

INFLATION CONTROL

HEARING

BEFORE THE

COMMITTEE ON BANKING AND CURRENCY

HOUSE OF REPRESENTATIVES

EIGHTIETH CONGRESS

SECOND SESSION

ON

S. J. Res. 157

JOINT RESOLUTION TO AID IN PROTECTING THE NATION'S
ECONOMY AGAINST INFLATIONARY PRESSURES

JULY 29, 30, AUGUST 2, 3, AND 4, 1948

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CONTENTS

Statement of—	Page
Dodge, Joseph M., president, American Bankers Association.....	274
Eccles, Marriner S., member of the Board of Governors of the Federal Reserve System.....	164
Evans, R. M., member of the Board of Governors of the Federal Reserve System.....	85, 109, 279
McCabe, Thomas B., Chairman, Board of Governors of the Federal Reserve System.....	85
Marsh, Benjamin C., secretary, People's Lobby, Inc., Washington, D. C.....	289
Miller, Hon. William J., a Representative in Congress from the First District of Connecticut.....	279
Porter, Paul A., special assistant to the President of the United States.....	4
Potter, Alden A., statement entitled, "Is Socialism Un-American?" ..	281
Snyder, Hon. John W., Secretary of the Treasury.....	220
Thomas, Woodlief, Director, Division of Research and Statistics, Federal Reserve Board.....	85
Additional information submitted:	
Adams, Nathan, telegram from.....	278
Behind the News, article by Ray Tucker.....	73
Budget expenditures estimated for legislation proposed by the President to the special session of the Eightieth Congress (assuming enactment by September 1, 1948).....	67
Items outside the budget total.....	68
Effect of minimum-wage increase.....	69
Comparison of increases in consumer credit before and after expiration of controls.....	234
Estimated change in selected types of debt from June 30, 1945, to June 30, 1948.....	146
Excess gold certificate reserves over requirements of 35 percent gold certificates against deposits and 40 percent against Federal Reserve notes, July 31, 1948.....	203-204
Exports of scarce commodities.....	59
Federal Reserve Board (charts):	
Bank deposits and currency and gross national product.....	87
Assets of life-insurance companies.....	92
Selected savings institutions.....	91
Illinois Bankers Association, questions proposed by, from letter to Hon. Rolla C. McMillen.....	252
Treasury Department statement.....	253
Iowa Bankers Association, telegram.....	236
"It could have happened here—How Canada licked inflation," article by Paul A. Porter.....	75
Power of Congress to require banks which are not members of the Federal Reserve System to maintain certain reserves—submitted by G. B. Vest, general counsel, Board of Governors, Federal Reserve System.....	124
Reserve requirements of nonmember commercial banks.....	137
Reserve requirements of State commercial banks and trust companies, by kinds of deposits (demand and time), December 31, 1947 (percent of deposits specified).....	149
Some of the more important handicaps upon members of the Federal Reserve System as compared with nonmembers.....	204

INFLATION CONTROL

THURSDAY, JULY 29, 1948

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee convened at 10 a. m., the Hon. Jesse P. Wolcott (chairman) presiding.

Present: Messrs. Wolcott, Smith, Kunkel, Talle, Sundstrom, McMillen, Buffett, Cole, Hull, Stratton, Banta, Fletcher, Nicholson, Spence, Brown, Monroney, Folger, Hays, Rains, Buchanan, and Multer.

The CHAIRMAN. The committee will come to order.

On Monday last the President read a message to Congress and stressed the problems of inflation and housing.

We are meeting on those issues this morning, and the hearings will continue until we have an understanding of the problems before us.

The hearing this morning is on the general subject of the President's message.

Before us this morning we have Mr. Paul Porter, special assistant to the President.

I understand that you are the coordinator of this program, Mr. Porter?

Mr. PORTER. Yes, sir; as far as the preparing of suggested legislation and the presentation of the matter to Congress is concerned. That is my assignment.

The CHAIRMAN. Without objection, Mr. Porter may proceed to make his statement; and if it is agreeable with the committee, we will wait until Mr. Porter completes his statement before we ask any questions.

Mr. MONRONEY. May I ask the exact status of the Taft-Wagner-Ellender bill which was favorably reported by this committee in the closing days of Congress and is now before the Rules Committee?

The CHAIRMAN. The Taft-Ellender-Wagner bill is not before the Rules Committee. That bill has never been reported out of this committee. S. 866, known as the Taft-Ellender-Wagner bill, is still on the calendar of the committee. The bill H. R. 6888 was reported out of this committee and is before the Rules Committee. That bill, as I understand it, is on the calendar.

Mr. MONRONEY. Technically, that is still before the Rules Committee. Action has not been rescinded by this committee.

The CHAIRMAN. We did not take any action rescinding the bill. We reported out H. R. 6888. As I understand it, it is on the Union Calendar.

Mr. SMITH. Mr. Chairman, I think we ought to have a résumé of Mr. Porter's full background before he proceeds with his statement.

The CHAIRMAN. Will you give us some of your background, Mr. Porter?

Mr. PORTER. I think when I last appeared before this committee I was the Administrator of the Office of Price Administration. I am, by profession, a lawyer now engaged in private practice and temporarily on an assignment at the President's request to perform the assignment that the chairman has described.

I do not know how much detail Mr. Smith wants.

Mr. SMITH. How long were you with the Office of Price Administration?

Mr. PORTER. I came to the Office of Price Administration in March of 1942, as the first Deputy Administrator in charge of rent control. Prior to that time I had been counsel—

Mr. SMITH. Pardon me for interrupting you. When did your services with the Office of Price Administration terminate?

Mr. PORTER. I left the Office of Price Administration, I believe in the summer of 1943, when I became Associate War Food Administrator, when Judge Marvin Jones was appointed to that assignment. Then, after a brief period of working with Judge Jones in organizing the War Food Administration, I became counsel to the present Chief Justice, Justice Vinson, who was then Director of Economic Stabilization. Then I returned, after that, to private life.

I returned as Chairman of the Federal Communications Commission—

Mr. SMITH. How long were you in private life in this period of which you speak?

Mr. PORTER. From January 1944 to November 1944.

Mr. SMITH. Then you went with the Federal Communications Commission?

Mr. PORTER. Yes, sir. Then I was requested by the President to become the Administrator of the Office of Price Administration, in February of 1946.

In December of 1946 I resigned and then was requested to head an economic mission to Greece in the early part of 1947.

I returned in March 1947 and returned to private life.

Mr. SMITH. Previous to your 1941 assignment, had you been continuously engaged in the private practice of law?

Mr. PORTER. I had been with the Government prior to that. In 1933 I came to Washington with the Department of Agriculture. I served there from 1933 until 1937. I resigned in 1937 and engaged in the practice of law as counsel for a radio network in Washington.

Mr. SMITH. Would you give the committee your age?

Mr. PORTER. I am 44.

Mr. SMITH. What is the total number of years, then, that you have been engaged in private activities of one kind or another?

Mr. PORTER. Since I was about 10.

Mr. SMITH. I mean since you graduated from law school.

Mr. PORTER. I graduated from law school in 1928. For 5 years thereafter I was engaged in the practice of law and the publication of small newspapers. I came to Washington in 1933.

Mr. SMITH. One more point I would like to have made clear before you begin with your testimony. You are speaking here this morning for the President of the United States?

Mr. PORTER. I have been appointed as a special assistant to coordinate this program, or the presentation of the program. I have not checked in detail the statement that I have with the President, but I think that it accurately reflects some details of the message which he presented here to Congress.

Mr. SMITH. It reflects what?

Mr. PORTER. It reflects the opinions and recommendations which he presented to the Congress on Tuesday.

Mr. SMITH. Substantially, then, you are speaking for the President of the United States.

Mr. PORTER. Well, as I say, I am his special assistant to present this program. I presume the President speaks for himself.

Mr. SMITH. Did he not designate you to speak for him?

Mr. PORTER. Yes; I was authorized to present this program to the Congress. I do not believe that there is anything in my statement that is in conflict with any views that he might entertain.

Mr. SMITH. Are they his views or your views?

Mr. PORTER. Basically, they are my views, but I think he agrees with them.

Mr. SMITH. You are not willing to say, then, that you are here in behalf of the President of the United States?

Mr. PORTER. I am perfectly prepared to say that; yes, sir. But I would not presume to say that every statement that I might make, either in my direct statement or on cross-examination, would accurately reflect in detail the views of the President of the United States.

Mr. SPENCE. Doctor, will you yield?

Mr. SMITH. I yield.

Mr. SPENCE. Mr. Porter, I know, is very well and favorably known to the people of Kentucky, as a citizen, a lawyer, and an administrator. They have respect for him and confidence in him.

Mr. SMITH. Mr. Porter, has the President seen your statement?

Mr. PORTER. No, sir.

Mr. SMITH. He does not know what is contained in it?

Mr. PORTER. I have discussed it with him.

Mr. SMITH. To what extent have you discussed it with him?

Mr. PORTER. I think, Mr. Smith, that I should not go into the details of the conversation I had with the President of the United States. I would prefer to stand on the statement I have made. I have discussed these problems with him, however. Obviously, I have not submitted my statement to him.

The CHAIRMAN. All right.

Mr. MONRONEY. You are here as a Government witness in support of the inflation-control program as expressed by the President?

Mr. PORTER. That is right.

Mr. MONRONEY. There has been no personality transference to you to speak as Mr. Truman?

Mr. PORTER. None whatsoever.

Mr. SPENCE. You would like to complete your statement without interruption and then submit yourself to interrogation?

Mr. PORTER. That is right.

Mr. NICHOLSON. Mr. Chairman, I would like to ask the gentleman if he was employed as an attorney in the Department of Agriculture from 1933 to 1940.

Mr. PORTER. I occupied various capacities there. I was special counsel to Chester Davis when he was Administrator.

Mr. NICHOLSON. You acted as an attorney, not as knowing anything about agriculture?

Mr. PORTER. That is correct.

Shall I proceed, Mr. Chairman?

The CHAIRMAN. You may proceed.

STATEMENT OF PAUL PORTER, SPECIAL ASSISTANT TO THE PRESIDENT OF THE UNITED STATES

Mr. PORTER. Mr. Chairman and members of the committee, I am appearing here as a special assistant to the President of the United States to urge the speedy enactment of a bill which will put into effect the recommendations submitted by the President to the Congress at a joint session on last Tuesday. My testimony will be brief and directed to the support of those recommendations dealing with high prices and the problems of inflation.

Members of the President's Cabinet and other officials of the executive branch will be available to this committee to testify in detail as to particular problems coming within their specific sphere of interest. In a sense, I am completing a return engagement with your committee after a 2-year interlude. When last I was here, we were engaged in a discussion of the renewal of price controls under the Office of Price Administration. I regret, as I know you do, that these problems of high prices and inflation which the majority of Congress then thought might solve themselves are still with us. But the fact that these problems are an unavailable and unpleasant reality cannot be ignored.

The simple truth is that the country is in more economic trouble now than 2 years ago. And, as the President emphasized in his message this week, the passage of time aggravates the critical nature of these highly complex conditions. It is therefore, to be hoped that this committee and the Congress as a whole will consider immediate action to deal with the mounting inflationary pressures before it is too late.

The country today is in the midst of an unprecedented prosperity. By an index of material welfare, the average American should be more contented than ever before. I scarcely need to point out that such is not the case. This is an uneasy prosperity, haunted by fears for the future. It is also an unfair prosperity in which the condition of large groups within the country has become progressively worse. This paradox of good times and bad tempers, and the quite justified fear that our present prosperity may be built on quicksand, are primarily rooted in one fact: higher and higher prices.

Prices have been rising rapidly for over 2 years, and they are still rising. There is, in fact, danger that some of us have become so hardened to this progress that we may assume that nothing can be done about it and thus forget the certain consequences. But for millions of people these consequences are very real today, as they see their purchasing power and living standards shrink.

Let us review briefly the price history of the last 2 years. Between June 1946 and June 1948 consumers' prices have, on the average, risen 29 percent; the retail price of food is up 47 percent, the retail price of

apparel is up 25 percent, and rents are up 8 percent. Consumer prices are now at the highest point in our history. Wholesale prices have shown even more substantial increases. Thus, the average of all wholesale prices is up 47 percent, the wholesale price of food is up 61 percent, farm products are up 40 percent, and all products other than farm products and foods are up 42 percent. Wholesale prices are now more than double their prewar level and the highest in our national history.

This drastic rise in prices has had its inevitable effect on the real income of the average man. While the per capita disposable income rose from an annual rate of \$1,086 in the first half of 1946 to \$1,273 in the first half of 1948, a rise of over 15 percent, its real purchasing power has been cut by almost 10 percent.

The point I want to make is that these price increases are not something that happened only in the second half of 1946. They happened again in the second half of 1947, when wholesale prices rose 10 percent and consumer prices rose 6 percent. They are happening again now. Since the temporary decline early this year, wholesale prices by June had risen 3 percent. Consumer prices had also risen about 3 percent. Price rises on a broad scale are taking place right now. The situation in retail food prices, which have risen 6 percent between March and June, is particularly acute. It might be noted that in the last few weeks alone wholesale food prices have risen around 6 percent. How far are we prepared to permit this inflationary spiral to go? Can the Government, under its responsibility to the people, risk the consequence of further increases, which will undermine the foundations of economic prosperity and bring still greater hardships? The weight of evidence indicates that this is what will happen unless effective action is undertaken quickly.

If we look at the present situation in historical perspective, the country's precarious economic position becomes apparent. A chart which has not arrived yet, Mr. Chairman, which shows the movement of wholesale prices since 1749, which I will submit to the committee when it arrives, brings out the fact that every previous inflation of this character has been followed by a sharp decline. Such declines have always been accompanied by unemployment and depression.

If we take effective action, even at this late date, there is reason to hope that the price readjustments which are inevitable in the future can take place without general depression and unemployment. The price increases which have already occurred have undoubtedly made such a successful readjustment difficult. If prices continue to rise, the possibility of successful readjustment will progressively diminish and may soon be lost entirely.

And there is every reason to believe that prices will continue to rise, unless we act to stop them. Many people may take false consolation in the hope that the peak of the postwar inflation has been reached, that salutary downward price readjustments are now in prospect. It is true that there are certain factors, such as the grain supply, which might tend to support that view.

However, from time to time during the postwar inflationary spiral, individual factors have appeared which seemed to herald the end of the inflation. Such hopes have on each occasion been false hopes. These particular stabilizing forces have served at best to halt the upward movement temporarily and have soon been outweighed by

other factors. You may recall that throughout the second quarter of 1947 prices remained stable, on the average, and early this year they actually declined. These pauses in the inflationary process misled many people into believing that the end had been reached. It is always hazardous to attempt to predict the future, but there is no reason for placing any more confidence in optimistic predictions now than there was before.

Prices in general are rising now. Recent wage and price increases in basic industries have not yet worked their way up through the price structure. Tax reduction has meant that the restraining influence of the Government surplus will be largely or wholly lost. Defense expenditures are being stepped up. Export demand remains high. There is no indication that the backlog demands of consumers and business, accumulated during the war, have yet been fully satisfied. The volume of liquid assets in the hands of individuals and corporations has scarcely been dented. These and similar factors portend continued inflationary pressure.

Two years ago many people expected that inflation would be solved by increased production. This expectation was disappointed. Industrial production did increase from 170 in June 1946 to 192 in June 1948, an increase of 13 percent. As a matter of fact, that 13 percent increase had been achieved by November of 1947, and the volume of production has remained virtually stable for the past 9 months. But increased production did not solve the price problem, and it cannot be relied upon now any more than it could 2 years ago.

The American economy as a whole is working at full blast. Under such conditions, expansion of total industrial production depends largely upon improvements in efficiency. In a short period such increases cannot be large. In agriculture, where weather is an important factor, crop prospects are favorable. Improved feed supplies will produce a modest expansion in the production of some foods within a period of a year but could encourage producers to hold animals back from the market for heavier feeding. Really significant increases require the building up of cattle and dairy herds. This takes time. And it should be remembered that even the favorable feed outlook depends on the continuation of favorable weather conditions. The only possible conclusion is that while increased production will make an important contribution, it cannot increase fast enough to meet the problem.

The President in his message has outlined a balanced and constructive program of eight measures to stop inflation. This program has been incorporated into the anti-inflation and excess-profits tax bills which, it is hoped, Congress will consider and adopt. These bills are designed to halt further increases in the general level of prices by a comprehensive program that attacks the problem at all the strategic points. This is necessary to deal both with the basic cause of the inflation and with the factors that cause it to spread through the whole price system. This is legislation, Mr. Chairman, which Mr. Spence advises me he will present to the House when it convenes at noon today.

The proposed bill deals with all of these points except taxation, which will be covered in another bill.

Title I of the present bill authorizes the reimposition of control for 2 years over consumer credit by the Board of Governors of the Federal Reserve System but only with respect to installment credit.

Title II authorizes the Federal Reserve System for 2 years to increase the reserves that member banks are required to hold against demand and time deposits.

Title III authorizes the reestablishment of control over key prices and wages and then only under specified conditions. I do not propose, at this time, to treat with the standards in the pricing and wage provisions. The committee has just received the bill, and I will be glad to appear in support of the criteria used at the pleasure of the committee and when the members have had the opportunity to study its provisions in greater detail.

Title IV gives the President power to establish allocations and inventory control over scarce materials or facilities that basically affect production or the cost of living and where they are necessary to fulfill defense requirements, carry out United States foreign policy or curb inflation, and also to establish priorities, where necessary, for these purposes. It is under this title that rationing would be established for key cost-of-living commodities in the event such rationing should become necessary. This title also extends export control powers to June 30, 1950.

Title V authorizes the Housing Expediter to establish or reestablish maximum rents and strengthen enforcement.

Title VI gives the Secretary of Agriculture authority to regulate margins in connection with trading on the commodity exchanges, a power which he does not now have.

Title VII establishes an Anti-Inflation Coordinator in the Executive Office of the President to coordinate the anti-inflation activities of the executive agencies and an Anti-Inflation Advisory Board to advise the Coordinator; requires the President to submit a report to Congress at least once every quarter on the progress made in controlling inflation and on desirable legislative action; and contains certain other miscellaneous provisions.

The process of inflation is characterized by three interrelated phases. First, there is the excess of total demand—by consumers, business, Government, and foreign countries—over available supplies at existing prices. The effects of this initial phase are then intensified by the price-wage spiral. Finally, an increasing credit and money supply is essential to support the operations of the economy at the higher income and price levels; and the increased money supply, in turn, tends to reinforce the excess demand.

An effective anti-inflation policy must, at the same time limit the increase in total demand and, by selective action, bring to a halt the inflationary spiral. Without support of other measures, a restrictive credit policy would have to be so drastic to combat inflation that it would run the risk of causing a depression.

No antiinflationary policy can be effective that does not deal with the basic cause of inflation, the excessive demand. Since Government expenditures and foreign aid are determined by considerations of national policy of high priority, consumer and business demand must be limited and brought in line with available supplies of goods.

Most business expansion is financed by undistributed profits, some by bank credit and some by new capital issues. Adoption of an excess profits tax and legislation that authorizes some tightening of bank credit control are the most suitable means for limiting business expansion without interfering with desirable investment in bottleneck industries.

One method of limiting consumer demand is the reestablishment of consumer credit control. Higher down payments and shorter maturities for installment credit will limit other consumer expenditures at a time when supplies are still scarce. It should be frankly recognized that the tax relief given by the Congress to many people who are not among those hardest hit by the price rise has added billions to consumer purchasing power and has made more difficult the task of limiting it.

The curtailment of total demand, unless pursued drastically at the danger of causing a depression, will not in itself do the whole job. There is a momentum in the inflationary spiral that will continue even if the basic cause, excess demand, is effectively reduced.

There are prices that will increase because of past developments. Meat supplies will be low and meat prices high because of last year's short corn crop and high feeding costs. Wage demands are related to the price increase of the past. A continued price-wage spiral may multiply even a small excess of demand that otherwise could be absorbed by an early increase in productivity and supplies.

With respect to such a price-wage spiral, it is true that the best way to stop inflation is to top it. If a price rise in items essential in the cost of living—like meat—or in industrial production—like steel—can be prevented, the basis is laid for a stabilization of prices and wages.

Labor leaders have stated repeatedly that wages can be stabilized if the cost of living is held and if excessive profits are taxed. Gradual increases in the amounts of profits and in wages and gradual reduction of prices would then again become the method by which producers and consumers share in the fruits of technological progress and increased productivity.

It has been said that price and wage controls try to cure the symptoms rather than the cause of inflation. This argument overlooks the fact that the price-wage spiral is not only the result of inflation but also causes further inflation.

A reasonable policy involving a minimum of risk, therefore, should provide for a combination of various measures, some designed to curtail total demand, others to halt the inflationary spiral. In such combination, no measure needs to be applied drastically because each gives support to the other.

What we want, therefore, is a program which will hold inflation without incurring the risk of causing a depression. All of these requirements, we believe, are met by the balanced program proposed by the President. This program is embodied in the two bills before the Congress.

These bills should be regarded as a means of reducing excess demand; of restraining increases in prices and wages at key points which, directly and indirectly, influence the entire price and wage structure, and, finally, of securing the most desirable distribution of the chief scarce commodities.

We do not expect these measures to reduce the general price level now. We do expect them to end the upward march of prices and to reduce, so far as is possible at this late date, the threat of future collapse.

I have attempted to give you only a brief outline of the seriousness of the present inflationary situation, of the need for effective action

by our Government, and a summary of the comprehensive program submitted by the President to supply this action. I have not attempted to present a detailed statistical picture of the many facets of our economic situation which support the need for this program. We stand ready to supply you with whatever facts or analysis on specific or general points you may desire in the consideration of this program. The collective impact of individual studies, however, can only emphasize the general conclusion indicated by the over-all picture; inflationary pressures are still with us, prices are still rising and the living standards of large numbers of our people are being progressively impaired. Thus the basis for national prosperity becomes increasingly precarious.

I have also attempted to approach this problem without the hysteria which too often accompanies a discussion of matters touching so closely the interests of various groups in the economy. American industry, labor, and agriculture are producing at a record rate. We are not faced with the hyperinflation or the intense general shortages that are present in most other parts of the world. The American dollar will not become worthless. Disaster may not be just around the corner. But the prospect that the patient will not die is no excuse for subjecting him to great suffering and misery.

There is also no point in attempting to assess the blame among the various groups in the community for what has happened, or is happening, to prices. I, for one, do not believe that such an assessment is possible. There is loose talk about profiteering by business or greediness on the part of labor and farmers. But despite some unfortunate monopolistic elements which exist, prices are still established throughout most of our economy in greater or less degree in the market place, by the interaction of supply and demand. We cannot expect the farmer to sell his wheat for less than the market price because you or I may feel that it would be in the public interest for him to do so; nor can we expect other groups individually to substitute your or my idea of the public interest for normal competitive practices in determining their returns.

Our present price structure is the natural result of the operation of our economic system of private enterprise under the abnormal conditions of this postwar period. History indicates that nothing so weakens a system of free private enterprise as extreme instability of the type we are now experiencing. The blame can be laid only at the door of a Government which miscalculates its responsibilities and neglects to provide measures to protect the system from the temporary and abnormal pressures carried over from the war. We propose, even at this late date, that this neglect be remedied.

That concludes my statement, Mr. Chairman.

The CHAIRMAN. Mr. Porter, were you Administrator of OPA when the Decontrol Act of 1946 was passed?

Mr. PORTER. The Decontrol Act of 1946?

The CHAIRMAN. Yes, sir.

Mr. PORTER. Yes, sir; I believe that act was passed in July of 1946, or was it passed prior to that time? I do not recall now. I think it was in June.

The CHAIRMAN. June 30 of 1946. I am referring now to the bill which the President vetoed.

Mr. PORTER. That is correct; yes, sir.

The CHAIRMAN. Do you recall that some time during the following month, July of 1946, Congress sent another bill down to the President on the question of prices?

Mr. PORTER. Are you talking about—

The CHAIRMAN. I am speaking now about the one he signed.

Mr. PORTER. Yes, sir. That was July 26, 1946, as I recall.

The CHAIRMAN. Do you recall the reasons given by the President for the veto of the first decontrol bill?

Mr. PORTER. Yes, sir.

The CHAIRMAN. Do you recall the formula contained in that bill?

Mr. PORTER. The formula?

The CHAIRMAN. Yes, sir, for the control of prices.

Mr. PORTER. As I recall, Mr. Chairman—I have not reviewed the bill recently and I am relying completely upon my recollection—there were a number of different standards spelled out in the original bill which was vetoed.

The CHAIRMAN. With respect to prices the formula was that we would take the 1941 price base, add to that the average production cost, industry-wide, and that would be our new maximum price.

Mr. PORTER. There were other standards which were contained in the bill, such as a profit on every product.

The CHAIRMAN. That was taken out later. I might say, by way of history of the bill, the bill the President vetoed would have kept control on prices, preventing them from going unreasonably high, and it was our objective, and we felt that we had met that objective in the formula, to encourage the maximum production of goods. The President vetoed that bill.

The President, in his acceptance speech the other night, was very critical of the Congress for not giving him a workable price-control bill in 1946. Do you recall whether the Democrats or the Republicans were in control of the Congress at that time?

Mr. PORTER. To the best of my recollection, the election was in November of 1946, in which there was a change.

Mr. KUNKEL. Elections are always in November.

Mr. PORTER. We have some important ones in August.

The CHAIRMAN. I guess we can take cognizance of the fact that the Seventy-ninth Congress, which was the Congress which passed that legislation, was controlled by the Democrats. That was the bill which the President was referring to when he said it was such a rotten bill that he could not sign it, was it not?

Mr. PORTER. I do not know that he used that expression.

The CHAIRMAN. Yes, he used the expression.

Mr. PORTER. I recall that he vetoed the bill.

The CHAIRMAN. You recall that he vetoed it?

Mr. PORTER. Yes, sir.

The CHAIRMAN. After the second bill was passed and signed by the President, do you recall the action taken by the President later that year with respect to controls?

Mr. PORTER. I think he signed that bill, again expressing his dissatisfaction.

The CHAIRMAN. What did he do with respect to price controls later that year? He took them off, did he not?

Mr. PORTER. A number of them were taken off; yes, sir.

The CHAIRMAN. Did the President do that, or did the Congress do it?

Mr. PORTER. I think, Mr. Wolcott, the statement was made at that time that meat was the principal item, in the fall of 1946, and that the legislation which he had reluctantly approved as being inadequate had proved to be unworkable, and that those were the reasons assigned at that time by the President for doing so.

The CHAIRMAN. You will recall that he made the statement or do you recall that he made the statement when he took the controls off at that time, that the law of supply and demand should now be allowed to operate?

Mr. PORTER. I do not remember that specific statement. I think the hope was expressed that it would.

The CHAIRMAN. In the fall of 1947, he asked for substantially the same program that you are presenting here today. At that time, it was commented upon quite generally, to the effect that the President and his advisers could give us no information as to how these controls could be exercised, specifically. If you are given these controls, under this proposed bill, price controls, allocation controls, priority controls, how do you expect to use them? What commodities will you place under price control for example and to what extent?

Mr. PORTER. Mr. Chairman, as I indicated in my statement, the heads of the departments under whose jurisdiction—

The CHAIRMAN. Well, you are going to be the coordinator, and you are going to advise the President, subject, of course, to this advisory board which is set up, as to what commodities you are going to control. Now, I think, surely, a week after the President sends a message to Congress you should be in a position to give us some indication as to how you are going to use these controls.

Mr. PORTER. Let me state this, Mr. Chairman, for the purpose of the record: You state there is provision in this bill for a coordinator. I have no idea of who that will be.

The CHAIRMAN. I think that in view of the press releases during the last week that we may assume you will be the coordinator.

Mr. PORTER. No, sir; I think that would be a most incorrect assumption. My assignment has been limited to help in the assisting of the drafting of this bill and preparation of the presentation.

The CHAIRMAN. Let us put it this way: Has the President ever indicated to you or anybody in your presence, or do you know what the President has in mind at the present time with respect to the use of these controls, if given to him?

Mr. PORTER. It has been the subject of a considerable discussion, Mr. Chairman, with the members of the Cabinet, and the affected departments, and I can state in general terms—

The CHAIRMAN. Who has he discussed it with in the Congress?

Mr. PORTER. That I do not know.

The CHAIRMAN. You said he had consultations with the Congress.

Mr. PORTER. No; I said with members of his Cabinet and the departments. I do not know what discussions have been had with Members of Congress.

The CHAIRMAN. Pardon me.

Mr. PORTER. But the approach proposed in this bill, as I have indicated, is a selective one. Certainly—

The CHAIRMAN. That was the same thing we had last December, Mr. Porter. What are you going to select to control? That is what we want to know.

Mr. PORTER. I would assume the Secretary of Agriculture would be prepared to tell you in considerable detail—I have discussed it with him—the specific commodities where he thinks prices, at this point, should be put under a maximum price regulation.

The CHAIRMAN. What are they?

Mr. PORTER. Certainly meat is the most conspicuous one. I do not have the detailed information on the supply situation with respect to other farm commodities. Mr. Brannan is prepared to submit that to the committee in as much detail as it would desire. I would think that any department which was administering these price control powers would have to present, before issuing a maximum price regulation, a detailed statement of their justification for so doing. There are a number of food commodities which are in trouble; as I have said, meat is one.

The CHAIRMAN. What are some of the others?

Mr. PORTER. The extent to which fluid milk and dairy products would be controlled is a matter that I would prefer the committee ask Mr. Brannan about, because the Department of Agriculture has been going into that question in great detail.

The CHAIRMAN. You think you might put controls on meat and dairy products, then?

Mr. PORTER. The extent to which controls would be placed on all dairy products, I do not know. But I would think that those would be two items which are important in the cost of living, and should be given immediate attention.

The CHAIRMAN. What other commodities have you talked about placing under price control?

Mr. PORTER. Under the bill, the standards provide that you could put no maximum price regulation on any commodity unless it had risen 20 percent above June of 1947. That would not exclude very many commodities, because prices have gone, on the most important commodities, considerably beyond that. I personally think that the apparel and clothing situation is one that should receive immediate attention. Certainly some of the basic nonferrous metals and basic steel should be given immediate consideration, but as to the—

The CHAIRMAN. You say giving consideration. Are you going to put controls on them? That is what we want to find out. Are you going to use these powers after they are given to you, and how are you going to use them? You almost wrecked our economy the last time you had OPA controls. It was not until we took controls off OPA that we had production, which the President contends and which you contend is absolutely necessary to stabilize our economy. We have got to proceed rather cautiously here to see that we do not do something that will reverse this trend. At the present time, as you have said, industry and agriculture are producing at a maximum rate.

Mr. PORTER. And prices are still going up.

The CHAIRMAN. What are the causes? You have stated what you think are the causes. What I am trying to get at is, how are you going to use the powers that we might give you to remove the causes for high prices?

Mr. PORTER. I certainly would agree, Mr. Chairman, that there is not in contemplation in this bill the putting into effect of the whole broad paraphernalia of OPA controls. Rather you would pick out the critical items which are in short supply and try to prevent further price increases by regulation.

Now, I recognize that there is a great deal of difference of opinion as to whether you can proceed on a selective basis. I personally do not think we have any alternative.

The CHAIRMAN. But you cannot tell us what you are going to select for controls, that is the point I am making.

Mr. PORTER. I have mentioned a few.

The CHAIRMAN. You mentioned meat and dairy products.

Mr. PORTER. A few key commodities, industrial commodities, nonferrous metals—I would not want at this time, with the information I have, Mr. Chairman, to suggest a detailed list of particular commodities.

The CHAIRMAN. Mr. Porter, the President has had since last November, as a matter of fact, since last October, to work out the details of this program and up to the present time we have had no detailed program presented to us. This is the same program, with a little different language, which he submitted to us last December. Surely in the 7 or 8 months which have transpired between then and now somebody in the administration should be able to tell us what they have in mind with respect to the use of these controls.

Mr. PORTER. As I said, I would not want to particularize by a list of specific commodities. I think that all commodities which have risen beyond 20 percent since June of 1947 should be analyzed on a specific basis.

The CHAIRMAN. Do you think this Congress is going to give the President carte blanche authority to control our economy without knowing how he is going to use those controls?

Mr. PORTER. Mr. Chairman, we are prepared, through the heads of these departments, to get as specific as needed.

The CHAIRMAN. You have talked with them; can you not give us some indication as to what use you are going to put these controls to?

Mr. PORTER. I would not want to go beyond the statement I have made, which I think is as specific as I can get at this time. As to the food commodities, which have risen beyond 20 percent, and threaten to rise more, and where the regulations are practicable and can be enforced, a maximum price regulation should be enacted to cover commodities both in the industrial and agricultural field.

Now, I don't think it is necessary to go into those that are not essential to the cost of living. I have mentioned clothing and apparel as one item which should be under consideration.

Meat, livestock, dairy products, and others. Certainly the grain situation does not require any immediate consideration of maximum price regulations because of supply conditions. The weather factors could change it.

The case of steel and some nonferrous metals seems clear. Building materials should come in for consideration, depending upon what this Congress does about the housing program.

The CHAIRMAN. When you are speaking about the imposition of price controls on these commodities, do you also include the allocation and inventory controls on the same commodities?

Mr. PORTER. I think that you can have, depending upon the distribution pattern and the supply situation, price controls in certain areas without allocation.

The CHAIRMAN. Do you think you could have price controls on meat without allocation controls?

Mr. PORTER. No, sir; I do not.

The CHAIRMAN. Do you think you could have price controls on steel without allocation controls?

Mr. PORTER. Well, I would prefer that Secretary Sawyer give the committee the benefit of his experience under Public Law 395. There are some voluntary allocation controls which are in effect with respect to steel. I think that you could handle steel better on the basis of price control without allocation than you could a commodity where there are more producers.

The CHAIRMAN. Let us get back to the basis for high prices. First, we have an unusually large supply of purchasing power, and some goods are still in short supply.

The next point is the very unusual demand, by foreign countries, for these American goods which are in short supply.

Those are, generally speaking, the causes, are they not?

Mr. PORTER. Yes, sir.

The CHAIRMAN. So, to attack inflation, we must try to remove the causes for inflation. Has the President had any conferences with the Federal Reserve Board looking to a stabilization of the value of the American dollar?

Mr. PORTER. I assume that the matter has been a question of concern. I am not aware of any specific discussion or conference. It is my understanding that Mr. McCabe, the Chairman of the Board, is going to appear before your committee, and I think he could advise you in greater detail than I can on that.

The CHAIRMAN. Do you know whether the President has ever asked the Congress for additional powers, or whether the Federal Reserve has ever asked the Congress for additional powers with respect to that matter?

Mr. PORTER. I think they did last November; yes.

The CHAIRMAN. The request was made by Mr. Eccles for a secondary reserve. I am speaking now of a primary reserve. The secondary reserve program is something new and untried. Now, Mr. Eccles' recommendations were with respect to a secondary reserve.

Do you know whether the administration has ever asked Congress for additional authority with respect to primary reserves?

Mr. PORTER. I am not aware that they have.

The CHAIRMAN. Well, they have not, as far as I know. Do you know whether they need any additional authority to raise rediscount rates?

Mr. PORTER. Again, that is a question that I think Mr. McCabe can answer more authoritatively. I think that they do have the power to increase rediscount rates.

The CHAIRMAN. Under existing law, the rediscount rates of the Federal Reserve System have been as high as 7 percent. They are 1½ percent now, I understand.

Mr. PORTER. Yes.

The CHAIRMAN. Do you not think that is a rather direct influence on the use of our money, and on the ease with which credit can be obtained?

Mr. PORTER. I think it may be a factor, but there are probably other considerations of fiscal policy which motivate the Federal Reserve Board to maintain the rediscount rate.

The CHAIRMAN. Do you think the policy of the Federal Reserve Board with respect to supporting the price of Government bonds

above par instead of par has some relationship to the value of our money?

MR. PORTER. I think it has a stabilizing influence.

THE CHAIRMAN. Do you recall why we reduced the reserves in 1945 from 35 and 40 to 25 percent?

MR. PORTER. No; I do not.

THE CHAIRMAN. The President at that time forecast we were going to have a depression. In consequence of that, as a hedge against it, the Democratic Congress reduced the reserves deposit liability from 35 to 25 percent, reduced the reserves against Federal Reserve notes from 40 to 25 percent. So the reserves now are 25 percent. As far as I know—

MR. SMITH. Was that not at the request of the President?

THE CHAIRMAN. I assume it was. At any rate, it was done by the Democratic Congress. That had a tendency to make money easier, did it not? Did it not naturally follow that the reduced bank reserves from 35 and 40 to 25 had a tendency to make credit easier?

MR. PORTER. I will agree, Mr. Chairman, that at that particular time, there was a wide body of opinion which felt that at the end of hostilities and the reconversion program there would be the prospect of lessening of industrial activity, and perhaps the threat of widespread unemployment. But that did not happen.

THE CHAIRMAN. Then, why has not the President asked for a restoration of these reserves, from 25 to 35 and 40? We suggested it last year, but he never asked for it.

MR. PORTER. As I say, I think you would have to discuss that with the appropriate official of the Federal Reserve Board.

THE CHAIRMAN. Is not the President concerned about the relationship between debt and the value of money?

MR. PORTER. Certainly.

THE CHAIRMAN. Then, why does he not ask the Congress to do something about the monetization of the debt, by way of, for example, the sterilization of a certain amount of our debt so that it cannot be used as security for Federal Reserve notes?

MR. PORTER. Well, that is, again, a question of fiscal policy that the Secretary of the Treasury should be asked, rather than myself.

THE CHAIRMAN. Why has not the Secretary of the Treasury asked us long before this, if these are the basic reasons?

MR. PORTER. I think you will have an opportunity—

THE CHAIRMAN. I have made speeches since last October, one in particular, calling attention to the basic causes of inflation, chief of which was the easy money policy of the Government. I think we are all in agreement that the easy money policy of the Government, whereby industry, agriculture, and everybody can go to a bank and get money for 2½ percent, at a profit to the bank, is one of the basic reasons for inflation, and something that the Federal Reserve Board should take cognizance of. We cannot administer the Federal Reserve Act, We are not going to try to administer the Federal Reserve Act, because it is too extensive. It is a pretty extensive proposition for us to try to administer. As you suggest in this program, that must be a very flexible program. I think this Congress would look with favor upon a program—and we have always looked with favor upon a program—to help the Federal Reserve, if they do not have the authority at the present time, to curtail the flow of credit, because we all agree that it is the volume and velocity of credit and money

which has had more influence on prices than anything else. We have been suggesting to the Federal Reserve, we have talked with the Federal Reserve, we have talked with the Treasury, about whether they need any additional authority, and they have never yet asked us for any additional authority with respect to reserve requirements, rediscount rates, the sterilization of any part of our gold hoard or any part of our debt.

Now, the President has got to do something besides give lip service to this inflation problem.

Mr. PORTER. Mr. Chairman, I attempted to point out in my statement that it is my belief that while the policies that you advocate may be important and necessary, I do not believe that one aspect of this alone is going to solve the problem of high prices.

The CHAIRMAN. Let us take up the second one, then, export controls. Last December we gave carte blanche authority to the President to control exports. I think perhaps because of an agreement with Canada—I am told—it might be difficult to control our exports to Canada. But to every other country, exports are under very strict control and the President is not hampered at all in the exercise of that control. We saw to it that he would not be embarrassed by too many standards with respect to export controls. Now, buying for foreign account, with the billions which we have made available, superimposed upon this unusual domestic demand for goods naturally affects prices. What has the President done with respect to the control of exports to balance domestic stability against foreign demand?

Mr. PORTER. I think that the program has been administered with a certain amount of rigidity.

The CHAIRMAN. Let us take that statement.

Mr. PORTER. But consistent with the commitments that we have made to western Europe.

The CHAIRMAN. Let us take that statement. When you were asking, last fall and last spring, for grain control, allocation of grain away from the American distillers, do you know that a situation similar to this confronted us: that in 1946, for example, there were only 666 bushels of rye exported to Canada for distillation purposes. Do you know how many were exported in 1947? Over 1,300,000 bushels of rye were exported to Canada for whisky-making purposes. At the same time the President was asking us to allocate grain away from our American distilleries, he was licensing the export of grain in increasingly large volumes to Canada and the United Kingdom. Do you know how much the exports of corn to the United Kingdom increased in 1947 over 1946? About 323,000 bushels in 1946 and almost 7,000,000 in 1947. At the same time the President was asking us for legislation to control the export of grain.

Mr. PORTER. But it is my information that a small proportion of that was used for distilling purposes.

The CHAIRMAN. This is just the grain that we know was exported, that could be used for alcoholic beverage-making purposes. And they are Commerce Department figures. When we gave the President authority to control exports last December, we made it very plain in our committee reports that he was being given this authority so that he could exercise the responsibility which we said was his, to balance domestic stability against foreign demand.

Now, what use has he made of that authority, and what does he mean by telling us now that this exceptionally large export of com-

modities is not having a direct effect upon domestic prices, and at the same time telling us it is necessary to continue these exports, even outside the European recovery program?

Mr. PORTER. Well, I would assume, Mr. Chairman, that that is a consideration of foreign policy, as I have indicated in my statement, which has high priority.

The CHAIRMAN. Then, if it is a question of foreign policy which is making American prices high, why not say so, and meet the situation and be honest with the American people and tell them that our foreign policy is keeping our prices high, and let it go at that?

Mr. PORTER. If that were the only factor, it would be relatively simple. I certainly would not assert that exports do not have an impact on prices.

The CHAIRMAN. I think we agree that the two basic factors are the easy money policies of the Government and our exports.

Mr. PORTER. I think, Mr. Chairman, that the figures will show that the volume of exports now as compared with our total national product are running at a lower rate than the prewar rate. Obviously it has some significance on the price level, but I do not think it has a decisive one, and I doubt very much if you would affect prices substantially, even with an embargo, which no one has ever suggested.

The CHAIRMAN. Well, it has been suggested, and I think I can say without fear of successful contradiction that the President and the Federal Reserve Board now have the authority to plunge this country into depression, which means that they may stabilize it with the powers they already have. If they do not have the powers to stabilize our economy, then, they should ask the Congress for them. If the Federal Reserve wants any more authority to raise reserve requirements, if the President wants any more authority to control exports, I do not think this Congress would hesitate to give them that authority. The responsibility has to be placed somewhere.

Mr. PORTER. I think I undertook to point out in my statement, Mr. Chairman, that, as you have indicated, the monetary field, reserve requirements, and fiscal policy constitute a very delicate kind of operation, and that the purpose of this program which is now before the committee is to attempt to achieve stability without the danger of a serious recession.

The CHAIRMAN. On the question of export controls, again, let me read an excerpt from a statement made in an address of the President on November 17, 1947, with respect to export controls. He said—keep in mind that he was discussing the European recovery program at the same time as he was discussing inflation, taking cognizance of the effect which exports might have on domestic prices. He says this: "Those goods which we cannot wisely export must be kept here." What has he done to keep the goods here to meet the domestic demand and to bring the prices down?

Mr. PORTER. Mr. Chairman, I think if you would ask any exporter who has customers abroad, where there is demand for commodities in short supply, that he would tell you that the export licensing controls by the Office of International Trade have been administered rather vigorously.

The CHAIRMAN. But those exporters are not responsible for the stability of the American economy, and the President is; is that the point?

Mr. PORTER. My point is that these powers have been used. Mr. Sawyer—the Office of International Trade is under his jurisdiction—can give you as much detailed information about the Office of International Trade as the committee would care to receive. But it is my impression that it has been difficult to get licenses, by American exporters, for commodities which are in short supply.

The CHAIRMAN. Mr. Porter, last year there must have been licensed—he had the authority last year as well as this year—exports totaling \$19,000,000,000; we imported about \$8,000,000,000 worth; a differential of about \$11,000,000,000. That \$11,000,000,000 was financed here in the United States, partly by Government, partly by private enterprise. The controls which the President had over that situation were export controls. Of course, everyone realizes that so long as that wide differential between exports and imports continues, the demand for American goods is going to continue against a reduced supply of goods and prices are going to be affected proportionately.

Mr. PORTER. That is right.

The CHAIRMAN. It is quite generally agreed also that the instability of foreign currencies had an effect upon the exports from those countries. In other words, western European countries, including Great Britain had priced themselves out of the American market by overvaluation of their own currencies, and at the present time, although France and Italy have done something about it, I do not think any sane American importer would pay \$4.03 for the British pound sterling, unless he just had to have the goods. What has the President done about trying to correct that situation which has resulted in our having to export goods and dollars to bridge the gap between the legal and the real value of foreign currencies?

Mr. PORTER. I think that the instrumentalities of the World Bank—

The CHAIRMAN. The World Bank is a loaning agency.

Mr. PORTER. That is correct; the Stabilization Fund, I mean, has not been applied with any widespread degree, to my knowledge.

The CHAIRMAN. Let us say that the International Fund has not exercised the leadership in the field of foreign currency stabilization that we had a right to expect of the fund. And it is rather difficult for me to say that, because Mr. Spence and I were at Bretton Woods, and this committee set up that program. So I think if anyone has the right to criticize it, we in this committee have, and I do criticize that fact—I criticize the managers of the fund—for not giving us the leadership with respect to world currency stabilization that we need at this time.

Now, the Monetary Fund, having failed, do you not think it was the prerogative, if not the duty, of the President, to call an international monetary conference to consider the stability of world currencies, in order that we might increase our imports to bridge the gap between the \$8,000,000,000 and the \$19,000,000,000?

Mr. PORTER. It seems to me that preceding that, Mr. Chairman, is the question of getting some stable economic and political conditions in those countries. I do not pretend to have the background and information and the expert views in this field that you have had, but I would assume that further monetary conferences, until there are stable economic and political conditions in those countries, would accomplish very little.

The CHAIRMAN. I think the answer to that is the fact that Italy and France, being realistic about the situation, did cut their franc and lira in value, and in consequence it is expected that our imports from France and Italy are going to be appreciably greater this year than they were before they were devalued.

Do you recall the Little Steel price formula?

Mr. PORTER. That is very reminiscent.

The CHAIRMAN. That was the formula which, in substance, said that steel prices could be raised, notwithstanding the fact that they were at that time controlled, if production costs and labor costs increased. They could increase the price of steel to offset production costs. Who started that formula? Who broke the line with respect to steel prices?

Mr. PORTER. I doubt if we ever had any rigid line. There has been, as a result of collective bargaining negotiations—

The CHAIRMAN. It does not make any difference how production costs were increased. Production costs were increased and steel prices were allowed to rise, though under control, to offset those production costs.

Mr. PORTER. That is correct.

The CHAIRMAN. That was the pattern set for industry generally, was it not?

Mr. PORTER. That is correct.

The CHAIRMAN. Who did that?

Mr. PORTER. That was done by the Director of Economic Stabilization, as I recall it.

The CHAIRMAN. Who did he answer to?

Mr. PORTER. In 1945?

The CHAIRMAN. Who did he answer to? He was the right-hand man of the President, was he not?

Mr. PORTER. I presume—yes; he was a Presidential appointee.

The CHAIRMAN. The Congress did not break the line, then, did it?

Mr. PORTER. Well, the line has been a thin and wavering one; but, nevertheless, even under the Little Steel formula, where you permitted wage increases because of rising costs of living, there was a relative stability, as long as there was the opportunity to exercise powers of direct price control.

The CHAIRMAN. To refer very briefly to your proposed bill, a copy of which I got this morning and have not yet had an opportunity to study, you recognize in the bill that the prices are the aftermath of World War II.

Mr. PORTER. That is right.

The CHAIRMAN. What you mean by that is they are the result of the Government spending incident to the war and the dislocation caused by the war?

Mr. PORTER. That is correct.

The CHAIRMAN. You ask for consumer credit controls. I suppose you mean by that a restoration of what we knew as regulation W.

Mr. PORTER. That is correct.

The CHAIRMAN. Promulgated under Executive Order 8843.

Mr. PORTER. That is correct.

The CHAIRMAN. Which we rescinded last year.

Mr. PORTER. That is correct, sir.

The CHAIRMAN. Do you think that there was such an economic emergency in the United States as to justify the President calling Congress into special session?

Mr. PORTER. Yes, sir; indeed I do.

The CHAIRMAN. Do you know that the President now has the authority, or can get the authority, without legislative action, to control consumer credit?

Mr. PORTER. Installment credit?

The CHAIRMAN. Yes.

Mr. PORTER. In the face of the action of Congress specifically repealing?

The CHAIRMAN. Yes.

Mr. PORTER. I have been advised by the Federal Reserve Board that no such power exists—by their counsel.

The CHAIRMAN. Let me read the law. It is about eight lines and specifically gives the President the authority to reactivate regulation W if he declares an emergency. Let me read it to you. This is Public Law 386 of the Eightieth Congress:

That after November 1, 1947, the Board of Governors of the Federal Reserve System shall not exercise consumer credit controls pursuant to Executive Order 8843, and no such consumer credit controls shall be exercised after such date, except during the time of war beginning after the date of the enactment of this joint resolution, or any national emergency declared by the President after the date of enactment of this joint resolution.

We were very careful not to disturb the basic law under which the President gets his power to control consumer credit, which is the Trading With the Enemy Act of 1917.

Now, the President can at this moment, under this law, declare an economic emergency, or declare any other kind of an emergency, because we do not specify what kind of an emergency he has to declare. We just say "or any national emergency." It seems to me that if there was a national emergency to an extent to justify recall of Congress into special session, that likewise there was national emergency sufficient to justify the President reactivating this legislation. So I think we can agree that you do not need any legislation with respect to consumer credit control. For that reason, the Congress has not acted on the recommendations of the President with respect to these controls. We felt that he had that authority.

Mr. KUNKEL. Mr. Chairman, may I ask you a question? Was not that language of the act phrased that way so that there would be no question as to whether a war emergency would have to be involved?

The CHAIRMAN. That is right.

Mr. KUNKEL. The language was carefully drawn with that in mind, to make it clear that the President would have that authority in an emergency, whether the emergency was connected with war or with the threat of war.

