

112-1-120
June 16, 1945. *Ref*

The Honorable Robert F. Wagner,
Chairman, Banking and Currency Committee,
United States Senate,
Washington 25, D. C.

Dear Senator Wagner:

This is in reply to your letter of March 3 addressed to various Government agencies and others, requesting preliminary comments relative to S. 380, now pending before your Committee. The Board of Governors has given consideration to this measure and it has been under study by our research staff for some time.

I understand that various changes have been made or are to be made in the text of the bill. Accordingly, at this stage and for the purpose of this reply, I am undertaking to make only some general comments without discussing the bill in detail or presenting a formal opinion of the Board covering a measure of such far-reaching magnitude and implications.

If this bill or some similar one is enacted, Congress for the first time will have recognized by a formal declaration that the Federal Government has a large measure of responsibility for maintaining a satisfactory level of business activity and employment and that there should be some broad guide and objective formally stated by the Congress to govern governmental acts and policies affecting the Nation's economic life. While this would, of itself, mark a new departure, it would merely be a recognition of the facts (1) that the Congress has step by step authorized the assumption by the Government of numerous responsibilities affecting industry, commerce, agriculture and labor; (2) that the way in which these responsibilities are discharged, the manner in which they are financed, and the timing and direction of various Government expenditures directly affect economic activity and stability; and (3) that, therefore, Government acts and policies need to be coordinated and harmonized so that their influence upon the economy may help to sustain and stabilize it at a high and expanding level of prosperity.

An over-all guide or mandate by the Congress is desirable. It was my view, when the Banking Act of 1935 was pending in Congress, that the Federal Reserve Act should contain some guide, or mandate, stating the objective towards which monetary and credit policy should be directed. As the Banking Act of 1935 passed the House of Representatives, it contained a mandate for the Federal Reserve Board to

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use its powers to promote conditions conducive to business stability and to counteract unstabilizing fluctuations in the general level of production, trade, prices, and employment so far as may be possible within the scope of monetary action and credit administration.

Although this explicit mandate was omitted from the bill in the Senate, the Reserve System has needed to have in mind an objective such as this section sought to state textually, and it has continued to be guided by such an objective in formulating and executing policy.

Regardless of whether there is a formal statement of an objective in the law, acts and policies of Government in general should be directed towards the goal of economic stability and progress. Otherwise, confusion and cross-purposes would result from uncoordinated action and policy undertaken by a host of different Federal agencies according to differing concepts or interests. Nevertheless, formal declaration by the Congress of a broad objective of policy would make for better coordination and would help to develop the basic criteria by which to judge whether given acts and policies should or should not be pursued.

As you are well aware, the drafting of appropriate language in which to state the broad objective or declaration of policy presents difficulties. The Board of Governors from time to time has given consideration to this matter in connection with bills introduced in Congress that proposed to direct monetary authorities to make their objective the achievement and maintenance of a specified domestic price level. In a public statement on July 30, 1937, commenting on such proposals, the Board said:

"The Board assumes that, while price stabilization is stated as the objective of such proposals, the authors regard stability of prices merely as a means toward a more important end, namely, the lessening of booms and depressions and the increase in the national output and well-being, in the belief that through the maintenance of a stable price level the broader objective will be achieved.

"The Board is in full agreement with the ultimate objective of the proposals to promote economic stability, which means the maintenance of as full employment of labor and of the productive capacity of the country as can be continuously sustained."

The statement said in conclusion:

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"To sum up, the Board believes that economic stability rather than price stability should be the general objective of public policy. It is convinced that this objective cannot be achieved by monetary policy alone, but that the goal should be sought through coordination of monetary and other major policies of the Government which influence business activity, including particularly policies with respect to taxation, expenditures, lending, foreign trade, agriculture and labor.

