everybody must share the common lot. There must be no escape for any from the common lot in times like the present. Just exactly as war makes no discrimination in the life it takes, values one man's life no more than another's; just as each man gives his life freely to the common cause, so in a time like this we must all be prepared to share the common lot if we expect a solution of our common difficulties. Peace no less than war has its trials and victories, and

if we would show one-half of the concern for our common interests in peace that we show in war, show one-half of the patriotic resolve to manfully accept whatever the present situation may require in order that it shall be corrected, we would expedite this business of post-war readjustment very materially. But unfortunately the forces of individual cupidity are apt to get the better of our generous impulses in time of peace just as in time of war there is a sort of forgetfulness of self that makes one almost court danger and welcome sacrifice, in order to justify our faith in ourselves and prove our devotion to country.

The papers this morning report that the United States Railroad Wage Board is about to hand down on the first of June its wage adjustment decision. That is a matter of great moment in helping improvement of the existing situation. It indicates the determination of this responsible agency to reduce wages as the cost of living is reduced. We may expect that they will go on with this work of wage adjustment, as the selling prices of clothing and fuel and food fall further, and particularly a reduction of house rents follow upon increased building operations. We may expect that the cost of operating the railroads so far as the wages bill is concerned will be reduced, and that in due course the Interstate Commerce Commission or the railroads of their own motion will reduce freight rates, thus eliminating another of the obstructive elements. The railroad wage situation is intimately interlocked with the whole problem of post-war readjustment.

The increase in railroad rates allowed last year, necessary as it

was in order to protect the investment status of the railroads and in order that the roads might have some hope of attracting the capital necessary to sustain them, was nevertheless so considerable as to work a very injurious interruption of the natural flow of commodities. We have great distances to cover between markets in the United States; the rates on certain traffic must necessarily be very low if goods are to move. Present high rates, if persisted in, would bring to pass some very disastrous results, and here and there some violently unfair results in breaking up established markets and industrial alignments.

I was talking with a manufacturer from the far West a few weeks ago. I asked him "What is the railroad situation doing to you?" He replied that it was one of the greatest things that had ever happened to his section. It was like a great wall of protection to local industry, he said. He went on to say that in his particular line of business there had never been as much activity - it was higher than in 1920. The eastern manufacturer could not get into his markets because of high freight rates. While that happened to be a satisfactory situation for this particular manufacturer, thus protected by railway rates, it was not a comforting condition for the manufacturer in Chicago or St. Louis or Kansas City who was thus excluded from access to a customary market. It does not make for a healthy economic situation, either, considering the country as a whole.

I would not leave you, however, with the impression that the completion of the readjustment process in this country is merely a domestic matter. Even if we get the retail price situation more

completely reconstructed, and wages adjusted on parallel lines, even if we get railroad rates satisfactorily revised downward, and even if the reserve rates of discount should be greatly lowered, we should still not be out of the woods. The foreign trade situation would be left as the fly in the ointment.

In 1920 ten commodities, mostly products of the soil, cotton leading the list with wheat following second, constituted 44 per cent of the export values from the United States. When we have ten commodities constituting close to one half of the goods we send overseas, and most of them the products of the farm, it is obvious that a shrinkage in the demand for those products must have a very serious effect upon the position of everybody in the agricultural sections and also upon manufacturing industries in non-agricultural sections which depend for a large part of their domestic market upon the buying power of the farmer. That sort of derangement works back, and this is what actually has been taking place in the last six or eight months. Europe is poor. Europe is not able to eat and dress and live as usual. Europe has not the buying power and cannot borrow. People there are consequently not eating as they ought for their own good, as well as for the good of the American farmer who has grown live stock to be eaten in Europe or who has grown cotton to be worn after it is manufactured, in Europe.

It is a curious phenomenon, but it is a fact that has been demonstrated over and over again, that even where a commodity is consumed perhaps as much as 90 per cent at home, and only ten per cent abroad, if the market for that ten per cent is destroyed or seriously curtailed it will break the price for the 90 per cent that is consumed at home. When

you have a commodity like cotton, that must find its principal market abroad, you can readily understand that the cessation of European buying or the serious diminution of European buying is sure to work havoc not only as regards the cotton planter but as regards everybody anywhere else who is dependent on the cotton planter as his customer.

We have had a shrinkage of 53 per cent in our exports in the course of the last year. The amazing thing to me is that such a shrinkage has not worked an even more violent effect upon our domestic situation. That shrinkage, it should be added, is of course a shrinkage in value, not a shrinkage in volume. Prices have gone down, so that the same bale of cotton as would have taken a higher value a year ago, or the same bushel of wheat, now takes a lower value. The percentage figure of shrinkage by value, therefore, in a certain sense gives an exaggerated impression of what has happened. Estimates of what the shrinkage of physical volume has been since the reaction set in a year ago indicate that it is about 30 per cent. That is to say, we are sending about 30 per cent less goods out of the country in point of physical volume,--measured by cargo capacity, etc.,--than a year ago. In other words, we are just about back where we were in 1913. We are shipping about the same volume of commodities to foreign markets as we did in 1913, if anything a little bit less, with the tendency still downward according to the latest indications. And this is making a very troublesome factor in our economic situation.