The CHAIRMAN. The gentleman is absolutely right. There was a question, in the basic law, as to whether the emergency referred to in the basic law did not relate to war. So we made it very clear in this that the emergency to activate these powers by proclamation did not have to be incident to a war. We made it very clear. We did it deliberately. It was planned that way.

Mr. PORTER. Well, if I might comment on that, Mr. Chairman, I would assume that if the President had concluded that the problem

of high prices could have been solved by the declaration of an emergency pursuant to that statute and the reimposition of credit controls and nothing else, it would have been unnecessary to call Congress back on the inflation problems. But this program—

The CHAIRMAN. I am going through this to find out why he called us back to meet this situation. As I have already said—and I repeat—the President and the Federal Reserve Board now have the power, under existing law, to plunge this country into a depression or anything short of a depression, by exercise of the controls they already have or can get, without any need for further legislative enactment.

Mr. SMITH. By which you mean, Mr. Chairman, that the President has the power to lower prices to any extent.

The CHAIRMAN. Dr. Smith, I mean that this is a problem of credit expansion, and it is through credit expansion that the value of our dollar is affected to the point where prices continue to go up. That is the contention in the message of the President, I believe. If that is so, the President, by simple request of the Federal Reserve Board, would at least cause the Federal Reserve Board to consider the advisability of tightening credit to a point where nobody could get a dollar of credit in this country. He would not need to be fooling around with consumer credit controls. He could make it impossible for any businessman, industrialist, or farmer to get a dollar of credit, under controls which he now has or can get.

Mr. PORTER. Certainly nobody would advocate that course.

The CHAIRMAN. Why not? I wouldn't advocate, of course going that far, but I think we have a right to expect that the orthodox methods of stabilizing our money and our economy will be used before new powers are given to the President. And the orthodox methods by which we have stabilized our currency and met the demand of industry and agriculture has been through the manipulation of reserve requirements and rediscount rates. If they are not there for that purpose, then they are there for no purpose whatsoever. They are there for that very purpose.

Mr. PORTER. I think the chairman put his finger on the essential weakness of using one device alone, and that is, if you were to go too far, you would be in real trouble as far as a major depression is concerned.

The CHAIRMAN. Let us see what happened when they did go just part way. In February, when the Government was not buying too much for export at that particular time, when the Federal Reserve started talking about raising reserve requirements, when Mr. Eccles started talking about a secondary reserve, and the ABA put on its program to restrict the use of credit for anything but essential purposes, prices started to go down, and we all hoped that that was the stabilizing recession which we felt was long overdue.

The Federal Reserve supported bond prices, as I recall it, at 101 to 102, as a part of that program.

The administration was getting panicky because prices were going down. I do not want to say that Mr. Eccles' removal was because he was not in sympathy with the President's proposals to keep prices up, but surely something was basically wrong between the President and Mr. Eccles. We have never found out about it. I think Mr. Eccles was rather sincere in wanting to use the powers which the Federal Reserve Board had to stabilize prices in our economy, and I

think until the contrary is shown, we have a right to assume that the basic trouble between the President and Mr. Eccles was with respect to the lowering of prices or the stabilization of the American dollar.

Then, the Government went into the market and started buying grain. Instead of supporting prices of agricultural commodities, they went in and bought large quantities, not spread over a month's time or 2 months' time, but they bought I do not know how many millions of bushels, in 1 day, which could have no other effect, of course, than to cause prices to go back up. Although the Commodity Credit Corporation and the Department of Agriculture had ample authority to support prices at 90 percent, and although they could have let them go down to that and the farmer would have been better off, because by increasing the price of commodities to the consumer he was increasing the price of everything which the farmer had to buy. We realized that, but instead of doing it that way, they went in and bought these huge stocks of grains and other commodities for export, forcing prices back up again.

Finally, the rediscount rate was increased to 1½, losing altogether the psychological effect of that by the increase in purchasing by the Government for foreign countries. Now, I dare say, Mr. Porter, that if the Federal Reserve and the President acting together today were to initiate a stabilization program, there would be a psychological reaction to it to the point where we would be able to stabilize prices, because I think that 50 percent of our inflation is due to psychological reaction. If people think prices are going higher, they are going to buy and force them higher. If they think prices are going lower, they are going to sell and bring them down lower.

The President wants power. He wanted this program in December to prevent prices from going up. In February of 1948 he wanted the same powers to prevent prices from going down. How do you reconcile that?

Mr. PORTER. I do not recall specifically what you refer to.

The CHAIRMAN. Well, I do. I think we all recall it.

I refer to the fact that when prices were going down, when we thought this stabilizing recession was starting, in February, the President was reiterating that he needed controls to prevent a depression. That was in 1948.

Mr. MONRONEY. Was there a message on that, Mr. Wolcott?

The CHAIRMAN. There were letters or messages of some kind.

Mr. MONRONEY. Did they come before this committee?

The CHAIRMAN. I don't know where they went.

Mr. MONRONEY. Wouldn't this be the committee they would come to?

The CHAIRMAN. They are available. There was a message or letter, or something of that nature—or perhaps press statements. We all remember it very well. We will get the specific language for you.

Mr. BUFFETT. Mr. Chairman, will you yield?

The CHAIRMAN. Yes.

Mr. BUFFETT. I find that according to the BLS index, on March 15, this year, the cost of food items was lower than it was on September 15 last.

Mr. BUCHANAN. How many points?

Mr. BUFFETT. It went down.

Mr. BUCHANAN. Where is it now?

The CHAIRMAN. It has gone up again.

Mr. PORTER. There is the chart which shows the index.

Did you say February?

Mr. BUFFETT. March 15.

Mr. PORTER. March 15?

Mr. BUFFETT. Yes. It was actually lower than it was on September 15 of last year.

Mr. PORTER. That would be that point there [indicating]. But in spite of that particular variation, the thrust has been continuously upward, as you can see by this chart.

Mr. STRATTON. Mr. Porter, your chart there says something about consumers with moderate incomes in large cities.

Mr. PORTER. This is the same index to which I think Mr. Buffett was referring. It is the BLS index.

Mr. STRATTON. That is not a general index.

Mr. PORTER. That is the one generally referred to as the consumer's retail price index; yes.

The CHAIRMAN. Let us get back to your statement and the statement of the President again.

The President, in his message, asked, in rather unusual language, for wage controls. In what industries do you expect to use wage controls if the power is given to you?

Mr. PORTER. There is no reference to the temporary wage board as set up in the bill in the event of any collective bargaining agreement where there is a maximum price regulation if the employer does not require a price increase. So wage controls would be limited to those industries or commodities covered by a maximum price regulation where the employer sought a price increase.

The CHAIRMAN. Sought a price increase or was given a price increase?

Mr. PORTER. Sought a price increase by virtue of increased wages.

The CHAIRMAN. Is that the Little Steel formula?

Mr. PORTER. It is analogous to it.

The CHAIRMAN. You are asking us to legislate the policy which broke the line back in 1946.

Mr. PORTER. That is a matter of opinion.

The CHAIRMAN. The President says the Government should have the authority, however, to limit wage adjustments which would force a break in price ceilings, except where wage adjustments are essential to remedy hardship, to correct inequities, or to prevent an actual lowering of the living standards. Does the President want the authority to manipulate prices to remedy hardship, to correct inequities, or to prevent the lowering generally of living standards?

Mr. PORTER. I think those were the standards, generally, Mr. Chairman, that were used and applied by the old War Labor Board.

The CHAIRMAN. Well, we assume that he means that he is talking generally of living standards and hardships and inequities, industry-wide, but I think we have a right to know how he is going to exercise the authority to control wages to correct these hardships and inequities or to prevent an actual lowering of living standards.

Mr. PORTER. I think where you would find a marginal industry which required a price increase——

The CHAIRMAN. Where is there one?

Mr. PORTER. I think you could probably take one of the textile industries as one that comes to mind.

The CHAIRMAN. Do you advocate raising the wages of the textile industry worker?

Mr. PORTER. No, sir.

The CHAIRMAN. Then what do you mean by taking the textile industry as an example?

Mr. PORTER. Well, I mean there are certain industries—one doesn't come to mind at the moment—where there are inequities in the wage structure. If that is arrived at and remedied by the collective bargaining agreement process and the Wage Board would approve such an agreement, then the employer could apply for a price increase.

As to what industries those are, I have no specific one in mind at the moment.

The CHAIRMAN. Surely there must be an example that you could give us as to how you would use this power?

Mr. PORTER. I will be glad to submit for the record the wage rates—

The CHAIRMAN. What do you mean by a marginal industry?

Mr. PORTER. Well, you could take a collective bargaining agreement in a small plant, for example—perhaps in lumber or building materials; but offhand the wage levels generally, it would seem to me, if prices could be held, would or should remain at about the present levels.

The CHAIRMAN. Do you think that wages are generally too high?

Mr. PORTER. No, sir; I do not. As a matter of fact, I think, as I pointed out in my statement, that price increases in the cost of living, in spite of the third round of wage increases that we have had, have more than taken away the benefits from those wage increases.

The CHAIRMAN. You take the position, I assume, with the President, that there are industries which could absorb wage increases and higher production costs without a rise in prices.

Mr. PORTER. Yes. I have not stated—

The CHAIRMAN. All right. Just a minute.

You say "Yes." Then you say, in the same breath, that there are industries which are making excessively large profits. There undoubtedly are. I will agree with you. Would you roll back the prices of the commodities produced by these industries making these excessively large profits which, according to your standards, are excessively large?

Mr. PORTER. It is permissible, in the standards, Mr. Chairman, to get prices back to November of 1947.

The CHAIRMAN. Can you tell us which are the commodities on which you think you will roll prices back?

Mr. PORTER. I would put it this way: I would think that if this bill prevented further increases it would have achieved its purpose.

The CHAIRMAN. Are we coming to the point that you expect to freeze all prices where they are at the present time until you can look at these commodities in their cost-production relationships and until you can make these adjustments?

Mr. PORTER. No, sir; I would not think so.

The CHAIRMAN. Well, what will you do? Will you freeze all prices where they are now? What will you do with your power, if given to you?

Mr. PORTER. I would suggest, Mr. Chairman, that this be a program which would not follow the pattern of the old general maximum price regulation of April of 1942; that it be administered, as I said, on a selective basis, taking both food and industrial commodities and issuing maximum price regulations covering those.

Now, there is the further authority in the bill—which, I think is a new device—which provides that in certain areas the Administrator, or the Department, may issue a temporary regulation, and then, if the industry itself wanted to increase prices, they would have to make application to the Department or to the Administrator; and if he did not act upon it within a period of 30 days, or hold a public hearing, the price increase would become effective.

The provision I refer to is contained in the bill: the requirement for a temporary regulation. But even that, I think, would be used selectively.

The CHAIRMAN. You would be given the power, however, under the bill, to freeze prices at their present level generally?

Mr. PORTER. Yes; the power would be there.

The CHAIRMAN. Do you want to discuss marginal requirements and excess profits taxes?

Mr. PORTER. I would prefer that the Secretary of the Treasury or the Chairman of the Federal Reserve Board discuss those questions with you. The bill is being prepared, as I understand it, and will be submitted.

Mr. BUCHANAN. Mr. Chairman, in view of the fact that we may have a short session on the floor, can we recess and come back?

The CHAIRMAN. We cannot. Would it be agreeable to you to come back tomorrow morning, Mr. Porter?

Mr. PORTER. Yes, sir.

Mr. BUCHANAN. Can we meet this afternoon?

The CHAIRMAN. No. We have a Republican conference this afternoon.

If it is agreeable with the committee, we will recess at this time to reconvene tomorrow morning at 10 o'clock.

(Whereupon, the committee recessed, to reconvene at 10 a. m., Friday, July 30, 1948.)

INFLATION CONTROL

FRIDAY, JULY 30, 1948

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee reconvened at 10 a. m., the Honorable Jesse P. Wolcott, chairman, presiding.

Present: Messrs. Wolcott, Smith, Talle, Sundstrom, McMillen, Buffett, Hull, Banta, Fletcher, Spence, Brown, Monroney, Folger, Buchanan, Boggs, and Multer.

The CHAIRMAN. The committee will come to order.

We will proceed with the consideration of inflation controls.

Mr. Porter, are you familiar with the Anti-Inflation Act of 1947?

STATEMENT OF PAUL PORTER, SPECIAL ASSISTANT TO THE PRESIDENT OF THE UNITED STATES—Resumed

Mr. PORTER. I have read it; yes.

The CHAIRMAN. Public Law 395?

Mr. PORTER. Yes, sir.

The CHAIRMAN. Do you have a copy of it before you?

Mr. PORTER. No; I have not.

The CHAIRMAN. Will you turn to section 6, page 3?

Mr. PORTER. Yes, sir; I am familiar with it.

The CHAIRMAN. In this anti-inflation bill which we passed last December, we provided a specific method of procedure, when the President found that there was any danger to our economy or to our safety or our defense with respect to shortages of commodities or materials.

I would like to read this, because I think it bears somewhat upon what we should do or what the President should do with respect to present conditions.

We provided in that law of last December, section 6 (a):

Whenever the President shall determine that there is or threatens to be a critical shortage of any raw material, commodity, or product which jeopardizes the health or safety of the people of the United States or its national security or welfare and that there is no prospect that such critical shortage may soon be remedied by an increase in the available supply without additional governmental action and that the situation cannot be solved by voluntary agreement under the provisions of this Act, he may prepare proposed measures for conserving such raw material, commodity, or product which he shall submit to the Congress in the following form:

(1) A statement of the circumstances which, in the President's judgment, required the proposed conservation measures.

(2) A detailed procedure for the administration of the proposed measures including the additional budget and additional personnel required for their enforcement.

(3) The proposed degree of curtailment in current and prospective use of each such raw material, commodity, or product by each processor and/or user thereof, including the specific formulae proposed for such curtailment with respect to each class or classes of processors or users and the criteria used in the establishment of such formulae.

(4) A complete record of the factual evidence upon which his recommendations are based, including all information provided by any agency of the Federal Government which may have been made available to him in the course of his consideration of the matter.

(b) Within fifteen days after the submission of such proposed conservation measures, the Joint Committee on the Economic Report shall conduct public hearings thereon and shall make such recommendations to the Congress for legislative action as in its judgment the recommendations of the President and any additional information disclosed at the public hearings may require.

Now, why has not the President followed the procedure under that law?

Mr. PORTER. It is my information, Mr. Chairman, that there has been one submission made—

The CHAIRMAN. Grain?

Mr. PORTER. On this, which is grain. And nothing came of it.

The CHAIRMAN. Did that discourage the President from making any further recommendation?

Mr. PORTER. Well, Congress then adjourned.

The CHAIRMAN. The recommendation on wheat was made along in last January or February?

Mr. PORTER. Yes, sir; and no hearings were held, to my knowledge.

The CHAIRMAN. Oh, yes; they had hearings.

Mr. PORTER. They had hearings before the Joint Committee.

The CHAIRMAN. And the Joint Committee on the Economic Report recommended to this committee that we allocate grain, and this committee did not take any action on it because the chairman never brought it up, I might say.

Mr. PORTER. I think that was probably one incident from which the administration concluded that this procedure, in a time of crisis when prices are increasing at the accelerated rate at which they are now, that to hold hearings on each specific commodity as provided by this bill would not only be time-consuming and unworkable, but no proper action could be obtained until it was too late. Certainly the experience on grain was not sufficient to justify any confidence that this procedure would be effective.

The CHAIRMAN. Of course, the President is bound to follow the law, whether he likes the law or not, and if he does not think that the law is effective, if he does not think that the law is workable, then, I think perhaps it is his duty under the Constitution to so advise the Congress.

Mr. PORTER. This is not mandatory, as I understand it, Mr. Chairman, and he has suggested an alternative method through the proposals now before this committee. It seems to me that that is the issue.

The CHAIRMAN. Well, he has not sent any recommendations to us excepting on grain.

Mr. PORTER. Yes; and, as I say, nothing came of that, so the special session has been called to deal with the problem generally.

Mr. BUCHANAN. How about consumer credit, Mr. Chairman?

The CHAIRMAN. He has the power to control consumer credit. He does not need to send any program to Congress for that purpose.

Mr. PORTER. I do not want my silence to be construed as acquiescing in the chairman's interpretation of that statute. I think it is

doubtful whether, under that Act, with its legislative history, the power does exist.

The CHAIRMAN. Mr. Porter, I think that could have been clarified weeks ago, had the administration been serious in its interpretation of the act to the effect that they did not have the authority, because I recall that on numerous occasions, publicly, I made that statement, and referred to that law. Not perhaps as specifically as we did yesterday, but it has been referred to, and at the time the law was passed, there were statements made that the reason why we were wording it as we did was to remove the uncertainty in the basic law with respect to whether an emergency must involve a war. It is very obvious that the clear intent of Congress at that time was that we were removing any uncertainty in the existing law, and giving the President the authority to declare an emergency and get these emergency powers.

Mr. PORTER. Might I comment on that very briefly?

The CHAIRMAN. Surely.

Mr. PORTER. You will recall that the Joint Economic Committee recommended that consumer credits be extended. The Senate approved that recommendation. The bill was disapproved in the House, and the language that the chairman read yesterday was substituted, and finally adopted, which language repealed authority to deal immediately with regulation W.

Now, with respect to the President declaring and invoking a national emergency for the limited purpose of restoring consumer credit and consumer credit alone, I would be very doubtful if a proclamation dealing only with consumer credit could be justified unless the President could make a finding that to invoke consumer credit controls and to restore something like regulation W would achieve the purpose of stopping inflation, and I do not think that finding could be made.

And, as I say, in view of the legislative history and the extreme opposition to the extension of consumer credit control as reflected by the final congressional enactment, it seems to be very doubtful whether the President could issue a proclamation in terms in which the general emergency, and where the only power existing was to deal with consumer credit, would justify such a proclamation.

The CHAIRMAN. Has he submitted any program to the Congress under the provisions of section 6 of the Anti-inflation Act, excepting on grain?

Mr. PORTER. It is my information that the disappointment with the grain allocation was such as to discourage further use of section 6 and so this program is proposed as the alternative.

The CHAIRMAN. Has he ever sent a detailed program down to the Congress, or is he now sending a detailed program down to the Congress, with respect to how he shall use the powers under the provisions of this law?

Mr. PORTER. We are undertaking to submit that now.

The CHAIRMAN. We wish that you would get to it because up to the present time we have not had any details excepting that you have said generally that you would probably use them with respect to meat, dairy products, steel, and one or two other things. You have not told us yet anything about any details with respect to the procedure for the administration of the proposed measures, including additional budget and additional personnel required therefor.

Mr. PORTER. We will be happy to.

The CHAIRMAN. The statement, in keeping with section 1, of the circumstances which, in the President's judgment, require the proposed conservation measures, are found in his speech at Philadelphia and his message to the Congress, and your statement here, which I guess we can all agree are in quite general terms. There is nothing detailed in that.

Mr. PORTER. I undertook to make it clear yesterday, Mr. Chairman, that we have other witnesses who are prepared to discuss commodity problems. I would be glad to undertake it myself, but the division of responsibility in the presentation of this case to Congress is that I would undertake to outline the general bases and explain the statutory provisions we are seeking. We have, as I say, other members of the President's executive department who are prepared now to come forward and present as much detail as the committee desires to hear.

Mr. BUCHANAN. Mr. Chairman, how about the state of the Union message of January 14?

The CHAIRMAN. Well, you can add that as well.

Mr. PORTER. And the special message in November of 1947.

The CHAIRMAN. You are a lawyer, Mr. Porter. It says:

He may prepare proposed measures for conserving such raw material, commodity or product, which he shall submit to the Congress in the following form.

Then we have the provisions with respect to the procedure he must follow. I suppose that you are familiar with the rules of the courts that in these cases quite frequently is mandatory.

Mr. PORTER. I think the President would be justified in making a finding, even under that section, that he had pretty much exhausted his congressional remedies.

The CHAIRMAN. Because he had made a recommendation on one product, grain, that discouraged the President from following what was clearly the intent of Congress with respect to what the procedure would be. Otherwise, of course, we would not have gone into such detail in telling the President what information we wanted with respect to the question.

Mr. PORTER. I construe this section, faced with the realities of the crisis that we now have, as not a provision for getting something done, but a provision for stopping something.

The CHAIRMAN. Mr. Porter, he has been submitting this same program which he submitted to us last Tuesday.

Mr. PORTER. And prices have continued to rise.

The CHAIRMAN. Since last January—and we have been asking him for detailed information as to what use he would put these powers—we have asked him for the information contained in these four subsections repeatedly—every time he has been to Congress with a request for price control and allocation control and all the other controls, such as rent control.

He says a "tightening of rent control." What does he mean by a tightening of rent controls? It says here that he should give us

the proposed degree of curtailment in current and prospective use of each such raw material, commodity, or product by each processor and/or user thereof, including the specific formulas proposed for such curtailment with respect to each class or classes of processors or users and the criteria used in the establishment of such formulas.

With respect to steel, textiles, meat, and foodstuffs generally, what is his detailed program with respect to what he is going to do with the powers given to him under the provisions of this law?

Mr. PORTER. We are prepared to offer that testimony through the members of the Cabinet, whose staffs have been working on the details of administration. We are prepared to submit, to this committee or the other appropriate committees of Congress, estimates on what will be required to administer this program. And I might say that the contemplation under this bill is that the responsibility shall be assigned to the several Departments within their particular spheres of interest.

I think that there is, not the formal compliance with section 6 (a) of Public Law 395, but I certainly say and repeat that the President is obviously justified in concluding that the time does not permit the application of the statute.

I think this section is probably unworkable. As a matter of legislative policy, Congress lays down the general standards and leaves it to the administrative agencies to work out the details of administration and apply those standards. If the committees of Congress want to undertake it, it seems to me this involves the administration of the statute as much as the justification for it.

But, as I say, we are prepared to submit testimony in as much detail as the committee would desire to hear.

The CHAIRMAN. Then we may expect that when Mr. McCabe comes before the committee he will make some specific recommendations with respect to credit control? We may expect that Mr. Brannan will make some very definite statements with respect to what foods he is going to place controls on, both in the matter of price and allocation? We may expect that Mr. Sawyer will state with respect to what commodities he is going to use the controls? We are to expect Mr. Krug to tell us whether he is going to place controls on petroleum, and so forth? Is that program in such shape?

Mr. PORTER. It is my understanding that they are prepared to discuss it in specific detail.

The CHAIRMAN. All right.

Mr. FOLGER. Mr. Chairman, is that Public Law 395 to which you had reference a moment ago?

The CHAIRMAN. Yes.

Are there any questions?

Mr. SPENCE. Mr. Chairman.

The CHAIRMAN. Mr. Spence.

Mr. SPENCE. Mr. Porter, the question has arisen as to the justification for the President calling a special session—as to whether or not the facts warrant it and as to whether or not an emergency exists. Is it not a fact that after the weakened controls were removed everybody who was opposed to them said that in a short time production would take care of the conditions that existed and that prices would level off and gradually be lowered until normal conditions obtained?

That is true, is it not?

Mr. PORTER. That is correct, sir.

Mr. SPENCE. Everybody said that, who was opposed to controls. And I remember that the president of the National Association of Manufacturers appeared before this committee, in the middle of the

war, and said he was opposed to controls, and, when he was asked when they should be removed, he replied: "Tonight."

Now, it seems to me that, as these predictions have not come true, the President was justified in calling this session of Congress to meet these conditions. And conditions are steadily growing worse. Not only are they robbing the people today, but they are fraught with perils which endanger our very institutions because it is the inevitable result that after booms like this there comes a bust unless there are controls.

Now, it seems to me that the President was thoroughly justified in calling this Congress into session to meet these conditions. It is not a condition that can be met next year. It is not a condition that can be met next month. It is a condition which ought to be met at the present time. And the President said he needs these controls to meet these conditions.

I do not know just what controls should be authorized, but I do know that we ought to make an honest and an earnest attempt to meet the conditions that exist now, which are fraught with so much peril to the American people.

You do not have to read statistics. I do not have to read statistics. I know. I can see the rise of prices from day to day. I can see the rise in my grocery bill, in my butcher bill, in everything I buy. It takes \$2 now to buy what a year or two ago it took \$1 to buy. That applies to everybody.

Raises in wages of labor are immediately nullified by a rise in prices, and it seems to me there is no reason to criticize the President for attempting to meet this condition, and that the Congress ought to endeavor to meet this condition at the present time.

Is that your opinion?

Mr. PORTER. Indeed it is, sir. And, if I might comment upon what you have said, Mr. Spence, it seems to me that there have been three major criticisms of the bases of the President's program, and that goes to what is alleged to be the underlying cause of inflation.

There are some who assert that our volume of exports and our foreign trade program is the primary cause of rising prices. I do not think that can be justified factually or statistically for the simple reason that the record shows that our proportion of net exports is running, in the first quarter of 1948, at around 2½ percent of our gross national product. Certainly that could not be the major cause of our inflation.

Secondly, it is alleged that the President has not made full utilization of the powers that now exist. I have had a discussion with the chairman on that point in which I have expressed doubts as to whether the President could reimpose consumer credit control. Certainly there is no power for the allocation or channeling of scarce materials to essential uses. Certainly there is no power to impose direct price ceilings.

And, finally, there is a school of thought that asserts that you can, by some fiscal or monetary manipulation, remove the causes of inflation. I do not think that is justified.

So it seems to me that the basic issue is as you have stated it: What are we going to do now about these increased prices?

I made reference, in my testimony yesterday, to the historic sweep of prices, and I have this chart which I intended to introduce yester-

day, but was unable to do so because it was not yet prepared, in which the movements indicate quite clearly the aftermath of inflationary peaks after every war.

Starting back as early as 1749, the wholesale price index reached as high as 180 and then came down, with all the consequences of unemployment, bankruptcy, business failures, and even hunger.

Similarly, after the war of 1812, the phenomenon repeated itself.

After the Mexican war the pattern was still followed, and certainly after the Civil War it was much worse.

After World War I we all recall, from our own experience what occurred.

Now we have reached, on the upside, the same economic level that has precipitated the declines which have followed the inflated price level. So the simple question, it seems to me, which is before the Congress now is whether we are going to undertake to employ measures, which no one claims are perfect, to prevent a repetition of what has happened in the past.

Mr. SPENCE. No one of those proposed measures would accomplish the results of itself, would it? For instance, the control of consumer credit. Is it not a fact that with the immense volume of money in circulation, and with the large earnings of the people, they have enough money in their pockets, in competition for the purchase of short supply goods, to keep prices pretty high?

Mr. PORTER. That is correct.

Mr. SPENCE. And those mechanisms cannot control that. I remember in normal times, when Mr. Eccles was here. There was a bill for the Federal Reserve to attempt to establish a price level. He said it could not be done—that reserve requirements, open market operations, discount rates and the control they had over the banks could not establish, through the control of money, uniform price levels. If we could not do it then, certainly, with this avalanche of money which is now in circulation, we could not do it now. And the control of margin requirements on commodity markets would have very little effect on the great problem we are trying to solve. Is that not true?

Mr. PORTER. That is correct.

Mr. SPENCE. I know that there have been powerful influences against any price control. There were before and there are now. The seller does not want any control. He does not want control on the price of his product. That condition is with us today, and those influences will be exerted against any control. But it certainly seems to me, in the light of conditions which now exist, that all of these things should be explored and that the President should be given the power that he asks for. If he makes a failure of it, it is his failure.

Mr. PORTER. Yes, sir.

Mr. SPENCE. And if the issue continues and our Republican friends are as confident as they seem to be of winning the next election—and I do not share in that confidence entirely—they will be responsible for conditions that will be a dangerous inheritance if they inherit the conditions which are now existing. So I think there is every reason for the Congress to stay in session to solve this problem—at least to exert every effort to attempt to arrive at a satisfactory solution of this problem—in order to insure the domestic economy of the Nation and the happiness of the people.

Mr. SMITH. Mr. Chairman.

The CHAIRMAN. Dr. Smith.

Mr. SMITH. Mr. Porter, you appear before the House Committee on Banking and Currency in behalf of the President of the United States.

The President has delegated you to present to this committee a bill, H. R. unnumbered, designated "confidential print," and to urge its consideration by this committee. The stated purpose of the bill is to aid in controlling inflation. The act is cited as the "Anti-inflation Act of 1948." It is supposed, of course, that you thoroughly understand what constitutes inflation, and its true nature, and that you possess a sufficient volume of knowledge bearing upon the subject to justify your appearance before this committee. We take it that you are well grounded in the principles of inflation, the cause or causes of this social malady, the effects upon society, and so forth.

Furthermore, that you have a solid background of knowledge of inflation as experienced by other nations, both presently and in the past. Otherwise, the President would not have assigned to you the task in which you are now engaged.

I notice, Mr. Porter, that nowhere in your testimony have you defined inflation. I know, of course, that this was an inadvertency, and wholly unintentional, perhaps the result of your having taken for granted that the members of this committee are so familiar with inflation that it would be unnecessary for you to take the time of the committee to define it. Nevertheless, just for the record, and in order to have a basis for evaluating the proposals which you are urging upon this committee, we would like to have you define inflation.

Mr. PORTER. Let me say first, Dr. Smith, as to your assumption of my special knowledge of this question, that I feel that I appear here in the role of an advocate, and not as a personal defendant. I have had experience in the administration of control measures. I have made a study of what seem to me the causes of inflation and their effects. There are many, many phenomena and many factors that enter into the question of inflation. I would not undertake, and I do not believe that anyone realistically could undertake, to give a precise definition of inflation. You have the fact of excess demand, you have the factor of velocity of money, you have such problems as the expansion of credit—all of which push up on the price level. There are many, many factors that enter into inflation, and I do not think that it is susceptible of a precise definition, nor do I think anyone can be dogmatic and intelligent about it at the same time.

Mr. SMITH. That is the best answer you can give to a request for a definition of inflation?

Mr. PORTER. Well, I think that we could have an economic seminar here that would consume a long period of time, as to precisely what is inflation. A short definition could be that it is the opposite of deflation. But, as I have indicated, all of these factors enter into—

Mr. SMITH. Now, Mr. Porter, would that be a definition of inflation: the opposite term of deflation?

Mr. PORTER. As I said, that could be one short definition. Inflation—

Mr. SMITH. Do you consider that a true definition?

Mr. PORTER. That was rhetoric and I do not consider it a true definition.

Mr. SMITH. Of course, it is rhetoric and I am not asking for rhetoric. I am asking for a definition.

Mr. PORTER. Dr. Smith, there have been many texts and many books—you could fill a library—on the discussion of the causes and effects of inflation. I have indicated some of the elements. Perhaps you had others in mind. I am certain that we could probably agree on what inflation is. I doubt very much if we could agree on the remedies in the present situation.

Mr. SMITH. Then, what is inflation? If you say we can agree on it, what is it?

Mr. PORTER. Well, I have mentioned some of the factors that go to cause it. Excess demand, the velocity of money, the excess of purchasing power, availability of supplies—it is the phenomenon of rapidly accelerating prices, and I think I pointed out in my statement yesterday that there are a number of these interrelated factors—excess demand, the price-wage spiral, which is another factor, increasing credit, and money supply that is necessary to support the level of higher incomes and prices—

Mr. SMITH. Just a minute, at that point. To increase credit for what, did you say? To support what?

Mr. PORTER. Increasing money supply and credit.

Mr. SMITH. Increasing credit and money supply?

Mr. PORTER. That is right. Which is essential to support the operation of the economy at higher income and price levels.

Mr. SMITH. So that unless it is essential for that purpose, it is not inflation?

Mr. PORTER. I think that inflation finds its expression primarily in the price level.

Mr. SMITH. It finds its expression in the price level. So that price level, then, is a symptom of something; is that the idea?

Mr. PORTER. It is both a symptom and a cause.

Mr. SMITH. The price level is both a symptom and a cause?

Mr. PORTER. That is right.

Mr. SMITH. You want that to stand in the record as a part of your definition of inflation?

Mr. PORTER. I am not undertaking to give a precise definition of inflation.

Mr. SMITH. Well, I do not know just what you mean by precise, or any other term you use, but perhaps we can get at it in another way, Mr. Porter. Would you mind giving the committee some examples of inflation which have taken place in other countries?

Mr. PORTER. Well, you have obviously the situation in China. I made a first-hand study—a personal analysis—of the situation in Greece. There was an excess of demand over the available supply of essential goods.

Mr. SMITH. In China? You say that the inflation was caused by an excess of demand over the available supply of goods?

Mr. PORTER. That was one of the causes.

Mr. SMITH. Would you tell the committee what part that played or is playing in the Chinese inflation at the present time?

Mr. PORTER. There is no question but what if there were available supplies of things that people need, and consumer goods, in sufficient quantities to absorb the excess of purchasing power, that you would achieve some kind of stabilization or equilibrium.

Mr. SMITH. What is the excess currency or payment medium in China at the present time?

Mr. PORTER. I do not know. I can give you an approximation of what it is in Greece.

Mr. SMITH. What is it in Greece?

Mr. PORTER. In the year ended in 1946—I was there in the early part of 1947—you had a total national income, measured in real terms, converted to the present value of the American dollar of about 700 million dollars. In addition to that, taking aside UNRRA and relief supplies, the Greek economy was producing, in consumer goods and essential products, less than half a sufficient amount to supply that demand.

Mr. SMITH. So that if they decreased their consumer goods, they would have more inflation?

Mr. PORTER. No, there probably would have been other causes.

Mr. SMITH. Let us take for example the German inflation. When there were in circulation in Germany 400 quintillion German marks, how much production would it have required there to stabilize prices or to bring them to what you might call normal?

Mr. PORTER. Obviously, you would have to revalue the currency. That was the printing-press problem.

Mr. SMITH. What was the problem in the Russian situation? Was it a printing-press problem there, too?

Mr. PORTER. I am not familiar with conditions in Russia.

Mr. SMITH. What is the problem which is confronting France at the present time and has confronted France ever since the end of World War I? Is that a printing-press money problem?

Mr. PORTER. No. I think France has recently taken steps to stabilize its currency, to tie it to the gold franc.

Mr. SMITH. What about the condition that prevailed when they stabilized their currency?

Mr. PORTER. I think they were pricing themselves out of the export market, they could not balance their export trade and—

Mr. SMITH. And the printing press had nothing to do with it?

Mr. PORTER. Oh, yes.

Mr. SMITH. How much did the printing press have to do with it?

Mr. PORTER. I do not have those statistics in mind.

Mr. SMITH. You do not know?

Mr. PORTER. No.

Mr. SMITH. What did the printing press have to do with inflation in the Colonies, the Original Thirteen Colonies of the United States?

Mr. PORTER. As I recall, that was back in the days when the phrase "not worth a continental" was coined.

Mr. SMITH. Why was that phrase coined?

Mr. PORTER. That referred to the continental currency and the continental dollar.

Mr. SMITH. Why that opprobrious reference to the continental dollar?

Mr. PORTER. As I recall my history, the soldiers were paid off by the printing press. Other currency was likewise circulated, and there are some historians who take the position that a group of gentlemen proceeded to buy up this continental currency at about 10 or 15 cents on the dollar and then got the Federal Treasury to redeem it at par. But nevertheless—

Mr. SMITH. That is your understanding of it. Did the Federal Treasury redeem it at par?

Mr. PORTER. No. But they redeemed it at a premium.

Mr. SMITH. The Federal Treasury redeemed the continental money at a premium?

Mr. PORTER. That is my recollection. Some of it.

Mr. SMITH. Mr. Porter, you ought to go back and read your history.

Mr. PORTER. Well, I am not so much interested in post mortems, Dr. Smith.

Mr. SMITH. Now, just wait one minute, sir. You are here as an expert.

Mr. BROWN. Dr. Smith, will you pardon me there?

Mr. SMITH. Let me just finish my questioning of Mr. Porter.

Mr. Porter is here telling us that we have inflation and he proposes a remedy. I want to know if Mr. Porter knows what inflation is. That is the thing I am getting at.

Now, Mr. Porter, you apparently are unfamiliar with the historical examples of inflation and what caused them.

Mr. PORTER. That is your interpretation of what I have said.

Mr. SMITH. That is not my interpretation. Let us go back to John Law's scheme in France. Does anybody question what that debauch was due to? Is there a man who has studied the problem who questions that that was due to printing-press money? Is there a man who questions that the inflation, during the French Revolution, was due to printing-press money? I ask you the question: Is there any authority or any student of the problem at all who questions the fact that those inflations were due to printing-press money?

Mr. PORTER. I assume that I could find you some authorities who would say that that was not the only cause, but certainly—

Mr. SMITH. And could you find an authority who would say that they did not have a tremendous excess of printing-press money?

Mr. PORTER. Oh, no. Certainly there was an excess of currency in circulation.

Mr. SMITH. An excess of what?

Mr. PORTER. An excess of currency in circulation.

Mr. SMITH. All right. Now, you have acknowledged, and, as I understand you, you have agreed that inflation can be defined as excess—

Mr. PORTER. Because of excess demand, which is reflected by the amount of currency in circulation.

Mr. SMITH. Let us get back again to the German inflation. Do you hitch your demand there, still, to the amount of currency in circulation? Was there any relation at all between demand and the amount of currency when the German mark had reached the point where there were in circulation 400 or more quintillion marks? Do you relate demand at all to that volume of currency?

Mr. PORTER. I relate the price level to it.

Mr. SMITH. Oh, yes, certainly. That is another thing.

Mr. PORTER. Well, you cannot separate them, Dr. Smith.

Mr. SMITH. The price level and demand?

Mr. PORTER. Certainly you cannot.

Mr. SMITH. Then, you say, Mr. Porter, that the demand for goods in Germany, when it took bushel baskets full of paper money almost

to ride on a streetcar—I remember I used to pay something like 10 billion marks to ride on a streetcar in Germany—you say, then, that my demand for riding on that street car had something to do with the value of currency?

Mr. PORTER. I would say that if you did not have the 10 billion marks, you would have no demand on the transportation facilities—if you had nothing to pay for it.

Mr. SMITH. That is your answer. Is that the question before us?

Mr. PORTER. Certainly, you can reduce purchasing power, in any economy, down to the point where there will be a limitation on demand. I mean that is axiomatic.

Mr. SMITH. We are not talking about purchasing power.

Mr. PORTER. Or you can reduce the amount of currency in circulation. You can restrict credit. The thing I alluded to yesterday. If you use any one of these mechanisms to attempt to solve the whole problem, then, you will run into the danger where demand will be restricted to the point where you will have a depression.

Mr. SMITH. Mr. Porter, please do not try to divert us from our subject. I am trying to find out what you know about inflation, because of your mission here. Let me ask you another question. Could you give the committee an example of inflation in countries where all purchasing media were convertible into gold at their face value at the option of the holder of such media of exchange?

Mr. PORTER. No, sir.

Mr. SMITH. Why not?

Mr. PORTER. I am not concerned, Dr. Smith, with this historical analysis. It seems to me that I have attempted to explain the basic causes of inflation. We are faced here with the practical condition of ever-increasing prices, and I will say that inflation is meat at \$1.50 a pound in the stores, and that is what we are here to stop.

Mr. SMITH. In other words, you do not think it is necessary to make post mortems?

Mr. PORTER. Not at this time, no, sir. This committee has been over this again and again, and we have submitted a program here.

Mr. SMITH. I happen to be in a position, Mr. Porter, to know that medical science is based on post mortems.

Mr. PORTER. Well, I trust that the patient is still alive before this one is completed.

Mr. SMITH. I beg your pardon?

Mr. PORTER. I say I trust that the patient is still alive before this post mortem is completed.

Mr. SMITH. Well, now, that sort of business is all right, Mr. Porter. The proposition I put to you is fair and square. I stated that the science of medicine is founded primarily upon post mortem examinations. What I wish to state is merely that we ought to have a historical background for our position. That is all I am saying. This is no place for levity.

Mr. PORTER. I agree with that completely.

Mr. SMITH. Now, you have been unable to cite any cases of inflation where gold was freely in circulation in the market, and where all forms of—

Mr. PORTER. Yes, I can cite one to you. I can cite a contemporary example—Greece. There the drachmas are freely convertible into gold sovereigns on the open market, and they still have a hyperinfla-

tion in Greece. You can go to the Bank of Greece and exchange and convert drachmas at the official rate.

Mr. SMITH. How many drachmas?

Mr. PORTER. For the gold sovereign, the last price that I saw was around 200,000.

Mr. SMITH. All right; 200,000. What was the normal, say before 1914? How many drachmas did it take to equal a sovereign?

Mr. PORTER. 1914?

Mr. SMITH. Yes; 1914.

Mr. PORTER. I can give you what it was before the war, in 1939. My recollection is—and this is subject to correction, as I have a poor memory for these things—it was around 300 to the sovereign.

Mr. SMITH. Now it is what?

Mr. PORTER. 200,000.

Mr. SMITH. And what is that due to?

Mr. PORTER. Again, it is due to a variety of causes. One of them was that during the Nazi occupation there was a systematic and scientific campaign to destroy the Greek economy as well as their physical resources. They revalued the drachma again and again, and increased the amount of currency in circulation with a result that after liberation the only stabilizing influence or the principal stabilizing influence on currency, which they adopted, was the utilization of their scant foreign exchange resources and their gold reserves, as a matter of stabilization. They canceled out the occupation currency, fixed an official rate of 5,000 drachmas to the dollar, factored that into the gold sovereign, which, at that time, I believe, was around 38,000 to 40,000. But since then, the pressure has increased, as Government deficit has increased, as production has not caught up with the amount of currency in circulation. But you can still convert your currency into gold.

Mr. SMITH. You can convert foreign currency into American gold now. I am not talking about that sort of conversion at all. I am talking about the conversion at a rate that remains stable, at face value. That is what I am talking about. For instance, as we had between 1900 and 1914. Now, then, you admit that the Greek Government printed money.

Mr. PORTER. That is right.

Mr. SMITH. It printed money. France printed money in 1716 to 1720, when John Law had things in his hands, and France printed a lot of money during the French Revolution. Germany printed a lot of money, which brought about her excess currency situation, and also all the other countries we are talking about. Now, we are coming to the question of the United States.

What is our situation here? What is the total amount of purchasing media now in the hands of the public and the Government of the United States?

Mr. PORTER. You mean currently?

Mr. SMITH. Yes.

Mr. PORTER. I think I have some indication here of the figures on money supply. In May of 1948, the total money supply was \$111,000,000,000. Currency outside banks was 25.4 billion dollars.

Mr. SMITH. The currency supply was what?

Mr. PORTER. Currency outside banks—that is, currency in the hands of individuals.

Mr. SMITH. That was how much, did you say?

Mr. PORTER. It is 25.4 billion dollars. The adjusted demand deposits—that includes demand deposits other than interbank and United States Government, less cash items in the process of collection—83.2 billion dollars. And United States Government deposits—a preliminary estimate—2.4 billion dollars.

Mr. SMITH. What were the other deposits? You mentioned only demand deposits. What were the time deposits?

Mr. PORTER. Time deposits and savings. I do not have that figure.

Mr. SMITH. Well, let us pass that. Does that complete your list?

Mr. PORTER. Oh, no; you could get into the question of consumer credit, which in May was 13.8 billion dollars.

Mr. SMITH. What does that include, Mr. Porter?

Mr. PORTER. It includes automobile and other credit sales, repair and modernization loans issued by the Federal Housing Administration, and other consumer credits. It includes single payment loans of commercial banks, pawnbrokers, and service credits.

The CHAIRMAN. What was it previous to that?

Mr. PORTER. In October the total was 12.1 billion dollars, and in May of this year it is 13.8 billion dollars.

The CHAIRMAN. When did controls come off?

Mr. PORTER. Controls went off on November 1, as I recall.

The CHAIRMAN. It was \$12,000,000,000 and it is now \$13,000,000,000, while they had the authority to control consumer credit?

Mr. PORTER. That is correct. I think that the figures for June and July, which I do not have available, I am advised would show a substantial increase above 13.8 billion dollars.

Mr. SMITH. Mr. Porter, does that complete your list?

Mr. PORTER. I think with respect to money supply, it does.

Mr. SMITH. I did not say money supply. I said purchasing media, instrumentalities that can be converted into things.

Mr. PORTER. Oh, yes, you have savings. You have, for example, the thing that we touched on yesterday, which is the Series E, F, and G bonds; which are held by small investors, which I understand are at an amount somewhat in excess of \$100,000,000,000. You have other kinds of liquid assets which are convertible.

Mr. SMITH. What other kinds?

Mr. PORTER. Stocks, bonds, private investments.

Mr. SMITH. Aside from those, what portion of the Federal debt can be converted into things?

Mr. PORTER. What portion of the Federal debt?

Mr. SMITH. Yes; what portion of the Federal debt can be converted into goods or services?

Mr. PORTER. I do not understand you.

Mr. SMITH. You mentioned savings bonds. Are there any other Government obligations which can be converted into cash?

Mr. PORTER. There are bank loans—

Mr. SMITH. What about Government securities?

Mr. PORTER. Investment in Government securities, certainly, by our banking system.

Mr. SMITH. What does that amount to?

Mr. PORTER. United States Government securities, you mean, in the hands of commercial banks?

Mr. SMITH. No. What I want to find out, Mr. Porter, is what portion of all Federal securities are convertible into goods or services, or goods and services.

Mr. PORTER. I do not know. I could try to supply that figure.

Mr. SMITH. You do not know?

Mr. PORTER. No. I think the Secretary of the Treasury can answer that.

Mr. SMITH. Then, how, Mr. Porter, if you do not know that, can you come here and testify on this important subject of inflation?

Mr. PORTER. If I do not know what—the amount of Government securities that are convertible into goods and services?

Mr. SMITH. Yes.

Mr. PORTER. What type of securities do you mean?

Mr. SMITH. I said all the Government securities. What portion of all the Government securities?

Mr. PORTER. Well, I do not have the detail on the convertibility of the different types of Government securities. I can give you the investment by the banking system in Government securities, which have different rates of convertibility.

Mr. SMITH. Of course, that is only a portion of the Federal debt.

Mr. PORTER. That is correct.

Mr. SMITH. What I am trying to get at is the volume of purchasing media which exists in the United States at the present time, and see whether or not it might have something to do with this inflation.

Mr. PORTER. I think I have given you the principal ones. If there are others that I have omitted, perhaps you could refresh my recollection.

Mr. SMITH. But you would not know what portion of the Federal debt, without having your memory refreshed, is convertible into goods and services?

Mr. PORTER. Do you mean the various types of Federal bonds and debentures which are in the hands of individuals or the banking system?

Mr. SMITH. Or the banking system, wherever they may be.

Mr. PORTER. Well, I think I have indicated that the total investment in United States Government securities by the banking system is about \$65,000,000,000. In the hands of individuals—I would have to get those figures.

Mr. MONRONEY. Would not those questions more properly be directed to the Federal Reserve?

Mr. SMITH. I beg your pardon. We are dealing with an expert, a man who claims to understand inflation.

Mr. BUCHANAN. Mr. Chairman.

Mr. SMITH. I do not care to be interrupted. I want the question answered. I want to know whether this man knows what he is talking about or whether he does not know what he is talking about.

Mr. PORTER, since you do not know the amount of purchasing media, I cannot, of course, ask you certain questions which I would like to ask you. What is the object of recommendations which you made with respect to the Federal Reserve? It is to curtail credit; is that not so?

Mr. PORTER. That is right.

Mr. SMITH. Would you be willing to have the House Banking and Currency Committee write a provision into this bill which would

prohibit the Federal Government from using the banking system, the Federal Reserve, and the commercial banks, to prohibit the Government from financing its obligations through those banks?

Mr. PORTER. No, I would not.

Mr. SMITH. Why?

Mr. PORTER. I think that you would then find that there would be an important stabilizing effect of the Government bond market which would be eliminated.

Mr. SMITH. Do you mean then, that you believe in the Government engaging in the rigging of the bond market as it is doing at the present time?

Mr. PORTER. I think the Government has an obligation, Dr. Smith, to protect the investment of those persons holding E, F, and G bonds to the extent of in excess of \$100,000,000,000, preventing them from declining to the point where that investment, made under the spur of patriotism, is diminished in any substantial degree.

Mr. SMITH. That was not what I asked you.

Mr. PORTER. I did not think you would like that answer.

Mr. SMITH. Well, I do not care anything about your answer. It is equivocal entirely. I would like to have some direct answers, Mr. Porter.

Mr. PORTER. Well, I would prefer that you would direct that question to the Federal Reserve Board, whose primary responsibility it is.

Mr. SMITH. And the reason for that is that you are not familiar with the situation?

Mr. PORTER. I know about it in a general way, and I have opinions on it, but I would prefer, as a witness here, for those whose primary responsibility it is to discuss it with this committee.

Mr. SMITH. When did the Federal Government acquire the power to finance its obligations through the banking system?

Mr. PORTER. Do you mean under what specific statute?

Mr. SMITH. Well, specific statutes or time, whichever you wish to give.

Mr. PORTER. I think it was the Banking Act of 1935.

Mr. SMITH. All right; the Banking Act of 1935. Did the Government of the United States finance its obligations through the banking system in World War I?

Mr. PORTER. Yes.

Mr. SMITH. So the act of 1935 did not originate that procedure; did it?

Mr. PORTER. It is my recollection that the securities, short-term loans, were negotiated directly. The Banking Act of 1935 gave the Government the authority to require investments in the banking system of certain Federal obligations.

The CHAIRMAN. Just a minute. May I clarify it?

Previous to the Banking Act of 1935, the open-market committee was in an advisory capacity only. In the Banking Act of 1935 they were given mandatory power.

Mr. SMITH. You are familiar with the process of monetizing the debt by financing Government obligations through the banking system, are you not?

Mr. PORTER. In a general way; yes, sir.

Mr. SMITH. Do you know of any monetary authority who denies that that is an indirect way of printing money? Do you know of any reputable monetary authority who denies that?

Mr. PORTER. I know of a number who support that process.

Mr. SMITH. I mean, do you know of any who deny that that is printing-press money, indirectly created?