"It should be the declared objective of the Government of the United States to maintain economic stability, and it should be the recognized duty of the Board of Governors of the Federal Reserve System to use all its powers to contribute to a concerted effort by all agencies of the Government toward the attainment of this objective."

In the draft of S. 380 enclosed with your letter, the objective is stated in terms of "continuing full employment". While this reflects a universal aspiration, it does not express with sufficient exactness what I believe the proponents of the bill have in mind. There might be continuing full employment in a primitive economy with a very low standard of living. That, manifestly, is not what is intended.

It would be equally incompatible with the bill's declared objective of "continuing full employment" to construe that phrase to mean that there should be "more jobs seeking men than there are men seeking jobs", as full employment has been defined, for instance, in some quarters in England. We have more jobs seeking men than men seeking jobs under wartime conditions, but the labor force is greatly expanded by many who in peacetime should be in school, or retired, or who would be occupied in the household, and maximum levels of employment and production are attained at the cost of heavy budgetary deficits. To curb the vast inflationary pressures generated by such wartime conditions, a degree of regimentation and control of the economy is necessary that would hardly be tolerated by the public in peacetime and, in any case, would be inconsistent with a democratic, free enterprise system. The inevitable result of forcing a peacetime economy to the levels of employment and production attained under the pressures of wartime would be uncontrollable inflation and subsequent economic collapse. In other words, full employment in this sense could not be long sustained.

The question, therefore, which I should like to raise in this letter is whether the over-all objective for Government policy should be stated in terms of "full employment" or "continuing full employment", or whether in re-drafting the bill, its proponents

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would wish to consider restating the objective in terms of maintaining economic stability at as high a level of employment and production as can be continuously sustained.

What is sought, it seems to me, is a general declaration that Government action and policy should be directed towards the goal of stabilized economic progress, with the greatest possible encouragement to individual initiative and private enterprise and with the fullest sustainable employment of labor. The Government, therefore, should be concerned primarily with such measures and policies as would create a climate favorable to private enterprise and private employment, and would prevent the irreparable losses resulting from deflation or inflation. The continued regimentation of the economy that is necessary to prevent inflation in wartime would be intolerable after peace has been restored and conversion to peacetime production has been completed.

I am in accord with suggestions already made to the authors of the bill for considering what may be done to stabilize such important sectors of the economy as, for example, the building and construction industry. And I agree with other comments you have received which point out that it would be preferable to place more emphasis upon the interrelationships of all sectors of the economy and on the responsibility of all groups to help in working out desirable long-range and counter-cyclical programs in various fields, and to place less emphasis upon the Federal Government's residual responsibility to intervene with large expenditures as offsets for deflationary conditions. In other words, the emphasis would be more on stability, rather than on what can be done when instability has been permitted to develop.

Other questions are raised by those parts of the bill dealing with procedure for formulating and presenting programs to the Congress. I shall not, however, attempt in this letter to discuss these provisions, on which you have already had suggestions from many in the executive as well as in the legislative branch of the Government.

In what I have said, I have had in mind the four questions in your letter without undertaking to answer them categorically. With regard to the question as to what assumptions, if any, have been made by the Federal Reserve with regard to the postwar level of the gross national product, the national income and employment, I perhaps should add that the Board of Governors has made no formal, official assumptions or forecasts, since there are many possible patterns that may develop, depending upon many unpredictable factors, including the military situation, governmental policies and programs

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and decisions of businesses and individuals in a situation for which there is no precedent. The Board, however, necessarily considers from time to time various possibilities of future developments, which are worked out in more or less detail and presented to the Board by its research staff.

Finally, I wish to express appreciation of this opportunity to make preliminary comments and to add that I hope the Board may be given an opportunity to present testimony at such time as the bill may be taken up in hearings before the Committee.

Sincerely yours,

(Signed) M. S. Eccles

M. S. Eccles,
Chairman.

ET:b

OK

Approved
MINUTES ON *L. J.*

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FOR FILES
Gladys Glover

L. J.