Since 1913 this country has grown a good deal. The census tells us that we have grown in population to about 106,000,000. But we have also grown in our productive power, in our ability to ship more wheat, more corn, more copper, iron and steel and bacon and cotton and so on. Yet Europe is

not now in a position to take as much of these as in 1913. It is evident, therefore, why the markets for certain commodities are glutted in this country. Under the strain something has got to give way. Something would have to give way even under more normal conditions. Where conditions are as abnormal as now, and where everybody is in a more or less apprehensive frame of mind, the effect of accumulated supplies of basic staples in breaking prices is of course much greater. The result is that certain of our industries have been so thoroughly readjusted that their prices are really below normal. Their prices are below what prices were in 1913 before the war broke upon the world. Until these prices, by coming up, meet certain other prices which have still to come down, the parallelism of prices will not have been reestablished and we shall not have a good condition. It is my opinion that we shall not have a good condition until Europe is once more able to come into the American market as a fairly normal buyer. We have a domestic economic situation in which the foreign factor cannot be neglected for a moment by anyone who wants to get a line on what we ought to do if we are to find a correction of it.

In this connection, I want to call your attention to a phenomenon that has been very striking and to my mind of alarming significance since the first of the year. I have in mind the tremendous flood of gold that has come to our shores from Europe.

When this movement first set in last autumn, there was a disposition on the part of some of the financial journals to take satisfaction and pride in it. They called attention to the fact that we were the great creditor nation of the world, that we were on a gold basis, and that gold was coming here for these reasons. It is true that gold is coming here

because we are the great creditor nation of the world. But it is well not to overlook that wherever there is a creditor there is also a debtor, and that on the average the prosperity of the creditor depends a good deal upon the prosperity of the debtor. A poor and distressed debtor is not a very good asset for a creditor who wants to be prosperous in the long run.

This great influx of gold that has been coming to us is evidence not of the riches of Europe but of the necessity of the situation in which Europe finds itself. The gold which the countries of Europe are sending us, - England, France, Sweden and the others - is a measure of their need. It is the measure of their need, first, and second the measure of their determination to show their good faith by going the limit in seeking to establish or maintain their credit in the American market. They are sending gold here partly in settlement of obligations already contracted and partly in order to create exchange to take care of their current purchases of things which are absolutely necessary to the functioning of their industries, and finally to keep their foreign exchanges from getting further demoralized. This gold movement, in brief, shows a disposition on their part to do their part as debtors and as business men who are long visioned and have great respect for the upbuilding of their credit to a high level in the American market.

We do not want this gold, we do not need it. We have got more gold now than we need. So has Argentina, so has Japan. Russia is practically stripped of her gold. A considerable part of the gold we are getting is undoubtedly of Russian origin. If not itself Russian gold, it is gold from European countries such as France or Sweden which replace the gold they send us with Russian gold. The rest is mainly the new gold that comes to the

London market from the South African mines and is bought in London for American account because the dollar is constantly at a premium. There is no better use that the man who has South African gold in London can put it to than to sell it to New York for dollars.

Practically all of this gold has accumulated in the hands of the Federal Reserve Banks. The Federal Reserve System has added in the course of the last twelve months about \$425,000,000 to its gold reserve. Since the first of this year when the flood-tide of the movement set in, we have added to our reserve holdings about \$340,000,000. These huge accessions have naturally had a pronounced effect in raising the reserve ratio of the Federal Reserve Banks, particularly as liquidation was going on at a rapid pace at the same time. A year ago our reserve was 42 per cent; today it is 56 per cent. This is a rise at the rate of 33 per cent in the course of a year. The reserve ratio has risen to the extent of at least one-half because of the great influx of gold into the Federal Reserve Banks. The rest of the rise is due to liquidation. We have reduced our note circulation in the past year something like \$275,000,000. We have reduced our loans and discounts by an amount something like \$850,000,000. So we have had two major influences that explain the change in the ratio of the reserve system: (1) increase in the gold reserves and (2) diminution in note liabilities. The diminution of the note liabilities is largely the result of the extinction of obligations owed by member banks to Federal Reserve Banks, and is reflected in the marked decline of the loans and discounts of the Federal Reserve Banks. But it is the foreign gold that has made much of this reduction possible.

When a customer country is so situated that it can buy only as it



pays in gold it is reasonably certain to expect that that country is going to buy just as little as possible and that its buying is going to diminish until conditions change. So far from its being a condition in which we should take satisfaction,-- this great stream of gold that is flowing to us from Europe,-- rather should it give us occasion to take pretty serious thought of what is implied in it. We cannot expect to sell much to Europe if we are going to sell only for cash, for gold. Nor will it be of very much use to us to get more gold unless we know how to use it. We have more gold than we need now. Too much gold is almost as serious an evil as too little gold. We may find that as our Federal Reserve ratio keeps rising with additions of new gold, the rise may set in operation before we see the end of it some very undesirable movements. A high gold reserve does not necessarily make for economic health. It does, however, make it possible for us, if we know how to go about it and if we have the vision and purpose, to develop a system of foreign trade financing in aid of Europe, through the agency of our banks with the assistance of the Federal Reserve Banks.