Mr. PORTER. Well, it is financing the Government debt. You can call it printing-press money or you can call it deferring obligations. I will agree with your definition of it, if it will expedite matters.

Mr. SMITH. You do not want to give up this power to print money, then, do you? Is that not why you are here this morning, or one of the reasons for which you are here this morning?

Mr. PORTER. No, sir. The object of my being here is to attempt to get certain direct powers to stop rising prices.

Mr. SMITH. But, at the same time, is it not a fact, Mr. Porter, that that is a part of your program? You are saying, on the one hand, that you want to control prices, and on the other hand you are saying that we must retain the power to inflate. Is that not a fact?

Mr. PORTER. This bill—

Mr. SMITH. Are you not asking for a retention of the power to inflate?

Mr. PORTER. That power already exists, according to your definition. This bill has no reference to that except in title II, with respect to bank reserves. It does not amend the Banking Act of 1935.

Mr. SMITH. Mr. Porter, do you know that the Federal Reserve banking system today could exercise extraordinary powers to do exactly what you want done?

Mr. PORTER. You mean through the open-market operations?

Mr. SMITH. The discount rate, and so forth.

Mr. PORTER. Yes. And again I say that that would probably have a serious impact upon the Government bond market to the detriment of the millions of small investors in Government securities.

Mr. SMITH. So you have got this thing in a situation where you must keep up some artificial prop; you must maintain an artificial prop for the financial structure; is that correct?

Mr. PORTER. I do not know what the term "artificial" means because in this field of money—banking and finance—there is a great difference of opinion as to what are natural causes and what are artificial causes. I do not think it is an exact science, so that you could say that a certain policy is artificial and another is natural. Unless you want to go back.

Mr. SMITH. Is the creation of credit now—any additional amount of credit poured into the economy—inflationary?

Mr. PORTER. To some extent, unless other measures were taken.

Mr. SMITH. To some extent? I merely asked you whether it tends to create inflation.

Mr. PORTER. Certainly, as you increase credit.

Mr. SMITH. All right. Now, you recommend in this bill, Mr. Porter, several things—at least the President has recommended several things. One is the voting of \$65,000,000 for a structure for the UN organization.

Mr. PORTER. That is not in this bill. You mean in the message.

Mr. SMITH. That is in the message?

Mr. PORTER. Yes, sir.

Mr. SMITH. Is that inflationary?

Mr. PORTER. Any demand upon materials is, to the extent that it makes itself felt on the price level, inflationary.

Mr. SMITH. So that would be inflationary.

Mr. PORTER. Well, I do not think that the adoption of that measure for a \$65,000,000 loan to the UN, which, I understand, has been fairly generally approved, would cause inflation.

Mr. SMITH. It would not cause inflation? How would you raise that money?

Mr. PORTER. I assume the Reconstruction Finance Corporation does.

Mr. SMITH. Where does the Reconstruction Finance Corporation get it?

Mr. PORTER. From the Treasury.

Mr. SMITH. Where does the Treasury get it?

Mr. PORTER. Either from the banking system or through the sale of its obligations to the public.

Mr. SMITH. It is a public debt transaction ultimately, is it not?

Mr. PORTER. Correct.

Mr. SMITH. And there is no other conclusion but that it would have the effect of creating inflation, is there?

Mr. PORTER. But I think that, as a matter of general policy, is to be desired, and its impact on the total situation is de minimis.

Mr. SMITH. All right. But, nevertheless, it is an impact.

Now, you asked for power, on the other hand, to control that impact with, using the President's own designation, police powers.

Mr. PORTER. With controls adopted by Congress, I hope, in a democratic fashion.

Mr. SMITH. Well, you still want control over prices, and so forth, to offset whatever small amount of inflation might be caused by the \$65,000,000 expenditure.

Mr. PORTER. I would say that if we had a relatively stabilized condition, at this point, that the \$65,000,000 would not justify the powers that are asked for in this bill.

Mr. SMITH. We are speaking, Mr. Porter, about a principle. We are speaking of principles here.

Mr. PORTER. Well, you could carry that principle, Dr. Smith, to the extent where we would stop the Marshall plan; that we should stop preparedness for the armed services; that we should cut out all Federal expenditures. Certainly that would make a contribution toward stabilization, but I do not think it would be seriously proposed.

Mr. SMITH. What about the wheat agreement which the President recommends? Is that inflationary or deflationary, or is it neutral?

Mr. PORTER. It is designed to have a stabilizing influence on world market conditions.

Mr. SMITH. That is not the question I asked you. What I asked you is: Is it inflationary?

Mr. PORTER. No.

Mr. SMITH. It is not?

Mr. PORTER. No.

Mr. SMITH. Positively not inflationary? It will not raise prices in this country, or have a tendency to raise prices in this country, in respect to certain commodities?

Mr. PORTER. It might. But there, again, the alternative is between stable prices and fluctuating prices.

Mr. SMITH. The President recommends the expenditure of Federal money for the building of power plants in connection with the Tennessee Valley Authority. Is that inflationary?

Mr. PORTER. It ultimately should be deflationary.

Mr. SMITH. How ultimately?

Mr. PORTER. Because it will increase the power supply, give cheaper electricity and increase total production. And if production is what we are after as one of the causes to stop inflation, that should make a substantial contribution.

Mr. SMITH. Temporarily it is inflationary; is that the idea?

Mr. PORTER. Well, anytime that you divert materials for any purpose, to that extent they are not used for something else.

Mr. SMITH. What about the housing program? Is that inflationary or deflationary?

Mr. PORTER. I think it can be handled in such a way that it will not be inflationary.

Mr. SMITH. How would you handle it?

Mr. PORTER. First I would suggest that Congress give consideration to those standards which would supply low-cost housing to people who need it. Secondly, that the materials that are presently being used for nonessential purposes be channeled to fulfill this great social need.

Mr. SMITH. Would you include in nonessential purposes the UN, for example?

Mr. PORTER. By no means.

Mr. SMITH. You think it is necessary to house foreigners in preference to our veterans?

Mr. PORTER. I think it is necessary to do both.

Mr. SMITH. Nevertheless, it is going to have an impact of \$65,000,000, which would buy some homes, would it not?

Mr. PORTER. I would say that you could stop, if the authority was given, the construction of enough gin mills, pool halls, and theaters to build the United Nations and have enough left over to build a great number of veterans' houses.

Mr. SMITH. Is that your purpose, if you get this power?

Mr. PORTER. Well, the housing bill is a separate bill, as I understand it.

Mr. SMITH. I am asking you: If you get this power, are you going to tell the owners of pool rooms and those places you mentioned that they cannot have their business anymore; that you are going to use the material they want for their structures to erect the UN capital?

Mr. PORTER. I have no idea what the ultimate policy would be, assuming that these powers are granted. I certainly personally would recommend that building materials be used for veterans' housing and essential purposes.

Mr. SMITH. Mr. Porter, is it not a fact that when your whole proposition is summed up it amounts simply to this: That here—but first let me ask you this question. Do you think that prices are too high now?

Mr. PORTER. Very definitely.

Mr. SMITH. And you would lower them?

Mr. PORTER. I would start out first by stopping them from going any higher, and then, if they can be reduced, I think the effort should be made to that end.

Mr. SMITH. In other words, according to your testimony here, you think that prices are greatly inflated; do you not?

Mr. PORTER. Certainly.

Mr. SMITH. You now say that you would stop them from rising any higher. What did you say about reducing them later?

Mr. PORTER. I say that, if it is possible, they should be brought to the minimum—

Mr. SMITH. What do you mean by "possible?" Would the question of feasibility not enter into it?

Mr. PORTER. Certainly. And that is written into the statute.

Mr. SMITH. In other words, if it is feasible—politically feasible, too—that would have something to do with it, would it not?

Mr. PORTER. I am not talking about politically feasible. I am saying if it is administratively and economically feasible.

Mr. SMITH. I know, but we are dealing with the political end of it here. Do you not think that might enter into it?

Mr. PORTER. I am afraid it will, much to the detriment of the country.

Mr. SMITH. So we are heading, with this program, into a question of politics, too, are we not?

Mr. PORTER. There is no statement that I have made, to my recollection, to inject any political aspects in this.

Mr. SMITH. No; but the political aspect is in this thing. I am just wondering what the President is going to do to really roll these prices back, who is going to be affected and when he is going to roll them back, or whether the President just wants power to manipulate this thing, to print money when it is feasible to pour more credit into the economy and possibly check it when he feels that prices are a little too difficult to control.

Mr. PORTER. It is my opinion that the President stated his position very forcefully in his message this week.

Mr. SMITH. You think that message is clear enough for us to understand precisely what is to be done? Mr. Porter, do you remember when you asked for the first price control bill?

Mr. PORTER. Yes, sir.

Mr. SMITH. You asked for selective price control, did you not?

Mr. PORTER. No.

Mr. SMITH. What did you ask for?

Mr. PORTER. We asked for the authority to control any price which would have an impact upon living standards or the effective prosecution of the war.

Mr. SMITH. Are you not asking for selective control in this bill?

Mr. PORTER. That is the theory of this bill; yes.

Mr. SMITH. Was that not the theory of the original Price Control Act?

Mr. PORTER. It was hoped that selective price control might work, but you will recall that we found, in April of 1942, that prices generally were such, with the upward pressures, that the general maximum price regulation was necessary.

Mr. SMITH. What evidence is there that the same situation will not develop if we give you this power?

Mr. PORTER. The evidence is abundant, Dr. Smith. We are producing now at a rate equivalent to, and in excess of, our full wartime capacity. An infinitely smaller percentage of that is going for military defense purposes. Therefore, the amount of goods available to civilian consumers is, roughly, twice—perhaps not in volume, but certainly in present dollar value—that that we had during the war period.

MR. SMITH. Are you telling this committee, Mr. Porter, that there is such a thing as effective selective control, and, if so, will you point out a single example, anywhere in the world, where it has been done?

MR. PORTER. One thing that comes to mind—you would not consider this a commodity price—is rents. The Government has managed to maintain rents at a relatively stable level since 1942.

Selective price control has its difficulties. I would certainly admit that. But I think it is better than attempting to let nature take its course; it is better than attempting to do nothing. And I certainly think it is worth trying.

MR. SMITH. For example, Russia has price control; Germany has price control; France has price control. The President has said that price control is a police-state method. Will you tell me where the police state ever actually succeeded in mastering this thing?

MR. PORTER. Well, I think we did a pretty good job—not being a police state—during the war.

MR. SMITH. We were not a police state during the war?

MR. PORTER. No, sir. I do not think there was any basic infringement on our civil liberties all during the war period.

MR. SMITH. Well, of course I did not know that anybody took that position. I thought that everybody took the position that in war we take it for granted that civil liberties are not what they are in periods when we are not at war. I did not know that anybody took that position, Mr. Porter. I certainly regarded my civil liberties as having been curtailed. I did not object to it because we were in a war. But you are about the first person I ever heard make that statement.

MR. PORTER. Well, obviously the requirements of national security come first in time of war.

MR. SMITH. That is true.

MR. PORTER. But, as I say, I do not think that there was any basic infringement upon any of your fundamental rights, or mine, by the exercise of those controls during the war; and I think we have a crisis now that is equivalent to that.

MR. SMITH. Of course you were on the controlling end——

MR. PORTER. And I was controlled, too.

MR. SMITH. And I would expect that you would naturally have that sort of idea.

MR. PORTER. I can assure you I got no pleasure out of it and got away from it as quickly as I could.

MR. SMITH. I do not believe you did, Mr. Porter, but, to conclude this interrogation, I notice that in your bill you use certain language: You say, on page 6, line 22, "establishment of maximum prices." That has to do with prices.

Now, turning to page 13, beginning on line 20, in relation to wages, you say "the adjustment of wages, salaries, or other benefits." In the one case you "establish"; in the other case you "adjust" through collective bargaining. In the one case you establish by edict; in the other case you adjust, through collective bargaining, wages. Why that differentiation?

MR. PORTER. Well, the maximum price regulation does establish a definite, specific price. The bill here provides that in the event an increase in wages made by the normal process of collective bargaining is ground for a price increase, then they must be reviewed, and some

adjustments are permissible under the title III, which contains the price standards.

The maximum price is, as I say, established by specific regulation. There is no regulation covering wages except under the conditions prescribed in the bill. So, in the first instance, there would be no regulation establishing any wage levels. It would come into effect only when an application was made, and, if the temporary wage board disapproved it, then, I assume, a regulation might issue establishing, for that particular industry, a maximum wage.

Mr. SMITH. Then the scheme you have outlined in this bill calls for political control of both wages and prices.

Mr. PORTER. I would say it calls for the utilization of Government restraints. It depends on the meaning in which you use the word "political." Used in its broadest sense, certainly the body politic would be exercising these controls in selected instances.

Mr. SMITH. That is what I have reference to. At any rate, you are asking for the power to control prices and wages.

Mr. PORTER. In selective causes; yes.

Mr. SMITH. Selective price control, selective wage control?

Mr. PORTER. Wage control only when the processes of collective bargaining have reached an agreement that would have an impact on a particular price that was under regulation.

Mr. SMITH. Still that would be selective wage control?

Mr. PORTER. Certainly.

Mr. SMITH. What did you ask for in the original price-control bill?

Mr. PORTER. In the original price-control bill, there were no provisions with respect to wage control.

Mr. SMITH. Do you remember the arguments that were made against that including wages?

Mr. PORTER. Indeed, I do.

Mr. SMITH. Are you not just sugar-coating this thing a little bit, for the wage earners, as you did the other time, and ultimately you may come around to controlling those wages just as you did in wartime?

Mr. PORTER. I do not think so, Dr. Smith, for this reason: I remember the many discussions that were had on the question of wage controls, and the matter was ultimately decided by the then President of the United States, Mr. Roosevelt, on this basis: that we could not, even in wartime, in this country, have the equivalent of the British essential works order, that is, to tell every man where he should go for a particular job. We needed full production for war purposes, and his concept of the thing, which I think was correct, was that you would use the wage system to get the approximate distribution of manpower, and then seal it off. In the meantime, trying to keep the cost of living at such a level that the wage demands would not be excessive. And I subscribe to that policy fully.

Mr. SMITH. On page 6 of your bill, you say:

The price of such commodity has risen or threatens to rise at least 20 percent above the price therefor prevailing in June 1946—

and you mentioned some things that would be included. What would you say about coal?

Mr. PORTER. Coal is certainly up more than 20 percent.

Mr. SMITH. Then you propose to fix a maximum price on coal?

Mr. PORTER. I would prefer that the Secretary of the Interior give you his views about that. If these standards are applicable, and coal

is in short supply and threatens to rise, it would be eligible for control under this proposal.

Mr. SMITH. In that event, you would have to control John L. Lewis, would you not?

Mr. PORTER. Well, that has been attempted from time to time, and whether it would be attempted under this bill, I think only the future would tell.

Mr. SMITH. What I am getting at is this—this is merely an example: There are other illustrations. For example, in the automobile industry. You made certain statements here, Mr. Porter. I do not want to take any more of the committee's time. I have probably taken too much time already. But you have made certain statements here which give the impression that wage earners are the ones who are being hardest hit in this up-surge of prices. You have given that impression. Am I mistaken about that?

Mr. PORTER. I think that the persons of fixed incomes and who depend upon annuities, are probably the hardest hit. I have stated further, and I think that the facts will justify it, that the recent wage increases which have been made have been more than absorbed by price increases. I have stated in my direct testimony that even though wages, or the per capita income, had gone up 15 percent, I believe, since 1946, real purchasing power had declined 10 percent. So in this race between wages and prices, labor obviously has used all of its power, all of its collective bargaining strength, to keep up, but I think it is still behind.

Mr. SMITH. You are not asking for any power, though, to cure inflation. You are just asking for power to repress its effects, is that the idea?

Mr. PORTER. I am asking for both, I think, Dr. Smith.

Mr. SMITH. For power to cure inflation?

Mr. PORTER. Well, we have degrees of inflation now. Again that gets back to a question of definition. I think that these powers would retard the upswing of prices, would give us an opportunity for stability and during the interim, perhaps working under the roof which this bill would undertake to put on the economy, we could undertake to bring out other programs which would bring more of a balance.

Mr. SMITH. It is a totalitarian device; is it not?

Mr. PORTER. No; I don't subscribe to that word in the United States.

Mr. SMITH. You do not agree with the President that it is a police state?

Mr. PORTER. I do not believe these are police-state methods; no, sir.

Mr. SMITH. You think he was wrong when he said that?

Mr. PORTER. I did not hear him say it.

Mr. SMITH. You know that he said it, however?

Mr. PORTER. I know that he was quoted as saying that the prolongation, permanently, of particular controls might fit that category. But—

Mr. SMITH. Was that the way he put it?

Mr. PORTER. I do not know. That is the interpretation I place on it.

Mr. SMITH. I just want to say for the benefit of this committee, Mr. Chairman, that it is very clear, and that it should be very clear to any student of this subject, that Mr. Porter has not shown the least indication here of understanding what really constitutes inflation, either from a historical standpoint or from the standpoint of its existence at the present time.

The powers for which you are asking are precisely the powers that the Bolsheviks instituted when they overthrew Russia, the same powers that Karl Marx advocated, that Lenin advocated, the same powers, exactly that Mussolini used, that Hitler used—precisely the same powers. And now it is simply a question of the American people understanding, very clearly, this one point: you are here now asking for the power not only to prevent inflation from going further, according to your conception of what constitutes inflation, but you are also asking for the power to inflate at will, because you would not give up the power possessed now by the Federal Government to finance its obligations through the banking system. That is true, is it not?

Mr. PORTER. I think I have answered your question on that, Dr. Smith. The Government has an obligation to protect small bondholders and apparently you would like to discard the present open market policies, tamper with the rediscount rates, and, because I do not embrace your particular view of treating with this problem—and I do not think we could ever agree on it—

Mr. SMITH. Oh, no; I am not recommending anything.

Mr. PORTER. Do you have a program, if I may ask?

Mr. SMITH. I have not recommended anything. You are here testifying on a program. And you say the Federal Government must absolutely retain the power to inflate at will. That is what you are saying. And: "We will, by police methods, see to it that these prices do not go beyond what we believe to be proper levels." That is the gist of your testimony?

Mr. PORTER. That is your interpretation of it, with which I thoroughly dissent.

Mr. SMITH. I would expect you to do that.

That is all.

The CHAIRMAN. Mr. Brown.

Mr. BROWN. Mr. Porter, you have suggested that the cost of living has increased about 13 percent in the past year.

Mr. PORTER. Yes, sir.

Mr. BROWN. And that it did not have very much effect on our production?

Mr. PORTER. That is correct, and I further stated, Mr. Brown, that the Federal Reserve index, on the volume, not the value of production, had reached the level of, I believe, about 170 in November of last year, and that it is at that point now.

Mr. BROWN. Now, if we had full production to meet the needs of our people here and in western Europe, do you not think that we could curb inflation?

Mr. PORTER. That would be the most important contribution that I can think of.

Mr. BROWN. I have been a member of this committee 14 years. All witnesses have testified that the main method of curbing inflation is full production. We want to be very careful and not do anything which would prevent full production. I am satisfied every member

of this committee wants to curb inflation. But as long as we have to export commodities to Europe and other countries, we are going to have inflation, and much inflation, until those countries are in a position to feed and clothe themselves.

I supported the Marshall plan because I think it is one weapon for prevention of war. It is a gamble. There may be only one chance in ten that it will work, I was willing to take this chance. If we pass any control laws, we must be very careful not to discourage production. We have got to offer an incentive in the way of profits. I want to do everything I can to curb inflation, but I certainly want to give all the incentives needed so that people will produce and so that we may have full production.

I notice the list of your proposed roll-back on commodities. I see here that corn has gone down from \$2.60¼ per bushel in 1947 to \$2.11½ in 1948.

I see that wheat has gone down from \$3.06¼ a bushel to \$2.16¼ per bushel this year.

I see flour has gone down from \$8 a barrel to \$6 a barrel.

Butter, from 83 to 76 cents.

Lard, from 27 cents to 22 cents.

Cocoa, from 49 to 44½ cents.

Sugar has gone down.

All meats have gone up. I cannot understand why we have to pay such high prices for meat. I think if you can just single out one or two things like meat and steel, you will be in a better position to ask for controls.

When it comes to clothing, print cloth was reduced from 28 cents to 17½ cents, and cotton has gone down \$25 a bale since last year. The people in the South who produce cotton as their only money crop, cannot make a living at the present price when they have to buy much fertilizer to make the crop.

Wool has not gone down. I am just wondering how you could put a ceiling on clothing made from a combination of wool and cotton. I do not see how you could arrive at a proper ceiling.

Another thing, while wool is going up, cotton is going down, and when you come to the mixed cotton and wool clothing, how can you reflect a fair price in that clothing to cotton and wool at the same time?

Again, you cannot place a ceiling on three-fourths of the wool consumed here because this is the amount we import. I think the exact figures last year indicated that we produced in this country 341,219,000 pounds, and we imported 923,814,000. I am just wondering how we can put a ceiling on clothing. I know the prices are too high. But I am speaking of raw materials.

You cannot place a ceiling on wool that we import from other countries.

Mr. MONRONEY. We can take the tariff off.

Mr. BROWN. This is not a bill involving tariffs. We would get into a real party fight if we considered that.

I do not want to give blanket authority to anyone to cover all commodities, especially the commodities that are not scarce. I want to do something to curb inflation, if we can do so without disturbing the production of the commodity. I think if you had in your bill something to guarantee a profit, if that could be enforced, it would be very helpful to your position.

Mr. PORTER. I think there is a provision in the pricing standards, Mr. Brown, in which consideration must be given, before a maximum price regulation is established, to the changes not only in cost of production, but distribution and transportation, and general increases or decreases since June 1946 in profits earned by sellers of the commodity or commodities.

I recognize, of course, the points that you make as to the difficulties. This is not an easy way. Obviously. No effort to regulate a maximum price is easy. We had the experience, I think, during the Office of Price Administration, that certain of our regulations could not be maintained because of increases in costs of raw materials, and so forth. But I am certain that this bill would not be, if the powers were granted, administered in such a way as to interfere with the normal profit margins. I do not think you can, under this bill.

Mr. BROWN. As long as we feed western Europe, we might just as well realize that we are going to have considerable inflation, until western Europe is in a position to feed and clothe itself. I hope that can be done within the next year. The American people might just as well realize that it is a difficult problem to control inflation if we are going to feed and clothe the United States and take on western Europe at the same time.

Mr. PORTER. I agree with that, sir.

Mr. BROWN. That is all.

The CHAIRMAN. Mr. Talle.

Mr. TALLE. Mr. Porter, in response to questions put to you yesterday, you mentioned the following products as those which you might consider for control: Meat, first of all.

Mr. PORTER. Yes, sir.

Mr. TALLE. Fluid milk and dairy products, clothing and apparel, steel, and other metals.

Mr. PORTER. Nonferrous metals.

Mr. TALLEE. Steel and nonferrous metals?

Mr. PORTER. Nonferrous metals; yes.

Mr. TALLEE. And building materials?

Mr. PORTER. Yes, sir; I think I neglected to mention petroleum and petroleum products.

Mr. TALLE. Petroleum and petroleum products?

Mr. PORTER. Yes, sir. I assume that would be one of the areas which would be given first consideration, I am sure. Secretary Krug is prepared to give the supply, market, and price situation in that field.

Mr. TALLE. If we were to classify those, they would come under the headings of food, clothing, shelter, equipment, transportation, and something more. It is a rather all-embracing group, in spite of the fact that the number of commodities is not great.

Mr. PORTER. It is a very substantial segment of the American production system, there is no question about that.

Mr. TALLE. And it is true, is it not, that prices are interdependent?

Mr. PORTER. Yes; to a varying degree, obviously.

Mr. TALLE. So that if the price of an article is controlled, and people do not like it, they will turn to whatever substitutes might be available?

Mr. PORTER. There is that factor, which obviously is a difficult one in a selective price system.

Mr. TALLE. And then the only alternative the Administrator would have, in order to enforce his control of the first product, would be to control the price of the substitute or substitutes?

Mr. PORTER. Well, as you well know, there is a great difference on that proposition—I say a great difference. There are various views on the effectiveness of selective price control, and the fact that you have to control all or nothing, the chain reaction that goes through the price level and so forth. But I think that among the countries which Dr. Smith enumerated as applying to totalitarian techniques, he eliminated the experience of Canada, England, and Australia, and the Low Countries, where there has been some experience, and to some extent a successful experience with selective price control. I would be the first to concede the imperfections which you have mentioned, but it seems to me that the choice is between attempting a selective system or courting the kind of collapse that this chart vividly illustrates.

Mr. TALLE. I would like to turn to the chart for a moment. What different kinds of price movements are depicted on that chart?

Mr. PORTER. This is the wholesale price index. Now, where they got their information dating back 1749 is a query that I have put to the Bureau of Labor Statistics, and they advised me that it was taken from contemporary literature, and that even at the time the inexact science of economics was constructing crude price indexes. This is the list of wholesale commodities and includes practically every category of consumer goods, durable goods, industrial products, food, and apparel.

Mr. TALLE. I am familiar with similar charts. Those mountain peaks on the curve represent one kind of price movement, and that is the inflationary movement following wars?

Mr. PORTER. That is correct.

Mr. TALLE. But there are some more movements depicted on the curve, too.

Mr. PORTER. That is correct.

Mr. TALLE. Take the long downward movement from 1814 to 1850.

Mr. PORTER. You mean about the War of 1812?

Mr. TALLE. From the War of 1812 to about 1850.

Mr. PORTER. Of course, this chart moves by decades. If it were extended, you would see that there were some plateaus during that period.

Mr. TALLE. Then, you have a long-term trend upward from 1850 to about 1873, because of the discovery of new gold mines.

Mr. PORTER. That is correct.

Mr. TALLE. Then, you have the downward trend from 1873 to 1896.

Mr. PORTER. That is right.

Mr. TALLE. Then you have an upward trend from 1896 to 1914, and so on. That is the second price movement, the long term price movement.

The third movement is the business cycle, which occurred repeatedly throughout the years covered on your chart. Offhand, I could name many dates usually associated with the panic aspects of the business cycle.

Mr. PORTER. That is right.

Mr. TALLE. Then, there are the seasonal variations of price, a fourth one, which were no doubt removed by the statisticians. Now, my question is: What are you going to do, if you can, to shape that curve from where you left off on the chart and move into the future? What is your hope for projecting it? Do you plan to control the price curve depicted on your chart?

Mr. PORTER. That, I think is the central dilemma of the whole American system of Government and free enterprise and capitalism. The question to me is, if in this pattern history repeats itself, whether we can maintain our whole system in the manner in which we are accustomed to.

I do not pretend that the measures that are proposed will answer the problem. We hope that they will have a chance. There are a great many economists who feel that this next period is inevitable, but I personally do not accept that defeatist attitude.

Mr. TALLE. You mean the steep drop down?

Mr. PORTER. That is correct.

Mr. TALLE. You expect to be able, through the devices asked for in this bill, to make that curve run as a horizontal line rather than up and down?

Mr. PORTER. I hope that it will level off at least for a sufficient period, so that the adjustments working on that could level out to a period of full production, full employment, and relative prosperity. That depends, of course, to a great degree on international conditions.

Mr. TALLE. What you are working on then at the moment is this steep downward movement which you fear. But suppose while you are working on that, you run into other situations, such as a long-term trend. You may have a pretty tough job on your hands.

Mr. PORTER. I recognize that it is going to be extraordinarily difficult, whatever is done.

Mr. TALLE. I will not take any more time, Mr. Chairman, in view of the fact that you would like to finish with Mr. Porter today.

The CHAIRMAN. Mr. Monroney.

Mr. MONRONEY. I am not going to delay you with trying to find out your definition of inflation, Mr. Porter. I think 135,000,000 people get their own definition about every month when they find the increases in their grocery bills and everything else. They are looking to this Congress, whether we are going to fiddle while Rome burns or whether we are going to seriously forget politics and blame placing and try to work out some kind of answer to the thing people want, and that is: Are we going to seriously approach this problem? Would not the right way for this committee to handle this situation be, if we do think that inflation is dangerous and is threatening the economy of this country, for this committee to go into executive session first and decide whether we are willing to do anything about controlling inflation or not, and if we are not willing to do anything about it, then not bother with further hearings? Are we not putting the cart before the horse in examining and cross-examining witnesses over various methods before the committee itself knows whether it is willing to do anything about it or not?

Mr. PORTER. Of course, Mr. Monroney, I have no participation in the committee's procedures, but I would say that I am certain that the American business community, the consumers, and, above all, the

housewife, want to know the answer. As you have indicated, I am not concerned about the causes or the placing of the blame, but merely in determining whether there is some possibility of working out a solution.

Mr. MONRONEY. Well, the committee can surely, with the evidence it already has, go into executive session and determine whether there is or is not an inflationary condition in this country, can it not?

Mr. PORTER. I would think that the evidence is complete.

Mr. MONRONEY. It seems to me that would be the first step. Then the Congress could decide whether it liked the President's proposed remedies or not, and if not, then it would seem to me that it would be honor bound to come up with remedies of its own.

The CHAIRMAN. We have a program.

Mr. MONRONEY. I would surely welcome seeing it.

The CHAIRMAN. There have been several speeches in the last few days. We intend to present a program.

Mr. MONRONEY. I have listened to your cross-examination on regulation W rather carefully, and I still remember that day in the House when regulation W was passed and we were assured that under no—

The CHAIRMAN. You mean the revision of regulation W.

Mr. MONRONEY. Yes. And we were assured that under no foreseeable circumstances short of war would anybody in Government have the right to reimpose regulation W, so carefully was the bill drawn.

The CHAIRMAN. I think you had better go back to the record.

Mr. BOGGS. Mr. Chairman, I have before me a press release from Governmental Affairs, legislative daily published by the Chamber of Commerce of the United States, in which it is stated that Chairman Wolcott announced that Congress would refuse to pass the President's anti-inflation program.

Now, it occurs to me that all of the charges that have been made about this being a political move are neither here nor there. Inflation affects all of the people, whether they are Democrats, Republicans, or neither. It seems to me that it is incumbent upon this committee to get the viewpoints of all Americans rather than simply to foreclose hearings and to state that we are not going to do anything.

I would like to make the suggestion that we invite Governor Dewey down to give his ideas about the inflation problem.

The CHAIRMAN. I see no particular objection to that if we invited all the candidates down.

Mr. BOGGS. I would agree to that, Mr. Chairman.

The CHAIRMAN. Do you want to invite the President of the United States to come in here?

Mr. BOGGS. Yes, sir.

The CHAIRMAN. It is a rather unusual procedure.

Mr. BOGGS. We have his representative here.

The CHAIRMAN. If we are going to have Governor Dewey, we want the President. We do not want any of the President's subalterns down here. We want the "big shot" himself.

Mr. BOGGS. Mr. Porter is the President's representative.

The CHAIRMAN. Mr. Dewey undoubtedly would be very happy to send a representative.

Mr. BOGGS. Can we be assured that Mr. Dewey will send a representative?

The CHAIRMAN. I am sure I do not know. We are first trying to find what the Government's program is about.

Mr. BOGGS. I suggest we ask him to send a representative.

The CHAIRMAN. If we are going to have any candidates before this committee, we will have all of them or none.

Mr. MONRONEY. I think that is begging the question, when the two principal parties in the country at least are concerned with this problem.

The CHAIRMAN. Whether the Democratic and Republican Parties are the principal parties is just a question of opinion. Mr. Wallace would probably not admit that.

Mr. BOGGS. Mr. Chairman, I think it is logical to assume that inflation is not a partisan matter. It affects the Democrats, Republicans, Wallaceites, and whatever else we have in America.

The CHAIRMAN. We have always tried to keep it on a nonpartisan basis.

Mr. FLETCHER. What about the Dixiecrats? We ought to have them here.

Mr. BOGGS. Yes; we will have them here.

The CHAIRMAN. I expected some reaction to that statement. Perhaps I should have qualified it by saying that until the President's speech at Philadelphia this has been kept on a reasonably nonpartisan basis because I do not think that any of the members of the committee will deny the fact that many of us Republicans have as much responsibility for the continuance of price control during the years as the Democrats.

We have sat in this committee for years and discussed price controls and rent controls on a very high plane and with as little partisanship as was possible. I recall very definitely when I was being besieged on the floor by Democrats to kill OPA; that I constantly tried to get them to write a bill, and we did write a bill. In those days of OPA we surely were on a reasonably nonpartisan basis. I am sorry it is on a partisan basis today. If it was not on a political basis we would not be here today, to be realistic about it.

Mr. BOGGS. Mr. Chairman, we could debate until this time tomorrow who is or who is not responsible for the present condition prevailing in our country. The fact remains that we are subject to inflation; that it affects all of the citizens of the United States—

The CHAIRMAN. We are all subject to it, but we are not necessarily all responsible for it.

Mr. BOGGS. It seems to me that rather than foreclose any action on the part of this Congress it is incumbent upon us to get the viewpoints of the principal candidates for the highest office in the land.

The CHAIRMAN. If you can get the President of the United States to come down here I will assure you—

Mr. MONRONEY. The President has been before the entire Congress.

The CHAIRMAN. He has never been before this committee, and Mr. Dewey, to my knowledge, has never been invited to come before the Congress of the United States to state his views.

Mr. MONRONEY. We would be glad to have him.

The CHAIRMAN. When you hear anything about the President of the United States saying that he will be glad to come down before

this committee I can assure you that I will personally invite Mr. Dewey, Mr. Thurmond, and Mr. Wallace to do likewise.

Mr. MONRONEY. And there are others, too.

The CHAIRMAN. Oh, yes; Mr. Thomas, and others. We will have them all here if we can get the President of the United States to come down and sit in this chair.

Mr. MONRONEY. Could we not expect some communication comparable to the President's message from Mr. Dewey?

The CHAIRMAN. In deference to the President, we have several matters on this afternoon and we would like to close with Mr. Porter this morning if we can.

Mr. SPENCE. Mr. Chairman, the President has sent his representative here.

The CHAIRMAN. We do not want anything under the "big shot" himself.

Mr. MONRONEY. The "big shot" has been before the Congress and has detailed his program.

The CHAIRMAN. Mr. Dewey is not going to be invited to come down here to answer Mr. Porter.

Mr. SPENCE. You admit Mr. Dewey is one of the leading candidates; do you not?

The CHAIRMAN. Mr. Dewey is the outstanding candidate.

Mr. MONRONEY. Did or did not Mr. Dewey mean what his emissary said?

The CHAIRMAN. Please address yourself to the witness, and we will decide whom we are going to have here later.

Mr. MONRONEY. Going back for a moment to the political suggestion, it seems to me that I remember a Republican slogan which was used in November of 1946. It was, "Had enough?" In some way I got the impression that it vaguely referred to OPA as a campaign issue.

The CHAIRMAN. I think that is something for the people to settle on November 2. We cannot settle it here in this committee.

Mr. MONRONEY. Getting back to the printing press money proposition which was developed this morning, Mr. Porter, is there any other way, other than adding to the public debt, in which the Government can defray its war expenses or its other necessary expenses other than borrowing if the Congress is unwilling to meet those obligations and outlay by taxation?

Mr. PORTER. I know of no other way.

Mr. MONRONEY. Was the Congress not urged repeatedly, even as late as this year, to try to operate on a Government surplus in order to carefully deflate the expansion of currency?

Mr. PORTER. And, as a part of the President's current recommendations, he is asking for the restoration of the excess-profits tax. That is destined to put the Treasury in a surplus position.

Mr. MONRONEY. And much of the so-called inflationary bond-holding bank credit could be dissolved by the application of an adequate surplus in Government income to retire those bonds which are in dangerous places?

Mr. PORTER. A substantial portion of it has been reduced this year.

Mr. MONRONEY. But it cannot be reduced next year, with the \$5,000,000,000 tax cut which is now finding its way into the spending stream and adding other inflationary pressures; is that right?

Mr. PORTER. That is correct.

MR. MONRONEY. This section 6 of the alleged anti-inflation bill that the Congress passed last November, directing the President, through a long series of mechanisms, to go through before he could come to Congress—do you think that the Congress has any constitutional right to override the Constitution and the method that the President has in calling attention to much needed legislation that he needed to present? In other words, this anti-inflation bill told him to go and do two dozen things and then come to the Congress for legislation.

The President did do that on one occasion and found himself rebuffed. He has all the right in the world, under the Constitution, to present these issues, as he has done in this case, to the Congress for consideration; has he not?

MR. PORTER. I do not construe section 6 (a) as any limitation on the President's right or duty to point out to the Congress what he pointed out.

MR. MONRONEY. And the bill gave him no powers that he did not have under the Constitution from the time the Nation started?

MR. PORTER. Furthermore, I think the section itself is an unworkable instrument to meet this problem.

MR. MONRONEY. Do you not think that, while the power to recommend legislation to Congress rests in the President, he has no power to secure passage or effective action as a result of his recommendation?

MR. PORTER. That is correct.

MR. MONRONEY. Only the Congress has that power?

MR. PORTER. That is right.

MR. MONRONEY. The Congress also has the power, if it does not like the President's recommendations, as it seemed not to have liked them during the days when OPA was holding the line, to come up with a program of its own to solve this situation as it sees fit.

MR. PORTER. I hope, if they do not follow these recommendations, that the Congress will develop a program of its own, because the situation demands it and demands it now.

MR. MONRONEY. You are not appearing here to say "this or nothing," but you are appearing here to say: "This is the danger; this is the President's recommendation, and we must have some legislation that can be effectively used to resist the repetition of that threat which has occurred so often after all the wars of our history."

MR. PORTER. That is correct.

MR. MONRONEY. And it is your studied and careful opinion that if no action is taken at this special session, and if this whirlwind of rising prices is allowed to run its course, the bust will be inevitable?

MR. PORTER. I think the repercussions of that are beyond what has been discussed in any of these current sessions of the committee. I think it has its impact on foreign policy; it has its impact on probable consequences of the war. And the President pointed out, in his message, that unless we can maintain a strong economy here, the communist's greatest ally, and what the Kremlin is counting on, is an economic collapse in America.

MR. MONRONEY. One other point. The foreign policy program and European aid have often been referred to in the hearings and used as an excuse for laying the blame when pointing to high prices. Are we exporting any meats under this program?

MR. PORTER. None that I know of. There may be some meat substitutes.

Mr. MONRONEY. Most of the meats are coming from Argentina and South America, which, under the sanitary pact, cannot possibly be used in this country; is that not true?

Mr. PORTER. That is correct.

Mr. MONRONEY. Yet meat is one of the highest items in the cost of living; and meat exports this year total only $\frac{1}{10}$ of 1 percent of our production.

Mr. PORTER. That is right.

Mr. MONRONEY. I have some figures before me which show that exports of lumber total 1.8 percent of our gross production, down considerably from the 1939 figure of 4.1 percent of lumber exports. In other fuels, we were exporting 6 percent in motor fuels in 1939; now we are exporting 3.2 percent or about half of what it was in 1939. In the case of heating fuels we are exporting now only 4.8 percent against 18 percent in 1939.

So all of the exports of the so-called scarce materials that I see here are substantially lower. The only thing that is even comparable to the exports of 1939 is finished steel, which was 7.1 percent in 1939 and is now 7.6 percent.

It seems to me that to point the finger of blame at the export program, for \$6,000,000,000 worth of exports, is trying to fasten guilt completely on the wrong party. I would like to include herewith a table showing these exports of scarce commodities. (The table referred to above is as follows:)

Exports of "scarce" commodities

Commodity	1939		1947		1948 estimate	
	Total supply	Percent exported	Total supply	Percent exported	Total supply	Percent exported
Lumber (billion board feet).....	25.7	4.1	37.9	3.0	37.1	1.8
Motor fuel (million barrels).....	64.0	6.0	745.6	4.3	791.0	3.2
Heating fuels (million barrels).....	162.0	18.9	316.0	8.2	372.0	4.8
Finished steel (million tons).....	35.0	7.1	53.0	10.3	65.0	7.6
Soil pipe (1,000 tons).....	417.0	3.2	577.0	1.0	570.0	.9
Hardwood flooring (million board feet)....	505.0	2.4	687.0	.3	830.0	.2
Meat (billion pounds).....	18.3	1.2	24.7	1.1	22.7	.8

Mr. PORTER. I personally always considered the advocacy or the utilization of that argument that exports are responsible for high prices and inflation as an excuse for inaction rather than a realistic analysis of the causes of the high price level.

Mr. MONRONEY. Thank you.

Mr. BUCHANAN. You mentioned that this year, Mr. Monroney, the ratio of net exports-imports surplus to gross national product was running at about $2\frac{1}{2}$ percent. How does that compare with 1947—the whole year 1947 or 1946—to a prewar normal period? Do you have any figures available?

Mr. MONRONEY. I think that in 1947 it was considerably in excess of that. The net export-import surplus was around 10 percent of our total national product. Now it is $2\frac{1}{2}$ percent.

Mr. BOGGS. Will you yield?

Mr. MONRONEY. I yield.

Mr. BOGGS. The argument has been advanced here that the complete answer to the problem of inflation is full production. I do not

believe that that argument could be contravened. But is it not a fact that that same argument was made 2 years ago, when controls were removed, and that either full production has not been attained or, because of economic stresses, the inflationary spiral has continued; is that not a fact?

Mr. PORTER. That is correct. We have 61,000,000 persons employed in gainful occupations in this country. Production is at an all-time civilian peak, and yet, nevertheless, prices still continue to rise.

Mr. BOGGS. I recall reading full-page advertisements, paid for by the National Association of Manufacturers, which stated that prices would come down within a matter of days and weeks as soon as controls were removed. Were those predictions accurate?

Mr. PORTER. It just has not happened. I, too, made a few inadequate predictions at that time. I said that meat prices would only double, but they have exceeded that.

Mr. BOGGS. If we do nothing and continue to rely on the time when full production will be attained, how much higher, in your opinion, will prices go?

Mr. PORTER. I think you would run into the kind of cycles that are illustrated on this chart. In certain commodities they could go undoubtedly considerably higher, particularly meat and perhaps some other foodstuffs, until the impact of this grain crop is felt. But, during the interim, you could have a psychological depression in which people, seeing this price level going up, would say: "We have to dispose of our savings and our Government bonds." And I think you would perhaps not have the phenomenon that we had in the twenties, where unemployment, bread lines, and that sort of thing resulted immediately—and runs on banks—but you would probably have wholesale liquidation of Government securities and an impossible kind of fiscal situation.

How much higher this price level can go, I do not think anybody can predict. New shortages may develop. We cannot continue to count on favorable weather. One of a number of things could happen that would precipitate the situation. Certainly one thing that has caused everybody in Government who has been concerned with this problem increasing concern is the rate of acceleration, during the past few months, both in the wholesale price index and in the consumer index. And if it keeps up at that rate it will pass 1778 very soon, on this chart.

Mr. MONRONEY. Do you hold any hope that the so-called orthodox method of just pushing the interest rate up would be enough to stop this runaway inflation?

Mr. PORTER. I think that a great many people in the banking community would welcome it, but it would increase the cost of servicing the public debt, and if the open market policy were discontinued you would have, I think, an inevitable decline in the bond market. And the people who would suffer from that are those who hold relatively small investments.

Mr. MONRONEY. Do you remember what happened in World War I?

Mr. PORTER. Yes, sir.

Mr. MONRONEY. When the bonds were dumped on the market without Government support? I think they went down as low as 80 cents on the dollar, did they not?

Mr. PORTER. That is my recollection.

Mr. MONRONEY. It is the Government support of the bond market that is keeping those bonds at par.

Mr. PORTER. Undoubtedly.

Mr. MONRONEY. And the increasing of the rate on a Government bond—a rate of 2 percent, say, to 4 percent—would automatically result in a lot of these bonds, which are guaranteed and cashable by the Government, immediately being turned in and refinanced at 4 percent; is that not right?

Mr. PORTER. That is right; yes, sir.

Mr. MONRONEY. So you would have to go through the major portion of the refinancing of the national debt, and you might easily re-double the present \$5,000,000,000 cost of that financing.

Mr. PORTER. That is correct.

Mr. MONRONEY. If you could get the bonds placed at all.

Mr. PORTER. I was going to say that. That is assuming that you have a market.

Mr. MONRONEY. So we are not only talking here about the painful, and, in some cases, disastrous effect upon the people's standard of living, but we are talking about the very cornerstone of capital itself.

Mr. PORTER. And you are talking also about the present confidence and security with which the small investors are now holding these bonds and are not converting them to increase a demand which is already excessive.

Mr. MONRONEY. It would seem that with all those possibilities apt to happen, this Congress could put a little serious study into this matter and come up with a program of its own if it does not like the program the President has submitted.

Mr. PORTER. I would certainly hope so.

Mr. MONRONEY. That is all.

The CHAIRMAN. Mr. McMillen.

Mr. McMillen. Mr. Chairman, I would like to ask two questions concerning the proposed legislation contained in the President's message of last week.

You are familiar with the so-called educational bill which provides for an expenditure of some \$300,000,000.

Mr. PORTER. I have not given that bill any study.

Mr. McMILLEN. Well, that bill provides for an expenditure by the Government of \$300,000,000, if passed, as the President requests, at the present session, and additional amounts thereafter.

In your opinion, do you think the passage of that bill at this time would or would not be inflationary? Just a simple answer to that simple question.

Mr. PORTER. I do not think, Mr. McMillen, that you can answer that question yes or no. In my discussion with Dr. Smith—and I think this is in the same category as the construction loan to the United Nations, as far as its economic effect is concerned—I indicated that I feel very strongly—

Mr. McMILLEN. It provides for additional credit for money to be furnished by the Government, and additional credit by the Government tends to increase inflation, does it not, Mr. Porter?

Mr. PORTER. But its effect on the total picture would not be significant, I believe.

Mr. McMILLEN. It is not enough to affect the picture?

Mr. PORTER. That is right.

Mr. McMILLEN. All right. Let us go from there to the request of the President to raise the minimum wage to at least 75 cents per hour. Do you think the enactment of that suggestion would not be inflationary, if enacted at the present time?

Mr. PORTER. First let me say that I think it is justified by every reason of social policy.

Mr. McMILLEN. It is not a question of justification. It is the question of the effect on which I am trying to get your opinion.

Mr. PORTER. To the extent to which that would increase consumer purchasing power it would have its impact on excess demand. I have no figures on that. I do not know by how much more that would increase the wage payments in this country. I certainly think that at present prices a minimum wage that is below 75 cents an hour is doing as much damage, as far as those individuals are concerned, as that the inflationary aspects of it, in my judgment, are completely outweighed by the social policy involved.

Mr. McMILLEN. Would the enactment of such a law, in your opinion, be inflationary or not?

Mr. PORTER. I would like to examine what impact it would have in increasing the total wage bill. I just do not know.

Mr. McMILLEN. Mr. Porter, you are the coordinator, as I understood it, of this program, appearing to suggest legislation and to present these matters to the Congress. That is the way you described your duties, and that includes a definite suggestion to Congress to pass numerous bills and suggested legislation. I am assuming that you are prepared, being the agent of the President, to discuss the provisions, and I expect you to discuss the suggestions of the President.

All the suggestions of the President are germane to the question of inflation. Possibly this particular bill does not have too much to do with it, but it is part of the problem. I am asking your opinion, as an expert, as to the effect of the President's suggested legislation on the question of inflation.

Now, let us go further. The President suggests that the old-age retirement, which now provides, for a man and wife, \$39 a month and for a widow with two children an average monthly benefit of \$39. These benefits are utterly inadequate. I urge that they be increased 50 percent and that the age at which widows can receive these benefits be lowered from 65 to 60 years. Now, as I understand it, there would be no return of services for that payment if that bill is enacted into law.

Now, in your opinion, do you think the enactment of that suggestion of the President, and the carrying out of those provisions, would or would not be inflationary?

Mr. PORTER. I would say that its inflationary consequences can be controlled if this bill is passed.

Mr. McMILLEN. But it is inflationary, directly speaking?

Mr. PORTER. As I have said, any increase in consumer purchasing power, from whatever source, is inflationary. But the President was faced with the alternative of insisting upon the measures which he has repeatedly asked Congress to adopt, in this inflationary cycle, as to whether he would attempt to shut off all desirable progress or whether he would attempt to treat with those things which were long deferred and at the same time ask for the measure before you now.

I certainly think that both can be done, and that they are not in and of themselves inconsistent or conflicting.

Mr. McMILLEN. You replied to Dr. Smith's questioning that the building of the headquarters for the United Nations in New York, in the amount of something like \$65,000,000, would not be inflationary. Now, let us assume that the President requested 100 times that amount for Federal buildings all over the country—and that is not an exaggerated figure, because there are demands being made to that extent—now, assuming that the President suggested such an authorization of funds, credit, or money, to construct such buildings all over this country, do you think that that legislation, if enacted and carried out, would be inflationary or not?

Mr. PORTER. I would put it this way: that there is obviously no need at this time for an extensive public building program, but at the same time—

Mr. McMILLEN. This is a public building.

Mr. PORTER. I said an extensive public building program.

Mr. McMILLEN. I am asking you that as a theoretical question.

Mr. PORTER. As a matter of theory, I would say that 65 million dollars, at the level of production that we have now, of 244 billion dollars, would not have any significant impact.

Mr. McMILLEN. None whatever?

Mr. PORTER. It might create some local shortages. There would be a demand for labor. But if it is essential, I think this country can afford to do it.

Mr. McMILLEN. How about a hundred times 65 million dollars?

Mr. PORTER. To that extent, as a matter of abstraction, obviously, as I have said repeatedly, any increase in the excess demand to that extent does put the pressure on the price level. But I do not believe that because of that fact, that it should be the policy of this Government to stop doing essential things. I understand, of course, the purpose of your inquiry, to establish that the President is in an inconsistent position in advocating price control at a time of inflation, and at the same time asking for other measures which are on the basis of basic public policy, health and welfare. I think the President is eminently correct in not saying that he is going to abandon all necessary public activities if he can at the same time get the powers to deal effectively with the problem of inflation.

