

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Statement for the Press

For release in morning newspapers of
Monday, December 26, 1938

December 23, 1938

Attached is a copy of a letter sent to
Senator Byrd of Virginia by Chairman Eccles in
answer to the Senator's address in Boston of
December 10.

R-367

December 22, 1938.

My dear Senator:

In the course of your speech attacking the Government which you delivered in Boston on December 10, you so grossly misrepresented my own views that I feel compelled to address this letter to you in order to keep the record straight. You professed to quote from my speech before the New York Chapter of the American Institute of Banking on December 1, but it would appear from your misquotations that you had not done me the justice of reading my speech before you assailed it.

I cannot leave uncorrected the impression conveyed by your speech that I am an advocate of reckless, wasteful, ever increasing spending by the Government. As a banker and business man for more than twenty years before I came to Washington, I have a vital interest in the maintenance of our economic system and of our democratic institutions. I am quite as concerned as you are to maintain the solvency of the Government and to avoid the evils of inflation. However, I am equally in favor of avoiding the evils of deflation. I think I may be forgiven for feeling some impatience when a responsible public official like yourself so misconstrues my viewpoint as to make it appear that my advocacy of properly directed and properly timed Federal expenditures, for the primary purpose of stimulating private enterprise, is based on any other principle or purpose than to aid in bringing about the greatest possible degree of sustained employment and production of real wealth by private activity and enterprise, which, in turn, is the surest safeguard of our democracy as it is of the solvency of our Government. Only in this way, by restoration of national income, can we reach and maintain the balanced budget which I am as desirous as you are of achieving. You have every right to disagree as to the efficacy of fiscal, monetary and other policy in effecting stimulation in depression or retardation in a period of unsound expansion. I, of course, reserve the right to present the other side of the case. But I am convinced that it deserves consideration on its merits, without rancor or misrepresentation.

It is evident from the program you presented in your Boston address that you and I have a fundamentally different conception of the responsibility of Government and of the functioning of the economic system. Your program makes only five specific recommendations, all calling for immediate and drastic curtailment of government expenditures.

You appear to believe that a large part of the Government's expenditure is "waste". You are fearful about the Government's credit and alarmed about the "burden" put upon the country by the public debt. There is not space within a letter adequately to discuss these matters, but in view of your program and since you saw fit to make a personal attack upon me, I feel that it is in order to raise a number of questions with respect to each of the foregoing considerations.

As to the "burden" of debt: The pertinent facts are the volume of total debt in the country, the interest on that debt, and the income out of which interest may be paid. You failed to mention any of these pertinent facts. Are you aware of studies made by a distinguished group of scholars, under the auspices of the Twentieth Century Fund, indicating that the total of all domestic debts, both public and private, is no greater today than it was in 1929? That being so, does it not give a one-sided and alarming picture of the country's debt situation to concentrate attention solely upon the increase in the public debt without regard to the contraction of private debt, and without regard to the increase in population and in the material wealth of the country since 1929? Is it of no significance that, owing to the decline in the rate of interest, the total of interest payments today is far less than in 1929? Is it of no significance that while the burden of interest payments has been lessened, national income, out of which debts are serviced, increased since the low point of 1932 until in 1937 it was \$30,000,000,000 more than in 1932? Is it of no significance that the interest on the Federal debt amounts to only a little more than 1 per cent of our national income? Finally, is it of no significance that as a nation we owe our debts to ourselves and not to a foreign country?

As to your concern about the burden of taxation, have you not overlooked the fact that as national income increases, tax revenues increase, even without a rise in tax rates? National income increased from less than \$40 billions in 1932 to approximately \$70 billions in 1937. Tax receipts of the Federal Government increased from \$2,080,000,000 for the fiscal year ending June 30, 1933, to \$6,242,000,000 for the fiscal year ending June 30, 1938. The country paid about \$4 billions more in taxes but it had \$30 billions more of income a year out of which to make these payments. Would you have the public believe that the country was better off in 1932 with lower taxes and a lower public debt than it was in 1937 with higher taxes and a higher public debt?

Since 1937, national income has temporarily contracted due to a combination of factors, one of which was a too sharp and too rapid reduction, amounting to more than \$3,000,000,000, in the Government's net contribution to community buying power in 1937 as compared with 1936. The Government's net contribution to purchasing power is the amount that the Government expends over and above the amount it collects. On this basis, the Government not only drastically withdrew its stimulus to consumption in 1937, but contrary to your apparent belief, actually had a balanced cash budget and a cash surplus of about \$100,000,000 for the period from June 30, 1937, to March 30, 1938.

So much for the debt "burden". Turning to the question of what is to be entered upon the credit side of the ledger as an offset to the increase of the public debt, you evidently contend that nothing is to be entered; that the Government's expenditures, for which the debt was incurred, represented "waste".

Is it "waste", as you seem to think, to have the Government borrow and put to use otherwise idle funds of individuals and corporations? Is it "waste" to have the Government, by borrowing from the commercial banks, replenish the supply of bank deposits which contracted by one-third because of debt liquidation during the deflation, and put this newly created money to work providing employment and thus utilizing man power and productive facilities that otherwise would have remained idle? Is it "waste" for the Government to expend these newly created and these otherwise idle funds for roads, slum clearance, bridges, school houses, hospitals, and a host of other useful and necessary things that are needed by the community but are not supplied by private enterprise? Are these additions to our national wealth, additions resulting from public expenditures that are based upon increase of public debt, more "wasteful" than the expenditures in the late twenties, based upon private debt, whereby billions of dollars were diverted to uncollectable foreign loans and to build at inflated prices huge skyscrapers, office buildings and apartment houses, many of which never have been sufficiently occupied to maintain the investment?