The last few months have made it so clear that there is no doubting that our economic recovery is dependent upon the economic restoration of Europe. We might as well give up as an idle day dream the thought that we can get out, altogether and safely out, of our present economic difficulties, except as Europe works back toward a more healthy and normal condition. Either we have got to reconstruct our whole internal economic organization,-- we have got to grow less cotton, we have got to grow less corn and wheat, we have got to grow less livestock, etc., and find other uses for the resources and people now employed in agriculture--

(these things are easily said but they are done with extreme difficulty and it takes a long time to do them!)-- or else we have got to help to restore the buying power, and that means restore the producing power, of the crippled peoples of Europe. That means, as the first step, that we have got to devise ways and means of financing the export of our surplus farm products and some of our surplus mineral products to Europe on credit.

Under the auspices of the Federal Reserve Board, Congress enacted a law known as the Edge Act because it was fathered by a member of the Senate who is vitally interested in what can be done by Federal legislation to open a way to cooperative banking effort in this country to finance exports. Something has been accomplished under that, but thus far too little. Considering our vaunted spirit of enterprise, our vaunted spirit of adventure, there has been, I think, a singular apathy in the last year and a half with respect to the need of finding or developing ways and means by which we can safely hook up with Europe in a commercial way. The gap or rift that exists in the international economic structure involving Europe and the United States must be bridged through the medium of adequate and protected credits. That is an urgent problem of concern to every section of the country. It can be solved, but it still awaits solution and national economic recovery waits on that solution.

I am not here to present any specific projects. I do not regard this as an appropriate occasion for that purpose. I am here to try to induce in you, and to get you to induce in others with whom you come in contact, an attitude of mind that will be hospitable toward the development and promotion of well-considered projects for the financing of our

export trade to Europe and other countries,-- but to Europe primarily,-- as they may be presented.

Let me tell you, simply as an example of the interest of the Federal Reserve Board in this matter of helping the financing of our export trade, that the Board recently issued a ruling authorizing the Federal Reserve Banks in their open market operations to buy bankers' acceptances of a maturity of six months. This step would not have been taken except under the pressure of a pretty real situation. In normal times reserve banks should restrict themselves to short maturities - not exceeding 90 days. That is a good principle for normal times. But these are not normal times. There are some things that are now more important than protecting the technical liquidity of the Federal Reserve Banks. We recognize that our first responsibility is to help business carry on and revive, to help business in every way as wisely as we know how. One thing I can say in this connection is to pledge that the Federal Reserve Board, as long as it is of its present frame of mind, will always test credit by what credit is doing to help the production and distribution of goods, to help the movement of goods from the farm to the factory and from the mine to the foundry and from factory and foundry into the markets of consumption, whether those markets be here or abroad. Recognizing that at the present it is the foreign market that particularly needs the assistance of new financial machinery, we have recently taken this step by which the exporter in this country is free to go to arrange an acceptance credit, and have six months bills drawn with the knowledge that they can be taken to a Federal Reserve Bank and that the Federal Reserve Bank is authorized to purchase them. More than this, the Federal Reserve Banks have the resources to make

investments in such bills to large amounts.

This may not appear to be a very striking contribution to our export financing problem. I think it a very important step, and one bound to yield results if exporters and bankers know how to avail themselves of it. At any rate, it represents all that the Federal Reserve Board under the statute can do. We have shown our disposition to go to the limit permitted by the law.

In conclusion, let me express my individual belief that gloomy as the situation of the world looks at the moment, it is far better than it looks. Things are mending. That ought to give us spirit and confidence for the future. The one thing I would urge at this time is that every business man should maintain belief in his country and its future and belief in himself; but also, beyond that, belief in the world. Do not imagine for a moment that the bottom has dropped out of civilization. Do not imagine for a moment that the people of France or Germany or Italy or England are essentially different from us. If we have common sense let us also credit them with common sense. If we have faith in our own integrity, let us have faith in their integrity. If we have faith in our determination and ability to meet our problems, let us have faith in their determination and ability to meet their problems. It is only as we distrust each other as nations that we have reason to be apprehensive of the future.

When I reflect upon what has taken place in the last seven years the amazing thing to me is that the world is going forward as rapidly as it is. When the whole structure of civilization has gotten such a jolt as it got by the war it takes some time to get things into working order. But every day that passes is a day further away from this condition of things

and a day nearer the attainment of a working basis. What we want at this time is to have an attitude and to help cultivate an attitude of confidence in ourselves, confidence in our future and confidence in the ability of the nations of Europe gradually to resume their normal relationship with us and the rest of the world. Civilization is going on. It is merely a question of whether with our aid the recovery will be rapid or whether without it it will have to be slow. With faith we can do all. Faith is the foundation of credit. Credit is the foundation of business, and just at this juncture it is particularly what is needed to give a fillip to our foreign trade, without whose recovery things are going to linger and drag.