Mr. McMILLEN. The President further suggests that there was discrimination and inequities in the bill passed in June providing for additional pay to Federal employees and he suggests that we change that and remedy it now, at the special session, which would require additional credit, additional money, furnished by the Government. Do you think the enactment of such a law would or would not be inflationary at this time?

Mr. PORTER. I believe that those categories of Federal employees who are now, because of the price level, in a desperate condition as far as their living standards are concerned, should not be penalized merely because we are in an inflationary cycle and I say that both can be done without significantly increasing the inflationary pressure.

Mr. McMILLEN. Would it increase it any whatsoever? Would it increase the tendency towards inflation in any amount? The additional pay for Federal workers?

Mr. PORTER. Every time you bring additional demands as represented by increased levels of pay into the market place, to that extent there is bidding for goods and services, but I want to emphasize that I do not think that the proposals that are made in any sense are inconsistent.

Mr. McMILLEN. It is just too small an amount?

Mr. PORTER. The cumulative total might have some effect but that is no reason why it should not be done.

Mr. McMILLEN. The President furthermore recommends that immediately, without any qualification as to the condition of the country financially or the inflation prevailing, that immediately upon a new Congress coming in in January, that the Congress pass a comprehensive health program based on health insurance. The Wagner-Dingell bill. That requires a vast amount of money to be furnished by the Government. Do you think that the enactment of that suggestion on the part of the President would or would not be inflationary if enacted into law?

Mr. PORTER. It could have counter-balancing tendencies. As the health of an employee was increased, maybe his productivity would increase.

Mr. McMILLEN. I am not asking you about the merits or demerits of this legislation. I am asking you what effect it would have upon the inflation that we are now facing in this country if this legislation were passed and the provisions of it were carried out, requiring more credit and money to be furnished by the Government.

Mr. PORTER. What I am saying is that in the event persons of low income who are now engaged in productive enterprise and do not have the resources with which to get medical care, that if provision were made for that, perhaps their production would increase.

Mr. McMILLEN. Mr. Porter, the President further recommends and insists that there be passed immediately upon the new Congress coming in, a universal military training program, which, as we know, would cost a vast amount of money. Do you think the enactment of such legislation would or would not be inflationary?

Mr. PORTER. I think we have no choice. We cannot abandon our national-defense requirements. Again, I say that the extent to which the public debt is increased, the extent to which new purchasing power and money is circulated, obviously its effect is not deflationary, but inflationary.

Mr. McMILLEN. I may not have disagreed with many of the answers you are attempting to make, but you are not answering my questions directly.

Mr. PORTER. You are trying to get me to say, so that the record will show here, I assume, that there is an essential conflict between the President's program and his request that he be given the powers to control inflation. I say there is not, that you cannot stop the clock on these essential things even though we are in an inflationary cycle. The effects of them, economically, I would concede, would be to aggravate in greater or lesser degree the inflationary problem, but I still insist that that is no reason for abandoning—

Mr. McMILLEN. In other words, you simply say it would not increase the inflation we have now if these bills were enacted; is that not true, Mr. Porter?

Mr. PORTER. I would say that if you would enact the entire program that it would be within manageable proportions, and I hope I

am not put in the position of saying that the President has advocated, on the one hand, that he be given the power to control inflation, and, on the other hand, taking steps which will produce inflation.

Mr. McMILLEN. Well, the President further suggests the enactment of a National Science Foundation immediately upon the new Congress coming in, which is less than 6 months from now, which would require an expenditure of additional money on the part of the Government. Do you think that would be inflationary?

Mr. PORTER. I do not think that would be significant. Maybe they would find new uses for productive enterprise, and develop methods which would increase total production. Certainly, as a defense measure, our scientific resources should be mobilized. You could abandon all functions of Government and decrease the inflationary problem. There is no question about that. Obviously that cannot be done.

Mr. McMILLEN. The President further suggests immediately upon the new Congress coming in, that there be an approval of the St. Lawrence seaway treaty which will require a vast sum of money or credit. The same question applies to that. Would it or would it not be inflationary, in your opinion?

Mr. PORTER. I think its long-term effects in increasing the amount of power available for productive purposes would be to increase production and would have a stabilizing influence. Immediately it would have a demand for manpower and materials.

Mr. McMILLEN. You are familiar with the terms of the Taft-Ellender-Wagner bill?

Mr. PORTER. In a general way, yes.

Mr. McMILLEN. You are familiar with it in detail, are you not, Mr. Porter? You have studied it diligently and have come here qualified to give your opinion on the program of the President?

Mr. PORTER. I have concentrated my attention upon the inflationary aspects.

Mr. McMILLEN. Let us, for a moment, have you concentrate your attention on this one question I am going to ask you, which, according to your statement, you are qualified to answer, as an assistant to the President, following up this message, which he has sent to the Congress. You know that the passage of that bill would require the expenditure of credit and money on the part of the Government or public housing, slum clearance—billions of dollars. The President asks for that bill to be passed now. Not by the next Congress, but now. In your opinion do you think the enactment of that bill into law, requiring the Government to furnish billions of dollars now, would that or would it not be inflationary?

Mr. PORTER. I think it can be handled with appropriate standards, and in such a way and with such emphasis on low-cost housing, with the proper use of priorities and allocations, that it will not be inflationary to the extent that it should not be done.

Mr. McMILLEN. You have qualified most of your answers by stating that they are justified because they are meritorious and the extent of the expenditures would be insignificant or of not such large amounts as to affect the inflationary pressures. The President has asked for the passage of every one of these bills I have mentioned, 12 or 15 of them, the more important ones, now, which would require a greater expenditure of money than the others in a few months, upon the new Congress coming in. Now, I am going to ask you this ques-

tion: Do you think that the enactment of all of those bills, as requested by the President, into law, and the carrying out of the terms of those bills, would, as an entire group, be or be not inflationary?

Mr. PORTER. Certainly, they would have their inflationary aspects, but you will recall the President, in his message, emphasized two things, prices and housing, and I think if those things are granted by this Congress, that it is manageable, that we can have houses without a more severe inflation.

Mr. McMILLEN. The naked truth of the matter, Mr. Porter, is this, is it not, in that, on the one hand, the President is asking for the passage of some legislation which he believes and you believe will at least halt this very serious inflation, and in the same message, at the same time, he advocates—not we ought to, but we must, at the first opportunity, pass many of these bills, within the next few weeks, in the special session of Congress, and the others upon the new Congress coming in, and enact legislation, according to your present testimony, almost every one, you have said, or several of them, would not tend to increase inflation, but taken as a whole would increase materially inflation, according to the present picture; is that not so?

Mr. PORTER. That is your interpretation of what seem to you the inconsistencies and conflicts of the message. I tried to make clear that my interpretation of the President's message is this: High prices are the No. 1 problem of this economy. At the same time the normal functions of Government, these matters of housing, desirable as a social policy, could not be abandoned. Government must continue to exercise its responsibilities and I believe both can be done.

Mr. McMILLEN. I missed one of these bills that I had marked. Perhaps I missed several. That is the new Tennessee steam plant.

Mr. PORTER. Yes.

Mr. McMILLEN. You answered that question for Dr. Smith and I will not go further, but I ask you whether or not just generally the enactment of that legislation would increase inflationary pressures.

Mr. PORTER. I said ultimately, with the shortage of power, it would have a stabilizing effect.

Mr. McMILLEN. Mr. Porter, do you advocate, yourself, the passage of these bills that I have mentioned, and any others like it, perhaps, that I have not mentioned? The enactment of those bills into law as suggested by the President?

Mr. PORTER. I certainly do.

Mr. McMILLEN. At the time and in the manner that he suggests?

Mr. PORTER. That is correct.

Mr. McMILLEN. In spite of the fact that you have said that some of them were at least somewhat inflationary? In spite of that, you want them enacted?

Mr. PORTER. I think that this is the least that can be done.

Mr. McMILLEN. How much would you estimate that it would be necessary for the Government to provide in the way of additional credit and money to carry out the provisions of the various things asked for by the President at the present and subsequent term of Congress? How many billions of dollars would that take?

Mr. PORTER. I have not totaled it up. I do not know what the estimates are on the St. Lawrence waterway. I think we can supply that for the record.

Mr. McMILLEN. It has a very direct and germane relationship to the bill presented here, and it is part of a program, and the principal business of this special session is to consider inflation and, in my opinion, we cannot consider that intelligently without taking into consideration the various provisions here asked by the President to be enacted into law. If you will, I wish you would break it down, and estimate it, as you have available figures, how much the proposed legislative program of the President will be required by the Government to provide cash and credit to carry out.

Mr. FLETCHER. Year by year?

Mr. McMILLEN. That is right.

Mr. TALLE. For the whole program.

Mr. McMILLEN. For the whole program suggested in the President's message.

Mr. PORTER. I will undertake to do that, but I would like to comment that I read the President's message as putting major emphasis on inflation and housing. I think that was where the priority was placed.

Mr. BANTA. Mr. McMillen wants you to put into the record the total cost of the program recommended by the President and not just the costs of one or two measures.

Mr. PORTER. I understand.

The CHAIRMAN. I do not think we have in the record yet an estimate as to the requirements for administration expenses. Will you provide that?

Mr. PORTER. We will undertake to provide that. I have asked for the submission of estimates to the Budget Bureau.

The CHAIRMAN. What do you estimate will be required?

Mr. PORTER. Those estimates are now being correlated.

The CHAIRMAN. All right. Will you put that in the record?

Mr. PORTER. Yes, sir.

(The information is as follows:)

The following table lists those programs which the President recommended for action at the special session for which there would be budget expenditures in the fiscal years 1949 and 1950.

Budget expenditures estimated for legislation proposed by the President to the special session of the 80th Congress (assuming enactment by Sept. 1, 1948)

Program	Fiscal year—	
	1949	1950
Anti-inflation program.....	\$51,000,000	\$62,000,000
Long-range housing program.....	28,000,000	84,000,000
Aid to elementary and secondary education.....	200,000,000	300,000,000
Minimum wage legislation.....	(1)	(1)
Displaced persons legislation.....	(1)	(1)
United Nations headquarters loan.....	25,000,000	35,000,000
International wheat agreement.....	59,000,000	59,000,000
Power projects.....	45,000,000
Pay increases for Federal personnel.....	80,000,000	100,000,000
Civil rights program.....	1,200,000	2,400,000
Total.....	489,200,000	642,400,000
Amount for these items included in the 1949 budget as transmitted last January and as projected into 1950 (see text).....	485,500,000	490,500,000

¹ See text.

The proposed legislation listed above would entail budget expenditures estimated at \$489,000,000 in the current fiscal year and \$642,000,000 in the fiscal year 1950. These items are not all new. The budget total of last January included \$441,000,000 for several of these items, and their projection into the fiscal year 1950 was expected to total \$490,000,000. The power projects, amounting to \$45,000,000, are for the most part restorations to the budget, rather than additions. Consequently, the proposals to the special session would have no substantial effect on the budget total for this fiscal year and would increase the total for 1950 by about \$152,000,000.

The expenditure estimates include \$51,000,000 in 1949 and \$62,000,000 in 1950 for the antiinflation program. No budget expenditures would be required for the credit-control programs. Only very small initial costs would be necessary for administration of the proposed excess profits tax. The net annual yield of this tax is estimated at \$4,300,000,000.

Most of the expenditure estimate of \$28,000,000 in 1949 and \$84,000,000 in 1950 for the long-range housing program represents repayable loans.

The proposal to increase the minimum wage rate to at least 75 cents an hour is expected to require little, if any, additional expenditure for enforcement in the present fiscal year. There may be some increased administrative cost but this would appear in fiscal 1950 and the amount would depend largely on experience following amendment of the act.

The proposed amendments to the Displaced Persons Act would not require any increase in budget expenditures in fiscal years 1949 and 1950 beyond amounts required under the law already enacted.

The recommended appropriations at this session for power projects represent for the most part a change in timing. Their approval would permit \$45,000,000 of expenditures for these projects in the fiscal year 1949, and would bring forward into 1950 some expenditures that would otherwise occur in 1951.

The President's recommendation for more equitable and realistic Federal pay legislation contemplates adjustments estimated at \$80,000,000 in the fiscal year 1949 and \$100,000,000 next year.

The President listed, in his message to the special session, certain other recommended legislation which the next Congress should take up immediately. He suggested that if the Congress finds time at this session to enact any of these measures, the country will greatly benefit. These include: A comprehensive health program, based on health insurance; a fair and sound labor-management relations law; a long-range farm program; a stronger Reciprocal Trade Agreements Act; a universal training program; a National Science Foundation; strengthened antitrust laws; and approval of the St. Lawrence Waterway Treaty.

The 1949 Budget of last January included \$400,000,000 as a tentative estimate of budget expenditures for universal training, \$15,000,000 for administrative expenses of health insurance, and \$5,000,000 for the National Science Foundation. Offsetting this were net receipts of \$150,000,000 in the health insurance trust accounts. The estimate for universal training requires revision in the light of recent legislation for enlistment of 18-year-olds and for selective service. Revised estimates for this group of recommendations will be included in the Budget for 1950.

ITEMS OUTSIDE THE BUDGET TOTAL

Certain recommendations which the President made to the second session do not involve budget expenditures but do affect payments by the Government to the public.

Old-age and survivors insurance.—The President recommended increased benefits under old-age and survivors insurance. The administration bill incorporating these changes (S. 2914 and H. R. 7044) provides for increasing benefit rates by 50 percent, lowering from 65 to 60 the age at which women can receive benefits, permitting higher outside earnings by annuitants, and also for making effective on January 1, 1949, the 1.5-percent contributions rate which, under present law, would become effective January 1, 1950. The effect of this legislation on trust account receipts and benefit payments would be as follows:

	Calendar 1949	Calendar 1950
Increase in trust account collections.....	\$675,000,000	\$200,000,000
Increase in benefit payments.....	500,000,000	560,000,000

In addition, the President recommended that the system be broadened to cover the millions of persons now excluded. This broadening of coverage, combined with an increase in the taxable wage base from \$3,000 a year to \$4,800, would add \$900,000,000 to the trust account collections from private employers and employees in the calendar year 1949 and about \$1,100,000,000 to collections in the calendar year 1950. Benefit payments from the trust accounts would not be increased materially in the first years of broadened coverage; they would rise gradually as the newly covered workers became eligible for benefits.

The net effect of the President's recommendation for strengthening of the old-age and survivors insurance system would be strongly anti-inflationary in the calendar year 1949, since it would result in increased collections from private employers and employees of \$1,600,000,000, compared to increased benefits to individuals of about \$500,000,000. Thus, the necessary reserves would be accumulated from which to pay future benefits as the newly covered workers become eligible for them.

District of Columbia.—Adjustment of the pay of employees of the District government, to correspond to the increase given Federal Government personnel, is estimated to require additional expenditures in the fiscal year 1949 of about \$5,800,000, and in 1950, \$5,900,000.

EFFECT OF MINIMUM WAGE INCREASE

Increase of the minimum wage rate to 75 cents an hour might add \$300,000,000 to wages received by employees covered by the Wages and Hours Act. This would represent an addition of six-tenths of 1 percent to the estimated wage total for workers now covered by this act. The estimate assumes that all of the 1,500,000 workers who are now receiving less than 75 cents an hour would have their pay rates increased to that amount and that they would work a full 40-hour week throughout the year. On this full-time basis their annual earnings would still be only \$1,560 a year and the average increase would be only about \$200 a year for each worker affected.

The CHAIRMAN. Mr. Folger.

Mr. FOLGER. I believe you suggested, Mr. Porter, that the matter of exports and the inflationary effect attributed to that was evidently overdone.

Mr. PORTER. That is my opinion; yes, sir.

Mr. FOLGER. What has been the increase of production since controls were removed? Do you have that figure there, or a percentage?

Mr. PORTER. Yes. Would you say since June of 1946?

Mr. FOLGER. Yes.

Mr. PORTER. Total industrial production was 170. That is industrial production. For June 1948, 192.

Mr. FOLGER. That is the figure I wanted. As a matter of fact, the controls were taken off in October?

Mr. PORTER. That is correct. I do not have the monthly figures for 1946. This is the entire average. I think it would probably be somewhat inaccurate to take the 1946 average. We were beginning.

Mr. FOLGER. Now, in consideration of these two facts—that is, imports do not show a sufficient impact upon our economy to have as great an effect on high prices as some have claimed, and the fact that our production has really increased to the proportion of 192—I want to ask you if it is not reasonable to attribute our extremely high prices, in a very important degree, to monopolistic control of our business.

Mr. PORTER. I certainly think that is a factor, as I said in my direct statement. There are a number of areas of important industrial commodities where there are a small number of producers. I think that Senator O'Mahoney has introduced a bill which would seal off all prices where I believe the criteria he used was of five or less manufacturers or industrial concerns are responsible for at least 30 percent of the total production.

Mr. FOLGER. And the bill he introduced proposes a 30-day investigatory period before prices are raised?

Mr. PORTER. That is correct.

Mr. FOLGER. Now, referring to section 101 (a) of this bill—

In order to protect the Nation's monetary, banking, and credit structure, and interstate and foreign commerce, against increased inflationary pressures, the Board of Governors of the Federal Reserve System are authorized, notwithstanding the Act of August 8, 1947 (Public Law 386, 80th Cong.), to exercise, up to and including June 30, 1950, consumer-credit controls in accordance with and to carry out the purposes of Executive Order Numbered 8843 (August 9, 1941) insofar as it relates to installment credit—

How comprehensive is that order, 8843?

Mr. PORTER. Executive Order 8843 was the basic order on which the Federal Reserve issued what is known as regulation W. The order itself stemmed from the powers conferred upon the President, the war powers, under the Trading With the Enemy Act. And regulation W, which was the detailed regulation promulgated pursuant to Executive Order 8843, covered a broad field of installment buying and consumer credit.

Mr. FOLGER. As I remember, that order does relate primarily to regulation W, then.

Mr. PORTER. That is correct.

Mr. FOLGER. That is all.

The CHAIRMAN. Mr. Fletcher.

Mr. FLETCHER. Mr. Chairman, I just want to ask a few short questions.

Mr. Porter, does the President have the power at the present time to directly or indirectly raise the Federal Reserve requirements?

Mr. PORTER. It is my understanding that the Federal Reserve Board has the reserve requirements to the maximum with a few exceptions. With the exception of 2 percent in Chicago and New York.

The CHAIRMAN. In Chicago and New York they can go up to 26 percent from the present level of 24 percent.

Mr. FLETCHER. The Federal Reserve Board has that power, so the President has that power. Directly or indirectly the President has that power. If the President thinks Federal Reserve requirements should be raised, there is no doubt about what would happen. Through his appointees, he very largely controls that matter.

Now, what about the discount rate? Does the same situation apply there?

Mr. PORTER. I think the rediscount rate has—I do not recall the exact limitations, but there is something further which could be done there.

Mr. FLETCHER. And directly or indirectly, through his appointees, something could be done there?

Mr. PORTER. Except that, as you know, there are differences of opinion as to the extent to which rediscount rates should be changed.

Mr. FLETCHER. That is true, but he can largely make up the minds of the boys if he wants to.

Mr. PORTER. I prefer to have you address that question to the Chairman of the Federal Reserve.

Mr. FLETCHER. But that is a fact, because those are his appointees. He removes them if he does not like the way they act.

Mr. PORTER. No. They are appointed by the President with the advice and consent of the Senate for 15-year periods.

The CHAIRMAN. He can remove the Chairman of the Board.

Mr. FLETCHER. It happened just recently.

Mr. PORTER. His term expired as Chairman.

Mr. FLETCHER. And he was demoted accordingly. The inference is that the President can do these things. The moral influence of the President's position is such that they can be done. Do you agree that he could reinstate regulation W?

Mr. PORTER. No, sir.

Mr. FLETCHER. There is a difference of opinion in that regard, then?

Mr. PORTER. That is right.

Mr. FLETCHER. I heard the chairman say yesterday that it was specifically the intent of this committee and this Congress that in the event of an emergency that could be reinstated by the declaration of an emergency. What about the margin requirements on the stock exchange? Do you not think the President could influence the raising of those margin requirements?

Mr. PORTER. I think they have been reduced to 75. Are you talking about the commodity exchange?

Mr. FLETCHER. I am going to mention that next. There is no question in my mind that if the President wanted to control inflation in this country he could exercise influence over both the commodity exchange and the stock exchange.

Mr. PORTER. I may remind you that we attempted, in 1946, to increase the margins on the cotton exchange using the powers in the Emergency Price Control Act, which gave the Administrator the authority to regulate manipulative practices. The commodity exchanges were advised that we did not have that power. There is no existing power on commodity exchanges.

Mr. FLETCHER. I am not saying it is a legal power. I say a moral influence that could be exerted. Cooperative effort on the part of industry. At this time I am certain that they would listen to the President. The finger is pointed at them publicly and if he said, "You people have to help us in this fight against inflation," there would be no question about his influence.

Mr. PORTER. I think there have been discussions on a voluntary basis with the managers of the commodity exchanges from time to time with the Department of Agriculture. I am advised that those conferences have not been successful in reaching agreement. I do not put too much emphasis on this power to regulate margins on commodity exchanges in dealing with the inflationary problem.

Mr. FLETCHER. Well, it is the sum total of all these things. No effort has been made. We have rigid supervision over export license controls. That has not been exercised properly.

Mr. PORTER. That is a matter of opinion.

Mr. FLETCHER. Yes; but we have pointed out instances of that kind. I have been getting message after message stating that critical materials have been going out of this country, not for the European recovery program, but for other reasons. There have been examples on the floor of Congress many, many times. That is my opinion, again.

Mr. PORTER. I think the over-all figures, though, certainly indicate, Mr. Fletcher, that there has been a decrease in the volume of exports.

Mr. FLETCHER. Now, this matter of voluntary allocations, this act passed in 1947, called the Anti-Inflation Act. I have not seen any effort to apply that. You say it is not workable. But I have not seen a real effort to make it work.

Mr. PORTER. I think Secretary Sawyer will tell you when he appears before the committee that there has been a great deal of activity in that field. Steel is a notable example. He has a group set up for the purpose of working out these voluntary allocation schemes.

Mr. FLETCHER. You mention here eight or nine different methods by which this whole problem of inflation can be attacked. As far as I can see, there has been no concerted effort to do the job by the powers that now exist. Instead of coming in with a program of price control, wage control—I suppose it is wage control, is it not?

Mr. PORTER. It is indirect wage control on a selective basis.

Mr. FLETCHER. Which is attacking the thing at the branches, why not attack this thing at the roots, which is easy credit, easy money, and lack of proper export controls, and all these other controls which I have mentioned, which could be exercised not to the degree that we send this country into a tailspin, but, through a little here and there, the psychological effect would be terrific. There has been no effort to curb it at the source, at the roots, in my opinion.

Mr. PORTER. Of course, Mr. Fletcher, I disagree with that, and I do not think that the existing powers, as I attempted to make clear, are adequate to stop this upward spiral of prices which is continuing everyday.

Mr. FLETCHER. I disagree with you on that. I believe we could throw this country into a depression every 60 days if they tightened on the controls they have at the present time.

Mr. PORTER. I am sure we want to avoid that, too.

Mr. FLETCHER. Certainly; this is a delicate machine. That is why a little bit of control here at the source, at its roots, will do the job. We have not made a sincere effort to do that job at the roots.

Mr. PORTER. If I might suggest, Mr. Fletcher, I would commend to your attention and to the attention of your colleagues the midyear Economic Report of the President's Council of Economic Advisers which is being transmitted to Congress today. It deals both with the symptoms, causes, and effects, and I think careful reading of that document will disclose that it supports, in general, proposals which you now have before your committee.

Mr. FLETCHER. The fundamental difference of opinion is right here as to whether an honest effort has been made to use controls which already exist.

Mr. BANTA. Do you know Mr. Tucker?

Mr. PORTER. Yes.

Mr. BANTA. Did you see his column in which he pointed out that that particular Council had advised against all of the things contained in the President's program?

Mr. PORTER. I do not think that is true at all.

Mr. BANTA. I do not know whether it is true or not, but Mr. Tucker says so.

Mr. PORTER. I have discussed these matters with members of the Council and I think there is substantial agreement. I would not want to speak for them. The report will speak for itself.

Mr. BANTA. I do not know what Mr. Tucker's authority is. I merely know that he has made that statement.

Mr. PORTER. I have too much respect and confidence in the Council to think that that could possibly be correct.

(The newspaper column of Mr. Tucker referred to is as follows:)

NEWS BEHIND THE NEWS

(By Ray Tucker)

WASHINGTON, July 24.—The men at Washington who were most startled and upset by President Truman's convention hall call for a special congressional session to discuss high prices and public housing were the members of the White House Council of Economic Advisers. He sought advice from his political managers, especially the two Rosenmans, rather than from the agency which Congress created as his official mentors in these matters.

In fact, at the moment he announced his plan to "put the Republicans on the spot," Dr. Edwin G. Nourse's experts were engaged in framing a midyear report expressing general satisfaction with current economic conditions forecasting 1 or 2 years of high economic activity and counseling against the very anti-inflation program which he will submit to Capitol Hill.

They were to have cautioned against any sharp, deflationary move at this unsettled moment lest it precipitate unemployment, business uncertainty, wage drops, a reduction of purchasing power, and a general downward dive like that which resulted from similar Federal policies from 1921 to 1922.

SPENDING

As against Mr. Truman's expected demands for billions for housing, health, education, and further minimum wage increases, they had planned to warn against excessive Federal spending. They intended to couple this proposal with a suggestion for Government-industry-labor cooperation designed to prevent strikes in such key industries as steel, coal, railroads, construction, etc.

Nor did President Truman consult John W. Snyder, Secretary of the Treasury and his Missouri crony. The latter has stubbornly resisted Federal Reserve Board's demands for further curtailment of credit by Government action. Indeed, this attitude lies behind his feud with Marriner S. Eccles, former head of the FRB.

Even as Mr. Truman was formulating his political strategy, Mr. Snyder was writing to Mr. Joseph M. Dodge, president of the American Bankers Association. In that letter the Government's chief financial officer appealed to bankers to fight inflation by "voluntary" curbs on credit, and a sharper scrutiny on applications for commercial and real estate loans. There was no mention of the drastic, 10-point, anti-inflation program advanced by the White House.

PEAK

The original Nourse report, which will probably be revised to accord with Mr. Truman's unexpected move, was to have said that the inflationary movement had reached its peak except for food, and that it would eventually be corrected by such natural causes as increasing production. Most private and public economists concur in this opinion.

Bumper corn-wheat crops, so the midyear summary would have said, should eventually lower the cost of meat to more reasonable levels. The market price for those grains is expected to fall to such an extent that it will profit the farmer to raise more and fatter cattle and hogs. Unexpectedly large foreign crops will also lessen the domestic drain that might have caused further shortages and higher prices.

OPTIMISTIC

The report was also to have offered the hope that a larger output of heavy and consumer goods—a trend borne out by all indexes save in a few fields—would make the current third round of wage boosts the last for some time to come. Lower living costs will eventually increase the take-home pay.

In short, the White House crystal gazers were working on a fairly optimistic digest for President Truman. Its basic thesis was that now was the time for nobody to "rock the boat," and that warning was to have included Government as well as industry, labor, finance, and consumers.

It might well have proved an excellent campaign document for the White House incumbent, had he not chosen to accept the political advice of Judge Samuel I. Rosenman and his extremely able wife.

VULNERABLE

Judge Rosenman was Franklin D. Roosevelt's most trusted adviser on questions of public and political psychology, although never a back-room, clubhouse boy himself. He also has a gift for apt and happy phraseology, and ghosted some of F. D. R.'s finest speeches. He has been taken over by Mr. Truman, and accompanied the Presidential party to Philadelphia.

It was he who divined the Republicans' congressional record as the enemy's possibly vulnerable spot. It was upon his advice that, instead of concentrating his fire on the Dewey-Warren ticket, Mr. Truman chose to assail a body which they had not controlled or advised.

It is generally forgotten, however, that his wife, Mrs. Dorothy Rosenman, has been one of the Nation's most eminent authorities on housing, with a sharp leaning toward a large scale, Federal program of subsidies.

She handled these problems for F. D. R. whenever interagency squabbles threatened difficulties, and it is understood that through her husband she has persuaded Mr. Truman to make low-cost homes financed by Washington one of the major issues of the forthcoming session and the Presidential campaign.

PARTISAN

Incidentally an angry Republican Congress may investigate all the circumstances behind the President's apparent disregard of the economic advisers it gave him, and his pursuit of an economic path entirely contrary to the direction which they had meant to map for him.

Such a development, in their opinion, will take them off the spot, and put Mr. Truman on it by revealing that he summoned the special session for partisan rather than statesmanlike purposes.

MR. TALLE. Mr. Porter, do you remember the work of the Temporary National Economic Committee?

MR. PORTER. Yes, sir.

MR. TALLE. That was in the 1930's, I believe.

MR. PORTER. Yes.

MR. TALLE. I have a set of the volumes that came out. It is a big one and occupies an entire shelf in my office. The question of monopoly has been raised here. My point is that so much was done on that matter in the late 1930's and inasmuch as it is referred to so frequently and was referred to here today, why is not the Department of Justice doing something about the enforcement of our anti-trust laws?

MR. PORTER. I think the Attorney General would say to you that they are doing everything they can with the resources and personnel they have. I think the Congress has gone along in maintaining the antitrust division at the relatively high level of personnel numerically. I do not know how many suits he has pending. I know an investigation was announced only this week on the distributive systems and the food industry, to see whether there were monopolistic actions resulting in price fixing. I know aggressive action has been taken. I know some was taken by my present law partner, Thurman Arnold, when he was Assistant Attorney General.

MR. TALLE. The Congress increased the appropriation for that purpose in the session recently ended, so that the attitude of the Congress is to assist the Department of Justice in the enforcement of antimonopoly laws.

Mr. PORTER. I hope it will continue.

Mr. TALLE. I might speak for myself and say that my attitude will be favorable to enforcement.

Mr. BUCHANAN. You have probably answered all the questions I have in mind, Mr. Porter. I wonder if you could give us a quick summary of the selective pricing system in Canada today. You have stated that they had a successful operation there.

Mr. PORTER. I recall, Mr. Buchanan, that during the time when I was Price Administrator, I had very close liaison with the Canadian officials, and with Mr. Donald Gordon, who was Chairman of the Wartime Prices and Trades Board. Naturally the Canadian economy is somewhat geared into that of the continental United States. When the time came for them to take off a number of their wartime controls, they lifted them gradually. They concentrated on those essential commodities and living costs, meat, butter, dairy products, and maintained selective price controls. I think if you would get—and I wrote an article about that recently—the Canadian papers, their food advertisements, and you contrasted them with the weekly food advertisements in the papers in Washington, for example, you would find a great disparity between the Canadian controlled prices, on a selective basis of meats, dairy products, and other items, and those that you see advertised here. I think that, as a generality, it can be said that Canada has managed to relinquish controls, while maintaining selective ones, with extraordinary success.

Mr. BUCHANAN. Would you mind furnishing that material for the record?

Mr. PORTER. Certainly.

Mr. BUCHANAN. Your recent article on selective price control in Canada?

Mr. PORTER. Very well.

Mr. TALLE (acting chairman). Without objection, the material will be included in the hearings.

Mr. BUCHANAN. That is all.

(The material referred to is as follows:)

[Reprinted from the July 1948 issue of the Democratic Digest, monthly publication of the Women's Division, Democratic National Committee, Ring Building, Washington 6, D. C.]

IT COULD HAVE HAPPENED HERE—HOW CANADA LICKED INFLATION

(By Paul A. Porter, former OPA Administrator)

Sirloin steak, 53 cents a pound.
Milk, 14 cents a quart.
Hamburger, 29 cents a pound.
Butter, 70 cents a pound.

To the American housewife this sounds like a prewar grocery bill. But for every Canadian housewife, this is her current 1948 price list.

Why does milk cost 5 to 10 cents more per quart in the United States than in Canada?

Why does American hamburger today cost almost twice as much as Canadian hamburger?

The answer is peacetime price control. Canada, unlike the United States, still has a democratic system of controlling some basic items in the cost of living. Present economic conditions warrant ceiling prices only on meat and butter, but there are "stand-by" controls in the event other prices threaten to get completely out of hand. (Canada also has an effective rent control law.)

Two years ago Senator Taft and Senator Wherry and others told the American people that peacetime price control was unworkable. Most Republicans and the National Association of Manufacturers said the law of supply and demand, without the aid of OPA, would lick inflation and keep prices stable.

Two years ago the Canadian Parliament followed Prime Minister W. L. Mackenzie King's proposals for extension of anti-inflation legislation permitting careful, gradual lifting of wartime economic powers.

Today, for every dollar an American spends for food, clothing, or rent, a Canadian has to spend only 75 cents.

TRUMAN CALLED FOR GRADUAL DECONTROL

The Canadian cost of living is 25 percent under American figures after 2 years of peacetime economic policies almost identical with those recommended by President Truman in 1946.

The cost of living indices of the two countries confirm statistically what a comparison of Canadian and American grocery store ads shows the housewife at a glance. Canada has an index similar to the consumers' price index of the United States Bureau of Labor Statistics (which the Republican-controlled Congress would make ineffectual, apparently to hide the impact on the consumer of their reckless policies).

The BLS index indicates the American cost of living has increased almost 70 percent since 1935-39. But the Dominion Bureau of Statistics demonstrates that Canada's cost of living has climbed only 52 percent over approximately the same period.

American food prices are up 108 percent over 1935-39 while Canadian food prices are up only 78 percent.

Canadian decontrol policy took shape in 1944 when the Wartime Prices and Trade Board decided that price and wage ceilings, rationing, subsidies, and other brakes on the country's economic life should be removed slowly and cautiously during the first two or three postwar years.

The Canadian price program, begun just before Pearl Harbor, is a practical demonstration of effective economic controls in a democratic society.

Almost all prices were frozen at levels prevailing in the fall of 1941. No price increases were allowed unless businessmen could prove they were operating at a loss. In many cases the Government subsidized producers and manufacturers instead of granting price increases.

Strategic materials were allocated. When meat, butter, sugar, or any other item became scarce, rationing was imposed.

The program worked well. Living costs were held almost stable from 1942 to 1946. Since 1946 prices have increased as the Canadian Government applied its policy of gradual decontrol.

Present Canadian price laws end March 31, 1949, unless Parliament decides to extend them.

This is the way Prime Minister Mackenzie King describes the Canadian postwar price policy:

"There is a great deal of difference between a gradual and planned policy of adjustment to postwar conditions, which may involve some modest increase in prices, and a policy of rapid removal of anti-inflation controls.

"The objective of the Government's policy is to continue to protect the people of Canada from a sharp upswing in prices and living costs, and from the inevitable aftermath of deflation, unemployment, and distress."

HOW CANADA DID IT

Canada embarked on its five-step decontrol program in the summer of 1945:

First. Government priority controls were released on such strategic wartime goods as steel, textiles, and fats and oils.

Second. Manufacturers and wholesalers were allowed more freedom in dividing supplies of goods among stores throughout the country.

Third. Requests for price increases were granted more frequently than during the war.

Fourth. Subsidies were ended gradually. Businessmen were allowed to compensate for their loss of subsidies by charging higher prices.

Fifth. Price ceilings were removed slowly. Rationing was ended gradually. But neither of these controls was lifted until the Canadian Government was certain that such suspensions would not push prices out of reach of low-income consumers.

Over-all price ceilings were held almost intact from 1941 until early in 1946. Then restrictions were removed on such nonessential goods as cosmetics, tobacco, and books.

Not until 1947 did Canada find it advisable to suspend price controls on essential cost-of-living items like meat and other foods, and clothing.

The key words in Canada's decontrol program are "suspension" and "stand-by." Wartime controls have been suspended only. The wartime economic restrictions are standing by, ready to protect Canadians from runaway inflation.

Last January, meat and butter prices started to get out of hand. The prices were low by present American standards: 75 cents a pound for butter and 59 cents a pound for sirloin steak. But Canada pulled its price ceilings off the shelf and applied them to meat and butter. The result: 70-cent butter and 53-cent sirloin steak.

The ceiling prices on meat and butter will be removed just as soon as economic factors indicate supply is sufficient to prevent skyrocketing. The Canadian Government dislikes controls as much as any democratic nation. But the Canadians believe selected controls for a short period now are better than a post-war depression in 5 or 10 years.

Thus far the Canadian people think their anti-inflation program has done a good job of holding down the cost of living. But Canadian officials point out they could have kept prices much lower if the United States had adopted a similar program of gradual, orderly decontrol coupled with stand-by economic authority.

The American and Canadian economies are so closely interrelated that inflation here almost of necessity means somewhat higher prices in Canada.

But would slow suspension of controls and stand-by price regulations have worked in this country?

The answer is an emphatic "Yes."

Canada's wartime control program was very similar to this Nation's OPA and War Production Board. And Canada accomplished an orderly transition from war to peace in the framework of its wartime economic policy.

America could have followed the same sort of procedure. Canada still is very much a democracy despite gradual decontrol and stand-by economic powers.

In 1946 President Truman called for a postwar anti-inflation program similar to the Canadian plan. But the Republicans said it wouldn't work—and they have refused to try it, even after their way proved wrong.

GOP—NAM—HCL

So Congress bowed to the big business combination of Republicans and the National Association of Manufacturers. These same big business pressures were found in Canada when price-control legislation was up for renewal each year. But the Canadian Parliament refused to yield. Canadian legislators put their faith in orderly decontrol while Republicans swallowed the NAM gospel.

No American housewife needs to be reminded of what happened in the United States in 1946 and 1947. Prices went up and up and up. And they're still climbing today.

All the American housewife can do is cut her servings of meat, eat less at almost every meal, and make last year's clothes do for another season at least.

The American economy is running wild under the Republican-NAM philosophy. But the NAM has no regrets. While the housewife struggles to fit even the essentials into her dwindling budget, the profits of big business are at all-time highs.

The contrast between the Canadian and the American postwar economies is striking. The Republican-controlled Congress has let big business take the reins in this country. But the Canadian people, through their Parliament, have asked their Government to keep a check on the nation's economy.

Canadians seem to remember 1929, 1930, 1931, and 1932. Apparently the Republicans have forgotten the days of Hoovervilles, soup kitchens, and bonus marchers.

WHAT TO DO NOW?

But this is 1948, not 1946. What can be done now to right the wrongs of 2 years ago?

President Truman proposed stand-by price controls when he addressed the special session of Congress last fall. The President said:

"Legislation should be enacted, authorizing the Government to impose price ceilings on vital commodities in short supply that basically affect the cost of living. Basic elements in the cost of living are food, clothing, fuel and rent.

"In addition, the legislation should be broad enough to authorize price ceilings on those vital commodities in short supply that basically affect industrial production. This will enable us to stamp out profiteering and speculation in these important areas.

"I, therefore, recommend that authority be granted, as a preparedness measure to ration basic cost-of-living items on a highly selective basis."

The President has repeated his proposals several times since last November. Prices have continued to increase since last November. But the Republicans still refuse to do anything about inflation.

The Democratic administration does not want over-all wartime price ceilings. Rather, it seeks stand-by authority to impose selective controls.

The President has called for an economic policy that Canada has demonstrated can work excellently in a democracy.

Stand-by controls at this time probably would not bring the American cost of living in line with Canada's relatively low prices. The lid has been off too long.

However, Americans would welcome any sort of relief, no matter how small, from inflation. And Canada's experience indicates stand-by controls can work.

CANADIAN BUSINESSMEN DIDN'T SUFFER

But won't peacetime controls hold back business? And, after all, isn't increased production essential to stabilizing the American economy? These arguments of the 1946 OPA-busting days can be dismissed with a look at the Canadian business profit sheet.

Last year corporate profits in Canada totaled \$1,800,000,000 before taxes. In 1938, corporate profits were only \$467,000,000 before taxes. In 1947, profits after taxes were \$804,000,000; in 1938, profits after taxes were only \$92,000,000.

The figures show profits before taxes have increased by more than 300 percent. And profits after taxes have increased by more than 700 percent. And Canada has peacetime price control. Yet the Canadian businessman still is doing all right.

In the United States corporate profits were \$3,300,000,000 before taxes in 1938. Last year profits before taxes were \$28,000,000,000. That is an increase of 700 percent.

Corporate profits were \$2,300,000,000 after taxes in the United States in 1938. Last year the figure was \$16,900,000,000. That is an increase of 600 percent.

Both the Canadian consumer and the Canadian businessman have profited from orderly decontrol and stand-by economic authority.

The NAM says, "What's good for business is good for the country." Canada's experience shows that peacetime controls are good for business.

Despite President Truman's repeated inflation warnings and pleas for some sort of economic brakes, the GOP continues to sit on the sidelines and watch prices move upward.

Apparently big business can't take care of inflation the way the NAM-GOP promised in 1946.

Canada offers convincing proof that a democratic nation can stabilize its economic life—if the country is not hamstrung by a Republican-controlled Congress.

Mr. TALLE. Are there further questions?

I understand, then, that your testimony, for the time being, at least, is concluded, Mr. Porter, and thank you for appearing here. Will you be available in the event we should require your appearance before the hearings are concluded?

Mr. PORTER. I certainly will.

Mr. TALLE. The committee will stand adjourned, to reconvene at 10 o'clock Monday morning.

(Whereupon, at 1:30 p. m., the committee adjourned, to reconvene on Monday, August 2, 1948, at 10 a. m.)

INFLATION CONTROL

MONDAY, AUGUST 2, 1948

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee reconvened, pursuant to adjournment, at 10 a. m., Hon. Jesse P. Wolcott (chairman) presiding.

Present: Messrs. Wolcott, Smith, Talle, Sundstrom, McMillen, Buffett, Hull, Stratton, Scott, Banta, Fletcher, Nicholson, Spence, Brown, Patman, Folger, Buchanan, Boggs, and Multer.

The CHAIRMAN. The committee will come to order.

We will proceed with the consideration of the problems of inflation.

Mr. Spence would like to make a few remarks.

Mr. SPENCE. Mr. Chairman, we are seeking for the causes of high prices, and I think it would not be inappropriate to investigate some of the rises in prices of commodities manufactured by the great corporations, notably the United States Steel Corp.

Some time ago the United States Steel Corp. raised the price of its products, I believe, 11 percent. I see in yesterday's New York Times that they are contemplating another rise in the price of steel.

Steel basically affects the cost of living. It goes into thousands and thousands of commodities which the people use daily. I have here some illuminating figures.

In 1938 there was a deficit in United States Steel of \$7,717,454.

These other figures are net earnings after taxes:

In 1939 they made \$41,119,934; in 1940 their earnings were \$102,-211,282; in 1941, \$116,171,075.

Then, in 1942, when price control came on, they earned \$71,248,569.

In 1943 they earned \$62,631,742; in 1944 they earned \$60,791,281; in 1945 their earnings were \$58,051,056; in 1946, \$88,622,475. That was when price control was weakened.

Then, in 1947, United States Steel net earnings, after taxes, were \$127,098,148.

In 1948, their earnings for the first quarter were \$33,957,541—net earnings after taxes.

Now, those were the peak earnings in the history of the corporation. It seems strange that after raising the price of their product 11 percent, they are considering making another rise. I think if we are searching for the cause of high prices, we might ask the chairman of the board of some of these great corporations to appear before the committee in an attempt to justify the increases in the cost of their products, which so basically affect the cost of living and the welfare of the American people.

Mr. BUFFETT. Would you yield, Mr. Spence?

Mr. SPENCE. I yield.

Mr. BUFFETT. Do your figures show the percentage the corporation earned on its invested capital?

Mr. SPENCE. No; that does not show.

Mr. BUFFETT. I suggest that might be added to clarify the situation.

Mr. SPENCE. These were net earnings, after taxes paid. It seems to me that is the test. I know all of the public utilities, before the Securities and Exchange was organized, were just filled with water, and they wanted dividends upon their stocks which could not be justified at all. I think the basis on which these things should be considered is on net earnings after taxes. This is their comparative statement. They made more in the first quarter of this year than they made in any quarter of the history of their corporation and still they want to raise the price of their product.

Mr. BUFFETT. You do not think that return on the invested capital is a decisive factor?

Mr. SPENCE. Not decisive, though we might consider it. I think, however, it justifies our sending for the chairmen of the boards of these corporations which have been constantly raising the prices of their product so that they might have an opportunity to justify their action.

Mr. FOLGER. Will you yield, Mr. Spence?

Mr. SPENCE. I yield.

Mr. FOLGER. You may recall, Mr. Spence, that Senator O'Mahoney has a bill which, if passed, would give authority to a competent department of the Government to prevent the raising of prices except upon investigation, and after a 30-day period—something on the order of the raising of wages. Do you not think that is a good idea?

Mr. SPENCE. I think that is a good idea, but I think if this committee wants a comprehensive view of the whole situation, and if this committee is going to deal with high prices, it would be appropriate to find out how these great corporations justify these raises in prices. I think we ought to have that information here.

Mr. FOLGER. I do not mean to preempt that course. As a matter of fact, would it not be helpful to the consideration of such a bill?

Mr. SPENCE. I think so. To what committee has that bill been referred?

Mr. FOLGER. Senator O'Mahoney introduced it in the Senate, and I think Mr. Mansfield introduced a similar bill in the House.

Mr. SMITH. Will the gentleman yield?

Mr. SPENCE. I yield.

Mr. SMITH. Do you mean that these corporations earned that amount net?

Mr. SPENCE. That is my information.

Mr. SMITH. Then, the net proceeds were distributed among stockholders; is that right?

Mr. SPENCE. I do not know. They earned it. I do not know what the distribution has been. This year United States Steel's net earnings after taxes were over \$33,000,000 for the first quarter. After that they raised the price of their product, as I understand it, 11 percent. Now, they are considering a further raise in prices. I think we ought to ask them for their justification for such action.

Mr. SMITH. Part of those net earnings are held back by the corporation for improvements and so forth.

Mr. SPENCE. That is true, but you cannot make improvements out of current earnings.

Mr. SMITH. I am just wondering why you did not include the earnings of United States Steel Corp. from 1931 on up to 1939.

Mr. SPENCE. I will get those figures and insert them in the record.

Mr. SMITH. Were there any net earnings?

Mr. SPENCE. There was a deficit in 1938. Then, the war came along, which increased their net earnings, and then price control came on, reducing their earnings. Then, when price control went off, their earnings skyrocketed again.

Mr. SMITH. At the same time, do you not think we ought to investigate the biggest corporation in all the world, the United States Government, and see what its profits are doing to the price structure?

Mr. SPENCE. Do you want to discontinue the investigation of these other corporations until we make a final report on the United States Government? Then there will be no action taken at all. I think now is the time to meet this situation. I do not know whether they are going to increase their prices or not, but the newspaper reports are that they are going to increase prices further. I think before they do that, we ought to know something about their justification.

Mr. SMITH. You think they should not increase their prices; is that it?

Mr. SPENCE. I think, on the basis of those figures, there is no justification for it.

Mr. SMITH. And that would take into consideration inventories, depreciation, obsolescence—

Mr. SPENCE. I suppose they set something aside for depreciation, and obsolescence. These are net earnings after taxes. At any rate, it would not be inappropriate to have them come here and tell us just what they have earned, what they have done with the money, and their justification for any further increase in the price of steel.

Mr. SMITH. We had an extensive investigation of those things by the TNEC, did we not? What became of it? It cost hundreds of thousands of dollars to make it, so I have been informed.

Mr. SPENCE. Doctor, just because one investigation resulted in nothing, do you feel we should discontinue all other investigations? I do not think that would be a very pertinent argument.

Mr. SMITH. It seems to me that almost anyone can take the figures of these corporations, go into them himself, and decide whether or not the corporations are the cause of the high cost of living. Farming is not a corporate matter. See where food prices are at the present time.

Mr. SPENCE. My suggestion is that we should ask them to come here to justify their action in raising the price of steel. Of course, what U. S. Steel Corp. does is very important. They have controlled the price of steel for years. They have permitted the smaller companies to live.

Mr. SMITH. It is not that I am opposed to finding out—

Mr. SPENCE. If they want to destroy them, they can destroy them at any time.

Mr. SMITH. But I think we ought to be careful and not try to make a scapegoat out of industry, which seems to be the order of the day around Washington, when, in reality, it is the politicians in Washington who are the sole cause of the high cost of living. There is no question about that. Let us put the blame where it belongs.

Mr. FOLGER. Will you yield, Mr. Smith?

Mr. SMITH. I yield.

Mr. FOLGER. With reference to farm prices and things of that kind, is it not probably a fact, taking meat, for example, that the great increases in prices occur after the meat gets into the hands of the packers? Do you not think those big corporations, according to Senator O'Mahoney, would come under that bill, thus controlling the major necessities of life? I will answer my own question and say "Yes."

Mr. SPENCE. That is a suggestion.

Mr. SMITH. I think the policy pursued by the United States Government in the last 15 years has brought on this inflation, every bit of it, and there is no use at all trying to blind ourselves to that important fact. Let us not try to cover that up. It is here before this country, and we must meet it. The New Deal has brought these high prices on us.

Mr. SPENCE. The only suggestion I make is that these corporation heads be brought here and be given an opportunity to justify their price structure. Certainly that is not doing anybody an injustice. We are taking action which affects the living standards of the American people, and it is a public question, and they ought to justify their price structures.

Mr. SMITH. My point is we ought to clean our own house first, before we barge off on problems of this kind.

Mr. SPENCE. You mean clean out all the Democrats?

Mr. SMITH. Not necessarily, Mr. Spence. I mean to clean out all this mess the New Deal has gotten us into in the last 15 years—socialism, communism.

Mr. FOLGER. I think the New Deal got us out of a mess.

Mr. SPENCE. We were in a pretty bad mess when the New Deal came in, I know that. We have never been in such a mess since that time.

The CHAIRMAN. I do not think, of course, that we should close the door against any witness testifying on any phase of this question who will enlighten the committee. I think we all share Mr. Spence's concern about the rise in steel prices. As to whether they are necessary or not, this committee does not have much information. The Joint Committee on the Economic Report held hearings last March, I believe it was, when the steel companies raised some of their prices. At that time the steel companies appeared before the Joint Committee on the Economic Report, and, because of the statements made, I assumed that the Joint Committee on the Economic Report made no recommendation at that time, indicating that they had perhaps justified the increase.