Do you think it was "natural forces" that produced the recovery after 1933? Do you think that the restoration of the national income from less than \$40 billions to approximately \$70 billions came about in spite of and not as a result of Government expenditures? If so, why was it that for more than three years after 1929, when we did not have the legislation or expenditures to which you so strenuously object, there was no recovery, but instead, a continuing deflation until

the Government intervened on a comprehensive scale, replenished bank deposits and put these funds, together with stagnant funds held by individuals and corporations, to work? This, of course, increased the public debt after private debt had rapidly contracted. Doubtless had the Government been adequately prepared, it could have spent money more efficiently and more productively. Yet, in the light of all of the foregoing considerations, how can it justly be said that the Government's expenditures were "waste"? What to my mind is the real and irreparable waste, which the nation can least afford, is that which results from failure to use our human and material resources productively.

As to the Government's credit: Why do you suppose it was that in 1932, when the Government's debt was about half of what it is now, 3% government bonds sold down as low as 83? If the Government's credit is as precarious as you told your Boston audience, why is it that 2½% government bonds today are selling at a premium of more than 102? How does it happen that since 1933 foreign capital has steadily flowed into the country from abroad, if the credit of the country is in jeopardy, as you contend?

Early in your speech you extolled "those time-old virtues of thrift, frugality, self-reliance and industry". Somewhat later, however, you expressed alarm at the increase in debt of the last five years. I am at a loss to understand how you reconcile these two ideas. Certainly if it is good for people to save, i.e., practice the virtues of thrift and frugality, it must also be good that someone should borrow money and put it to productive uses. Private enterprise has in the years since the depression began been in no position to employ profitably anywhere near the total of the country's savings, because there was not sufficient buying power in the hands of the public to purchase the output of existing facilities of production.

In connection with the question of debt, you also make the curious statement that some day the whole amount must be repaid. Such a statement reflects a misunderstanding of the fundamental nature of our capitalist economy. Debts and obligations of various kinds are but the other side of investment, and if we ever tried to liquidate the whole amount of them, or even any substantial fraction, we would precipitate a crisis so severe that general economic paralysis would result. When there is contraction of total debt, private and public, we have deflation. We have never had prosperous conditions without an accompanying expansion of debt, either private or public, or both.

Do you think, as your speech seemed to indicate, that in a democracy the Government has no responsibility for creating debt in order to give employment at times when private indebtedness is contracting and private enterprise is unable to do so? Do you consider, as your speech implies, that government debt is evil, whereas private debt is not? One would gather from your attitude that if a private contractor, for example, borrows money to build houses you would commend him for "raising capital for private enterprise", whereas, if a government housing authority borrows money for the same purpose, you would denounce it for "incurring debt".

Do not the same general economic considerations apply to both private and public debt? Is it not true that the creation of too much debt relative to the creation of real wealth is inflationary and, therefore, bad, whether that debt be created by public or private activity, or both? Can it be said that the creation of debt, either public or private, that utilizes productively otherwise unused human and material resources, that creates real wealth, that adds both to existing real wealth and to national income, is an evil? Is not the exact opposite true?

While you say that everyone in need should be provided for, I find this statement hard to reconcile with your broadside attack on the organization that has carried most of the task of seeing to it that those in need are kept from want and starvation. You assert that "millions of able-bodied citizens rely upon the Government for support and have ceased to exert their efforts for self-help to obtain private employment". So far as I know, there is not the slightest evidence to support such a sweeping assertion. Any honest American citizen must resent the insult this implies to millions of self-respecting men and women.

You stated that you are concerned about "the character of the individual citizen" and "the dignity and the rights of the individual". So am I. I believe, however, that the most basic right of all is the right to live and next to that, the right to work. I do not think empty stomachs build character, nor do I think the substitution of idleness and a dole for useful work relief will improve either the dignity or the character of the people affected. We cannot expect to preserve our free institutions in this country if we condemn a substantial proportion of our people to prolonged idleness on a bare subsistence level of existence. Further than the right to eat and the right to a position, I think the individual, whether rich or poor, has a right to a decent place to live. I think he has a right to security in old age and to protection against temporary unemployment. I think he has a right to adequate medical

attention and to equal educational opportunities with the rest of his countrymen. The government expenditures which you condemn have in large part been the means of translating these basic rights into realities. Anyone who is genuinely sincere in his concern about the rights, the dignity, and the character of the individual citizen, far from seeking to tear down what has already been done, will want to have a hand in expanding and improving this work for the future.

There are many other questions which it seems to me your address and your attitude leave unanswered. I do not profess to know all the answers to the many complex and difficult economic problems confronting the nation, but I am convinced that if your program of sudden, drastic retrenchment were followed, we would witness another sharp reversal and renewed deflation. And I, for one, am not prepared to believe that this nation is doomed to stagnation, to a low level of national income, to a wholly unsatisfactory standard of living instead of the high standards, the achievement of which depends only upon our correct understanding of the operations of our economic system. I am convinced that your program is not only a defeatist one, a program of retrogression and not of progress, but that it would jeopardize the salvation of our democracy which I know you are as sincerely desirous of preserving as I am.

We disagree fundamentally and completely on how best to accomplish that end, but of one other thing I am also persuaded, that we will not find the answers by indulgence in name-calling, such as marred your Boston address. We will find the answers by recognizing clearly what the problems are, by understanding how our economy functions, and by working out practical solutions in an atmosphere of calm reason instead of intemperate denunciation.

Very truly yours,

(signed) M. S. Eccles.

Chairman.

Honorable Harry F. Byrd,
United States Senate,
Washington, D. C.