Mr. SMITH. Mr. Chairman, that is a nonpartisan body, the Committee on the Economic Report.

The CHAIRMAN. Yes.

Mr. SPENCE. These increases have been made since that time.

The CHAIRMAN. But I think they have lowered their prices on certain of their products and increased them on others. At that time they told us, as I recall it, that their increases were to balance their total price structure. Their prices were too low on part of their output and too high on the rest of it.

But I do not know what the situation is now. I do not think any of us know whether there is any justification for that last rise or not. If we decide later on that it is important to the point of enlightening us on what we should do, we will ask them to come down and tell us why they have increased their prices. I have said that while it is unfortunate that there should be any increase in the prices of basic materials—and steel certainly is one of them—if they are operating at a loss, then of course it is up to them to determine whether they can justify an increase in prices.

I do not know whether their increase is necessary. They may be able to justify their increase in price. This rise in the price of steel which took place a couple or three weeks ago took place after wages were adjusted upward, which perhaps changed the situation somewhat from last year, when, as I recall it, they raised the price of steel in the anticipation of wage increases, which I personally thought was a very bad thing to do. I thought it invited a wage increase at that time. This time they waited until after the wage increases were granted before raising the price of steel.

Perhaps later in the week it will be possible to get some one down here to tell us about it.

Mr. SPENCE. I think the President contemplated an increase because of proposed expansion. If you are going to increase the price of a product because you expect to expand your industry, there would be no limit to it. That would seem to be their theory—that they are contemplating a vast expansion of their facilities and, therefore, they are going to raise the price of their product.

The CHAIRMAN. I am not so sure but what that might not be justified, under the circumstances. Basic industry cannot be expected to broaden their capital base to meet an emergency, to the extent that when we get back to normal demand they would have a top-heavy capital structure, and perhaps continue to operate at a deficit and finally have to close down. I think if their increase in price is in anticipation of an expanded capital base which will result in increased production, probably it might be justified.

That is similar to the attitude American bankers take with respect to loans. They have done a pretty good job—at least the Federal Reserve feels they have—on the matter of curtailment of credit. They have tried to cooperate with the Treasury in keeping down credit expansion, and they are withholding money for loans except for the expansion of production. That is a similar situation.

Mr. SPENCE. Mr. Chairman, if they raise prices in order to meet the contemplated expansion of the industry, they do not meet the emergency. The objective, in meeting the emergency, is to lower prices.

The CHAIRMAN. Ultimately, if they expanded production, it would result in a lowering of prices. We have been encouraging them to do that, and they have been having conferences under the act which we passed last December. I assume that in these conferences they considered an expansion of the production effort and ways and means by which it could be done. If the expansion of plant is such as to wipe out present reserves, that might be a problem, of course. That may be their justification. I do not know, however; that is just conjecture.

Mr. SPENCE. Suppose we let them come down here and tell us about it?

The CHAIRMAN. Well, we probably will.

Mr. SMITH. What is the rate of steel production at the present time?

Mr. PATMAN. I think it is around 90,000,000 tons.

The CHAIRMAN. Around 95 percent of capacity, I believe.

We have with us this morning Mr. Thomas McCabe, Chairman of the Board of Governors of the Federal Reserve System. This is Mr. McCabe's first appearance before the committee. I know that Mr. McCabe will receive the utmost courtesy from the members of the committee.

Mr. McCabe has a statement, but the mimeographed copies have not yet arrived, have they, Mr. McCabe?

Mr. McCABE. They will be over in a minute. They have already left the office.

The CHAIRMAN. Does the committee prefer to wait a few minutes until we get the mimeographed copies? Is there any other subject matter which the committee would like to take up while we are waiting?

Mr. SMITH. The Federal Reserve Bulletin for July gives iron and steel production, as of May 1948, as 207,000,000 tons.

Mr. PATMAN. Annually? That cannot be right, Dr. Smith.

Mr. SMITH. I beg your pardon, that is an index number—over the average of 1935-39. So it is more than double.

Mr. PATMAN. It is certainly not over a hundred million tons. I would guess it is somewhere around 95,000,000 tons.

Mr. SMITH. It says here 222. That is the index figure, over 1935-39 average, which is 100.

Pig-iron production is at about the same rate.

Mr. PATMAN. On page 80 of the Federal Reserve Bulletin there are charts showing the production of steel which indicate that it has been running at around 95 to 98 million tons a year.

Mr. SMITH. Page 80?

Mr. PATMAN. Yes.

Mr. NICHOLSON. Will you tell me what the price of corn is today and what it was in 1938? And that is a basic food commodity in this country.

Mr. SMITH. I do not have the figures on those, but it is very, very much higher.

Mr. NICHOLSON. Has it doubled or trebled?

Mr. SMITH. I would say it has trebled. But I do not know. I do not have the exact figures.

Mr. NICHOLSON. We eat food, but we cannot eat steel.

Mr. SMITH. There is one point which we should not overlook in connection with the cost of living at the present time, and that is mainly that corporations cannot replenish their capital structure as they did previous to the high oppressive taxes. High taxes now take from individuals who have stocks in these corporations so much of their income that from that source capital structure is not being replenished as it was prior to these high tax rates. I am not saying that a corporation does earn more, but if it does earn more than it did previously, before you could say that those earnings were not justified you would have to go into the matter of the inability to provide capital to replenish our tools of production.

If anybody thinks that corporations in this country are riding high under the present inflationary debauch, they just have another guess coming. All we need to do is to wait a while and see whether that is a fact or not. They are as uncertain of the future as any other segment of the economy, if not more so.

The CHAIRMAN. I think we had better go ahead, Mr. McCabe. When the copies of your statement arrive they will be distributed.

Mr. McCABE. Very well, sir.

STATEMENT OF THOMAS B. McCABE, CHAIRMAN, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ACCOMPANIED BY GOV. R. M. EVANS AND WOODLIEF THOMAS

Mr. McCABE. Chairman Wolcott and members of the committee, I deeply appreciate the consideration your chairman has extended to me in making the time of my appearance here as convenient as possible. Although Congressman Wolcott had asked me to come before you earlier, he kindly consented, in deference to my request, to wait until this morning.

I therefore acceded to the urgent request of Senator Tobey to appear before the Senate Banking and Currency Committee last Thursday morning. Since your committee has been fully occupied with the testimony of Mr. Porter, I trust that the postponement until this morning has not caused you inconvenience.

On the evening before going to the Senate committee I canvassed the members of the Board by telephone to ascertain their views on the two titles of the proposed anti-inflation bill which relate to consumer credit and bank reserves. The members of the Board agreed unanimously to the following statement:

ANTI-INFLATION ACT OF 1948

The proposed Anti-Inflation Act of 1948 includes two titles relating to credit controls. Both are, in substance, part of the comprehensive anti-inflationary program which the Board of Governors has previously recommended to Congress. Title 1 relates to the regulation of consumer credit and title 2 relates to bank reserves. As you gentlemen know, the proposed regulation of consumer credit is identical, except for the date, with the bill passed by the Senate, and acceptable to the Board of Governors as one part of an over-all program.

The proposal with respect to bank reserves is similar to that advanced by the Board in April, except that the increased requirements would be applicable only to member banks, whereas the Board had recommended that they be made applicable to all commercial banks. This is a significant difference. We feel deeply that it is not fair to member banks in their competitive relations to non-member banks to require that they be singled out to carry the additional reserves that may be necessary to combat this inflationary situation. As an emergency measure, however, the bill would be adequate to meet the immediate need for additional authority to deal with reserves.

In thus stating the views of the Board on these two titles of direct concern to the System, I do not want to create the impression that action in the credit field alone will solve our inflationary problems. Other areas, particularly a budgetary surplus, are more important.

Since I presented that statement to the Senate committee, the Board had this morning had an opportunity to meet and to discuss the proposed legislation at length.

The Board are agreed that the inclusion of the nonmember banks is essential to make the proposed legislation fully effective. I have also been in touch with several of the presidents of the Federal Reserve banks, and others. There is strong concurrence with the statement

that it would be very unfair to single out member banks to carry the additional reserves to combat this inflationary situation. This is particularly true of the presidents from those districts where there are large numbers of nonmember banks, which would be given a competitive advantage as against member banks. It might result in a serious loss of membership in the System and weaken the effectiveness of its policies. As you know, the effective reserve requirements in most States are substantially below those carried by member banks, and thus nonmember banks have greater latitude and earning power.

The question of the inclusion of non-member banks is very important and we would appreciate it greatly if the committee would give this problem serious consideration. Unquestionably, from the point of view of effectiveness as well as equity, the proposed legislation should apply to all commercial banks.

Now, I would like to give you some of my personal observations concerning the impact of the inflationary forces on our credit control mechanism. These remarks are substantially the same as those I made last week before the Senate Banking and Currency Committee, except for the elaboration on a few points on which questions were asked by the Senators.

Consideration of the pressures now at work in our economy must be based on an understanding of the fact that the financial forces generated in a great war are among the most disrupting factors that can affect the economic system. We are now dealing, and for years shall be forced to deal, with the monetary backwash of the greatest and most costly war of all time. We are faced with the problems of liquidating the effects of that war upon our own economy, and, indeed, upon the economy of the world. If history is a guide, we must realize that these problems will not be solved in a day. They will extend over a number of years—how many will depend upon how wisely and how courageously we devote ourselves to the task.

The financial cost of the last war, if all conceivable items of cost were included, perhaps could never be accurately summed up. Suffice it to say that our national debt rose to approximately \$280,000,000,000 and is still above \$250,000,000,000.

Gentlemen, I shall refer from time to time to the book of charts—Federal Reserve Charts on Bank Credit, Money Rates, and Business, July 1948—which I have passed around to each of the members. You will find, on page 28, a chart on the debt of the United States Government.

The solution of our present problems does not require us to determine whether the debt should have risen so high, whether we should have spent so much, whether we should have taxed ourselves more and borrowed less, or whether the pattern of our borrowing was well conceived. What has been done is in the realm of fact and the consequences must be dealt with accordingly.

One of the important facts is that the creation of our national debt resulted in a tremendous expansion of the money supply. While the Government borrowed vast sums from nonbank lenders, other vast sums were supplied by the commercial banking system. And let me say right here that this Nation owes a debt of gratitude to commercial bankers generally, for their service in the task of financing the war. The rapid expansion of the money supply which resulted from

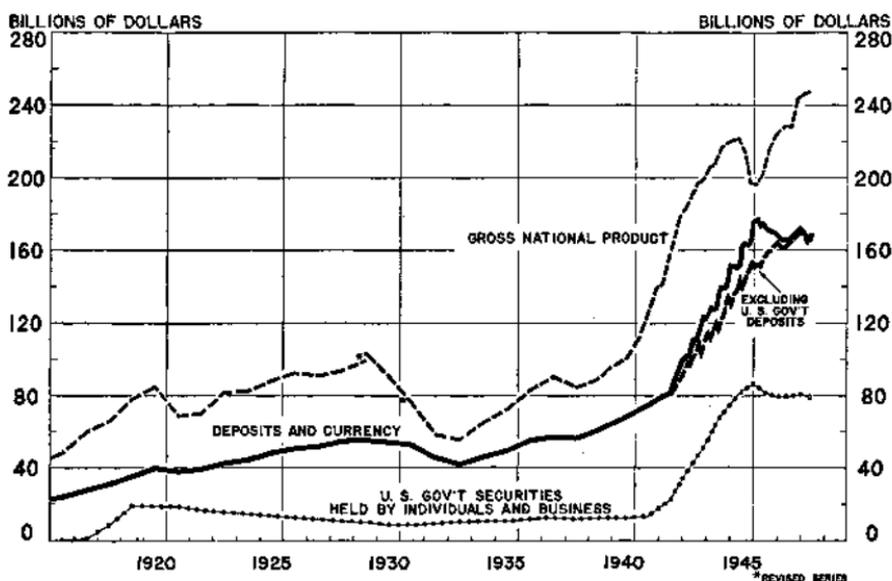
their contributions must not be permitted to rise and plague them as if they had cunningly contrived it for their own selfish ends.

Nevertheless, as a net result of war financing, there were increases in the public's holdings of demand deposits and currency from less than 40 billion in 1940 to 110 at present; of time deposits from less than 30 billion to nearly 60 billion; of United States Government securities, which are readily convertible into money, from a few billion to over 90 billion. And you can see that trend on the chart which I have before me, gentlemen.

Mr. PATMAN. Do you have that particular chart in this book of charts, Mr. McCabe?

CHART 1

BANK DEPOSITS AND CURRENCY AND GROSS NATIONAL PRODUCT



Mr. THOMAS. The deposit figures are shown in the chart on page 10, but the public holdings of Government securities are not shown on that same chart. They are shown on page 29.

Mr. McCABE. The total supply of these forms of money and potential money is now more than three times the prewar total.

The productive capacity of the Nation was largely devoted to war purposes for almost 5 years. At the peak more than 50 percent of our record production was for war use. While millions of people were coming into possession of more money than any people had ever had to spend and save, there was a scarcity of things to spend it for. Consequently, two great backlogs rapidly accumulated—a backlog of unfilled wants and a backlog of money savings. With removal of controls this pent-up spending power, plus an unprecedented volume of current income, were turned loose in a market characterized by scarcities and shortages. Prices, wages, and profits rose rapidly, and the spiral of inflation was on its way.

At present, with a supply of money or potential money readily available to buy the current output of goods and services about three

times the prewar level, the over-all physical volume of production of goods and services, so far as it can be measured, is probably little over a half larger than the prewar maximum.

Production, it is important to emphasize, is practically at capacity; there has been little increase in its physical volume during the past year and a half, notwithstanding the great pressure of unsatisfied demands, expanding credit and rising prices.

The trend of industrial production—manufacturing and mining—is indicated on page 57 of your chart book.

Prices, on the average, have risen by nearly three-fourths since before the war and two-thirds of this increase has occurred in the past 2 years. (See pp. 70-73 of chart book.) The dollar value of the total national product, at nearly \$250,000,000,000 a year, as shown on chart previously presented, is over 2½ times the prewar maximum.

The CHAIRMAN. Mr. McCabe, copies of your statement have arrived. If you do not mind, we will interrupt for a moment to make the distribution.

Mr. McCABE. Thank you, sir.

On the basis of the present volume of money, the turn-over of which is low relative to past periods of high activity and could be greatly increased, prices could rise even further. Further expansion of bank credit, the capacity for which is tremendous, would add to the already excessive money supply and could do little to increase output.

Capacity for still further credit expansion also grew out of war finance. In helping to finance the Government's large war expenditures and to provide the money demanded by the expanding and abnormal war economy, the commercial banks of the country and also the Federal Reserve banks greatly expanded their holdings of Government securities.

Commercial bank holdings of Government securities of all types increased from about 16 billion in 1940 to a peak of 90 billion at the end of 1945 and then were reduced, during 1946, to 70 billion, largely by Treasury use of its excess bank deposits to retire debt. Subsequently, to meet the demands of rapidly expanding private economy in the postwar period, banks have further reduced their holdings of Government securities, but they still hold \$65,000,000,000 of them. Other investors have also sold or redeemed some of the holdings of Government securities in order to obtain funds for other uses. (See p. 11 of chart book.)

Sales of United States Government securities in the market by banks and others have not been absorbed by purchases on the part of other investors. In order to keep the prices of Government securities from declining, the Federal Reserve System has continued to carry out its wartime responsibility of supporting the market by buying at relatively stable prices securities offered for sale and not purchased by others. The result of these purchases by the Federal Reserve banks is to supply additional reserve funds to banks. Because of the fractional system of reserve requirements, these new reserves, in turn, provide the basis for an increase in bank credit that may be many times the amount of new reserves obtained.

In the postwar period these reserves supplied the basis for an increase in bank credit in response to an active demand for loans to finance the operations and expansion of the business system in an era

of high demand, accelerated activity, rising costs and rising prices. There is ample evidence that bank credit is also being used for purposes ordinarily served by the capital market. As a result, despite a reduction of \$25,000,000,000 in the volume of Government securities held by commercial banks, deposits and currency held by the public have increased by an additional \$15,000,000,000 since the end of 1945. This has been largely the result of an increase of \$15,000,000,000 in bank loans.

Pages 10 and 11 of your chart book will indicate that trend.

The Board of Governors has kept the Congress and the public informed concerning these results of supporting the market for Government securities. It has repeatedly pointed out that the effect has been to increase significantly, and, it may be, dangerously, the money supply. The need for market support of Government securities has greatly increased the problem faced by the System in adopting policies to regulate the supply of money and credit to the justifiable needs of a stable, full-employment economy. As long as various holders of Government securities endeavor to sell more of their holdings than other investors are willing to buy, the Federal Reserve banks must purchase the balance, and these purchases create bank reserves.

It is my view that the System is obligated to maintain a market for Government securities and to insure orderly conditions in that market, not primarily because of an implied commitment to wartime investors that their savings would be protected, nor to aid the Treasury in refunding maturing debt, but because of the widespread repercussions that would ensue throughout the economy if the vast holdings of the public debt were felt to be of unstable value.

The Federal Reserve System and the Treasury have, nevertheless, been able to adopt some policies designed to offset the expansive effect on bank reserves of market purchases of Government securities by the Federal Reserve System.

The first and quantitatively more effective of these measures has been the use of the Treasury surplus to retire maturing securities, particularly those held by the Federal Reserve Banks. The debt retirement program was made possible first by a large cash balance built up by the Treasury in the Victory Loan drive in 1945 and later by a substantial surplus of cash receipts over expenditures. In paying out a large part of the excess cash collected, from the public to the Federal Reserve for retirement of debt, that amount of money was eliminated from the money supply and also from bank reserves.

As a second measure of restraint, about a year ago the Federal Reserve and the Treasury embarked upon a program of permitting the yield rates on short-term Government securities to rise from the very low levels at which they had been pegged during the war. The purpose of this action was to encourage banks and others to invest available funds in short-term securities. This enabled the Federal Reserve to reduce its holdings of short-term securities and thus offset the effect on reserves of its purchases of longer term bonds. The rate on 90-day Treasury bills rose from $\frac{3}{8}$ of 1 percent to about 1 percent and that on 1-year Treasury certificates from $\frac{7}{8}$ to $1\frac{1}{8}$ percent. The Federal Reserve banks early in 1948 raised their discount rates from 1 to $1\frac{1}{4}$ percent.

That is indicated on pages 34 and 35 of your chart book.

Late in 1947, market yields on Government bonds also rose; that is, prices of bonds, which had been selling at large premiums, declined in the market. This adjustment was in large part inaugurated by sales by financial institutions to obtain funds to invest in corporate securities and mortgages, but it was accelerated by sales made in fear of further declines in prices of bonds from their high levels. In order to check this decline, the Federal Reserve System adopted a policy of freely purchasing bonds at an established series of prices, which maintained yields in accordance with a pattern ranging from 1½ percent for 1-year issues to 2½ percent for the longest-term bonds. This pattern kept the prices of all except a few very short issues of securities at par or higher.

It may be of interest to review credit developments and the effects of these policies during the past 12 months.

Again you might refer to pages 10 and 11 in the chart book.

In the year ending June 30, 1948, commercial banks showed a small increase in their deposits and their total loans and investments, although there were some wide fluctuations during the period. In the 12 months, commercial banks increased their total loans and their holdings of corporate and State and local government securities by a total of \$7,000,000,000. Most of this growth occurred in the latter half of 1947 and was accompanied by an expansion in bank deposits and reserves.

In the early months of 1948, however, deposits were withdrawn to make seasonal heavy tax payments, which were not offset by Treasury expenditures. Banks met these needs largely by reducing their holdings of Treasury bonds. Some maturing bonds were exchanged for certificates and a part of these issues were sold. At the same time banks in general purchased added amounts of Treasury bills, an indication of the effect of the higher short-term rates in attracting available funds.

Banks also continued to increase their loans in the first half of 1948 by about 1.7 billion dollars—a somewhat slower rate of growth than in 1947. Most of the dollar increase in bank loans during 1947, particularly in the last half, was in commercial and industrial loans, but the increase in consumer loans and real estate loans showed larger percentage increases in 1947 and have continued to expand in 1948. (See p. 13 of chart book.)

Savings institutions, particularly insurance companies, also considerably expanded their holdings of mortgages and investments other than United States Government securities during the past year. In the aggregate, as shown on the chart, these assets of selected groups of financial institutions increased by 8.6 billion dollars in the period, of which 6.4 billion was met by receipts of new savings from the public and 2.2 billion by a reduction in their holdings of Government securities. Nonbank investors, as a group, sold and redeemed bonds, but purchased certificates and bills, reflecting increased popularity of these issues with the rise in rates. Another chart shows how life insurance companies substantially increased their holdings of Government securities during the war and then, in the postwar period, reduced these holdings while increasing their mortgages and other investments.

Sales of Treasury bonds by nonbank investors and by banks in the past year have been largely purchased by the Federal Reserve System.

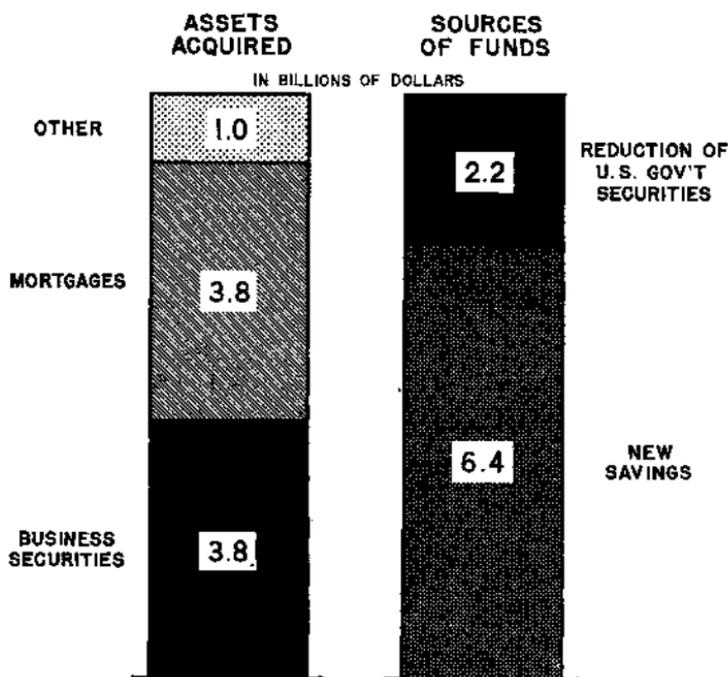
The System purchased 5.7 billion dollars of Treasury bonds in the market and also purchased in the market a net amount of about 2.6 billion dollars of notes and certificates, but sold on balance nearly 4 billion dollars of bills to banks and other investors.

In the same period the Treasury redeemed for cash about 5 billion dollars of maturing issues of various kinds held by the Federal Reserve banks. With all of these wide shifts in holdings of different types of securities, there was only a small net decline in the System's aggregate

CHART 2

SELECTED SAVINGS INSTITUTIONS

JUNE 1947 - JUNE 1948



SALES OF U. S. GOVERNMENT SECURITIES BY SAVINGS INSTITUTIONS HAVE FINANCED ONE-QUARTER OF THEIR NEW PRIVATE INVESTMENTS IN THE PAST YEAR.

holdings of Government securities, although the total fluctuated considerably from time to time. (See p. 3 of chart book.)

The purpose of this detailed survey of figures is to illustrate how shifts in holdings of the public debt are being used to finance inflationary spending, and how Federal Reserve and Treasury policies endeavor to offset these tendencies.

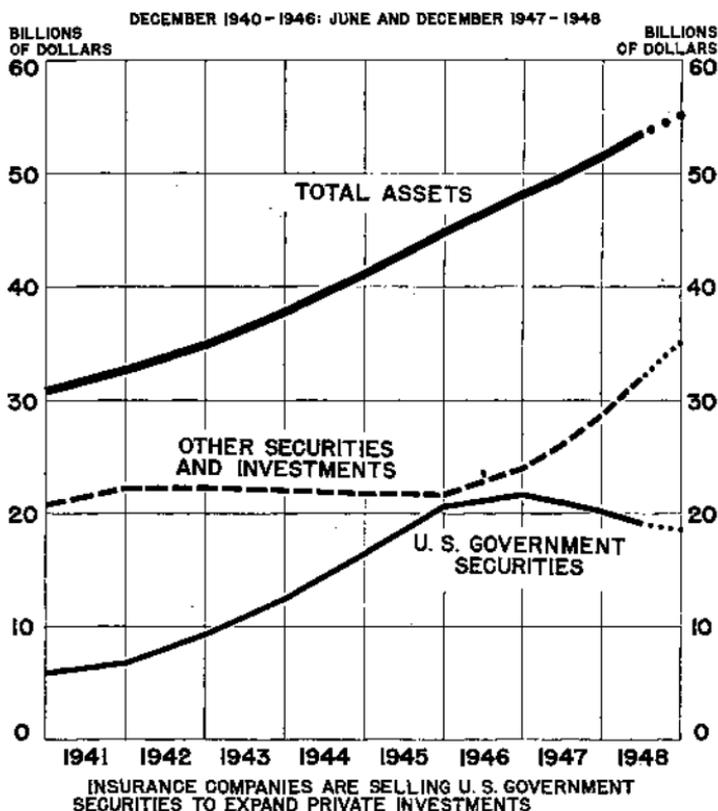
Treasury use of surplus funds to retire securities held by the Federal Reserve drains reserves from banks and makes it necessary for them to sell securities if they wish to maintain their loans, and even more so if they want to expand credit. The higher rate on Treasury bills encourages banks and other holders of liquid funds to buy bills rather than invest in other assets. Since most of the bills have been held

by the Federal Reserve, a reduction in system holdings is made possible and bank reserves are thereby absorbed. Nevertheless, sales of bonds to the Federal Reserve, primarily by nonbank investors, have been so large that the restrictive effect of the other policies has been fully offset.

A third method of restraint used by the Federal Reserve authorities during the past year was to increase reserve requirements at central reserve city banks in New York and Chicago by 2 percent of demand

CHART 3

ASSETS OF LIFE INSURANCE COMPANIES



deposits in February and again in June. This added about a billion dollars to member bank required reserves and immobilized that amount of bank assets. The effects of these changes, however, were concentrated on New York City and Chicago banks, where loan expansion has been less than at other banks. Under existing law there is no further power to increase requirements except in central reserve cities.

It should be mentioned that bank reserves have been supplied in the past year by an inflow of gold amounting to 2.2 billion dollars and also by a decline of about half a billion in currency in circulation.

That is indicated on page 2 of the book of charts.

A temporary increase of 1.3 billion in Treasury deposits at the Federal Reserve offset in part these factors. The total growth in

reserves was 1.4 billion, sufficient to cover the increases in reserve requirements at central reserve city banks and also increased requirements resulting from deposit growth. The Federal Reserve System was not able, through its policies, to prevent some continued expansion of bank credit.

Now we come to prospective demands for credit.

Economic prospects indicate a continuation of strong inflationary pressures during the next several months and perhaps for a much longer period. Individual incomes have continued at a high level, with a tendency to increase as prices and wages have risen and employment has grown with the labor force. Consumer spending, based on current incomes, the use of past savings, and borrowing, also has continued to expand. Construction volumes seem likely to remain for a while at capacity levels, with possible further rises in prices. Business expenditures are also expected to continue in large volume. Government expenditures are increasing, while the recent income-tax reduction will lower receipts, thereby sharply reducing the Treasury surplus.

Continuation of these tendencies will call forth further credit expansion. Borrowing by consumers and home owners will no doubt continue to expand and thereby add to consumer spending and to demands for housing, which are already excessive. Prospective large outlays by business for expansion of inventories and plants will probably exceed internal funds available and also amounts obtained by flotation of new securities. Over-all demands for funds may continue in excess of the current volume of savings readily available for lending for such purposes. To help meet the demands for credit and capital, corporations, individuals, and financial institutions will sell some of their holdings of Government securities and also increase their borrowings from banks.

If these tendencies continue, sales of Government securities by nonbank investors may exceed 1.5 billion in the last half of 1948 and perhaps be much greater early in 1949. These sales will keep the Government bond market under pressure and require support purchases by the Federal Reserve, if the policy of maintaining the 2½-percent yield level on long-term Treasury bonds is continued. Thus additional reserve funds would be made available to banks which, unless otherwise offset, could sustain a further very large inflationary expansion of bank credit. Additional reserves supplied through the gold inflow may be approximately offset by the drain resulting from seasonal currency demands.

To avoid an abundance of reserves, an easy short-term money market, and continued inflationary credit expansion, positive measures to absorb reserves will be needed. In view of the pressure of current demands, the continued shortages of many goods, the limited capacity for increased output, and the available accumulations of liquid assets, further credit expansion will add to the pressure for rising prices. Continued credit expansion will store up trouble for the future and make the inevitable adjustment more dangerous for the stability of the economy.

This course of economic and monetary developments has been the source of increasing concern to the Federal Reserve authorities. We are convinced that, so long as the present situation lasts, it is important to restrict further credit expansion and to promote a psy-

chology of restraint on the part of both borrowers and lenders. To keep the reserve position of banks under pressure and discourage further inflationary credit expansion will require carefully coordinated operating measures on the part of both the Treasury and the Federal Reserve System.

Of the three sets of measures used to restrain the growth of bank reserves during the past year—namely (1) use of the Treasury cash surplus to retire Federal Reserve-held securities, (2) reduction in Federal Reserve holdings of Treasury bills through a rise in short-term rates, and (3) increases in reserve requirements at central reserve city banks—the first and most important has been greatly reduced in its potency and the third has been almost wholly exhausted.

Whereas the Treasury showed an excess of cash income over cash outgo of \$9,000,000,000 in the fiscal year 1947-48, the prospects for the current year, on the basis of very tentative and unofficial estimates, are for a cash surplus of only about three billion, most of which will be concentrated in the first quarter of 1949. This difference in the surplus reduces considerably the most important anti-inflationary influence in the situation during the past year. The Treasury cash surplus was a particularly effective device because it exercised a drain on bank reserves. As a result, the banks losing reserves had to sell securities in order to maintain their reserve positions. While under these pressures they are less likely to be seeking new loans and, in some cases, less willing to meet loan applications.

This brings us to the various ways in which restraint may be exercised over credit expansion.

The first means is voluntary self-restraint on the part of borrowers and lenders. I am convinced that the voluntary program originated and actively developed by the American Bankers Association has had a significant effect in developing a more cautious and critical attitude on the part of bankers toward so-called unproductive or speculative loans. If inflationary pressures were mild, voluntary restraint might be adequate to hold them in check. Continued and intensified voluntary restraint will make our joint task easier.

There are a number of reasons, however, why voluntary restraint cannot be relied upon to do the whole job alone when inflationary pressures are as strong as they are at the present time. Perhaps the most important reason is that a loan which may appear productive when viewed by itself may not add to the total output of the economy as a whole.

For example, a customer may increase his production by borrowing funds to purchase needed parts that are in short supply. Such a loan would appear to be productive from the individual point of view of both the borrower and the lender. But will the loan increase the supply of the parts or total output? If all resources are being used to capacity, the loan may merely enable the borrower to secure parts that otherwise would have been bought by another firm. From the point of view of the economy as a whole, the loan has increased the demand for goods but it may not have increased total supply at all, with a bidding up of prices as the only result. Basically, that is why I believe that self-restraint, though important, is inadequate to check a strong inflationary development.

Another reason is the force of competition not only among banks but among all lenders. We have in the United States 14,000 com-

mercial banks and many thousands of other lending agencies. If, because of concern for the general interest, a bank should refuse to lend even to a good customer, this does not mean that the customer will not secure the funds. It may merely result in a permanent loss of the customer to some other lender. And, unfortunately, the new lender may secure the funds from the sale of Government securities, with the result that the loan may be just as inflationary as if the bank had made it in the first instance.

I want to emphasize that I support strongly the self-restraint program developed by the American Bankers Association and would like to see it pursued aggressively, not only by banks but by all lenders. It is an important step in the right direction. Primarily for the reasons I have mentioned, however, I do not think it can do the job alone.

Another approach to the problem is through control over member bank reserves. Bank credit cannot expand unless banks acquire or have reserves on which to expand. One way in which the System has supplied reserves has been through purchases of long-term Government securities. A means of restraint would be for the System to limit its purchases of such securities either by refusal to buy or by reducing its prices sufficiently to attract other purchasers.

As you know, the System has made a public commitment to support the 2½-percent yield level on long-term Government bonds for the foreseeable future. I gave my reasons for subscribing to that commitment when my confirmation was under consideration by the Senate Committee on Banking and Currency. Although that commitment substantially limits our freedom of action, I believe there is a better way to operate against credit expansion than now to abandon that commitment.

Our basic problem is to absorb reserves. Increases in reserves may be anticipated from three principal sources: (1) Imports of gold; (2) return of currency from circulation; and (3) purchases of Government bonds by the Federal Reserve banks to support the long-term yield level. The principal problem before the System is to absorb or offset reserves arising from these sources. The only way it could do this effectively, under present authority, is to liquidate part of its holdings of Government securities. It would be necessary, of course, to sell them at prices the market would pay.

The System has a large portfolio of bills, certificates, and other short maturities that it could use. If the inflationary demand for bank credit is strong, sale of these holdings to absorb reserves would result in a further stiffening of short-term interest rates. The Open Market Committee of the Federal Reserve System feel that a policy of endeavoring to sell short-term securities in order to absorb any additions to reserves is a necessary and desirable step. If an increase in the short rate should result, it would tend to attract funds from other uses to investment in short-term Government securities. As I have pointed out, the policy of allowing short-term rates to rise was begun about a year ago and has had some success.

At this point the necessity for teamwork between the Treasury and the Federal Reserve becomes apparent. I am keenly sensitive to the necessities of the Treasury in its task of managing the public debt. I thoroughly understand the Treasury's responsibility to keep the interest cost of the debt as low as possible consistent with all relevant factors. I know that the Treasury Department is equally sensitive

to the responsibilities of the Federal Reserve in the field of monetary and credit policy. The problems of mutual concern to the Treasury and the Reserve System in their respective fields are being approached in a continued spirit of cooperation.

The rediscount rate is another instrument of policy in the short-term market. It should not be written off. Although its effectiveness is diminished in times like these when the volume of member bank borrowings is small, and when banks can readily obtain needed funds by selling some of their large holdings of Government securities, higher discount rates would have some restrictive effect. If, for example, the yield on short-term Government rises, it would become appropriate under these circumstances to increase the discount rate. This action would discourage the market from reacquiring through the discount window any funds that had been withdrawn through the disposal by the Reserve System of short-term Governments.

An increase in the discount rate has great psychological effect. Each increase repeats the warning that credit is in need of continued restraint. Changes in the Federal Reserve discount rate and open market operations supplement each other as necessary parts of an over-all credit policy.

These two related instruments influence the total volume of reserves of member banks. The third general instrument—reserve requirements—is designed to influence the amount of bank credit that can be based on a given volume of reserves. An increase in requirements immobilizes reserves, and makes them unavailable for further lending and investing. As you know, the Board of Governors has, on previous occasions, presented various ways of dealing with the problem of reserves or immobilizing certain bank assets.

The method proposed in the bill before you is simple and direct, and involves no departures from existing principles. The bill would authorize the Board of Governors to increase by 10 and 4 percentage points the reserves that member banks may be required to maintain against their demand and time deposits, respectively. The authorization would be granted for a period of 2 years. As I have already explained, we feel deeply that it is not fair to member banks in their competitive relations with nonmember banks to require that they be singled out to carry the additional reserves that may be necessary to combat this inflationary situation. I earnestly hope that Congress will, during this interval, reconsider the whole structure of reserve requirements, possibly along the lines developed recently before the Joint Committee on the Economic Report.

I should like to indicate briefly what can and cannot be accomplished through increases in reserve requirements. Changes in requirements cannot, of course, be considered in isolation. They must be related to other instruments of policy. In practice they are closely related to open market operations. One method that banks use to adjust their positions to the pressure exerted by an increase in requirements is to sell Government securities. This is not the whole story, nor does it happen invariably, but it does illustrate the complexity of our problem. An increase in requirements immobilizes a larger portion of the assets of member banks and makes them unavailable for sale in order to obtain funds to increase loans. It, therefore, reduces the liquidity of banks and lowers the ratio of multiple credit expansion that can occur on the basis of any increase in available reserves.

The purpose of increasing authority over reserve requirements is not to obviate the possible need for open market operations and a rise in short-term rates. That problem would still be with us.

In conclusion, I should like to state emphatically the Board's view that the use of its powers over the supply of reserves under present conditions should be directed toward restraining further credit expansion and not toward forcing liquidation of the outstanding volume of credit. The Federal Reserve System was established to provide for flexibility in our monetary system. It was not designed to make available any amount of money that borrowers might demand without regard to the productive capacity of the economy and the speculative nature of the commitments. The System would be derelict in its duty if it did not exercise a proper measure of restraint.

Expansion of the public debt because of war and the necessity of maintaining a degree of stability in the value of the vast holdings of that debt by financial institutions and individuals has confronted the System with formidable difficulties in the exercise of restraint over credit expansion. The proper handling of this problem requires the most careful management. It can be facilitated by the extension of the System's powers, as proposed in the bill before you, which extension is thoroughly consistent with existing powers and traditional methods.

As I have pointed out, there are possibilities and prospects for a continuation of inflationary pressures which will call forth additional demands for credit. I feel confident that the Federal Reserve authorities will use their existing powers to the fullest extent possible to restrain these tendencies without depriving the economy of the credit needed to maintain production and employment at the highest sustainable levels. We would endeavor to use the additional powers proposed in the same way.

Finally, it should be emphasized as strongly as possible that action in the monetary field alone cannot readjust the unbalanced relationships within the economic structure which have already been created by inflationary forces, and cannot check further inflationary pressures arising from nonmonetary causes.

The additional powers sought would enable the Reserve System to exert a very necessary degree of restraint upon the now unrestrained expansion of credit. For that reason they are urgently needed, even though they are not and should not be regarded by the Congress or by the public generally as a cure-all.

Now, Mr. Chairman, there are two phases of this problem: One is bank credit control and the other is consumer credit control. I have asked Governor Evans of the Federal Reserve Board to come here with me this morning to handle the consumer credit control problem, and I will ask the chairman's pleasure as to which one he would like to have us take up first.

The CHAIRMAN. Let me ask this general question before we proceed further: Could you give us some information on how much the Federal Reserve would raise reserve requirements immediately if you were given the power to do so now?

Mr. McCABE. Mr. Chairman, that would be given very, very careful study after the Congress had passed this measure. I think that we would survey the whole field and determine where there are unbalances existing today.

The CHAIRMAN. Has not the Board, up to the present time, given any consideration to the amount to which it might be necessary to raise reserve requirements to stop the further expansion of credit?

Mr. McCABE. Well, you see, sir, this authority would be used in conjunction with the other authorities which the Board possesses, and I could not give you any idea as to the exact amount of the increase that would be made first.

The CHAIRMAN. You have asked for an increase of almost 40 percent in your authority. Has not the Board given any consideration to the amount to which it might be necessary to raise reserve requirements in the various bank categories?

Mr. McCABE. As it exists today, there is a maximum authority of 26 percent in the central reserve cities, 20 percent in the reserve cities, 14 percent in the outside banks, and 6 percent on time deposits. We would consider each of those segments of the banking system and determine where the increased requirements should apply. We would have no idea on the next day after this is granted of going up to the maximum. It would only be done, sir, with great care, and after studying the excess reserves of the banks in the various areas.

The CHAIRMAN. Why have you not raised the reserve requirements in the central city banks up to 26 percent?

Mr. McCABE. Well, we have made increases of 2 percent in New York and Chicago, at two different times within the last few months. There remains only an additional 2 percent, and the reason we have not as yet gone to that additional 2 percent is because the trend of loans in the New York and Chicago areas is not increasing to the extent to which it is in the outside areas.

The CHAIRMAN. I might say just by way of history that last spring, when the matter of reserves was called to our attention, you will recall that at that time some dispute arose between the Treasury and the Federal Reserve as to whether the primary reserves should be increased, or whether secondary reserves should be adopted, because you had not exhausted all of the power which you had at that time in the central city banks, I do not think, because of those two situations, that we felt that you were pressuring very much for increased bank services. We did not have any hearings. We were not asked for hearings. I think the matter was discussed somewhat before the Joint Committee on the Economic Report mostly in connection with the dispute between the directors and Mr. Snyder with respect to how the job should be done.

As early as last November the President was cognizant of this increase in the volume and velocity of credit, and, to my knowledge, the President has never sent any message to Congress heretofore asking for an increase in the primary reserves.

Mr. McCABE. I think there was a general statement in one of his reports.

Mr. THOMAS. The Economic Report in January.

Mr. McCABE. Dr. Thomas tells me the Economic Report in January pointed out the necessity for curbing.

The CHAIRMAN. That was what the Joint Committee on the Economic Report based its hearings on at the time. We were not asked, as far as I know—and we have never been asked directly—to increase the primary reserves of the banks. What limitation, if any, is there upon your authority to raise rediscount rates?

Mr. McCABE. We can continue to increase the rediscount rates, sir. The borrowings by the banks from the Federal Reserve have been comparatively light—running somewhere in the neighborhood of two to three hundred million dollars, and generally for very short periods, to meet a particular situation for some day or a few days. The effect of increasing the rediscount rate, thus far, has been largely a psychological one and not a realistic one.

The CHAIRMAN. Do you remember last fall, when we were talking about raising rediscount rates, that there was surely a very healthy psychological effect, to the extent that prices started to move downwards? The Federal Reserve did not get around to increase the discount rate until when?

Mr. McCABE. January.

The CHAIRMAN. January?

Mr. McCABE. Yes, sir.

The CHAIRMAN. They raised it from one to one and a quarter?

Mr. McCABE. Yes, sir.

The CHAIRMAN. You have made no increases since then—psychological or otherwise?

Mr. McCABE. No, sir.

The CHAIRMAN. Do you recall why we reduced the reserves from 40 percent and 35 percent to 25 percent in 1945?

Mr. McCABE. You are speaking of the gold reserves now?

The CHAIRMAN. Yes.

Mr. McCABE. I will let Dr. Thomas answer that. You see, I have been Chairman of the Board only since the 15th of April.

The CHAIRMAN. We appreciate that.

Mr. McCABE. On these questions of history of the System, I would prefer to have his assistance.

The CHAIRMAN. That is perfectly all right.

Mr. THOMAS. At that time, in view of the monetary expansion that resulted because of the war—the increased demand for currency particularly, but also the increase in bank deposits and consequent increase in required reserves—the liabilities of the Federal Reserve banks were growing rapidly and approaching the limits of the then established reserve requirements. The Board, therefore, requested that Congress lower the ratio, in view of the possibility that the System would be handicapped in its task of aiding in supplying the money needed for an expanding and abnormal war economy. It was pointed out at the time that the reserve requirements of the Federal Reserve banks in themselves do not place a limit on the demand for credit at the member banks. They only limit the ability of the Federal Reserve System to supply those demands.

The limitations that are placed by the System on the member banks' reserves have not traditionally been based upon the reserve requirements of the Federal Reserve banks. They have been based upon the System's view as to the needs of the economy for money, and not upon the amount of gold that the System happens to hold. Even when the System had close to a hundred percent gold reserves, it did follow a restrictive policy except when it felt that credit was expanding too rapidly. If the gold reserves are low, it might find it necessary to follow an expansionary policy, even when economy needed more money.

The CHAIRMAN. Let us put it very simply so that even we can understand it. When you reduce your gold reserve requirements, you increase the potential volumes of your currency.

Mr. THOMAS. You increase the potential volume of currency that the Federal Reserve could supply if it was requested to supply it.

The CHAIRMAN. That psychology has an inflationary effect, has it not?

Mr. THOMAS. I do not think so. I think the inflationary effect occurs—

The CHAIRMAN. Well, considering the effect which the expansion of currency has upon prices, it would seem to me a reversal of the process might have a healthy psychological effect on prices.

Mr. THOMAS. The reduction of reserve requirements on Federal Reserve banks has nothing to do with the need for borrowing or for money. It may have something to do with the ability of banks to get money. But that depends on what the Federal Reserve does about restricting them. That is the purpose of this legislation at this time, and that is why the Board is before the Congress, to get additional powers to restrict the source of the demand and not simply to put a limitation on the ability of the System to supply it.

The CHAIRMAN. I might mention that through the open market committee you could offset all the practical effects of raising the gold reserve requirements, but if the two were balanced, one against the other, then it surely would have a stabilizing effect, would it not?

Mr. THOMAS. Oh, certainly, if the System could sell Government securities, it could absorb bank reserves and reduce the amount of its liabilities.

The CHAIRMAN. And if they continued to buy Governments, as you say, it would not make any difference what the gold reserves were, if they continued to buy Governments, then they would completely offset all the effect which might otherwise be obtained by increasing the gold reserves, by the buying of Governments. Now, did you reduce the gold reserves in order to give you somewhat more latitude in the support of the Government bond market?

Mr. THOMAS. That was one of the reasons that was stated, and it was stated in the report of this committee in presenting the legislation; that is, it was to enable to Federal Reserve System and the banking system to aid in meeting the wartime demands for money and credit.

The CHAIRMAN. Then, if at the present time, when we are enjoying temporarily, at least, Treasury surpluses, do you not think it might be well to reverse the processes by which we made money cheap, and see what effect it might have on inflationary trends?

Mr. THOMAS. It would not give the system any additional powers to deal with the situation. It would make it necessary for the System at some time in the future, when those limits were reached, to impose restrictions. But I would like to say there that the 40-percent reserve requirements would still leave room for considerable expansion in the amount of bank reserves, and a very substantial expansion in the amount of bank credit that could be based on those reserves, unless the System was able to follow policies which would put restrictions on the banks in making loans.

The CHAIRMAN. Let us get right down to the meat of the situation. Mr. McCabe, do you think that we have to continue to support bond prices, Government bond prices, at par?

Mr. McCABE. Mr. Chairman, I have a very strong conviction that it is vitally necessary to support the 2½-percent bonds.

The CHAIRMAN. Then, you mean by that it is going to be your continued policy—Federal Reserve policy, I mean—to buy Governments in the open market?

Mr. McCABE. I would not say that it is our policy forever. I say for the foreseeable future.

The CHAIRMAN. Let us put it that way, then, for the foreseeable future, it is going to be the policy of the Federal Reserve to buy Governments?

Mr. McCABE. That would be my judgment, sir.

The CHAIRMAN. That is, to support our debt?

Mr. McCABE. That is to support our debt; yes, sir.

The CHAIRMAN. Then, are you saying that it is necessary to continue inflation in order to carry the national debt?

Mr. McCABE. I would not like to put it that way, sir.

The CHAIRMAN. I think that is the problem before the Congress today.

Mr. McCABE. It is a very grave problem that is before the country, sir.

The CHAIRMAN. We realize it.

Mr. McCABE. The thing that we have to consider is the colossal magnitude of this debt—\$250,000,000,000. It is one and a half times all the rest of the debt in the United States put together. When we compare that debt with the debt after World War I—which was something like \$26,000,000,000—the magnitude of the debt is such that no one ever dreamed of any such thing 10 years ago.

The CHAIRMAN. We propounded these questions last spring, and we did not get a very satisfactory answer then. Nobody in the administration then wanted to admit that we would have to continue inflation in order to carry the national debt in accordance with their policies and purposes. But many of us since then have been wondering whether or not it is the administration's feeling that it is necessary to carry the national debt; of course, if it is, I am going to put this question to you: What would be the practical effect of sterilizing a portion of the debt so that it could not be monetized? What effect would that have?

Mr. McCABE. I think that could be considered, sir, but I think the present policy is the more desirable one. I would just like to say, in connection with this supporting of the debt—

The CHAIRMAN. Well, let me ask you this, first: We have been criticized for not being too direct in this approach to inflation. The people are crying for the Congress to do something about high prices. Now, I think we all recognize that there are two or three basic reasons for high prices: One of them is credit expansion, currency expansion. What can we do to stop it?

If we directly sterilize a portion of this debt so that it cannot be monetized, that is the answer. Let us meet that problem directly, and I think this committee and this Congress is prepared to meet it if you will recommend it.

Mr. McCABE. Mr. Chairman, I would like to say this: We are talking about inflation and ways and means to curb inflation. I think we have to start with the various factors that influence inflation. I think we have to start first with the Government's fiscal policy,

because I am convinced, in my own mind, that substantial surpluses—that is, excess receipts over expenditures, by the Government—are one of the strongest factors in combating inflation.

Second, I think—

The CHAIRMAN. Just on that point: Of course, the alternative to high taxes, in order to do that, is to reduce Government expenditures. That is why we are so concerned about reducing Government expenditures.

Mr. McCABE. And, of course, that is a responsibility of the Congress, to determine whether taxes are reduced or expenditures are lowered, but I say from the standpoint of assisting in the management of this public debt, that substantial surpluses, such as we created last year, are a very vital force in the control of inflation.

Secondly, I come to the consumers. I have always regretted that the campaign which was inaugurated some year or so ago, appealing to the consumer to restrain their desire for more merchandise, has not been carried forward. To my mind, if we could get 140,000,000 people to just partially restrain their purchases, we could correct this thing very quickly.

The CHAIRMAN. You were speaking about consumer credit?

Mr. McCABE. I was talking about the voluntary action which was inaugurated some time ago, and which ran for a short period and then was dropped.

When you come to consumer credit, I think controlling consumer credit, such as we suggest here, is a very desirable thing. I do not think it should be considered alone. I think it has to be taken in conjunction with other policies.

In other words, I think we can control inflation in this country if we want to control it. Up to date I have not been convinced that the public generally wants to control inflation enough to pay the price. Paying the price is creating very substantial surpluses in the Treasury with which to pay off this debt. When you have an excess of receipts over expenditures, that causes a great drain on bank reserves. The strongest remedy I could suggest to you gentlemen would be for you to give serious consideration to a program for increasing the difference between receipts and expenditures so that we could have a surplus with which to pay off a substantial portion of this public debt. Now, as to how it is to be accomplished, sir—

The CHAIRMAN. You do not mention the reduction of Government expenditures.

Mr. McCABE. I am not suggesting to you, sir, how you would do it. You can either do it through taxes or you can do it through decrease of expenditures. But I say it is vitally important.

The CHAIRMAN. Let us be realistic about this. We have not met with much encouragement from the administration in our attempts during the last 2 years to reduce Government expenditures. Notwithstanding that, we have reduced them materially, considerably below budget estimates. Now, the President comes along with this same message, as called attention to the other day by Mr. McMillen—that is, the President's program—asking us to give immediate consideration, or next January, 5 months from now, to bills which would increase the estimated Government expenditures so that our total budget would be about \$60,000,000,000 instead of \$40,000,000,000. If we were to absorb those increased expenditures by taxation, we

would have a tax load here that I do not think we in this committee would be quite in favor of.

Mr. McCABE. I am not proposing any method to this committee, because I realize that the gentlemen of this committee know a lot more about how this could be done than I do. I am just saying that, from the standpoint of operating the central bank, we know what a powerful factor that is in curbing inflation.

The CHAIRMAN. Do you believe in increasing excess-profits taxes?

Mr. McCABE. Do I personally believe in increasing them?

The CHAIRMAN. Yes.

Mr. McCABE. I participated for some few years in the activities of the Committee for Economic Development. I think their tax proposals, which many of you gentlemen have seen, are the most constructive proposals which have thus far been made to the Congress. I am thoroughly in accord with the program of the Committee for Economic Development, as it was developed prior to the time that I was appointed to the position I now hold.

The CHAIRMAN. I do not think we are familiar with them enough to say whether they advocated an increase in excess-profits taxes. Do you recall?

Mr. McCABE. If you do not mind, sir, I do not want to get into that particular phase. I know that is a debatable question, and I have problems enough of my own in the central bank without getting involved in that.

The CHAIRMAN. You would rather have us discuss that problem with Mr. Snyder?

Mr. McCABE. Yes, sir.

The CHAIRMAN. Consumer-credit controls were taken off last November 1, I believe, when the Congress rescinded the Executive order under which the regulation had been adopted by the Federal Reserve System. At the time that the regulation was rescinded, they were exercising consumer credit-controls on only 12 commodities. Would you suggest that we take this up with Mr. Evans?

Mr. McCABE. Yes; if you will, sir.

The CHAIRMAN. I would like to bring out this one point in that particular, and see if my facts are approximately correct. When controls came off, Governor Evans, outstanding consumer-credit obligations, I am told, were \$12,055,000,000. Would that be substantially correct?

Mr. EVANS. Do you have this chart before you, Mr. Chairman?

The CHAIRMAN. Yes.

Mr. EVANS. I think that figure is about correct.

The CHAIRMAN. Let us get at it in this way: What were the outstanding credit obligations as of November 1, 1947?

Mr. EVANS. Just about \$13,000,000,000, Mr. Chairman. A little below that, probably.

The CHAIRMAN. The figure I have is \$12,055,000,000.

Mr. EVANS. I expect that is approximately correct.

The CHAIRMAN. How much of that was installment credit?

Mr. EVANS. About half.

The CHAIRMAN. I have the figure of \$5,463,000,000. Would that be substantially correct?

Mr. EVANS. I am just interpolating from the chart here. I cannot gage that quite that accurately, but that would seem about right.

The CHAIRMAN. What is the outstanding credit obligation as of today, or the last figure you have?

Mr. EVANS. \$14,000,000,000. Just a little over.

The CHAIRMAN. \$13,804,000,000; is that about right?

Mr. EVANS. There is a new figure, Mr. Chairman, and that would be a little over \$14,000,000,000.

The CHAIRMAN. So that since last November, when we removed controls on consumer credit, the total volume of credit obligations has increased by about \$2,000,000,000?

Mr. EVANS. Here is a paragraph which might give you that information:

Installment credit outstanding rose—

that is just installment credit, that is the only part that we advocate covering by legislation—

rose 2.3 billion dollars from June 1947, to June 1948—about 15 percent—more than the \$2,000,000,000 increase of the previous 12 months. The rate of advance appeared to be falling off in the first quarter of 1948, but in the second quarter there was a pick-up in activity, and the net gain in outstanding credit was again 15 percent above that of the corresponding period of the previous year.

The CHAIRMAN. I have these figures: As of November 1, the installment-credit volume was \$5,463,000,000; as of now it is about \$7,000,000,000.

Mr. EVANS. That is right.

The CHAIRMAN. The total volume now is, you say, about \$14,000,000,000, and on November 1 it was a little over \$12,000,000,000?

Mr. EVANS. Yes, sir.

The CHAIRMAN. Are you acquainted with the powers granted to the President for the control of credit under the Trading With the Enemy Act?

Mr. EVANS. Only slightly.

The CHAIRMAN. They are not confined to consumer-credit controls, are they?

Mr. EVANS. I would not think so. I think they cover everything.

The CHAIRMAN. They cover quite generally credit obligations?

Mr. EVANS. I think so; yes, sir.

The CHAIRMAN. But the President, in his message, is only asking for the restoration of installment-credit controls; is that correct?

Mr. EVANS. That is right. That is the volatile section of consumer credit. It is the one that goes up and down with most rapidity.

The CHAIRMAN. Can we agree that the population of the United States has increased perhaps 10,000,000 since 1939? Or since 1940, perhaps?

Mr. EVANS. The population? I do not know, Mr. Chairman, what the figures are, but I suppose it has increased.

The CHAIRMAN. We do know that since the 1940 census it has increased substantially?

Mr. EVANS. Yes; the census figures would show that.

The CHAIRMAN. Have you any figures to show the number of family units represented in this credit volume as of today? The figure given here is about 9,000,000. Is that substantially correct?

Mr. EVANS. Forty-nine million is the number of spending units, I think, in the country.

The CHAIRMAN. That is spending units. I mean family units. Let me call your attention to a study made by the University of

Michigan for the Federal Reserve Board. Do you have that before you?

Mr. EVANS. No; but I am fairly familiar with it.

The CHAIRMAN. That is one of the sources of our information. They show that in 1948 there were 9,000,000 family units using installment credit, as compared to between 18,000,000 to 20,000,000 family units just before the war. Less than half of the family units today are using installment credit than were using it before the war, and when we take into consideration the increase in population, percentagewise, that is much less than 50 percent; is it not?

Mr. EVANS. Mr. Chairman, I do not know the figure of 18,000,000, but I do know—

The CHAIRMAN. That is what the University of Michigan study shows, the study having been made for the Federal Reserve Board.

Mr. EVANS. I do not think our study, Mr. Chairman, covered prewar. Our study was to determine the assets at the present time and any changes that have taken place in the three surveys that we have had. I think there is one part of this statement, however, that bears on the point you are bringing out. That is on page 2:

An indication of the increasing frequency of the use of installment credit is given in the consumer's financial survey made by the Board of Governors.

That is the University of Michigan's information obtained by an interview of a selected sample of consumer spending units in the country, each unit being a group of persons in the same family and dwelling who pool incomes to meet major expenses. Data from the survey showed that one of out every four consumer spending units, or approximately 12,000,000 spending units, bought on the installment plan—that is, installment sales credit—in 1947 as compared with a ratio of one out of every seven or eight in 1946. That is just 1 year between the two surveys. You now have one out of four, where you had one out of seven or eight.

The CHAIRMAN. In 1946?

Mr. EVANS. Yes.

The CHAIRMAN. How does that compare with what it was just before the outbreak of war—1940, let us say?

Mr. EVANS. We have no figures on that. The figures were not in operation at that time.

The CHAIRMAN. The figures I have here indicate that.

Mr. EVANS. We just have three surveys, 1946, 1947, and 1945. It has increased, and at a time when you have the largest income among individuals that you have ever had, when you have practically full employment, when you have a scarcity of goods and services. It seems as though, if there ever was a time when people should reduce indebtedness and accumulate savings, it is at the present time.

(Additional statement by Mr. Evans appears at p. 279.)

The CHAIRMAN. One of the objections to consumer credit control came from the veterans groups. The veterans took the attitude generally that they were at a decided disadvantage in acquiring home furnishings, because that was one of the items which was kept under control. And although the Government had made it possible for a veteran to buy a home without any down payment, it made it impossible for him to buy any furniture or fixtures or appliances for the home. A GI coming back from the service was not buying an ice box to replace a refrigerator or to replace an old one. He had to buy everything to furnish that home. It was not a replacement problem with

him. He was starting from scratch. He had to buy his furniture, his rugs, his electrical appliances, his heating appliances, perhaps, and things of that nature; his stove, his refrigerator, his kitchen utensils; he had to buy them all, and it became prohibitive, under those regulations which provided that he should pay 33½ percent down. It was not a replacement problem with him, was it?

Mr. EVANS. Twenty percent down on furniture, I think, and a third on the rest.

The CHAIRMAN. Yes. It became prohibitive. And it was because of that inconsistency that we removed credit controls. They had been removed from all but 12 commodities by the Federal Reserve Board previous to that. I think that you will find that between October of 1946 and November of 1947—November 1, 1946, and November 1, 1947—the volume of installment credit increased \$3,000,000,000, while it was still under controls—not very rigid controls, but the power was there. Yet since November 1, 1947, to the present time they have increased something less than \$2,000,000,000, while not under controls. Why should we put back consumer credit controls under those circumstances?

Mr. EVANS. You did not have very many things available when the war ended. You cannot tell how much they would have purchased at that time, because they could not get them even if they had the money. Now things are becoming more available.

The CHAIRMAN. The war ended in 1945. I am speaking now about the last 2 months in 1946 and all of 1947—almost all of 1947.

Mr. EVANS. Still, many of the durable goods are not in very great supply. But answering your question as a GI, I can only say this to you, Mr. Chairman—that I occupied that position when I returned from the First World War. I had to start out, and I felt at that time—and I would feel today, and I would tell my children or anybody else's children that the best thing for them to do is to pay as much as humanly possible as they go along and not go deeply into debt, not to mortgage their future—and, if necessary, for the time being to do without.

The CHAIRMAN. I think that is fundamental.

Mr. EVANS. I think that is the American way of life.

The CHAIRMAN. The American people, and the American GI, have been led to understand that they could come to the Government and get easy credit with which to buy what are now considered the necessities of life. Are you now asking this Congress to undertake to offset, in this session of Congress, all of the psychological reactions of loose money policies on the buying public that have been going on all these years? Of course, it is impossible.

Mr. EVANS. Mr. Chairman, all I am doing in urging that consumer credit controls be reinstated, in accordance with the bill that was passed by the Senate, and changing the date, is to recommend to this body a measure that, in my judgment, will aid in controlling inflation. And if this country does not control inflation, then you are creating far more problems for the future than you may be able to solve.

The CHAIRMAN. I think we are in hearty accord. All of us heartily agree with that statement. The question is as to how we should do it.

Mr. EVANS. That is right.

The CHAIRMAN. I think we all agree that almost everything which we have been doing, in Government, since 1935, at any rate, and

possibly before that, was to make money and credit easy. I will not attempt to enumerate them, but I think before the committee gets through we will have a substantial list of actions which the Congress and the administration have taken during the last 12 or 15 years to lick a depression and win the war. In the depression they wanted to make credit and money easy. We even went to the extent of authorizing the very unusual monetization of debt. We abandoned the idea of putting up commercial paper as partial security Federal Reserve notes, and thereby adjusting the volume of Federal Reserve notes to business needs. That was criticized at the time as being too inflationary, that it might result in almost uncontrolled inflation. We removed the differential between total debt, the limitation on the total debt, and the bonded debt, thereby bringing debt into such close affiliation with the value of our currency as to make it almost *isop facto* that the debt went up as the value of our dollar went down. We did all of those things to lick a depression and win a war. Now, would not the reversal of those processes lick inflation?

MR. EVANS. Tom, I think that is your question. I mean, we are in agreement on the answer. I do not want any question about that. I do not see how anybody could answer your question without writing a book on the subject. We have to deal with inflation that is here today.

THE CHAIRMAN. I know that. And we dealt with a depression which was here back in the thirties. We dealt with it by increasing the value of the dollar and the value of gold, which, of course, we all recognize, did not do the job now, but it might have had a psychological effect. We did it in these hundreds of other ways. Now, if we made money cheaper—in other words, if we depreciated the value of the American dollar by the action which we took to deliberately do it—why can we not reverse that process and stabilize it? Under judicial management, of course.

MR. McCABE. Mr. Chairman, from my business experience, I have learned that you cannot completely reverse any process in its entirety.

THE CHAIRMAN. You can start a reversal, can you not?

MR. McCABE. What you can do—

THE CHAIRMAN. Can you not start a reversal?

MR. McCABE. I respect the chairman for analyzing those factors in our economy and in our monetary system of the past, to ascertain those things that we could apply to the present. I am in full sympathy with that approach, Mr. Chairman. I think today we are in a situation where we have to appraise every factor. I have pointed out a few of the things that I think we could do to curb inflation. I see that in all directions there is credit expansion. Let us take total consumer credit, of which installment credit is a part. We have increased total consumer credit, if you go back to the year 1939, from \$7,900,000,000 to \$14,000,000,000 today. And it is going up at a rate that I think causes us to pause and look at it; that is, total consumer credit, including installment credit, single payment loans, charge accounts, and all the other things. They are all going up, month by month: In January, from \$13,000,000,000 to \$12,900,000,000 in February, 13.4 billion dollars in March, 13.6 billion dollars in April, 13.8 billion dollars in May, and 14.1 billion in June.

THE CHAIRMAN. Do you actually think that it reduces the demand for consumer goods to put on consumer credit controls?

MR. McCABE. Pardon me? I did not hear that question.

The CHAIRMAN. Do you actually think that to impose consumer credit controls reduces the demand for consumer goods?

Mr. McCABE. I think it would restrain it to some extent.

The CHAIRMAN. Is that not what you do? If we have a shortage of goods—automobiles, for example. Let us take that as an example, because there is surely no surplus of automobiles, and the demand has continued notwithstanding the increased prices.

Mr. McCABE. And the black-market operations.

The CHAIRMAN. The 33½ percent down payment on automobiles did not curtail the demand at all. There was more of a demand than the automobile industry could even reasonably meet, and that demand is continuing notwithstanding that prices have gone up. Now, do you not think, Mr. McCabe, that if you were to put installment credit controls back on—to continue the illustration—automobiles, and say that henceforth a person must put 50 percent down, still the automobile companies could not meet the demand, because the wealthy people—I do not like to distinguish between these two, because I do not want to be charged with demagoguery, but I think it is nevertheless true—the wealthy people have the savings and the income with which to make that down payment, and the poor fellow who is trying to get a little delivery service started cannot meet that 50-percent requirement and get himself a little pick-up truck. Those are very serious consequences with respect to installment credit to which we gave full and complete consideration. I do not like to see us just wave them aside now, and forget all of the arguments used against installment buying, and yield to these pressures at the present time. I think we should have in mind the actual consequences: That we do not necessarily reduce the demand for goods, but we do create gross discriminations between those who have and those who have not.

Mr. McCABE. I think you make a very strong point, sir. I would just say that there would undoubtedly be scores of people who could not raise this down payment if it was increased substantially. I just do not see, though, how you are going to curb inflation unless you are willing to hit it in all directions.

The CHAIRMAN. Well, there have been orthodox ways of controlling it heretofore. Every since 1914 we have controlled the volume of credit by the manipulation of reserve requirements and rediscount rates. I do not know why we have to supplement those with consumer credit controls at the present time, any more than we did before.

Mr. McCABE. I say to you, sir, if it is the wisdom of this Congress that the Federal Reserve Board should not support the Government bond market, then I think Congress should so direct the Federal Reserve. My own feeling is—

The CHAIRMAN. I do not think we are going to direct you not to support the Government bond market. I do not think we are going to direct you to support the Government bond market at a particular figure. It seems to me that there is a golden mean here somewhere, which the Federal Reserve Board should find, with respect to the support of the Government bond market and at the same time give a degree of stability to our economy.

Mr. McCABE. The Federal Reserve has been working with the Treasury in raising the rate on short-term securities, bills, and certificates, and thus attempting to find a market for the short securities which it holds. I think it is only through trial and error and our

ability to try out the different things that the Federal Reserve has tried out to find the combination that will reasonably stop credit expansion; that is, not stop it completely but retard it substantially and without causing a serious catastrophe. You know, I often think—let us go back to the automobile for a moment—that we are riding in an automobile which used to travel at a speed of 30 or 40 miles an hour. We have now got the speed of this old car up to 80 or 90 miles an hour. And we have these controls in front of us, and we have to pull the controls delicately so that we can retard, partially, the speed of the car without throwing it off the road.

The CHAIRMAN. Mr. McCabe and Mr. Evans, would it be convenient for you to be back here at 2:30?

Mr. McCABE. Yes, sir.

The CHAIRMAN. We will recess until 2:30.

(Whereupon, at 12:37 p. m., the committee recessed, to reconvene at 2:30 p. m.)

AFTERNOON SESSION

Present: Messrs. Wolcott, Smith, Talle, Sundstrom, McMillen, Kilburn, Buffett, Hull, Stratton, Scott, Banta, Nicholson, Spence, Brown, Patman, Folger, Buchanan and Multer.

The CHAIRMAN. The committee will come to order.

Mr. McCabe, do you prefer to have Mr. Evans proceed with his statement or do you prefer to have us proceed with our questioning of you?

Mr. McCABE. Either one, sir.

The CHAIRMAN. Possibly it might be advisable to have Mr. Evans read his statement, and then we will proceed with the questioning of both of you.

Mr. McCABE. Very well.

STATEMENT OF R. M. EVANS, GOVERNOR, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Mr. EVANS. The Board of Governors of the Federal Reserve System on several occasions in the past has recommended to the Congress legislation which would authorize the regulation of consumer installment credit. This is the sector of consumer credit which has been subject to wide fluctuations in the past, thereby contributing to instability and unemployment. The Board believes that measures permitting the moderation of these fluctuations, which are tending to increase in size and influence, are an essential part of a program to achieve stable production and employment at maximum levels, a declared national goal of this country.

The Congress has before it at this time a resolution which would restore, insofar as installment credit is concerned, the authority that was exercised from 1941 to 1947 through regulation W. This would be a temporary measure designed to help meet the special inflationary pressures which exist today. The Board's opinion is that, while permanent legislation would be preferable, conditions are such as most urgently to require action and a temporary measure is better than none. To have any real usefulness, however, the authority should be provided for a sufficiently long period so that persons subject to regulation will realize their responsibility and adhere to its provisions.

For this reason, we believe that any legislation on this subject should extend at least until June 30, 1950. During this period, of course, the Board would be able to modify the regulation to meet changing conditions.

Regulation under the proposed legislation would be in much the same form as it was under the Board's regulation W, when that was last in force. It would cover installment credit, not only installment credit for financing the purchase of consumers' durable goods, but also installment credit for other consumer purposes, both of which are inflationary under present conditions. It would prescribe maximum maturities and minimum down payments as did regulation W, but not necessarily at the same levels. The proposed legislation includes provision for more appropriate enforcement machinery than was available under Executive Order No. 8843 which authorized regulation W. Courts of equity would be empowered to aid enforcement by enjoining violations, as provided in legislation dealing with similar matters.

The case for this legislation seems to the Board to be particularly strong in the light of the general conditions which now exist. During the 3 years that have elapsed since VJ-day, the American public has gone into debt more rapidly than in any other period in our history. At the same time consumers in general have been fully employed, have received a record amount of income, and have continued to increase their exceptionally large holdings of liquid assets. The large volume of consumer spending from current incomes, rapid turn-over of accumulated savings, and increased borrowing, accompanied by limits on output of goods and services, have contributed to the upward spiral of prices.

Consumer credit consists of both installment credit and single-payment credit. Wide fluctuations in the total volume of consumer credit over the years have reflected principally changes in installment credit. The importance of these changes is indicated by the chart. The 1942-43 decline in this type of credit accounted for more than 85 percent of the decline in total consumer credit, while the postwar rise in installment credit accounted for 60 percent of the total rise. Other forms of consumer credit fell very little in the early war period and began to increase earlier than installment credit. The greatest growth occurred in 1946, and in recent months a tendency to level out has appeared. Installment credit, on the other hand, has continued upward.

Installment credit outstanding rose 2.3 billion dollars from June 1947 to June 1948, about 15 percent more than the \$2,000,000,000 increase of the previous 12 months. The rate of advance appeared to be falling off in the first quarter of 1948, but in the second quarter there was a pick-up in activity and the net gain in outstanding credit was again 15 percent above that of the corresponding period of the previous year.

An indication of the increasing frequency of the use of installment credit is given in the Consumer Finances Survey made for the Board of Governors. The information was obtained by interview of a selected sample of consumer spending units in the country, each unit being a group of persons in the same family and dwelling who pool incomes to meet major expenses. Data from the survey show that 1 out of every 4 consumer spending units, or approximately 12,000,000 spending

units, bought on the installment plan (installment sale credit) in 1947 as compared with a ratio of 1 out of every 7 or 8 in 1946. Installment loans at banks, loan companies, credit unions, and other such agencies were obtained by 15 percent of all consumer spending units in 1947 (7,000,000 spending units) as compared with 13 percent in the preceding year. There was some evidence to indicate that the new users of such credit were concentrated in the middle and upper income classes, principally those with incomes of above \$3,000 a year.

Reports on installment buying terms throughout the country indicate that when regulation W was terminated many credit grantors adopted credit policies that were considerably less restrictive than those required by the regulation but somewhat more restrictive than those prevailing before the war. In recent months there has been a further relaxation in the down payment and maturity requirements in installment credits for practically all categories of durable goods. Competition has been the primary factor leading to lower down payments and longer maturities; when one important retail outlet in a community relaxed terms, other stores soon felt that it was necessary to follow.

The prospect for the balance of this year is for increased use of consumer installment credit, further reduction in down payments, and lengthening of maturities. Together with the seasonal rise in the use of installment credit during the late months of the year, these factors suggest a growth exceeding that which occurred in the first 6 months.

The increase in installment credit this year is of special significance because it is taking place notwithstanding the fact that the output of consumers' durable goods is no longer growing. With a rise of 85 percent in durable goods in 1946, there was an increase of 65 percent in installment credit. In 1947 the percentage increase in installment credit of 55 percent accompanied a growth of but one-third in durable goods.

Gradually the increases in credit have outstripped the expansions in the output of goods. By the middle of 1947, durable goods production had stabilized at a level that has been maintained up to the present time. Yet installment credit continued to rise—one billion dollars for the first 6 months of 1948 and more in prospect.

In view of the current tight situation in supplies of labor and materials, further expansion of installment credit can neither increase output nor put more people to work. It can only add more purchasing power to the already swollen spending stream and reinforce inflationary pressures. International developments, moreover, inevitably add pressures in the markets for consumers' durable goods.

Because more purchasing power is being added to a supply of funds already excessive in relation to available goods, expansion of installment credit under present conditions is of an inflationary character irrespective of its relative level as compared, for example, with national income. While credit outstanding now amounts to no more than 3.9 percent of annual disposable income in the United States, as compared with a range of 5.5 percent to 7.1 percent in the years just preceding the war—the highest levels on record—conditions today are much different. In the year 1940, for example, when the percentage was at its peak, average unemployment was 14.5 percent of the total labor force, according to the Bureau of Census estimates,

as compared with 3.5 percent in 1947. In other words, there is no slack today. More credit cannot call forth more goods—it can only add to the upward pressure on prices.

It should be noted that the Board's position on regulation of installment credit is not to be taken as in any way indicating a feeling that all installment credit is undesirable. The problem is to prevent the abuse—not the use—of credit. A damping of disruptive fluctuations is what we are interested in, and more stability at levels related to the conditions of the time.

Since the end of regulation W, a number of trade associations of credit grantors have urged their members to exercise caution in liberalizing terms and expanding portfolios. Such efforts have undoubtedly had some effect in moderating the increase in installment debt. These voluntary efforts, however, have not succeeded in preventing gradual reduction in the down payments and lengthening of the maturities advertised by credit grantors. Easy terms are rapidly approaching those which were offered before the war.

Now is the time when it is in the best interest of all consumers to save more and spend less. This is the time to reduce—not to increase—debt. This is a time for restraint—voluntary, yes, but reinforced, much as we all dislike compulsions, so far as necessary to protect the real interests of all of us.

Finally, the Board has asked me to reiterate as strongly as possible that regulation of installment credit is a tool—but only a supplementary tool—for dealing with the problem of inflationary credit. By itself it cannot do the job. To be adequately effective, it must be buttressed by the basic bank-credit controls which the Board has advocated repeatedly, beginning with its 1945 annual report to Congress.

The CHAIRMAN. What is the procedure whereby a person gets credit for the purchase of consumer goods? Whence does the money come which the processor, the distributor and the manufacturer get?

Mr. EVANS. Do you mean how does the man who made the machine get paid for it?

The CHAIRMAN. Yes.

Mr. EVANS. I suppose the person who granted the credit would either have funds of their own or they would have borrowed funds to enable them to pay for the goods that they sold on installment terms.

The CHAIRMAN. It usually comes from the banks, does it not?

Mr. EVANS. Well, it comes from the banks—some of them I guess get them from other sources. There are finance companies which handle that type of business.

Mr. NICHOLSON. Mr. Chairman, may I ask a question?

The CHAIRMAN. Mr. Nicholson.

Mr. NICHOLSON. You say in your next to last paragraph, "Now is the time when it is in the best interests of all consumers to save more and spend less." Why has that not always been true in this country, not just now?

Mr. EVANS. Well, it is good advice at any time. At this particular time prices are so greatly inflated, at this particular time when everybody is fully employed at wages unprecedented, at least in my lifetime, it looks as though it is a time to dispose of debt, pay it off, and accumulate reserves for any contingencies which might arise.

Mr. NICHOLSON. Well, that has always been so, has it not, in our country?

Mr. EVANS. It is always good sound advice, but it is particularly so at this time when we have these inflationary pressures coupled with the other events I mentioned.

Mr. NICHOLSON. Why have we arrived at this time? There must be something leading up to it. Was it war?

Mr. EVANS. Well the war, of course—

Mr. NICHOLSON. Was it, as Dr. Smith points out, the New Deal, or what was it?

Mr. EVANS. The war is primarily responsible for the present conditions.

Mr. NICHOLSON. Do you think, then—

Mr. EVANS. Shortages of goods and so on.

Mr. NICHOLSON. Do you know how much corn sold for in 1938?

Mr. EVANS. Well, I sold—

Mr. NICHOLSON. That is a basic commodity, is it not?

Mr. EVANS. I sold quite a little along about that time.

Mr. NICHOLSON. You ought to know, then.

Mr. EVANS. That is 10 years ago. I have forgotten for sure, but I think it was around 75 cents. Something like that.

Mr. NICHOLSON. Now what is it selling for?

Mr. EVANS. At the same place it is selling for right at \$2. Pretty close to \$2.

Mr. NICHOLSON. That is all, Mr. Chairman.

Mr. EVANS. But that will not last.

Mr. NICHOLSON. You mean it will go higher?

Mr. EVANS. It will go lower.

The CHAIRMAN. Mr. Evans, or Mr. McCabe, what I was getting at was the powers which the Federal Reserve banks and the Board of Governors of the Federal Reserve System have now to control the volume of consumer credit at the source, which we can assume to be the bank. How could you control that credit at the source now?

Mr. McCABE. That, Mr. Chairman, is what I was discussing this morning. Ways and means for that. We were asking for specific legislation which might curb the further expansion of credit.

The CHAIRMAN. Let me put the question in such a way as to bring out the point. Could you not, under the authority which you now have in the Federal Reserve Act—and I am referring specifically to paragraph 8 of section 4—to provide that no more than a certain percentage of a bank's capital reserve can be invested in consumer paper? I think in order to be fair with you—and I want to be fair with you—I will read the law and see if perhaps we cannot approach this a little differently.

Mr. BUCHANAN. Is this the Trading With the Enemy Act?

The CHAIRMAN. This is the Federal Reserve Act. Do you have this before you?

Mr. McCABE. Yes, sir. This covers the question of rediscounting. The Federal Reserve, of course, has the power to rediscout any paper which they bring there, and could refuse to rediscout if the collateral was not good. But I see nothing in this section, sir, which empowers the Board of Governors to restrict consumer credit.

The CHAIRMAN. Let us review it. First, here, speaking of the Federal Reserve Banks:

Said board of directors shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and may, subject to the provisions of law and the orders of the Board of

Governors of the Federal Reserve System, extend to each member bank such discounts, advancements, and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks, the maintenance of sound credit conditions, and the accommodation of commerce, industry, and agriculture.

The next section is what I particularly have in mind:

The Board of Governors of the Federal Reserve System may prescribe regulations further defining within the limitations of this Act the conditions under which discounts, advancements, and the accommodations may be extended to member banks. Each Federal Reserve bank shall keep itself informed of the general character and amount of the loans and investments of its member banks with a view to ascertaining whether undue use is being made of bank credit for the speculative carrying of or trading in securities, real estate, or commodities, or for any other purpose inconsistent with the maintenance of sound credit conditions; and, in determining whether to grant or refuse advances, rediscounts, or other credit accommodations, the Federal Reserve bank shall give consideration to such information. The chairman of the Federal Reserve bank shall report to the Board of Governors of the Federal Reserve System any such undue use of bank credit by any member bank, together with his recommendation. Whenever, in the judgment of the Board of Governors of the Federal Reserve System, any member bank is making such undue use of bank credit, the Board may, in its discretion, after reasonable notice and an opportunity for a hearing, suspend such bank from the use of the credit facilities of the Federal Reserve System and may terminate such suspension or may renew it from time to time.

Now, what prevents the Federal Reserve System, under that authority, from writing formulas and standards for the expansion or contraction of credit in any field, among the member banks, and enforce it by prohibiting the member banks from using the credit of the Federal Reserve System?

Mr. McCABE. Well, I would like to answer the question first from a practical standpoint, since this refers to rediscounts. As I said this morning, the great bulk of the banks do not have to rediscount today, because they have sufficient Government bonds of which they can dispose without rediscount. There is only a relatively small number of banks that are rediscount banks.

The figure that I have in mind, which is the last figure, is to the effect that rediscounts ran in the neighborhood of \$300,000,000 for all the banks of the Federal Reserve System. So that from a practical standpoint they are not rediscounting.

Now, as to the power of the Board to single out a single type of paper, and to prohibit the banks from loaning on that paper, that, of course, is something on which I would have to consult with our lawyers.

The CHAIRMAN. When you invoke regulation W, you tell the people that they shall not get credit in particular fields. What difference is there between that and telling the banks that they shall not make credit available in those same fields?

Mr. EVANS. Not that they shall not get credit, Mr. Chairman, but that they shall not get loose credit.

The CHAIRMAN. Why would you not, as a matter of standards, require that the same limitations be placed upon the granting of bank credit for consumer sales to which an individual is limited?

Mr. EVANS. The individual, of course, is not shut off from credit under this installment credit proposal.

The CHAIRMAN. All right. Let us take that example. By way of example, you tell the public that they shall not buy an automobile unless they put up fifty percent of the price.

Mr. EVANS. Well, one-third was the greatest it ever was.

The CHAIRMAN. Well, let us say for example that is 50 percent. And that they shall amortize the balance over 12 or 15 months' time. Could you not just as well say to the banks that they could not or shall not extend credit or buy any paper incident to financing consumer sales, unless at least 33½ of 50 percent of it is paid down and the balance amortized over the same period of time?

Mr. EVANS. Well, in the first place, Mr. Chairman, as long as the banks have around \$60,000,000,000 worth of Government securities which they can cash at their option, that condition just is not going to come up to the Federal Reserve Board.

The CHAIRMAN. Well, they would have to sell some of their Government securities to raise the money, then?

Mr. EVANS. Yes, sir; and that is what they do.

The CHAIRMAN. Otherwise they would not be able to use credit facilities of the Federal Reserve System. Do you think the member banks want to put themselves in a position where they are going to be denied, for any infraction of regulations, the credit facilities of the Federal Reserve? Of course, they do not know how long it is going to be before they would have to use the credit facilities of the Federal Reserve. That is about the only reason they are in the Federal Reserve in the first place; is it not?

Mr. EVANS. Well, that is one of the reasons. There are many others. It would take a long, long time before the banks sold their \$60,000,000,000 of Government securities.

The CHAIRMAN. What I was driving at was whether the Federal Reserve and the administration have utilized all the powers they now have to curb credit and whether they should be given any new and unused powers to curb credit if they have not already used the powers they have. You admit that this power is a power to restrict, or could be used to restrict credit.

Mr. McCABE. There is no question about that, Mr. Chairman.

The CHAIRMAN. It has never been used; has it? Has the power ever been used?

Mr. McCABE. This power to restrict credit in a specific field?

The CHAIRMAN. Yes.

Mr. McCABE. By the Federal Reserve?

The CHAIRMAN. Yes.

Mr. McCABE. Not in my memory, sir.

The CHAIRMAN. Nor in mine.

Mr. McCABE. Of course, mine is short in the system.

The CHAIRMAN. Here it states "extraordinary circumstances" and that was written into the law for some reason.

Mr. McCABE. This law, however, refers specifically to individual banks and how they will be dealt with, instead of banks as a group.

The CHAIRMAN. Yes, but the individual is the one who violates the standards. I am talking about standards which you could set up for the guidance of all banks, and then if any individual bank violates the standards, of course, you would apply the sanctions in the law against that individual bank.

Mr. McCABE. I think without a specific mandate from the Congress, Mr. Chairman, to single out—

The CHAIRMAN. You have the mandate from the Congress.

Mr. McCABE. I say, to single out a specific type of business, and attempt to control that through this mechanism which has been suggested here, I think the Board would have to give that extraordinary consideration first.

The CHAIRMAN. Let me read this again to you:

Whenever in the judgment of the Board of Governors of the Federal Reserve System any member bank is making such undue use of bank credit—

Now, the undue use of the bank credit, of course, would be the use of bank credit in violation of the standards which the directors of the bank or the board set up. That would be an undue use of bank credit?

Mr. McCABE. That is right.

The CHAIRMAN. Then you would apply these sanctions. If that means anything, it means that they shall operate in accordance with standards and rules and so forth, which you set up, and if they do not do so, then it will follow, as it naturally should, that they are making undue use of that bank credit, and should be penalized and the sanctions of the law invoked.

Mr. McCABE. It says here when we are extending credit to an individual bank. Then it seems to me that we are dealing with individual banks that come up to the Federal Reserve for credit, and not dealing with banks as a group.

Then you have to consider the point that I brought out in my statement this morning. If this individual bank refuses this type of credit to that customer or this customer, then they will go to the insurance companies, or they will go to other sources of credit.

I would like to repeat that it would be futile for the Board to attempt to regulate consumer installment credit through its control over the borrowings of member banks from the Federal Reserve banks.

In the first place, member banks, as I have said before, are not borrowing in any appreciable amount and are not likely to have to borrow. They can get all the funds they want by selling Government securities in the open market. They could simply ignore any standards we might prescribe under the provision you suggest, since they would not have to come to us to borrow.

In the second place, even if it were possible to make such a control effective as to member banks—which it isn't—it would still be practically meaningless because it would simply drive the business away from member banks to others—such as sales finance companies, non-member banks, loan companies and the like—who would be eager to take over the business. Control over member banks could not exercise any effective control over those other credit institutions.

Finally the purpose of specific regulation of consumer credit, like that of stock-market credit, is to restrain by direct measures expansion of a particular type of credit that by its nature is subject to wide fluctuations with widespread effects on the economy in general. To attempt to restrain these types of credit by general measures of control over bank reserves would impose restrictions on other types of credit that are less subject to excessive fluctuations.

The only way to control consumer credit is by authorizing a control like regulation W which can apply directly to the sellers and lenders that generate the credit.

The CHAIRMAN. Let us take that as an example. I have, let us say, a thousand dollars. There is a restriction against my buying an

automobile, but there is no restriction against my buying a house. I want both an automobile and a house. I borrow the money with which to pay for the house, but buy the automobile with it. I take the money that I would have paid for the automobile and buy the house with it. That is what we have under regulation W constantly. You would merely take it out of your left pocket and put it in your right pocket. How are you going to avoid that?

Let us take another example—and you cannot get away from this: Here is a man who has \$500 and who wants to buy an automobile. He has a wife in the hospital. He has to get her out of the hospital. It costs him \$500 to do it. He can go to the bank to borrow the \$500 to pay his hospital bill. He cannot go to the bank to borrow the \$500 to make a down payment on a car.

Mr. EVANS. That is right.

The CHAIRMAN. So he goes to the bank, he has the \$500, and instead of using it to pay the hospital bill he goes to the bank and borrows the \$500 to pay the hospital bill, and takes the \$500 and makes a down payment on the car. How do you restrict consumer credit in that way?

Mr. EVANS. You do not restrict that fellow at all, because he is making the full down payment, as I understand it, on the automobile.

The CHAIRMAN. Yes, sir; but he is getting his credit indirectly from the bank.

Mr. EVANS. Well, or directly.

The CHAIRMAN. He is making a loan of five hundred to pay his hospital bill.

Mr. EVANS. That is right.

The CHAIRMAN. When he otherwise could use the \$500 which he has saved up to buy his automobile with. You do not have any control over the use of the money after the loan has once been made?

Mr. EVANS. No, sir.

The CHAIRMAN. You cannot follow that cash to see whether it is actually used for that purpose or not. That is the point, and the reason why consumer credit controls have never worked and probably never will work.

Mr. EVANS. Of course, you are assuming that this fellow would take the \$500 and buy the automobile and borrow \$500 for the operation. I think it would be just as reasonable to assume that the man would avoid going into debt and use the \$500 to pay for the operation, and wait until his savings were of sufficient size so that he could make the down payment on an automobile.

The CHAIRMAN. Mr. EVANS, if everybody took that attitude, there would not be any reason why we should put controls on consumer credit. Nobody would buy anything until they had the cash to pay for it. The reason you are asking for these controls is because there are millions of people in the United States who want refrigerators, and who do not have the two or three hundred dollars to pay for them, but they have \$50 with which to make a down payment and reasonable assurance that they are going to have sufficient income to pay the remainder later on. That is the way business has been done in America for generations.

Mr. EVANS. Well, installment credit, of course, has its part to play in the whole American economy, just as other credit has its part to play. It is important, it is valuable, and it is worth while, just as

long as it is soundly administered. But it certainly would not be a good thing for a government, or anybody else, to encourage people to mortgage their future earning capacity by going head over heels in debt to purchase something at a time like this, when prices are certainly high and inflationary pressures are as great as they are.

That is, if we want to moderate the forces of this inflation, then we must make some of the sacrifices as a people that are required to accomplish that end.

It is not going to be accomplished in any other way. I just do not believe there is any easy way out of it.

The CHAIRMAN. I do not like to reiterate what I said this morning, of course, but I think the complete answer to what you have just said there is that you create a situation where you discriminate between the fellow who really needs these things and the fellow who perhaps does not need them.

Mr. EVANS. Then you should give priority, Mr. Chairman, because you cannot increase the number of automobiles.

The CHAIRMAN. Then I hope you will not advocate this: The next step beyond priorities is to subsidize the fellow who cannot pay the price for it.

Mr. EVANS. No; I did not advocate that, but I said that if you want to take the automobiles and distribute them according to the need of the individuals, then credit will not be a mechanism through which, Mr. Chairman, you can accomplish that result.

The CHAIRMAN. You know we cannot do that.

Mr. EVANS. I know you cannot, yes, sir; and I do not think you should.

The CHAIRMAN. I am very much concerned—

Mr. EVANS. But what we are interested in doing—

The CHAIRMAN. You say this is easy credit. Now here is the GI. He can get a house without paying a cent down. He can buy a brand new house without paying a cent down. Then we tell him he cannot furnish the house because you have put consumer credit controls on all his furnishings and appliances.

Mr. EVANS. Well, he only has to pay 20 percent down, Mr. Chairman. If he is in the position where he cannot make that 20-percent payment—

The CHAIRMAN. Twenty percent down on a whole houseful of things which you had under control means an awful lot to the GI who is establishing a home for himself.

Mr. EVANS. Yes, sir, Mr. Chairman, but—

The CHAIRMAN. It does not mean very much to you and me who were here during the war, and when the refrigerator wears out it is just one item and we replace it. A GI has bought himself a home and has to furnish it entirely. It is quite a hardship when he is buying a couple of thousand dollars worth of stuff.

Mr. EVANS. But on the first of every month, Mr. Chairman, that GI will have to meet the installment payments.

The CHAIRMAN. That is right, if he has a good job he can. But he has not been able to save enough to make his down payments.

Mr. EVANS. If he has not been able to save the down payments, how is he going to save enough to pay the installments?

The CHAIRMAN. Because he has not been here. He was away at war. That is the point. The fellow working at high wages in the

factories during the war accumulating bonds, accumulating savings, he can go down there and meet these commitments. He can make these 33½ percent down payments, out of savings. Out of his bonds. A GI coming back here has not been able to save that money. That is the point and that is why we removed these controls to begin with. That was where there was discrimination and we are going to hesitate to put them back on unless you can make out a better case for them than you have made up to the present time.

Mr. EVANS. There is only one reason why the Congress should put them back, Mr. Chairman, and that is that they are one of the tools that will aid in combating inflation.

The CHAIRMAN. Mr. Evans, would you tell me that the Federal Reserve Board would apply these controls right across the board on all consumer credit?

Mr. EVANS. No, sir.

The CHAIRMAN. No.

Mr. EVANS. They would be applied just about the way they were applied.

The CHAIRMAN. Selective, the way you did it before?

Mr. EVANS. Yes, sir.

The CHAIRMAN. And the Board is going to determine what items shall be selected?

Mr. EVANS. Under this law.

The CHAIRMAN. What items are going to be in greater demand?

Mr. EVANS. Well, just take the statistics on the situation. It is not so difficult to determine.

The CHAIRMAN. Let me call your attention to the fact that last November, last December, when you asked for restoration of these controls, the Board came down here and asked us to restore these controls for the reason that consumer credit had increased \$3,000,000,000 the year before that, and that \$3,000,000,000 increase had been when you had the controls on, and you did not exercise them. But you used the fact that consumer credit had expanded by \$3,000,000,000 in the first 11 months of 1947 as a justification for reimposing the controls when you had the power at that time and you did not control the situation. You had selective controls which were highly discriminatory. It did not work, and it will not work now any more than it did then.

Mr. EVANS. Mr. Chairman, if you will look at that chart which is attached to my statement, and if you will take a look at that line marked "Installment credit," I think you will get the answer to your question. You can see how they have gone up and are continuing to go up.

The CHAIRMAN. Of course they have gone up. The total volume of sales has gone up. The dollar volume of sales has gone up tremendously.

Mr. EVANS. That is right.

The CHAIRMAN. It is expected that credit incident to those sales would go up proportionately. I do not want to take up too much time, however.

Mr. Brown.

Mr. BROWN. Mr. Witness, I believe you stated this morning that the banks had sold something like \$25,000,000,000 worth of Government securities; is that right?

Mr. McCABE. That much has been retired; yes, sir.

Mr. BROWN. Of course, you would like to prevent just as much as possible the banks selling their Government securities, would you not?

Mr. McCABE. I did not get the end of your question, sir.

Mr. BROWN. You would like some way to stop the banks from selling Government securities. In that event you have to buy them yourself; is that not correct?

Mr. McCABE. What we would like is—yes, sir, a more stabilized condition in the whole Government market.

Mr. BROWN. Of course, when the banks sell them you have to buy them, and you cannot purchase all of them.

Mr. McCABE. We have not bought them all; no, sir.

Mr. BROWN. I know, but if they are offered for sale, under the law you have to take them if they cannot sell them to anyone else.

Mr. McCABE. Not under the law; no, sir.

Mr. BROWN. Why do you buy them then?

Mr. McCABE. We are acting to stabilize the market, because we feel that is our obligation to stabilize the market.

Mr. BROWN. I am getting back to that point. I think you should give some study to the other side of this question. If a bank wants to loan money and you are going to increase their reserves, you know full well that they are going to sell these securities in order to get money to loan to their customers. That is the other side of the case.

Mr. McCABE. Yes, sir.

Mr. BROWN. Do you not agree with me on that?

Mr. McCABE. Yes, sir.

Mr. BROWN. Well, I would like to have that developed. I would like to hear you on this point.

Mr. McCABE. First of all, the securities might go down, Mr. Brown, if the Federal Reserve did not support that market. I think it is quite likely that they might. If we put this provision into effect, and we should increase the reserve requirements, the bank then will, one, either sell its Government bonds, as you suggest, or scrutinize its loan account and decide that there are certain types of marginal loans that it has which it might call. It might get some of its funds with which to meet this increased reserve from a lightening of its loan account or from the sale of its Government securities or bonds. We feel, in this situation we are in, that it is highly desirable to restrict the further expansion of bank credit. Otherwise we think it might just add fuel to the flame.

Mr. BROWN. Another thing, there are a lot of small banks in this country which are not making very much money. The operation cost has increased considerably. These banks would like to hold their securities, but in order to accommodate and make loans to their customers they will be forced to sell much of their securities. Their customers have not wanted so much money in recent years, but they do now, and these banks have always supplied their customers, and I think you will find that if you raise the reserves, these small banks might sell all the United States securities they have.

Mr. McCABE. I think they will sell their securities to meet their reserve requirements to a considerable extent.

Mr. BROWN. The public is not now buying Government securities.

Mr. McCABE. Not to a great extent; no, sir.

It comes right down to this, sir: If we are vitally interested in curbing this inflationary spiral, we have to take action in certain directions, and you cannot curb inflation, to our minds, unless you give us this additional authority.

Mr. BROWN. I think you are right; I think we should curb it. But at the same time we want to carry out our promise to the people who purchased Government securities.

Mr. McCABE. That is right.

Mr. BROWN. We want to keep them stable.

Mr. McCABE. That is right.

Mr. NICHOLSON. Would you yield, Mr. Brown?

Mr. BROWN. I yield.

Mr. NICHOLSON. Every bank statement that I have read in the last few years, whether it was a savings bank, or a trust company, or a national bank, indicated that they had 60 percent of their assets in Government bonds. Will you tell me how they can reconvert them? If I go in and say, "I want my hundred dollars back," what are they going to give me, a Government bond? They cannot give me the money, can they?

Mr. McCABE. The bank?

Mr. NICHOLSON. If 60 percent of their assets are in Government bonds, they have to give me a bond.

Mr. McCABE. Thank goodness today they can give you your money.

Mr. NICHOLSON. Well, we have faith in our Government, that is why. Otherwise it would be a pretty serious situation, would it not?

Mr. McCABE. And sir, I think we are in a wonderful situation—that is a wonderful situation from the standpoint of your going into that bank to get your money—when you consider as a result of handling this \$250,000,000,000 portfolio of Government bonds that we have as much stability as we have in the Government bond market. I think it is perfectly wonderful. Some of us have memories that go back to World War I.

Mr. NICHOLSON. But what you want to do, as I understand it, is to stop people from borrowing what money there is there, to buy the things that they think they need. Or am I wrong about that?

Mr. McCABE. Well, sir, what we are attempting to do here is to restrict the further extension of credit in a great many of what we feel are not vital needs.

Mr. NICHOLSON. Well, they have only about 40 percent of the money that we put there, to lend.

Mr. McCABE. May I explain to you, sir, that in the expansion of loans today, through the banks, the chief expansion has taken place in consumer loans and in real estate loans. A smaller expansion has taken place in so-called commercial loans.

Mr. NICHOLSON. Well, they do not do that in national banks, do they—make mortgages? I supposed they did that in savings banks and cooperative banks and such as those. They have to put up collateral in a national bank or trust company.

Mr. McCABE. National banks have the authority of extending real estate loans. Generally we are noticing that the greatest expansion today is in real estate loans and consumer loans and there is a big question as to the extent that should go on, because most of us who

have memories that go back to 1929 remember what happened in the banks when they were overloaded with real estate loans.

Mr. NICHOLSON. Well, we have been overloaded now for some time, ever since 1932, and we passed more laws to overload them and now we say, "This is the time." The time was in 1932 and not in 1948. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Brown.

Mr. BROWN. This bill would apply to nonmember banks, too?

Mr. McCABE. That is right.

Mr. NICHOLSON. Well, I think we had a bill here that would make everybody come under the same provisions, did we not, a short time ago?

Mr. McCABE. The bill you have here is confined to the members of the Federal Reserve System.

Mr. NICHOLSON. You can force other people to come in.

Mr. BROWN. Mr. Chairman, do I have the witness or does Mr. Nicholson?

Mr. NICHOLSON. Excuse me, Mr. Brown.

Mr. McCABE. Mr. Chairman, there is just one point I would like to make at this particular part of the hearing. Being comparatively new in the position that I am in, I want my view toward this distinctly understood. I am not looking for unnecessary authority. There is nothing in my philosophy as a businessman, or my upbringing, that makes me want any sort of a planned economy in the United States. I think that most of my background is like that of most of you. In coming in here, we see a condition, this inflationary condition, which exists in this country, and we are trying to find out what we can do to retard this inflationary spiral. We are counseling with you. We have made suggestions as to how we think we can best do that. I would like to make that absolutely clear, because so far as I personally am concerned, I do not want to see any undue authority or any steps taken that will be abnormally curbing any worth-while economic force in this country.

Mr. NICHOLSON. Mr. Chairman, I am not trying to find any fault with you. All I am trying to do is to find out what I am doing.

Mr. McCABE. I have appraised this thing as honestly as I could. I think that on the question of consumer controls that that alone will not do this job. I think perhaps it would be a mistake for you to grant that authority to the Federal Reserve, if that is the only one, just that one thing alone.

I think consumer-credit control, though, with a bank-credit control, the two things in unison, would enable us to do a creditable job.

Now, coming back to the question of the nonmember banks. The only question—and the real question—in our minds is this: On the one hand, you have these members of the Federal Reserve; on the other, you have a little larger number of nonmembers. If Congress enacts this bill and gives us authority to put on the extra reserves on the member banks, we feel it desirable to have that same provision apply to the nonmember banks. Otherwise, from a competitive position, you put the member banks at a distinct disadvantage. It is as simple as that.

The CHAIRMAN. Mr. McCabe, I intended to ask you this morning, is your legal staff satisfied that Congress has the authority to authorize you to impose these requirements on nonmember banks?

Mr. McCABE. They think so.

Mr. BROWN. Do you mean State banks?

Mr. McCABE. State member banks.

Mr. BROWN. Or nonmember State banks?

Mr. McCABE. Nonmember State banks, I beg your pardon.

Mr. BROWN. I do not see how you could do that. I think you better have your counsel look into that again.

Mr. McCABE. Of course, that has been under consideration before, in the recommendations that the Board has made to the Congress, and there is not much doubt.

Mr. BROWN. I think it will be a long time before you are able to put all the State banks under the Federal Reserve.

Mr. McCABE. I beg your pardon, I would like to make that point clear, because I do not want any misunderstanding on that point. This is not a proposal to bring nonmember banks into the Federal Reserve System.

Mr. BROWN. Well, you are doing it.

Mr. McCABE. If the Congress enacts the same authority to increase the reserves on the nonmember banks, I would assume that in the law it would be perfectly right for you to state that the Federal Reserve would accept certification of the commissioners of banking in each of the respective States as to the bank's compliance with this provision. It has been done in other things. The provision for the control of margin requirements—that applies to all banks. The carrying out of regulation W, when it was in effect, applied to all banks.

The CHAIRMAN. Of course, regulation W might apply because that is a general authority contained in a general statute.

Mr. McCABE. I would not anticipate any difficulty in carrying that out.

Mr. TALLE. Will you yield to me, Mr. Brown?

Mr. BROWN. I yield.

Mr. TALLE. Inasmuch as the question of authority has been raised, and you, as a witness, Mr. McCabe, have stated that you do have the authority to impose reserve requirements on nonmember banks, I should like to have the record show at this point the source of that authority.

Mr. McCABE. What would be the source of the authority?

Mr. TALLE. Yes.

Mr. McCABE. It would be the congressional enactment. We do not have it now. It would be the congressional enactment here.

Mr. TALLE. Does that assume we have the constitutional right to do it?

Mr. McCABE. Our legal department says "Yes."

Mr. TALLE. Then, I want the legal department to explain why, in the record. I do not want a mere "Yes" answer. I want an explanation setting forth legal support for the conclusion.

The CHAIRMAN. I think you are liable to run into the question, if you freeze any part of their reserves, you run into the question of taking property without due process of law.

Mr. McCABE. The legal department says they will be glad to give you a memorandum for the record that would spell that out, in answer to your question.

Mr. TALLE. I should like to have it.

Mr. McCABE. We will see that you have that.

(The document referred to is as follows:)

POWER OF CONGRESS TO REQUIRE BANKS WHICH ARE NOT MEMBERS OF THE FEDERAL RESERVE SYSTEM TO MAINTAIN CERTAIN RESERVES

As a measure to aid in protecting interstate commerce and the Nation's monetary, banking, and financial structure against the dangers arising from further inflationary pressures, it has been proposed that Congress enact legislation requiring all commercial banks to maintain certain reserves in the form of balances with Federal Reserve banks. This proposal encompasses banks which are not members as well as those which are members of the Federal Reserve System because, as has been pointed out, the proposal would be both ineffective and unfair if the reserve requirements in question were made applicable only to those banks that happen to be members of the Federal Reserve System.

A question has been raised as to the authority of Congress to enact such legislation requiring nonmember banks to comply with such reserve requirements, and the purpose of this memorandum is to show in brief compass the clear authority which Congress has in the matter.

PREVIOUS LEGISLATION APPLICABLE TO NONMEMBER BANKS

Before discussing the legal considerations and the decisions of the Federal courts which clearly sustain this authority on the part of Congress, it should be pointed out that Congress has heretofore enacted legislation which subjects banks to certain requirements regardless of whether or not they are members of the Federal Reserve System.

In the Banking Act of 1933, Congress included a provision (sec. 21 of that act) which provides that it shall be unlawful for any person engaged in underwriting securities to engage at the same time in receiving deposits. In other words, banks were required by that act to give up any underwriting business in which they were then engaged. That provision applied to all persons engaged in the banking business, regardless of whether or not members of the Federal Reserve System. Likewise in 1934, in the Securities Exchange Act of that year, Congress authorized the Board of Governors of the Federal Reserve System to issue regulations prescribing the amount of credit which could be extended for the purpose of purchasing or carrying registered stocks, and the Board, pursuant to that authority, has for years had in effect a regulation which applies to all banks, whether or not members of the Federal Reserve System. Moreover, it goes without saying that Congress could, as a condition of insurance of deposits of banks by the Federal Deposit Insurance Corporation, make any reserve or other requirements of such banks which it deemed appropriate. But as will be demonstrated below, the decisions make clear the power of Congress to enact the proposed legislation regardless of whether the banks affected by it are insured by the FDIC or are members of the Federal Reserve System.

The first part of the discussion which follows relates to the power of Congress to take the proposed action under its authority over interstate commerce, and this power alone is fully sufficient to authorize the proposed legislation. In addition, however, there is discussed the authority of Congress to take this action in order to protect the banking system which Congress has established and in order to protect the Nation's monetary system. All these grounds are related, but it is convenient to consider them separately.

AUTHORITY OF CONGRESS

Power over interstate commerce.—The power of Congress to enact the legislation in question is sustained by the plenary authority granted to Congress by section 8 of article I of the Constitution, "To regulate Commerce with foreign Nations, and among the several States, * * *," and "To make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers * * *." (U. S. Code, p. XXXIX, 1946 Ed.) That banking—whether chartered by the Federal or State Governments—is an activity within the reach of this congressional authority has been decided specifically by court decisions under both the National Labor Relations Act and the Fair Labor Standards Act which, of course, were enacted in pursuance of the "commerce power."

In *National Labor Relations Board v. Bank of America National Trust & Savings Association* (130 F. (2d) 624 (C. C. A. 9th, 1942)), a petition for enforcement of a Board order based on violations of the National Labor Relations Act, the bank contended in defense that it was not "engaged in commerce" and that its operations did not "affect commerce" within the meaning and intent of that act.

In sustaining the order and, therefore, overruling the bank's contentions, the Court reviewed the bank's activities, including, among others, the financing of business operations, both interstate and intrastate in character; the collection of commercial paper, much of which covered interstate shipments of goods; the interstate transfers of funds; and the facilitation of the sale and shipment of goods in the channels of commerce through the discounting of trade acceptances, the issuance of letters of credit, bank drafts, etc. The Court said that the bank's operations had an "undeniable effect * * * upon commerce among the States," lending "vital support to the commercial life of the Nation." Furthermore, the Court said that the bank was "itself directly and every hour of the business day engaged in interstate activities not describable otherwise than as commerce * * * within the meaning of the Constitution." The United States Supreme Court denied certiorari and rehearing (318 U. S. 791-792; 319 U. S. 782).

A similar case is that of *Bozant v. Bank of New York* (156 F (2d) 787 (C. C. A. 2d, 1946)), which held that the bank was subject to the Fair Labor Standards Act because of the relationship of the bank's activities to interstate commerce. The close relationship of credit activities to interstate commerce is further illustrated by *United States v. General Motors Corporation* (121 F (2d) 376 (C. C. A. 7th, 1941), certiorari and rehearing denied 314 U. S. 579, 618, 710), holding that the local retail and wholesale financing of products moving in interstate commerce is a matter within the power of Congress under the "commerce power" as expressed in the Federal antitrust laws.

The above decisions demonstrate fully the application to banking of the principle, established by the courts in dealing with other but analogous situations, that the regulation of commerce may extend properly to the regulation of all aspects of commerce and of all instrumentalities upon which the carrying on of commerce depends. This general principle was reiterated in *United States v. Darby* (312 U. S. 100, 118 (1940)), wherein the Court, in holding a local manufacturer subject to the Fair Labor Standards Act, said that "The power of Congress over interstate commerce * * * extends to those activities intrastate which so affects interstate commerce or the exercise of the power of Congress over it as to make regulation of them appropriate means to the attainment of a legitimate end, the exercise of the granted power of Congress to regulate interstate commerce." For earlier examples, it has long since been settled that stockyards, although engaged in dealing locally in livestock, are subject to Federal control, because they are essential cogs in the machinery of interstate commerce (*Stafford v. Wallace*, 258 U. S. 495 (1922)). The same is true of a local grain exchange. *Board of Trade of City of Chicago v. Olsen* (262 U. S. 1 (1923)). The issuance of fraudulent bills of lading is punishable under Federal statute, although they cover no interstate shipment. *United States v. Ferger* (250 U. S. 199 (1919)). Indeed, the Supreme Court has frequently rejected arguments which, by the application of "artificial" or "mechanical" concepts, would disregard the "economic continuity" of either individual or collective processes or activity and, hence, ignoring actuality, try to limit or impair the constitutional power of Congress over interstate commerce (*Mandeville Island Farms, Inc. v. American Crystal Sugar Co.*, 68 S. Ct. 996 (1948)). (See also *United States v. Sullivan*, 68 S. Ct. 331 (1948).)

While no useful purpose would be served by referring to the many court decisions cumulative of the foregoing, no discussion of the "commerce power" would be complete without mention of *United States v. South-Eastern Underwriters Association* (322 U. S. 533 (1944)), holding that the business of insurance, notwithstanding local regulation, constitutes commerce, and hence, is subject to the Federal antitrust laws. (See also *Darr v. Mutual Life Insurance Co. of New York* (17 L. W. 2035 (C. C. A., 2d, July 8, 1948)), holding that "insurance policies are goods produced for commerce" within the coverage of the Fair Labor Standards Act; and *Smolove v. Delendo Corporation* (136 F. (2d) 231 (C. C. A., 2d, 1943), certiorari denied, 320 U. S. 751), holding that, as "private sales" on national security exchanges affect stock quotations thereon, such sales are not purely intrastate activities, but are subject to congressional regulation as interstate commerce under the Securities Exchange Act of 1934.

In conclusion on this point may be noted *Wickard v. Filburn*, (317 U. S. 111 (1942)), in which the Court sustained as validly within the "commerce power" of Congress, the wheat-marketing quota and attendant penalty provisions of the Agricultural Adjustment Act of 1938, as amended, although the facts before the Court involved wheat not intended in any part for commerce but wholly for consumption on the farm where grown.

In so holding, the Court observed that the general scheme of the act was "to control the volume" of wheat "moving in interstate and foreign commerce in order to avoid surpluses and shortages and the consequent abnormally low or high wheat prices and obstructions to commerce." In overruling the argument that the act was unconstitutional as an interference with local matters, i. e., "production" and "consumption," which, at most, would have only an "indirect" effect on interstate commerce, the Court said:

"But even if appellee's activity be local and though it may not be regarded as commerce, it may still, whatever its nature, be reached by Congress if it exerts a substantial economic effect on interstate commerce, and this irrespective of whether such effect is what might at some earlier time have been defined as 'direct' or 'indirect' * * *. That appellee's own contribution to the demand for wheat may be trivial by itself is not enough to remove him from the scope of Federal regulations where, as here, his contribution, taken together with that of many others similarly situated, is far from trivial * * *. * * * Congress may properly have considered that wheat consumed on the farm where grown, if wholly outside the scheme of regulation, would have a substantial effect in defeating and obstructing its purpose to stimulate trade therein * * *."

The Wickard case is particularly apposite to the question here. If it is constitutional to regulate as interstate commerce wheat grown locally and in a "trivial" amount for home consumption, as held in the Wickard case, so also is local banking subject to such regulation even though, in a given case, it might be considered to be of equally "trivial" proportions in interstate commerce. Here, as in the legislation involved there, Congress, may properly consider that any such banking, no less than local farming, if left outside the scheme of regulation, "would have a substantial effect in defeating and obstructing" its lawful purpose and, therefore, apply its regulation to all banks, large and small alike, and whether nonmembers or members of the Federal Reserve System.

Protection of the banking and monetary systems.—Although, as indicated above, the "commerce power" is ample authorization for the proposed legislation, the Congress also has authority for such action under its power to protect the banking system and the Nation's monetary system.

The authority of Congress to protect the national banking system and the Federal Reserve System has been reaffirmed many times since the famous case of *McCulloch v. Maryland* (4 Wheat (U. S.) 316 (1819)), which held that a bank chartered by Congress could not be taxed by a State because such taxation would interfere with the power of Congress. In that case, Chief Justice Marshall stated (p. 426) the basic doctrine that "a power to create implies a power to preserve."

The authority of Congress to authorize national banks to act in certain circumstances as trustees, executors, and administrators as against the contention that such action infringed State authority, was sustained in *First National Bank v. Union Trust Co.* (244 U. S. 416 (1917)), on the ground that Congress could lawfully authorize national banks to act in such capacities in order to enable them to compete with State corporations having such power. And, in *State of Missouri v. Duncan* (265 U. S. 17 (1924)), the Court held, in effect, that, although the local law did not authorize national banks to act as executors, a State probate court could not discriminate against national banks by refusing to appoint them executors and thereby deprive such banks of "their power to compete that Congress is authorized to sustain."

The banks to which Congress can lawfully extend protection, however, need not be federally chartered. Thus, in *Westfall v. United States* (274 U. S. 256 (1927)), a defendant was indicted for aiding and procuring a branch manager of a member bank of the Federal Reserve System to misapply bank funds in violation of Federal statute. The application of the statute to the defendant, although not a bank official, was sustained on the ground that it was proper to prevent the weakening of the System. The authority of Congress similarly to protect nonmember banks whose deposits are insured by the Federal Deposit Insurance Corporation also has been upheld (*Doherty v. United States*, 94 F. (2d) 495 (C. C. A., 8th 1938) and *Weir v. United States*, 92 F. (2d) 634 (C. C. A., 7th, 1937), certiorari denied, 302 U. S. 761).

The authority of Congress to protect the Nation's monetary system was long ago held to authorize measures far more sweeping than the legislative proposal in question (*Veazie Bank v. Fenno*, 8 Wall (U. S.) 533 (1869)), sustained a 10-percent Federal tax imposed on the circulating notes of State banks. Although clearly recognizing that the tax was intended to, and did, bring to an end the practice of State banks of issuing such notes, the Court stated the monetary authority for such action as follows:

"Having undertaken to provide a currency for the whole country, it cannot be questioned that Congress may, constitutionally, secure the benefit of it to the people by appropriate legislation. To this end, * * * Congress may restrain, by suitable enactments, the circulation as money of any notes not issued under its own authority."

It will be noted that the statute sustained by the court in the Veazie Bank case singled out State banks and applied the burden of the control exclusively to them. That statute, by comparison illustrates the far milder effect which the present proposal would have on State banks. Instead of laying special burdens on State banks as was done in the Veazie Bank case, the present proposal would merely have all banks, member and nonmember alike, conform to the requirements which would be ineffective and unfair if applied only to members of the Federal Reserve System and which are necessary for aid in the protection of interstate commerce and the banking and monetary systems established by Congress.

The congressional powers to protect the banking and monetary systems are, of course, clearly related. They stem not only from several specific provisions of the Constitution but from a blending thereof and from its general purposes.

Norman v. B. & O. R. R. Co. (294 U. S. 240 (1935)) is one of many cases illustrating the broad sweep of these powers. There the Court sustained the power of Congress to strike down "gold clauses" not only in contracts made by individuals, but also in contracts of States and their subdivisions. The Court not only quoted with approval from the Veazie Bank case, above, but clearly stated and reaffirmed the comprehensive character of such powers:

"The Constitution grants to the Congress power 'To coin money, regulate the value thereof, and of foreign coin,' (art. I, sec. 8, par. 5). But the Court in the legal tender cases [12 Wall. 457] did not derive from that express grant alone the full authority of the Congress in relation to the currency. The Court found the source of that authority in all the related powers conferred upon the Congress and appropriated to achieve 'the great objects for which the government was framed'—'a national government, with sovereign powers.' *McCulloch v. Maryland* (4 Wheat. 316, 404-407; *Knox v. Lee*, supra, pp. 532, 536; *Juilliard v. Greeman*, supra, p. 438). The broad and comprehensive national authority over the subjects of revenue, finance, and currency is derived from the aggregate of the powers granted to the Congress, embracing the powers to lay and collect taxes, to borrow money, to regulate commerce with foreign nations and among the several States, to coin money, regulate the value thereof, and of foreign coin, and fix the standards of weights and measures, and the added express power 'to make all laws which shall be necessary and proper for carrying into execution' the other enumerated powers."

Clearly the legislative proposal in question, which would operate prospectively and which would be merely regulatory rather than prohibitory, is nothing like as drastic as the congressional action sustained by the court in the Norman and Veazie Bank cases. Thus, if the congressional power can be lawfully used as demonstrated by these cases to adjust matters of vital national interest, there can be no room for doubt as to the validity of the congressional action now proposed.

—Submitted by George B. Vest, general counsel, Board of Governors of the Federal Reserve System.

AUGUST 4, 1948.

Mr. SMITH. Mr. Chairman.

The CHAIRMAN. Dr. Smith.

Mr. SMITH. Mr. McCabe, do you think that the amount of installment credit now outstanding is excessive?

Mr. EVANS. The amount of installment credit outstanding at the present time is the highest on record. The main thing, Congressman, is that it is going up, and if you are to restrain inflationary pressures, we would like to see it level off, until such time as conditions are different from what they are now.

Mr. SMITH. You are saying to this committee that the amount of goods bought under installment credit is the highest that it has been in history?

Mr. EVANS. Dollarwise; yes.

Mr. SMITH. Dollar volume. Now you are talking about something else. I think you should have brought that out right at the beginning. What is the actual volume of goods bought through installment credit, as compared with some of the periods in the past? The cost of living has risen since 1938—using that figure as a base—100—the cost of living has risen to 170.5. Where would that put the volume of consumer goods that is now being purchased under the installment-credit arrangement?

Mr. EVANS. In 1937 there were 3.9 billion dollars of installment credit, and now it is over 7 billion dollars, 7.2 billion dollars, to be exact. An increase, just since June of 1947, of 2.2 billion dollars.

Mr. SMITH. In dollars?

Mr. EVANS. Yes, sir.

Mr. SMITH. What is the increase in the amount of goods?

Mr. EVANS. I do not know.

Mr. SMITH. Just roughly.

Mr. EVANS. Because different things have gone up different amounts—automobiles, refrigerators, and so forth.

Mr. SMITH. I did a little rough figuring here, and possibly my figures are off a little bit, so I want that taken into consideration. But let us look at this picture and see just what you are really asking for here. In 1937 the dollar volume was \$3,971,000,000?

Mr. EVANS. Yes, sir.

Mr. SMITH. I have May 1948, with \$6,957,000,000. According to my figures, the people who engaged in this sort of buying bought just about as much goods in May of 1948—a fraction less—than they bought in 1937. Are you gentlemen before the committee telling the people of this country, telling those people who feel that they would like to avail themselves of that type of credit, installment credit, are you here telling them now that they cannot buy any more or possibly must buy less than they bought in 1937? Is that your mission here?

Mr. EVANS. No, sir.

Mr. SMITH. Well, just what are you asking for?

Mr. EVANS. The only mission I have here is a mission that the Board empowered me to come up here on, and that is to advocate to the Congress steps that will curb the inflationary pressures. Industrial output is practically at its peak and has been for some little time. There is not much opportunity, Mr. Congressman, to increase production. If you want to do something about leveling off the cost of living insofar as these items would contribute to it, then, in some way, you will have to take steps that will moderate the demand until it is more closely in line with the supply, and until such time as they are in balance. As long as credit is injected into this picture in an ever-increasing volume while the line of production is pretty well level, prices will continue to go up on these particular things.

Mr. SMITH. But, nevertheless, you are here before this committee of Congress importuning it, or asking it, to give you power to either reduce the amount of consumer purchases to the 1937 level, or the power to prevent those purchasers from buying any more than they purchased in 1937. That is your exact proposition. Do you deny that?

Mr. EVANS. Well, sir, I would not put it that way; no, I would not.

Mr. SMITH. How would you put it, then? And hold specifically Mr. Evans, to my proposition.

Mr. EVANS. Well, maybe I do not understand your proposition, Mr. Congressman. Let me ask you if I do. You are relating the volume of installment credit in 1937 to the volume of installment credit now, and are relating that to the price level in 1937, of these commodities, and the price level in 1948; is that it?

Mr. SMITH. Yes; they are all involved.

Mr. EVANS. In other words, is what you are saying that the volume of installment credit today is no greater—

Mr. SMITH. Not in terms of dollars, but in terms of goods.

Mr. EVANS. That is just about the same as 1937.

Mr. SMITH. That is right.

Mr. McCABE. Dr. Smith, to ascertain that accurately you would have to take individual items and trace those individual items back, to see what the price advance has been in the individual items.

Mr. SMITH. I am taking an over-all picture. You are not asking here for the control of individual items. You would have that power more or less, but we are not talking about that. We are talking about installment credit in general. That is what you want to control?

Mr. EVANS. Yes, sir.

Mr. SMITH. That is what I am talking about.

Mr. EVANS. That is right.

Mr. NICHOLSON. Dr. Smith, may I ask a question? Are you advocating, then, that never a lender or a borrower be?

Mr. EVANS. No, sir; I think in my prepared statement I made that quite clear [reading]:

It should be noted that the Board's position on the regulation of installment credit is not to be taken as in any way indicating a feeling that all installment credit is undesirable. The problem is to prevent the abuse—and not the use—of the credit.

Credit is something we have had since the dawn of civilization.

Mr. NICHOLSON. Well, that was good advice that I gave, was it not?

Mr. EVANS. Yes; it was. In my youth it was so considered, anyhow.

Mr. SMITH. Now, this involves principally a certain class of income wage earners. There is no question about that. It does not involve you, it does not involve me. But it involves a certain class of people, at a certain level of income; is that not so?

Mr. EVANS. It involves anyone who would use installment credit, Mr. Congressman.

Mr. SMITH. Well, now, you can answer my question as to whether that is true or whether it is not true.

Mr. EVANS. A great many people use installment credit; in fact, in my statement I have said that there was some evidence to lead us to believe that the new users of such credit were concentrated in the middle and upper income classes, principally those with incomes of above \$3,000 a year.

Mr. SMITH. Above \$3,000 a year?

Mr. EVANS. Yes, sir. That is the new users.

Mr. SMITH. In any event, this involves class legislation. There is no question about that at all. Do you advocate class legislation?

Mr. EVANS. I would not be prepared to say it is class legislation, Mr. Congressman. It is credit legislation designed to retard the use of credit at this inflationary time.

Mr. SMITH. You yourself designated classes.

Mr. EVANS. Well, I merely used it—yes, the income classes. That is all. Different people have different incomes.

Mr. SMITH. Let me put another question to you. These prices are rising, and here is a young couple. They have just gotten married, and they want to move into a home and furnish it. The chairman has brought out that phase. They are not allowed to do it. You get this power, and you say, "No; you cannot furnish that apartment." They cannot buy, and so there is nothing left for that family to do but to save money until they have enough for this down payment. Meanwhile the price is rising. What do you do to that fellow?

Mr. McCABE. Dr. Smith, suppose we have a condition such as happened in 1929, and prices should go down abruptly? Perhaps we have done that couple a great favor.

Mr. SMITH. What danger is there of anything like that being done under the New Deal? As long as you have power to rig the bond market, you have got power to inflate, and, Mr. McCABE, you know that there is no power greater than that, unless it is that of direct financing of Government obligations through the banking system. Is that right or not?

Mr. McCABE. Dr. Smith, do you think it is a mistake to protect the Government bond market?

Mr. SMITH. I did not say whether it is a mistake or otherwise. We are talking about inflation here now. You come in here and you ask for power to curb inflation. Yet you want to have in your hands the most inflationary powers. That is the point I am making, Mr. McCABE.

Mr. McCABE. Can you think of an alternative to these suggestions that we have made?

Mr. SMITH. Let us not worry about this alternative. I am not at the head of the Federal Reserve Banking System. Consequently, I am not responsible. I am responsible, however, insofar as my small place in this picture is concerned, for getting at the facts and showing just where we stand.

Mr. McCABE. That is right.

Mr. SMITH. That is the point I am trying to bring out. You have the power to rig the Government bond market. Now, let me ask you in connection with that power: how long do you think you can continue that sort of operation?

Mr. McCABE. Well, I used the words this morning "foreseeable future." I can see that we have the strength and the resources to continue it for certainly some considerable time.

Mr. SMITH. Is it not a fact that the pressure is becoming greater and greater all the time?

Mr. McCABE. The total amount of Government bonds that we own today is a little less than it was several months ago.

Mr. SMITH. You have got about \$20,000,000,000 worth.

Mr. McCABE. Well, it is slightly over \$21,000,000,000. And it was up over \$22,000,000,000.

Mr. SMITH. It was a little higher than that, I think, at one time. I think it was nearer \$24,000,000,000 at one time, if my memory serves me correctly.

Mr. McCABE. Yes. It is down a little over \$2,000,000,000 from its peak.

Mr. SMITH. But you took out of the general fund of the Treasury something like \$23,000,000,000, which had accumulated there, at the close of the war, to pay on the Federal debt; is that not true?

Mr. McCABE. I assume that your figure is correct. I have not checked it back.

Mr. SMITH. I think it was about \$23,000,000,000. So when you talk about this reduction, you are involving, are you not, this \$23,000,000,000—when you speak of the reduction of the amount of securities which the Federal Reserve Banking System owns?

Mr. McCABE. Well, the Treasury did retire some of the debt held by the Federal Reserve.

Mr. SMITH. Yes. So that, as a matter of fact, the amount of securities that the Federal Reserve System holds is relatively greater than at any time?

Mr. McCABE. I think you could make an argument on that.

Mr. SMITH. Now, what rate of interest are you paying on these bonds that you are refunding?

Mr. McCABE. That are being refunded?

Mr. SMITH. Yes.

Mr. McCABE. That is, the bonds that are coming due? The Government bonds that are coming due, sir? I do not understand your question.

Mr. SMITH. Well, you have a number of issues that you are refunding at different rates; that is true, is it not?

Mr. McCABE. Yes.

Mr. SMITH. Generally speaking, your rates are rising; is that not true?

Mr. McCABE. Well, you see, you have the bills that are yielding today approximately 1 percent, you have the certificates, yielding approximately 1%.

Mr. SMITH. You mean they have increased one-eighth?

Mr. McCABE. They have increased from $\frac{3}{8}$ to 1%. And then you have the bonds. The bulk of them are in the 2, 2 $\frac{1}{4}$, and 2 $\frac{1}{2}$ percent bracket. The longer-term bonds are mostly in the 2 $\frac{1}{2}$ percent bracket.

Mr. SMITH. The effect of your policy there is to raise the rate of interest in order to keep the securities in the hands of private individuals, is it not?

Mr. McCABE. Well, recently most of the refunding has been done in bills and certificates, the bills yielding, as I say, approximately 1 percent, and the certificates 1%. The average rate over-all is in the neighborhood of 1.8 percent.

Mr. SMITH. But I come back to my proposition. Your objective is to bring these interest rates up high enough to keep the securities in the hands of private individuals and institutions, is it not?

Mr. McCABE. Nonbanking investors and bank investors. You see, the rates that have gone up are the rates on the bills and certificates. The bills have gone up from three-eighths of 1 percent to approximately 1 percent, and the certificates have gone up from seven-eighths to one and one-eighth.

Mr. SMITH. You still have not answered my question.

Mr. McCABE. I still do not know that I exactly understand it.

Mr. SMITH. What is your object in raising these rates except to keep these securities in the hands of private individuals and nonbanking investors?

Mr. McCABE. Our reason for getting up the short-term rate is to have those securities more attractive, so that when the Federal Reserve finds it necessary, in order to reduce bank reserves, to push out some of the securities, that we can sell these securities and there will be a better market for them.

Mr. SMITH. A better demand?

Mr. McCABE. Sure.

Mr. SMITH. That is the point exactly. That answers in the affirmative the question I asked you.

Mr. McCABE. Then, we would prefer to see the banks, if possible, hold a substantial amount of the bills and certificates and feel they have a sufficient return on those in order not to reach out for the risky or marginal loans. That is one of our strong objectives.

Mr. SMITH. I want you to understand me, Mr. McCabe. I know that you have a very difficult task.

Mr. McCABE. I understand.

Mr. SMITH. I am not criticizing you.

Mr. McCABE. I understand you, Dr. Smith.

Mr. SMITH. I see your problem. I just want to bring out these facts so the Congress and the country will know where we stand.

Mr. McCABE. We appreciate that.

Mr. SMITH. This is a situation we have gotten into—you did not, except that you helped as did almost everybody else—but you are in the situation now where you have the pressure on the part of holders of Government securities—Treasury issues—being brought to bear upon the Federal Reserve, to the extent where the Federal Reserve is forced to maintain a policy which permits it at any time to buy the securities held outside of the banking system. That is correct, is it not? And that pressure is growing and consequently, along with it, there is an upward pressure against the the interest rates. That is established, is it not?

Mr. McCABE. And that is quite natural, sir.

Mr. SMITH. This is a rather vicious cycle, is it not? I am sure you do not feel too confident about it. I do not. And I know that people who have given this thing thought do not feel too confident about it. What is going to be the outcome? You spoke about doing something to reduce taxes. I grant you that that is necessary.

Mr. McCABE. I did not say reduce taxes. I said it was highly desirable to have a substantial excess of receipts over expenditures.

Mr. SMITH. I beg your pardon. I did not mean reduce taxes, but to supply enough taxes to meet these maturities, perhaps, and thus to relieve the pressure from that standpoint. I know it is not in your province, but it is a problem for the Secretary of the Treasury who is finally responsible for the financial structure of the Federal Government, but, on the other hand, it is partly your responsibility because the Federal Reserve Banking System is not a private institution, or you would not be here speaking to us today. It is a government by controlled affair all the way through, and, therefore, I feel that it is your responsibility to help us in Congress, to do what we can to provide this surplus of revenue in order to break into this vicious spiral which the Federal Reserve System is in at the present time. I have not heard, in the 10 years I have been in Congress, anybody from the Federal Reserve come up here and say, "Now, the Federal Reserve is in a difficult position" which it is right now, and has been for many

years, for that matter—though it has not been sufficiently noticed, and something must be done to better your situation, because the life of the Nation is at stake, and it is my opinion that unless something is done, that your spiral is going to become more and more vicious. That is your idea, too, is it not?

Mr. McCABE. I share a good many of your points of view.

Mr. SMITH. All right. Now, then, we come to the matter of taxation. We could get some of this money by reducing Government costs. There are some Government costs which can be reduced. There has been advocated here an excess-profits tax. I notice that you did not particularly care to express yourself on that point. Nevertheless, it has been advocated. May I ask you, do you think that would be a feasible thing to apply at the present time: an excess-profits tax?

Mr. McCABE. As I said this morning, Dr. Smith, I feel that that is not within my province. That is within the province of the Congress. You have the recommendation of the Secretary of the Treasury, whom I assume you will hear. That is a matter on which I do not have enough information to give you an intelligent opinion.

Mr. SMITH. Are you acquainted with the risk capital market in the United States at the present time?

Mr. McCABE. Well, sir, until 3½ months ago I was very actively engaged in a business which required capital, so I do have some idea of it.

Mr. SMITH. Do you think we can stand any more Federal taxes, and preserve even a semblance of keeping up the volume of risk capital that is necessary to finance our productive plant?

Mr. McCABE. I would say this, that we are running a very, very heavy Federal budget. There is not the slightest question in my mind of that. And, as a taxpayer, I would like to see the budget reduced.

Mr. SMITH. You know, Mr. McCabe, the deplorable situation the risk capital field is in at the present time?

Mr. McCABE. I understand. As I say, I think I have a very good knowledge of it.

Mr. SMITH. Dr. Kuznets—and you recognize Dr. Kuznets as an authority, I am sure—tells us that new capital invested annually in tools of production from 1920–29 averaged \$15,000,000,000, and from 1930 and 1945 less than half that amount, \$7,000,000,000, roundly. It has been recently estimated that the per capita investment in tools of production is back to the 1909 level. That it would require something like \$71,000,000,000 of current purchasing power to bring our tools of production up to the capacity of 1930. Is that not a challenging situation?

I know, Mr. McCabe, that you want to be helpful. I merely bring these things out to try to show that your position is not an easy one, and ours is not an easy one.

Mr. McCABE. I certainly agree with you.

Mr. SMITH. But nevertheless, the point I brought out is that you are in this vicious spiral. You need more money to reduce the Federal debt. On the other hand, the administration is asking for more taxes, which will cut into risk capital and still further reduce America's capacity to produce. One thing, Mr. McCabe, that is not understood in this country is that some of these shortages which are now

plaguing us are not temporary shortages. They are here to stay, and they are going to continue to become worse until this trend in which risk capital is in at the present time is reversed. So this whole proposition is extraordinarily serious, and I hope that you, Mr. McCabe, in your position, will go down to the White House and tell the President: "You have got to cut out this spending." This Nation is in the process of being destroyed by this spending, and if we are going to save it, Mr. McCabe, we must depend very much on men in your position.

Mr. McCABE. Thank you, sir.

The CHAIRMAN. Mr. Patman.

Mr. PATMAN. Mr. McCabe, I presume, from your statement, that you are not trying to reduce the amount of credit available; you are just trying to prevent it from being increased.

Mr. McCABE. We are trying to prevent an undue expansion. I would like to put it that way.

Mr. PATMAN. Well, do you contemplate a reduction in the aggregate amount of credit?

Mr. McCABE. As I foresee it today, Congressman Patman, I would say that the chances are that if the factors do not change materially, that the amount of credit would not be reduced very much.

Mr. PATMAN. Would not be reduced very much?

Mr. McCABE. No. It would be a question of controlling the expansion.

Mr. PATMAN. Preventing it from expanding more?

Mr. McCABE. Unduly expanding, yes.

Mr. PATMAN. You would permit a wholesome or justified expansion?

Mr. McCABE. What we would say would be a reasonable expansion of credit. But you see the expansion has been very great over the past 2 years.

Mr. PATMAN. How much of a national income do you think we should try to maintain in order to pay off the national debt and take care of our budget annually, with the least inconvenience?

Mr. McCABE. Well, not having gone thoroughly into that subject, I assume you just want me to give you a personal opinion?

Mr. PATMAN. Yes, or the Board's opinion.

Mr. McCABE. I could not give you the Board's opinion, because that has not been expressed.

Mr. PATMAN. I would think that the Board would pass upon an important question such as that, Mr. McCabe. I mean they would give some consideration to it.

Mr. McCABE. Well, it is being considered. Of course, all these factors which affect the economy and affect the finances of the country are considered. Of course, with the governmental budget that we have today, I should think you would have to have a national income of somewhere close to the present national income to sustain it.

Mr. PATMAN. Around \$200,000,000,000, or a little more than that?

Mr. McCABE. In fact, it would be a desirable feature to have just a little bit more leeway in our Federal budget than we have today. That is, our estimate for this coming year is that there might be a Treasury surplus of something like \$3,000,000,000. I think it would be desirable to have a little bit more.

Mr. PATMAN. I thoroughly agree with you. That is the reason I voted against the tax-reduction bill. I wanted to keep that money in the Treasury and pay it on the national debt.

Mr. McCABE. I would say with taxes where they are, and the budget where it is, that you would have to have a national product of pretty close to \$250,000,000,000.

Mr. PATMAN. \$250,000,000,000?

Mr. McCABE. Yes, sir.

Mr. PATMAN. That would make a national income of around \$210,000,000,000?

Mr. McCABE. Roughly, yes.

Mr. PATMAN. Is it not a fact, Mr. McCabe, that we are compelled to have a high national income in order to pay the high national debt and the budget? We have just got to have it, whether we want to do it or not?

Mr. McCABE. That is right.

Mr. PATMAN. And is it not further a fact that it is easier on the people to pay \$40,000,000,000 in taxes out of a national income of \$200,000,000,000 than it is for the people to pay \$8,000,000,000 in taxes out of an income of \$40,000,000,000?

Mr. McCABE. Well, it seems easier today than it used to, when we did have the other.

Mr. PATMAN. The higher the national income, the easier taxes are to pay; are they not?

Mr. McCABE. You see, Congressman Patman, the thing that gives me serious concern in this situation is the unbalances in this whole picture. That is, there are large segments of the people who are proportionately so much better off than they have ever been before. There are others that are far worse off than they have ever been before. I am thinking of these people at the extreme, who are worse off, such as people with fixed incomes, pensioners, people who live from fixed income of all kinds. Then, of course, you have the next group, the so-called white-collar class. They are also at a disadvantage in the situation we are in. The thing that we have to grope for, if we are going to maintain this high national income, is to see how we can correct these inequities. That is the thing we must study.

Mr. PATMAN. In the interest of the general welfare?

Mr. McCABE. In the interest of the general welfare.

Mr. PATMAN. On these reserve requirements, Mr. McCabe, do you propose to get them increased by law, or get the authority to increase them a maximum of 10 percent on demand deposits and 4 percent on time deposits?

Mr. McCABE. The latter is correct.

Mr. PATMAN. I see your chart here, on page 4—that lower line. Suppose you had this power, and you immediately put into effect 50 percent of the power that you would have. How would that affect the lower line, on page 4 of the book of charts, where you have excess reserves now of approximately three-quarters of a billion dollars? Would it wipe out that excess entirely?

Mr. McCABE. If we put in what you say there, sir, and it applied to nonmember banks as well as member banks, it would require about 5½ billion dollars of additional reserves.

Mr. PATMAN. In addition to what they have?

Mr. McCABE. In addition to what they have.

Mr. PATMAN. I am afraid that would seriously affect our economy, Mr. McCabe.

Mr. McCABE. Well, the question there is this: The banks have about \$65,000,000,000.

Mr. PATMAN. I know, but those are all the banks. I am afraid you are assuming that it will affect all banks in the same way. It would unfavorably affect some and it would not hurt others.

Mr. McCABE. Well, all these things do not affect them all alike, but if you should apply your 5 percent across the board, as you suggested, it would take about five to five and a half billion dollars of additional reserves for the banks to meet that requirement.

Mr. PATMAN. That means they would have to sell about five and a half billion dollars of their Government bonds in order to be even.

Mr. McCABE. They would do that, or, as I say, cut down on their loan account, and get a portion of it from that account.

Mr. PATMAN. That is the part that I am apprehensive about—this cutting down on the loan account. You know that is what started the depression in 1920, was it not? Did not the Federal Reserve Board issue an order which scared all the banks, and they commenced cutting down on their loan accounts and calling their loans, and thus forcing us into a panic?

Mr. McCABE. Historically, when you get into that, you are just a little out of my field.

Mr. PATMAN. But you remember that panic; do you not, Mr. McCabe?

Mr. McCABE. Very well, sir.

Mr. PATMAN. And it started just like this, did it not, by calling loans?

Mr. McCABE. We are not suggesting that any drastic cutting down of loans or calling of loans take place.

Mr. PATMAN. I know, but if you scare these banks much they are likely to do it anyway. Probably the Federal Reserve Board in 1920 did not anticipate what happened.

Mr. McCABE. Congressman, I see here that the member banks of the Federal Reserve System have about \$13,890,000,000 of what we call short-term Governments; that is, Treasury bills, certificates, and others. Then, they have what are considered reasonably short-term maturities, which mature in 5 years; they have \$11,000,000,000 worth of those.

In the 5- to 10-year maturities, they have close to \$20,000,000,000.

I think they could meet it.

Mr. PATMAN. You are speaking about member banks?

Mr. McCABE. Yes, sir.

Mr. PATMAN. Does your book of charts anywhere disclose the excess reserves of all banks, as distinguished from just member banks?

Mr. McCABE. We do not have those.

Mr. THOMAS. It is very difficult to compute.

Mr. PATMAN. You are asking for the power. Do you not think we ought to have that information?

Mr. McCABE. I do not think the over-all situation, Congressman Patman, proportionately, would vary too much from that of the member banks.

Mr. PATMAN. But that would be material information, I would think. We should know it before entering that field.

Mr. McCABE. We can get it for you.

Mr. PATMAN. It would be a rather drastic step to force these nonmember State banks under this law without knowing fully and thoroughly what the consequences might be.

Mr. McCABE. If you would be interested, I have with me the reserve requirements of all the States. The State reserve requirements are ever so much less—the percentage requirements—in the main, than those of the Federal Reserve. So that their requirements today, their legal requirements, are quite a bit lower than those of the member banks. I would say it would be less hardship on the nonmember banks than it would be on the member banks.

Mr. PATMAN. But that information, it occurs to me, would be important.

Mr. McCABE. I have that here, sir, if you would be interested in any State or any groups of States.

Mr. PATMAN. No, I am just interested in the over-all situation. In other words, I would like to have the same information for the nonmember banks which you propose to bring in under this law that you now have on page 4 of your book of charts, relating to excess reserves of member banks.

Mr. MULTER. Mr. Patman, may I suggest: Do not the charts on pages 10 and 11 of the booklet give that information?

Mr. THOMAS. They do not give the reserves.

Mr. MULTER. That relates to nonmember banks, does it not?

Mr. THOMAS. It does not show their required reserves.

Mr. McCABE. I have here, however, if you are interested in the required reserves —

Mr. PATMAN. You mean by States?

Mr. McCABE. By States. And you can run down it quickly enough to determine —

Mr. PATMAN. I think we need more than that, Mr. McCabe. I think we need not only the excess reserves, but we would like to have, too, the amount of Government securities held by these banks, State banks.

Mr. McCABE. That we can get you very, very quickly.

(The following information was inserted in the record in response to Mr. Patman's request.)

RESERVE REQUIREMENTS OF NONMEMBER COMMERCIAL BANKS

It is not possible to compute the amounts of required and excess reserves for nonmember banks on the same basis as for member banks. Member banks are required to hold a certain amount of reserves with the Federal Reserve banks and the term "excess reserves" for member banks relates only to balances held by member banks with Federal Reserve banks in excess of requirements. In addition, member banks hold, for operating or other purposes, vault cash and substantial amounts of balances with correspondent banks. For most nonmember banks State reserve requirements may be met in whole or in part by bankers' balances and vault cash and, in some cases, by securities of specified kinds.

The most common reserve requirement on demand deposits in the laws of various States is 15 percent, compared with the current 14-percent requirements for member banks not in reserve cities. The range of requirements, however, runs all the way from 7 percent in a few States to 20 percent in some other States. The most common reserve requirements on time or savings deposits (where there are such requirements) are 5 percent and 3 percent, compared with the current member bank requirement of 6 percent.

Approximate computations have been made of cash assets held by nonmember commercial banks in excess of the amount of reserves required to be held in the

form of cash and bankers' balances. These computations show that nonmember banks on December 31, 1947, held \$4,700,000,000 of cash assets against requirements of \$1,800,000,000 (excluding \$400,000,000 of requirements which may be satisfied by holdings of specified kinds of securities) giving them excess cash assets of \$2,800,000,000, or about 155 percent of requirements. Member banks not in reserve cities, on the basis of similar computations to include all cash assets, held \$10,800,000,000 against reserve requirements of \$4,400,000,000, an excess of \$6,400,000,000, or 145 percent of requirements.

Mr. PATMAN. To look at it in the way you do, it does not look frightening to me at all, but if you were to just issue an order—if this bill were to become law—saying that the banks had to sell 10 percent of their Government securities, which would be the effect of it, that is likely to scare the banks to the extent that they might begin to call their loans, as they did in 1920, and scare the people to death, and cause a panicky condition in the country as they did in 1920.

Mr. McCABE. Of course, as we analyze the whole picture, Congressman Patman, we would exercise this authority with due caution and care, to take into account all those factors which you are bringing out.

Mr. PATMAN. Yes, sir; I think the Federal Reserve Board in 1920 possibly had the same thing in mind, but they could not control it. It got out of hand very quickly. You cannot control people who are scared, you know.

Mr. McCABE. Well, the question of confidence, I realize, is terribly important.

Mr. PATMAN. Mr. EVANS states in his statement that we only have a limited number of units, anyway, and that it is necessary to have some sort of priority. You did not indicate any rationing or anything like that, but you indicated that we needed some way to cut down on the competition between purchasers of scarce supplies.

Mr. EVANS. That is right.

Mr. PATMAN. It occurs to me that that power could be greatly abused, and possibly there were cases before of abuse. Some were called to my attention. For instance, an automobile is needed in a person's business at times. He just has to have one. Well, perhaps he does not have the amount of money to make the down payment under regulation W, and he is thereby deprived of an automobile, thereby deprived of a means to make a living. However, the law does not prevent him from paying twice the rental price of an automobile.

Or you can take the case of a veteran, as suggested by Mr. Wolcott. Perhaps he wants to furnish an apartment. He is not able to make the payment on the furniture and he must rent the furniture. Of course, in renting furniture, you pay about two or three times as much as you do when purchasing it. So you would be putting that veteran in a position of having to pay two or three times as much to the landlord as he would have to pay if he could borrow the money on better terms and buy the furniture himself. So, of course, we will have a lot of inequalities, no matter how you take it. However, I can see where there is some justification for the charge that it discriminates against the poor people. It is giving the priority to the people who have the money, of course, and it makes money the standard, when character, I think, is just as good, sometimes, as money.

Mr. McCABE. Congressman Patman, if there is any discrimination, the discrimination is on the down payment. Over the period of the term of the credit—the 12 months or 18 months, or whatever period

you have—they have to pay just as much under whatever regulation the Federal Reserve has proposed as they do now. It is just a question that you throw up the stop-look-listen sign on the first move.

Mr. PATMAN. I know; but just for the benefit of a few people, Mr. McCabe. That is the point that I am concerned about.

Take the case of the veteran who wants to buy the furniture to furnish his apartment. He cannot buy that furniture. He has to rent it. He has to pay two or three times the value of it in order to obtain furniture. I think that people will testify that that is a customary rate.

You say he must wait and save up enough to make the down payment. Well, he never seems to be able to save enough to make that down payment.

Mr. McCABE. You know, in the curbing of the inflationary forces there is nothing you touch which is pleasant to any segment or any group of the economy. That is, most of us—and I am speaking now individually—most of us generally want to curb inflation providing it does not touch us, or does not touch our business.

Mr. PATMAN. That is very true. Selfishness enters into all these things, and we are all more or less selfish in a private enterprise system.

Mr. McCABE. All we have done here is to survey the field and pick out the two things that we think would contribute, realizing that even in the case of the two that we have picked some people will be pinched.

Mr. PATMAN. If you were to have these powers, and if you were to exercise them to the extent that you have discussed, how would it affect farm prices?

Mr. EVANS. Farm prices, Mr. Congressman, are, of course, protected by the farm price support program at the present time. I think if you will go back in your memory to the trouble which occurred in the first part of 1920—

Mr. PATMAN. I am speaking of reserve requirements now.

Mr. EVANS. They would not have any effect on farm prices whatsoever.

Mr. PATMAN. You mean the change in reserve requirements would not? If you make money less plentiful, that would change the price of everything; would it not?

Mr. McCABE. If you make credit less plentiful.

Mr. PATMAN. Well, of course credit is money.

Mr. EVANS. Credit and money are a good deal the same. But I do not think it would have any effect whatsoever on farm prices.

Mr. PATMAN. Most of the people advocating this are stressing that it would reduce the cost of living and you cannot reduce the cost of living without affecting them.

Mr. EVANS. That is only one of the items. And, as far as farm prices are concerned—and I am just giving my own opinion—I do not think there is any question but what they will decline if this crop matures.

Mr. PATMAN. I know that is true as to corn, and possibly it is true as to wheat. But as to other items, I am not so sure.

Mr. EVANS. What other items?

Mr. PATMAN. Take dairy products, for instance. Do you think the price of dairy products will decline?

Mr. EVANS. Not every much. But I will tell you—

Mr. PATMAN. Do you think the price of meat will decline very much?

Mr. EVANS. Yes, sir. Not right today, but if you will plot two curves—one showing the price of livestock and the other showing the price of feed grain—you will find that the price of livestock and livestock products will follow the price of feed grain with a lag of 12 to 18 months.

Mr. PATMAN. I am sure there must be a relationship there, Mr. Evans.

Mr. EVANS. Because feed grains are the raw material from which livestock products are manufactured.

Mr. PATMAN. Yes; but suppose they begin to bid up the prices of these feeder cattle, and, as they bid them up, they feed this cheaper grain to them? That would not lower the price of livestock. The price of feeders go up in proportion to the price of grain.

Mr. EVANS. You just plot that curve, Mr. Congressman, and you will see it holds true, because wherever the rate of conversion between feed grains and livestock is very favorable, as it is at the present time or will be after this crop comes in, you increase livestock production.

Mr. PATMAN. I would not attempt to question your analysis. And I am sure that under normal conditions it is correct. But I do not feel that we are in normal conditions now.

Suppose the price of feeders goes up, and people begin to buy these feeders, based upon lowered prices of grain. The price of beef will not go down, will it, Mr. Evans?

Mr. EVANS. I do not know what your experience has been in feeding cattle, but over a long period of years I have not found too close a relationship between the price I paid for the feeders and the price I got for them when they were fat.

Mr. BROWN. You take the position, then, that your proposal here will not affect the cost of living; is that right?

Mr. EVANS. No, sir.

Mr. BROWN. Your explanation in answer to Mr. Patman's questions would bear that out.

Mr. EVANS. No. In my discussion with Congressman Patman we were talking about farm prices.

Mr. BROWN. I know.

Mr. EVANS. Which are only a part of the items going into the cost of living.

Mr. BROWN. Let us limit it, then, to beef, wheat, corn, clothing, cotton, and those things, which would be affected.

Mr. EVANS. If this crop matures, I think they will come down, regardless of whether you increase reserve requirements. That is only a part of the cost of living.

Mr. BROWN. I would like to know what part of the cost of living it will affect.

Mr. EVANS. Anything else—manufactured goods. As far as installment credit is concerned, it is limited to automobiles, cooking stoves, dish washers, ironers, refrigerators, washing machines, combination units, air conditioners, radios, phonographs, sewing machines, suction cleaners, and furnishings.

Mr. BROWN. I think you have listed a great many things not necessary to the cost of living.

Mr. EVANS. That may be. We worked at this, Mr. Congressman, for 6 years—working with the industry all the time—and we have this satisfaction—that, after all that time, most of the people would prefer to have installment credit returned.

Mr. PATMAN. You mean installment-credit restrictions returned.
Mr. EVANS. Yes.

Mr. PATMAN. But I am talking about these reserve requirements. At one time I wanted the Congress to authorize the payment of what would be considered now a comparatively small amount of money—\$2,000,000,000—for the veterans of World War I, and I remember that Mr. Morgenthau testified here at one time and he opposed it on the grounds that it would scare the people to death.

I think if we start out doing what we did in 1920—compelling these banks to sell their Government securities—that we will scare the banks to death and they will start calling loans, and, in turn, scare the people to death.

Mr. McCABE. You have a very much different situation, Congressman Patman, today, from what you had in 1920.

Mr. PATMAN. Yes; I know we have a different situation.

Mr. McCABE. You had the banks in debt, then, to a degree much greater than they are today.

Mr. PATMAN. We had what?

Mr. McCABE. The banks were in debt to a much greater degree than today, on a proportional basis; and, further, you have the banks today in a situation where they can dispose of far more liquid assets than they possessed at that time.

Mr. PATMAN. One sure way of having a surplus of practically everything in this country would be to scare the people and to cause banks to call all these loans and create a lack of purchasing power. Then we will soon have plenty of automobiles and everything else, and prices will be going down instead of up. But I do not think we will pay off our huge national debt that way. So any power that the Federal Reserve gets, I hope the Federal Reserve will keep in mind what did happen in 1920 and not start out on that road again.

Mr. McCABE. Yes; I think that is right.

Mr. PATMAN. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Talle.

Mr. TALLE. Mr. McCabe, the act which you administer was enacted into law in December of 1913 and put into effect the following year. The gold reserves required under the law were 40 percent for Federal Reserve notes and 35 percent for deposits, making the average 37½ percent for the two.

Do you recall the theory which was advanced for the setting up of these gold-reserve requirements at that time?

Mr. McCABE. I would ask Dr. Thomas to answer that, if he will.

Mr. THOMAS. I could not say what theory was advanced at that time. I think the idea was that by such a process some limitation would be put on the Federal Reserve, and, also, there was a common impression that the amount of gold that the country had, had something to do with the soundness of its currency.

Mr. TALLE. But at the time all currencies were directly or indirectly convertible into gold; is that right?

Mr. THOMAS. That is right.

Mr. TALLE. The other 60 percent back of Federal Reserve notes was made up of eligible paper, was it not?

Mr. THOMAS. Either eligible paper or gold.

Mr. TALLE. Yes. You did not have to limit the gold back of the notes to the 40 percent reserve. It could be higher.

Mr. THOMAS. It could be 100 percent gold, if necessary; otherwise, eligible paper.

Mr. TALLE. And the 60 percent collateral was scrutinized on the basis of whether the paper originated for an industrial, agricultural, or commercial purpose; is that not correct? The theory behind that was that as trade and commerce increased and required more currency, more currency could be brought into circulation, flowing from the eligible paper.

Mr. THOMAS. That was the theory.

Mr. TALLE. That is what I asked about at the outset. And if trade requirements did not need so much currency, this paper would go out of existence and the currency would be retired; in other words, a contraction and expansion idea, in response to trade requirements.

I will stop with the theory at that point. There is scarcely any opportunity for contraction now, is there, with 60 percent being represented by Government bonds and the debt being over \$250,000,000,000?

Mr. THOMAS. There is as much opportunity for contraction now as there was then. The contraction and expansion was in accordance with the demands of the economy, until it reached certain limits.

Mr. TALLE. If that be true, then you could contract the currency if you chose to.

Mr. THOMAS. The public contracts the currency on the basis of whether it wants its money in the form of currency or wants it in the form of deposits in the banks, or wants to hold it in the form of a Government bond—whatever it wants to do.

Mr. TALLE. Well, the President signed a bill which became law on the 12th of June, as I remember it, of 1945. Under that law the new reserve requirement, for both Federal Reserve notes and deposits, was 25 percent in each category. That is present law.

Mr. McCABE. That is right.

Mr. TALLE. Do you remember why that change was asked for in 1945?

Mr. McCABE. Dr. Thomas explained that this morning, sir. I will ask him to answer your question again, sir.

Mr. THOMAS. I can probably explain it most effectively by reading from the Senate report—and I think the House report was quite similar at the time.

The bill provides for a direct reduction of the minimum ratio. Such enactment would be entirely consistent with the changes in conditions which have occurred since the ratio was first established by Congress. The original purposes of the ratio were (1) to assure adequate resources for the Federal Reserve banks to meet demands for gold or lawful money by depositors and note holders; (2) to limit the expansion of Federal Reserve credit; and (3) to assure the public that there was at least 40 percent in gold back of the Federal Reserve notes which were then being introduced for the first time.

The first purpose is no longer compelling since gold redemption is now not permitted for domestic use, and gold can be exported only under license. While the country's aggregate gold reserves are ample to meet any conceivable foreign demand, a reserve ratio high enough to meet possible demands for both domestic and foreign use is no longer appropriate under present conditions.

The second purpose—limitation of Federal Reserve bank expansion—is not relevant at a time when expansion by the Reserve banks is essential to needs of war finance.

Thirdly, confidence in Federal Reserve notes is well established, and whether the amount of gold back of the notes is 40 percent or 25 percent makes no practical difference.

Mr. TALLE. I think we might stop there, Dr. Thomas. I remember that it was being said rather generally, back there in June of 1945, by people representing the administration, that there was fear of deflation and that a greater expansion would occur on the basis of 25 percent than on the basis of 40 and 35. So the real practical reason, based on the theory that the administration believed in, was to bring reserves down, thus permitting greater expansion of money and credit, and thereby preventing a nosedive in prices which the administration feared after VE-day, in 1945.

Now, if that was good medicine in 1945, although the deflation did not occur, could it not be good medicine now to lift those reserves back to 40 and 35, respectively?

Mr. McCABE. Congressman Talle, anticipating that question, I prepared a very, very short statement here in reply, and, with your permission, I would just like to give you this reply to your question.

Mr. TALLE. I am very glad to have it.

Mr. McCABE. The suggestion that the reserve requirements of Federal Reserve banks be increased from their present level of 25 percent against both notes and deposits to their earlier level of 40 percent against notes and 35 percent against deposits would not contribute to the fight against inflation. The 12 Federal Reserve banks now hold \$22,000,000,000 of gold certificates against \$44,000,000,000 of liabilities, of which \$24,000,000,000 is notes and \$20,000,000,000 is deposits. That is a ratio of 50 percent. In other words, they now hold excess gold reserves of 25 percent, or \$11,000,000,000. They could meet the suggested higher requirements and still have five and a half billion dollars of gold reserves.

Even at the new and higher ratios this would enable them to expand their Government security portfolio by \$15,000,000,000. This would permit a much larger expansion of our money supply. How much larger would depend on the distribution of the expansion between notes and deposits. If it were all in deposits, \$15,000,000,000 of excess reserves could support about \$90,000,000,000 of member bank deposits.

If it is the purpose of this artificial limitation actually to prevent the Reserve banks from purchasing any more Government securities, or issuing currency, member banks then would be unable to supply their customers with needed currency and credit.

The result could precipitate the kind of money panic which the Federal Reserve System was created to prevent. Likewise, the System would be unable to maintain an orderly market for Government securities and the effects would well be demoralizing in the Government bond market.

Although the Reserve System as a whole has gold certificate reserves in excess of the proposed higher requirements, there is considerable variation among individual Federal Reserve banks. The requirement applies to each of the 12 banks. As a practical operating matter these banks cannot permit the ratios to go down to the vanishing point and hence must retain a working margin of at least 3 percent.

If the higher requirement was restored, some Federal Reserve banks would have a substantial deficiency. Others would be below or close to the necessary operating margin, while still others would have a large excess. Reserve banks with a deficiency would be obligated to

sell some of their Government securities to borrow from Reserve banks which had an excess.

Mr. TALLE. Just at that point, may I interrupt for a moment?

You have authority, however, to shift gold among banks so that you could supply gold to those who were deficient from those who had surplus through the mechanism of the Gold Settlement Fund.

Mr. McCABE. Well, you have authority to shift the portfolio of the system, and the gold certificates, in the manner that I have indicated. But the operating difficulties are quite pronounced.

Mr. TALLE. Could you not do it merely by telegraph and on book accounts?

Mr. McCABE. The people in the Federal Reserve tell me that the operating difficulties were very great when they had to shift. May I just carry on?

Mr. TALLE. Yes, sir.

Mr. McCABE. The reserve position of the individual Federal Reserve banks is constantly changing with seasonal and other movements of funds in the economy. Therefore, the proposal would entail operating difficulties and constant inconvenience without accomplishing any useful purpose.

In considering reserves and reserve requirements it is important to distinguish sharply between commercial banks and Federal Reserve banks. Commercial banks are properly operated for profit and usually lend all the money they can. By requiring such banks to hold reserves to the amount that they can lend is limited. The reason for requesting increased authority over commercial bank reserves is to limit the amount they can extend.

The Federal Reserve banks, on the other hand, are operated in the public interest. They do not increase their credit to make profit, as is shown by the fact that their present gold-certificate holdings are twice as great as the minimum they are required to hold.

Mr. TALLE. Suppose the law that became law on the 12th of June 1945 had never been enacted. Then we would have the old 40-percent and 35-percent relationship. What difference would it have made now?

Mr. McCABE. Today?

Mr. TALLE. Yes.

Mr. McCABE. You mean if that had continued?

Mr. TALLE. If nothing had been done on the 12th of June 1945.

Mr. McCABE. The reduction in requirements was designed to give the System more leeway. Thus far that additional leeway has not been needed and therefore has not been used. Today you might make a case that there is still some leeway between the 35 percent and 40 percent, or the 37½ percent average and 50 percent. But it is not what we consider an excessive leeway. We feel that the leeway that exists today between the 25 percent statutory requirement and the 50 percent that actually exists is very desirable and is not being abused in any possible way.

Mr. TALLE. No; I do not make that charge.

Mr. McCABE. I understand that, sir.

Mr. TALLE. I should like now to turn to another matter.

Whether we talk about money in circulation or credit, either one really rests upon Federal debt, does it not?

Mr. McCABE. The Federal debt certainly contributed to it; yes.

Mr. TALLE. In fact, the controlling force, in both our money system and our banking system, is the Federal debt, is it not?

Mr. McCABE. I will ask Mr. Thomas to answer that question.

Mr. TALLE. There was a time when we had a money system, in the days when "hard" money was the customary thing, and we had a banking system that was distinct from it. At the present time I see no difference between the two. Our money system is our banking system and our banking system is our money system. They are identical.

Mr. THOMAS. That is right. But the money system does not rest entirely on the public debt. It rests in part on the loans that banks make to private people. Commercial banks have \$40,000,000,000 of loans. They have \$10,000,000,000 of corporate securities and State and local Government securities, and they have \$65,000,000,000 of Government securities. So that less than 60 percent of the total, about, is now on the basis of the Federal debt, you might say. Then, in addition, some of the money that we have has been derived originally from gold—some twenty-odd billion dollars.

Mr. TALLE. That is right. But there is enough of the Federal debt in there to make it the controlling force, for both money and banking.

Mr. THOMAS. Loans in the past year have been the controlling force.

Mr. TALLE. Well, there has been some sale of bonds, so that the banks would have more money to lend.

Now, the proposal that you have in mind is to control credit, is it not?

Mr. McCABE. That is right.

Mr. TALLE. The next step beyond that is the hope that you can control the price level; is that not right?

Mr. McCABE. No, sir; not so far as the Federal Reserve is concerned.

Mr. TALLE. You do not have in mind to control the price level?

Mr. McCABE. We would influence it, undoubtedly, but there is no thought to control the price level.

Mr. TALLE. You do hope to get prices down?

Mr. McCABE. We would like to see prices come down; yes, sir.

Mr. TALLE. That was something I was trying to get at a little bit the other day when Mr. Porter was here. I asked him to project his wholesale price curve into the future, which he has not been able to do, and I do not blame him for it. But I was wondering if the Federal Reserve believes now that it can control the price level by controlling credit?

Mr. McCABE. I do not think it is any question of controlling the price level. It is a question of what the Federal Reserve can contribute to retarding the inflationary spiral.

Mr. TALLE. Do you recall that back in 1923 there was something of a controversy on that point? I believe Mr. Strong was chairman of the Federal Reserve System at that time, was he not?

Mr. THOMAS. 1926.

Mr. TALLE. Do you remember that controversy, Dr. Thomas?

Mr. THOMAS. I remember it very well.

Mr. TALLE. Do you remember the conclusion that was arrived at?

Mr. THOMAS. I think different people arrived at different conclusions, depending upon their predilections when they went into session.

Mr. TALLE. Do you mean to say that they did not approach the problem with detached or open minds?

Turning to your testimony, Mr. Evans, I note, at the bottom of the first page of your statement, the following:

During the 3 years that have elapsed since VJ-day, the American public has gone into debt more rapidly than in any other period in our history.

I have not seen any figures on that, Mr. Evans. Do you have any which you can supply?

Mr. EVANS. Surely. That statement is based upon the figures we have, Mr. Congressman. If you wish me to, I will furnish them to you.

Mr. TALLE. I do not want to ask for a lot of figures, but if you could furnish some comparative figures, they would be interesting, especially if you could show debt by occupations. The farmers in the Middle West have been paying off their debts, have they not?

Mr. EVANS. Yes, sir.

Mr. TALLE. And I have advocated that for quite a while, and so have you.

Mr. EVANS. Yes, sir.

Mr. TALLE. It is good sense.

Mr. EVANS. And I hope they keep it up. This is the first time they have ever been in that enviable position in your lifetime and in mine.

Mr. TALLE. That is right. Therefore, it would be interesting, if you have the data, to furnish something about the occupations as well.

Mr. EVANS. We will break it down in whatever categories we have it, Mr. Congressman.

(The information above referred to is as follows:)

Estimated change in selected types of debt from June 30, 1945, to June 30, 1948¹

[Billions of dollars]

Short-term consumer debt, total.....		+ 8. 5
Installment.....	+ 5. 3	
Charge account.....	+ 1. 8	
Other ²	+ 1. 4	
Mortgage debt on		
Nonfarm 1- to 4-family houses.....		+ 13. 1
Farm real estate ³		- . 1
Commercial and industrial bank loans.....		+ 10. 2
Farm debt, other than real-estate mortgages and consumer debt ³		+ . 4
Corporate bonds ⁴		+ 5. 6
State and local net debt.....		+ 2. 0

¹ Changes in debt by occupation not available.

² Includes single-payment loans and service credit.

³ Change from Jan. 1, 1945, to Jan. 1, 1948.

⁴ Corporate issues for net new money. Includes private placements. Stock issues for net new money amounted to \$3,600,000,000, in this period.

Mr. TALLE. I was wondering, too, Mr. Evans, what the debt was incurred for. This is all consumer credit, is it not?

Mr. EVANS. No.

Mr. TALLE. This is general?

Mr. EVANS. Yes.

Mr. TALLE. There is a statement, at the middle of page 3, in the last sentence of your middle paragraph, as follows:

International developments, moreover, inevitably add pressures in the markets for consumers' durable goods.

You refer there, do you not, to the large quantities of consumer durable goods which have been, and are being, shipped from our country to foreign countries?

Mr. EVANS. Yes, sir; plus the military expenditures for defense purposes.

Mr. TALLE. That is right. I am very glad you put that into your statement because so frequently I hear people say that these shipments make no difference, and that does not make sense to me. They must make a difference.

Mr. EVANS. Well, they are part of the demand, Mr. Talle.

Mr. TALLE. That is right. Foreign demand should not be overlooked.

That increase in consumer credit in the second quarter of 1948, could we not explain that, in part at least, by the fact that during the first quarter there was a prospect of declining prices, whereas people discovered that these large shipments were going to continue, and they felt: "Well, since they are going to continue, prices are not coming down; so we will go in and buy."

Mr. EVANS. I think the break in commodity prices—that is, corn and wheat—gave people some reason for believing that maybe other prices would follow, and I think your statement is quite correct.

Mr. TALLE. It is my hope that quite a little constructive effect may come from the psychological reactions of the people to some of the things which have been discussed at these hearings.

I have another point, but I will withhold it until other members of the committee have had an opportunity to ask questions.

Mr. SMITH. Mr. Folger.

Mr. FOLGER. Mr. McCabe, I suppose my questions should be addressed more to the legal staff than to you, but I am interested, in the question of bank reserves, as to the power of Congress to include nonmember banks in these requirements as set forth in this bill—

notwithstanding any of the provisions of the law the Board of Governors of the Federal Reserve System, in order to prevent injurious credit expansion, may, by regulation, change the requirements as to reserves to be maintained, pursuant to this section, against demand or time deposits, or both, (1) by member banks in the central Reserve cities; (2) by member banks in Reserve cities; (3) by member banks not in Reserve or central Reserve cities, and (4) by all member banks.

Now, the reserve requirements of the nonmember banks are fixed in the different States by the State laws, and the commissioners of banking in those several States see that the reserve requirements are observed. Now, how the Congress, by any legislation, can say that the States are wrong or that they are unwise in the amount of reserve requirement, as to reserve requirements as to nonmember banks, and impose these requirements as to member banks on nonmember State banks, I am at a loss to ferret out. By what authority could we, and how would we, enforce it, if we should declare that this should apply to nonmember banks? How would it ever be enforced?

Mr. McCABE. Congressman Folger, I am going on the opinion of our legal department, when they say that it is within the power of Congress to enact such a law to include nonmember banks. However, for the benefit of this committee, we will furnish you with an opinion of our legal department and a suggested amendment as to how this could be accomplished.

We hope to have that to you very shortly.

(The information above referred to appears at p. 124.)

Mr. SMITH. Will you include in your statement the basis for making the statement?

Mr. McCABE. Yes, sir.

Mr. FOLGER. The service that a member bank expects, for its membership, and the incentive to be a member, is the protection that every member bank has in calling on the Federal Reserve System when it needs rediscounts and accommodations, to call upon that institution to furnish that assistance. A nonmember bank has no such privilege.

Mr. McCABE. That is right. Well, I would say this: Having been in one of the Federal Reserve districts as chairman of the board in that district, the Federal Reserve maintains the finest kind of relationships with the nonmember banks. If any bank wanted some particular service or some particular help from the Federal Reserve bank, I know in that district, and I am sure in all districts, the Federal Reserve would do everything in its power to be of assistance to that bank, whether it was a member or a nonmember.

Mr. FOLGER. Do you mean to the extent of rediscounting its paper?

Mr. McCABE. No. I am saying within its power, it would try to be of assistance. But those banks have very close relationships with their correspondents, and in most instances those correspondents are members of the Federal Reserve System.

Mr. FOLGER. However, it is more a friendly situation than anything else?

Mr. McCABE. Yes; I think, of course, that a member of the Federal Reserve System has a distinct advantage.

Mr. FOLGER. What was troubling me was this: That situation obtaining, what would happen if a nonmember bank, whose reserves are fixed by State law, and the law administered by State banking commissioner, were to say, "No, I have nothing to do with the Federal Reserve System and they have nothing to do with me."

Mr. McCABE. Congressman Folger, you are pretty close to this banking picture. If you are interested, I can give you a digest which we have made, of the reserve requirements of the State banks.

Mr. FOLGER. I would like to have that, Mr. McCabe.

Mr. McCABE. This will give you what their reserve requirements are on all deposits, demand and time deposits. Then the States allow great latitude in the make-up of these reserves. That is, many States allow them to include their cash. Some of them allow them to include their Government bonds. Some of them allow them to include the State bonds they own.

Mr. FOLGER. But is it not true—

Mr. SMITH. Mr. Folger, do you wish that included in the record.

Mr. FOLGER. Yes, sir; I would like to have it.

Mr. McCABE. Would you let me introduce for the record a statement that might either be this one or one that is better? I will see that it is included promptly—either this statement or one that we think will serve your purposes better.

Mr. SMITH. Without objection that will be done.

(The information referred to is as follows:)

Reserve requirements of State commercial banks and trust companies, by kinds of deposits (demand and time), Dec. 31, 1947¹ (percent of deposits specified)

State	Uniform reserve requirements on all deposits ²	Different reserve requirements on—	
		Demand deposits ²	Time deposits ^{2,3}
Alabama		15.0	4.0
Arizona		15.0, 20.0	10.0
Arkansas	15.0, 20.0, 50.0		
California		12.0, 15.0, 18.0	5.0
Colorado	15.0, 25.0		
Connecticut		12.0	0
Delaware		14.0	6.0
District of Columbia		20.0	6.0
Florida	20.0		
Georgia		15.0	5.0
Idaho			
Illinois			
Indiana	(*) 15.0	(*)	(*)
Iowa		12.5	3.0
Kansas		7.0, 10.0	3.0
Kentucky		12.5, 20.0, 25.0	5.0, 10.0
Louisiana		7.0, 10.0	3.0
Maine		20.0	0
Maryland		14.0	6.0
Massachusetts		15.0	3.0
Michigan	12.0	15.0, 20.0	0
Minnesota		12.0, 15.0	5.0
Mississippi		15.0, 25.0	7.0, 10.0
Missouri		15.0, 18.0	3.0
Montana	10.0, 15.0		
Nebraska		15.0, 20.0	5.0
Nevada	15.0, 25.0		
New Hampshire		15.0	5.0
New Jersey		15.0	3.0
New Mexico	12.0		
New York		14.0, 20.0	0
North Carolina		15.0	5.0
North Dakota		10.0	5.0, 10.0
Ohio		15.0	10.0
Oklahoma		15.0, 18.0	5.0
Oregon		15.0	5.0, 10.0
Pennsylvania		14.0	6.0
Rhode Island		15.0	0
South Carolina		7.0	3.0
South Dakota	17.5		
Tennessee		10.0	3.0
Texas		15.0, 20.0	5.0
Utah		15.0, 20.0	5.0
Vermont		15.0	3.0
Virginia		10.0	3.0
Washington	15.0		
West Virginia		10.0	5.0
Wisconsin	20.0, 20.0		
Wyoming		12.0	10.0

¹ In most cases these are the rates prescribed in the State law itself. Where the law empowers banking authorities to change reserve requirements, the rates actually in effect on Dec. 31, 1947, were ascertained by correspondence or otherwise.

² Where 2 or 3 percentages are shown, the second and third apply to banks designated or approved as reserve depositories, or to banks in reserve cities, specified cities, cities with specified population, etc., as follows:

Arizona: The 20-percent requirement applies to banks in places with population of 50,000 or more.
Arkansas: The 20-percent requirement applies to banks designated as reserve agents; 50 percent to banks in places with less than 1,500 population with capital of \$10,000 or more but less than \$25,000.

California: The 18-percent requirement applies to banks in places with population of 100,000 or more; 15 percent to banks in places with population of 50,000 to 100,000.

Colorado: The 25-percent requirement applies to banks designated as reserve banks.

Iowa: The higher requirement applies to banks in reserve cities (designated as such under the Federal Reserve Act).

Kansas: The 20-percent requirement applies to demand deposits due to banks in State banks. For all trust companies, the reserve requirements are 25 percent of demand and 10 percent of time deposits, but there are only 4 trust companies (with little or no deposits) in the State.

Kentucky: 13 percent of demand deposits for central reserve city banks, but there never has been a central reserve city in the State.

Massachusetts: The 20-percent requirement applies only to trust companies located in Boston and within 3 miles of the State House.

Minnesota: The higher requirement applies to banks in reserve cities (designated as such under the Federal Reserve Act).

Footnotes continued at bottom of page 150.

Mr. FOLGER. It is true, Mr. McCabe, that it would be an almost idle thing to include member banks in these requirements as to reserves unless you included nonmember banks by legislation, is it not?

Mr. McCABE. It would be very, very unfair.

Mr. FOLGER. Well, in the first place it would be unfair.

Mr. McCABE. That is right.

Mr. FOLGER. In the second place it would hardly have the effect of curbing inflation?

Mr. McCABE. That is right.

Mr. FOLGER. Reckless lending for unproductive purposes.

Mr. McCABE. That is right. That is why I make that point, and the Board makes the point very strong in the statement I presented here this morning.

Mr. FOLGER. You called special attention to that as an amendment to your statement given to the Senate committee.

Mr. McCABE. We had a special meeting on that this morning and gave it special consideration.

Mr. FOLGER. I think you stated that the productive capacity was now about at its peak. That we could not go any further.

Mr. McCABE. No, I did not say we could not go any further. The gist of what I said was that it has not substantially increased over last year. I think the actual increase is 2 or 3 percent.

Mr. FOLGER. I am wrong. Here is what you stated:

At present, with the supply of money, or potential of money, readily available to buy the current output of goods and services at about three times the prewar level, the over-all physical volume of production of goods and services, so far as it can be measured, is probably a little over a half larger than the prewar maximum. Production, it is important to emphasize, is practically at capacity.

Mr. McCABE. Well, we have had an increase of say roughly 2 or 3 percent over last year, so that would indicate that we were practically at capacity, because we have certainly as near full employment as we can attain in this country.

Mr. FOLGER. That was rather based upon the idea that our labor is practically fully employed?

Mr. McCABE. Yes, sir.

Mr. FOLGER. And that perhaps for some other physical reasons we are near our present capacity, but that capacity could be enlarged if

Footnotes continued from page 149.

Mississippi: The 25-percent requirements against demand deposits and 10 percent against time deposits apply to banks in places with population over 50,000.

Missouri: The 18-percent requirement applies to banks in places with population of 200,000 or more.

Nebraska: The 20-percent requirement applies to banks in places with population of 25,000 or more.

Nevada: An additional reserve of 10 percent is required against reserve deposits due to other banks, but no State bank reported any such deposits on June 30, 1947.

New York: The 20-percent requirement applied on Dec. 31, 1947, to banks in the Boroughs of Manhattan, Brooklyn, and Bronx, in New York City, and Buffalo. Since that date the requirement for Manhattan has been increased to 24 percent.

North Dakota: The 10-percent requirement in the "Time deposits" column applies to "secured savings deposits."

Oklahoma: The 18-percent requirement applies to approved depositories.

Oregon: The 10-percent requirement applies to time deposits in noninsured banks, but there was only one such bank in December 1947 and it had no deposits (in June 1947).

Texas: The 20-percent requirement applies to banks with capital stock less than \$25,000.

Utah: The 20-percent requirement applies to banks in places with population of 50,000 or more.

Wisconsin: The 20-percent requirement applies to banks designated as reserve banks.

¹ The reserve requirements shown in the "Time deposits" column for Arizona, California, Connecticut, Massachusetts, Nebraska, Rhode Island, Utah, and Wyoming apply only to deposits in the savings departments of commercial banks and trust companies. Other time deposits are subject to higher requirements, but inspection of State banking department annual reports discloses that such deposits in California, Connecticut, Massachusetts, and Rhode Island are relatively small in comparison with deposits in savings departments; the same thing probably is true in the other States, to the extent they have separately operated savings departments in commercial banks.

² No statutory reserve requirements.

we could get the labor, could it not, and machine tools and factories could be constructed?

Mr. McCABE. Yes, sir.

Mr. FOLGER. In addition to those that we already have?

Mr. McCABE. Yes, it is a slow process. There is a possibility that you could lengthen out the workweek, per employee, and get a little more output, if the capacity is there. That would be in some industries and not in others.

Mr. FOLGER. Is there a danger, Mr. McCabe, that insistence upon this restriction of credit would have the effect of minimizing our production and our ability to purchase, and so on, rather than enlarging, or giving attention to enlarging production, and the national income put up to \$250,000,000,000 if we could. We do not want to restrict. We want to go ahead with full production.

Mr. McCABE. No, and if you will notice, the various charts, the expansion of loans currently are taking place primarily in the field of real estate and consumer credit and I would think that it would be the policy of the banks—and certainly of the Federal Reserve System—not to unduly hamper the expansion of credit for productive purposes.

Mr. FOLGER. As a matter of your observation, is it not a fact that the banks themselves are voluntarily, and as a business proposition, rather slow to make loans except for productive purposes?

Mr. McCABE. I think the voluntary program, as I said in my statement, of the American Bankers Association—and I know those activities are going along in other directions—is very constructive, and I hope it will be continued.

Mr. FOLGER. The banks and other lending agencies, such as building and loan associations, have loaned a lot of money for the construction of houses lately?

Mr. McCABE. Yes, sir. I think what will happen when you pass this legislation is that the psychological effect of it is going to be considerable. I think if we never upped the reserve requirements, the psychological effect would be a very desirable one.

Mr. TALLE. Will you yield, Mr. Folger?

Mr. FOLGER. I yield.

Mr. TALLE. That is exactly the point I had in mind when I made the statement that I did make at the conclusion of my interrogation, Mr. McCabe, and I wanted to ask you if you do not think that the psychological effect would be even stronger if we went back to the 40 and 35 percent reserve?

Mr. McCABE. I thought you had that in mind, sir.

Mr. TALLE. That is what I had in mind.

Mr. McCABE. I would say that there would be a psychological effect or psychological factor there. On the other hand, I would be strongly opposed to that move, sir, on the ground that I would not want to see that limiting factor put on the Federal Reserve at this stage.

Mr. TALLE. It is true, is it not, that credit has been pretty easy to get for a long, long time?

Mr. McCABE. And very cheap.

Mr. TALLE. And at a very cheap price, that is right.

Mr. McCABE. Yes, sir.

Mr. TALLE. And such positive action, in my opinion, as lifting those reserves back to 40 and 35 percent, would be concrete notice to the public generally that the too free, too easy, credit policy had come to an end. At least, that further credit expansion would be scrutinized with great care.

Mr. McCABE. I would say this, though: That if you should limit the Federal Reserve to that extent, it might be a very dangerous thing as I pointed out in my statement.

Mr. TALLE. You think the psychological effect would be too great?

Mr. McCABE. No, I am not thinking of the psychological effect. I am thinking of the fact that if you had continued further expansion, and you should run into a condition where an extraordinary amount of credit would have to be supplied, that you would not want that limiting factor.

Mr. TALLE. In other words, you favor the opportunity to expand credit even more than it is being expanded now?

Mr. McCABE. I think there are two reasons for that suggestion, Congressman Talle. One is the psychological factor which you have mentioned. I think there might be another one, and that is to limit the volume of Government bonds which the Federal Reserve might purchase.

If it is the desire of Congress to limit the amount of Government bonds that the Federal Reserve might purchase, I would rather see it done in a direct way rather than through that method.

Mr. TALLE. You think it would be interfering with your ability to protect the market?

Mr. McCABE. As I brought out in my statement, there are not only the factors which I mentioned, but also the operational factor should be considered.

Mr. TALLE. Thank you, Mr. Folger, for yielding to me.

Mr. FOLGER. Mr. Evans, I was trying to follow the chairman's analysis of this consumer credit. I am reading the last paragraph of your statement, I believe.

The Board has asked me to reiterate as strongly as possible that regulation of installment credit is a tool—but only a supplementary tool—for dealing with the problem of inflationary credit.

Now, the population has increased since 1939 by about 10,000,000. More buyers have come upon the market and you will find an increase in consumer credit. Based upon that realization that we have 10,000,000 more people, that increase in consumer credit is not so alarming. Is that a very necessary approach to make toward the handling of this inflationary situation?

Mr. EVANS. Mr. Congressman, it is not nearly as important as the bank credit and reserves. It is important in the whole credit picture. It is particularly so in that it has some control over the spending of a great number of people. There are many reasons to believe that the boom of 1929 was carried on beyond where it would have been without installment credit, and that the liquidation of that debt incurred at those very high prices prolonged the depression of the thirties. I think it is an important credit control tool. It cannot curb inflation by itself, and that is the point the Board wanted this committee to be sure of. But it is an important tool and would be very useful in connection with the tool of increased bank reserves.

Mr. FOLGER. Is it contemplated to restrict the prohibition against this consumer credit, or installment buying, rather, to the articles that you named a while ago?

Mr. EVANS. Yes, sir; where it is instalment buying. The regulation would also cover loans for other consumer purposes.

Mr. FOLGER. Well, outside of automobiles, those are mostly household goods, are they not?

Mr. EVANS. A good many of them; yes, sir. That is right. They are durable goods.

Mr. FOLGER. But really necessary to the life of every family, whether they have a small income or a large income?

Mr. EVANS. Well, a lot of people have them, and some people do not. It depends, I suppose, on their ability to pay for them. The down payment does not complete the sale transaction. I think that is the point that Chairman McCabe brought out, and which should be thought out very carefully. The down payment is just the first payment. Then you have to go forward and pay the balance. I would like to emphasize the point, if I may, that everybody, young or old, starting out in life, or well along the way, have always got to face the problem of their own personal budget. Should they go ahead and continue to go into debt for things that they cannot pay for, in a reasonable length of time, or should they just go ahead and mortgage their future earnings without any thought of when and how they are going to pay for them?

These regulations which were, in effect, under regulation W, provided for a reasonable down payment and a relatively short time to make the balance of the payments. Then the person was out of debt.

Mr. FOLGER. The thought occurs to me that these goods, contained in the list that you have, outside of one or two items, are goods that a person has to have to live, and there may be thinking along the line that we are trying to cut them off the ability to have a home in which to live.

Mr. EVANS. It did not appear to work that way during the 6 years of its operation, Mr. Congressman.

Mr. FOLGER. That was over what period, and until when, 1946?

Mr. EVANS. 1941 to 1947.

Mr. FOLGER. The thought was that unless it is a serious proposition, it is a restriction that people of moderate means and without money to buy things should not be prohibited from buying if they are necessities of life, unless it is a serious proposition.

Mr. EVANS. Of course, there is no prohibition. It is a case of whether the person can afford to make the purchase or not.

Mr. FOLGER. That is all, Mr. Chairman.

Mr. SMITH. Mr. Buffett.

Mr. BUFFETT. Mr. McCabe, I will not keep you long. It is getting late, but this is an important problem. You have spoken of various inflationary pressures and as I study your statement I get the impression very strongly that it is not your contention that these powers will enable the Federal Reserve System to stop credit expansion in the case of the banks and thus stop the inflationary spiral, is that correct?

Mr. McCABE. We think it will be a contributing factor to the retarding of the spiral.

Mr. BUFFETT. Do you think the entire bill would give a person in this country entire confidence that prices in the inflationary spiral would not be higher a year or two or five from now?

Mr. McCABE. No, I would not say it would give them complete confidence, but it would indicate to them that the Congress was reaching out to try to find those things which it could find to assist in this critical situation that we are in.

Mr. BUFFETT. You do not think, of course, that psychological measures are going to solve this problem permanently; do you?

Mr. McCABE. No, not entirely, and I certainly would not think this is entirely psychological either.

Mr. BUFFETT. Well, there have been some people who say that this is all a matter of public psychology.

Mr. McCABE. Well, I will say this, being a former businessman: Public psychology is a very important factor. On the other hand, it is certainly not everything, by a long shot.

Mr. BUFFETT. Do you know of any way of measuring the inflationary pressure resulting from the issuance of irredeemable paper money?

Mr. McCABE. No, I do not. Dr. Thomas could probably give you something on that.

Mr. BUFFETT. Has the Board made any studies in that direction. Dr. Thomas?

Mr. THOMAS. The paper money which is in circulation is the result of the individual's desire to hold money in that form rather than in the form of a bank deposit, and there is no great distinction between one or the other from the standpoint of the inflationary pressures. It does not make any difference at all what the money is redeemable in, as long as it is there and is being used, unless you have an assumption that because of its redeemability or the nature of its redeemability, you would have more money outstanding than you otherwise would have and there is no evidence of such a situation existing in this country.

Mr. BUFFETT. You think not?

Mr. THOMAS. No, sir.

Mr. BUFFETT. Do you know of any nation which has issued irredeemable paper money over a period of time, that has permanently halted inflation while it was so doing?

Mr. THOMAS. Any number of them, yes.

Mr. BUFFETT. Which ones?

Mr. THOMAS. Throughout the thirties, we had any number of, or any amount of irredeemable paper money in a period of inflation.

Mr. BUFFETT. Where was inflation halted?

Mr. THOMAS. Well, the British had paper money which was not redeemable during the thirties, and you had a depression, and not inflation.

Mr. BUFFETT. And Britain is using a police state as a consequence of that paper money.

Mr. THOMAS. That is because of war, not because of irredeemable paper money.

Mr. BUFFETT. Why is not Belgium or France using a police state, then?

Mr. THOMAS. Because they had a war which gave them a shortage of goods and they had to issue a lot of money to finance the war.

Mr. BUFFETT. Now wait a minute——

Mr. THOMAS. Of course, they could not have financed the war if they had had their money redeemable in something they did not have any of, but you do not stop fighting a war because you do not have any gold.

Mr. BUFFETT. Have you studied how the War of 1812 ended?

Mr. THOMAS. How it was financed?

Mr. BUFFETT. Yes, sir.

Mr. THOMAS. No, I have not.

Mr. BUFFETT. That might be illuminating. I want to get back to my original question. Do you know of any nation which over a period of years has halted rising prices where it was using irredeemable paper money?

Mr. THOMAS. I say, there have been any number of instances of nations that have had irredeemable paper money where you have not had rising prices.

Mr. BUFFETT. Over a period of time?

Mr. THOMAS. Certainly.

Mr. BUFFETT. Which ones?

Mr. THOMAS. The British during the thirties.

Mr. BUFFETT. Well, they are in the middle of irredeemable——

Mr. THOMAS. Any number of countries during the thirties.

Mr. BUFFETT. Well, they are in the middle of an irredeemable operation, and they have not come out from under the anesthetic, so those certainly are not sound examples.

Mr. THOMAS. What creates inflation is the amount of money that is in use; whether it is redeemable or not redeemable has very little to do with the case.

The only purpose of redeemability is to put a limitation on the money that can be issued. That is the only effect of redeemability from a domestic standpoint. You put a limit, and you can put the limit by other means than redeemability. In fact, redeemability might put a limit at times which is uneconomic.

Mr. SMITH. Will you yield, Mr. Buffett?

Mr. BUFFETT. Yes.

Mr. SMITH. What about the British pound sterling? Was it redeemable at face value, in gold?

Mr. THOMAS. Not during the 1930's.

Mr. SMITH. That is the point that Mr. Buffett is making.

Mr. THOMAS. And in the 1920's it was only redeemable in gold for certain purposes, and in certain amounts.

Mr. SMITH. And they changed the value at a certain time, did they not? I think that is what Mr. Buffett has reference to. He is speaking about the paper money that is redeemable at its face value, at the option of the holder thereof. That is your point, is it not, Mr. Buffett?

Mr. BUFFETT. Certainly.

Mr. THOMAS. Of course, if you had paper money redeemable in gold, and you had no gold, or only a limited amount of gold, there would only be a limited amount of money that could be issued. There would also be a limited amount of money that would be available for the economy, and if you wished to relate your money supply to the amount of gold that happens to be available regardless of whether the economy needed more money or less money to grow on, you could keep it in check in that manner, yes, sir.

Mr. SMITH. Pardon me again, Mr. Buffett.

Mr. BUFFETT. Surely.

Mr. SMITH. Would you let your statement stand that England had, during the twenties, I believe you said, redeemable paper, and no increase in prices?

Mr. THOMAS. In the 1930's, yes.

Mr. SMITH. But she had devalued, and therefore her paper was no longer convertible at the old value, at its old face value. We want to get that point clear because it is very important.

Mr. BUFFETT. Who has been better off in this country, Mr. Thomas, in the last 10 years, the person who converted dollar obligations into real property, or the person who converted real property into dollars?

Mr. THOMAS. Naturally the person who has property that has gone up in price in a period of inflation is better off than if he did not have it.

Mr. BUFFETT. Have you ever seen that process effectively reversed? As long as the country was using irredeemable paper money, that is?

Mr. THOMAS. I do not know, I do not think it has anything to do with it, sir. If you try to have redemption, you may force a deflation.

Mr. BUFFETT. Well, you said that you have no way of measuring the inflationary pressure resulting from the issuance of irredeemable paper money. Perhaps that is the greatest factor in this situation. Is that not possible?

Mr. THOMAS. I do not think so. I think there are plenty of evidences that we have inflation, and redemption is not one of them.

Mr. BUFFETT. Mr. McCabe, you were in the paper business for many years, were you not?

Mr. McCABE. Yes, sir.

Mr. BUFFETT. Are you buying pulp now as cheaply as you did 10 years ago?

Mr. McCABE. No, sir.

Mr. BUFFETT. Do you think you ever will buy pulp as cheaply as you did 10 years ago?

Mr. McCABE. I doubt it, sir.

Mr. BUFFETT. Let me ask you this about the business of contracts for pulp: Are the pulp producers willing to contract to deliver pulp over a period, at a fixed price, for as long as they did 10 years ago?

Mr. McCABE. No, sir, except that now there is some sign of their weakening just a little. They have gotten the price up so high that there are signs of some weakening.

Mr. BUFFETT. Yes, the supply and demand factor is entering into the picture.

Mr. McCABE. And then, of course, the price is so abnormally high now.

Mr. BUFFETT. How can you measure whether or not it is abnormal when you are measuring it against an irredeemable paper money? You are measuring it against "X" and you do not know what "X" is.

Mr. McCABE. Well, you are measuring it in comparison with other commodities, and when you do, it is out of proportion to the general level.

Mr. BUFFETT. You think that pulp has gone up more, as a raw material, than other raw materials?

Mr. McCABE. Yes, sir.

Mr. BUFFETT. But other raw materials are catching up pretty fast, are they not, of late?

Mr. McCABE. That is one of the critical points in manufacturing today. It is a question of raw materials. We were talking about credit controls a few minutes ago, for example. Take paper, and the pulp industry, which you have just mentioned. The dollars that go today into expanding pulp plants, or building of new pulp plants, are, to my mind, constructive dollars. It is questionable, however, whether the dollars spent for increasing or for making of paper are constructive dollars, in this particular period in which we find ourselves, because of the shortage.

Mr. BUFFETT. Of course, if you try to regulate that—

Mr. McCABE. I do not say regulate, but when you appraise, when the public talks of dollars for productive purposes—

Mr. BUFFETT. Well, maybe the person who is building the paper mill is doing that because he has lost confidence in the value of our currency 5 years from now. In that event he is making a good deal, is he not?

Mr. McCABE. Well, there is a considerable amount of money being spent today for the expansion of paper facilities, a lot of money. I would like to see the proportion a little heavier on the production of wood pulp, opening up new fields, Alaska, and other parts of the world, and have less go for the processing of paper. Do you get my point?

Mr. BUFFETT. Yes, certainly.

Mr. McCABE. If there was some way in which, through all industry, you could have a closer over-all scrutiny of the dollars expended in this area and in any other area—I am not advocating that, understand, but I say if there were some way in which you could more constructively funnel the dollar credits into those things that would constructively add to production, it would be very desirable.

Mr. BUFFETT. Is there any evidence in the history books that the men at the top who are political, who depend on politics for their position, would make such decisions in a constructive manner?

Mr. McCABE. I say I do not recommend it. I am just saying to you, in analyzing the extension of credit, where dollars go, that you do have to look at many factors.

Mr. BUFFETT. In proposing this regulation W, has the Board given any consideration to the lowered productivity that might result as a result of this restriction on purchases by working people in this country who use it?

Mr. McCABE. Governor Evans can answer that. I would say that certainly, as a member of the Board, I am sure that the policy of the Board will be pursued, if the Congress enacts this legislation, that a thorough and complete survey will be made of the whole field of installment buying, and then the various principals in that field will be called in for consultation as they were in the operation of this control for the 6 years during which it was in effect, and in order to make sure that when the control is put into effect that the items selected are the ones, that it is the general consensus of opinion that they are the ones to control.

Mr. BUFFETT. The political management in France, in England, and in Germany, somehow, have not done too brilliant a job along that line up to date, have they?

Mr. McCABE. I think that the situation, particularly in Germany—and I happened to be there last summer, and I had been there twice

before since the end of the war—is such that we tackled a very, very tough problem, and of course it is aggravated by the fact that we started out with four partners and are having great difficulty with one of the partners.

Mr. SMITH. Did you say “partners”?

Mr. McCABE. Should I say “allies”?

Mr. SMITH. Would you really call them allies?

Mr. McCABE. Perhaps, Dr. Smith, you could substitute a better word.

Mr. BUFFETT. Mr. McCabe, do you see any evidence that the political authorities will restrain inflationary pressures in this country effectively so long as they are enabled to issue bonds and currency without effective restraint?

Mr. McCABE. Of course, we are not adding to our total issue of outstanding bonds.

Mr. BUFFETT. Suppose that——

Mr. McCABE. We are reducing the outstanding volume of bonds.

Mr. BUFFETT. Suppose that this activity that is in discussion now should result in a recession in business, and two or three or four million people should be unemployed, do you think that Congress would be firm against any further tinkering with our deteriorating currency?

Mr. McCABE. Congressman Buffett, if I could read the mind of the Congress as to what they just might do in the future, I guess I would be a very wise man. I just have no idea what the Congress would do under such a set of circumstances.

Mr. BUFFETT. You probably have some notions based upon what has happened in the last several years, but I would not ask you to elaborate on them here.

Do you think that if this bill were passed in its entirety, that this problem would be solved for the foreseeable future?

Mr. McCABE. When you talk about——

Mr. BUFFETT. The entire bill.

Mr. McCABE. You are not just talking about our segments?

Mr. BUFFETT. No.

Mr. McCABE. I have confined my remarks to our two segments because I know a little something about those segments—not as much as I would like to know—and I know very little about the other segments.

Mr. BUFFETT. If you keep the price of Government bonds pegged, and the people who have capital in this country feel that the value of our money is being diluted, do you think that you can stop the inflationary spiral?

Mr. McCABE. I think that the enactment of these two bills would assist us in retarding the inflationary spiral, as I said before. As far as public confidence goes, I am amazed that the confidence is as strong as it is, in Government bonds, in our currency.

Mr. BUFFETT. Why are you amazed?

Mr. McCABE. Pardon?

Mr. BUFFETT. Why are you amazed?

Mr. McCABE. I would put it in another way: I am amazed that there is such strong confidence on the part of the people generally in the safety of Government bonds and the safety of our currency.

Take our currency, for example. Every place you travel in the world—and I have traveled in a great many of the countries of the

world in the last 2 years—everywhere you go, people want American dollars. Our own people have great confidence today in the dollar. Even though it is worthless—I mean it will buy less than it did 2 or 3 years ago—their confidence is very strong.

Mr. BUFFETT. Do you think that confidence is being strengthened by the present rate of Government spending, or lessened?

Mr. McCABE. I think that does alarm the people somewhat, the fact that they see that there is not as wide a margin between governmental receipts and expenditures as we had last year.

Mr. BUFFETT. Do you think that that in itself is a decisive factor in the situation?

Mr. McCABE. I do not say it is a decisive factor, but I say it is an important factor.

Mr. BUFFETT. That is all, Mr. Chairman.

Mr. McCABE. Mr. Chairman, may I say to Congressman Buffett, because he has such an interest in the subject he has brought up, that there is nothing that we would like better than to have you come over to the Federal Reserve for an hour or 2 hours, or whatever time you would like, and meet with Dr. Thomas and Dr. Bopp of the Philadelphia bank, a keen student of finance, and take as much time as you would like to explore these questions as fully as you would like to explore them.

Mr. BUFFETT. If you will permit, I will give them something to do right now. Tell them to direct my attention to any place in history where a nation using irredeemable paper currency over a period of years has been able to stabilize its economy during that time.

Mr. BOPP. We have had a curious case in that respect, Congressman Buffett. It is the case of Sweden, during the First World War when the rest of the world was inflating and shipping gold to Sweden to purchase war materials. The Swedish Government refused to buy gold. It backed off the gold standard and the interesting thing is that the value of the Swedish kroner became greater than the gold content. The reason, of course, is that the amount was limited. So you have the odd case of a specific country which was on a paper standard, in which the money was worth more than the gold into which it was redeemable because they would not buy gold rather than not sell it. So it is a reverse sort of situation. It is a curious one, but it is an historically accurate one.

Mr. BUFFETT. That is probably the exception that proves the rule.

Mr. SMITH. That was due to the fact that more gold was offered to Sweden than Sweden was capable of absorbing. As I understand it, there was a similar situation in Switzerland.

Mr. BOPP. Yes, so that it is an international problem and a gold-standard problem. An individual country is affected by what the rest do and it is forced to have inflation if it insists on remaining on the gold standard. So you can have inflation—to say nothing of deflation—with gold and with redeemability.

Mr. BUFFETT. You never have any disastrous inflations in such circumstances.

Mr. BOPP. Well, the Swedish felt that the inflation was serious enough to refuse to go ahead buying gold.

Mr. BUFFETT. That was the Government, of course. I do not know whether their price level went up a hundred percent or two hundred percent. Certainly it was not anything like the inflation which has taken place in Germany, Italy, and other countries.

Mr. BOPP. Quite right. Yet, as I recall, it was as great as we have had in the United States since 1940.

Mr. BUFFETT. Yes; the inflation we have had to date is just a small part of the potential inflation of our banking system. Is that correct?

Mr. BOPP. Which is one of the reasons why we are here.

Mr. BUFFETT. You do not think this bill will cure it?

Mr. BOPP. It is one aspect of it.

Mr. MULTER. Mr. Chairman.

Mr. SMITH. Mr. Multer.

Mr. MULTER. I know the witnesses have had a long day and I will be very brief.

Do you believe that anything that would tend to curb the inflationary spiral will strengthen the people's confidence in our Government's ability to meet its obligations?

Mr. McCABE. I think so; yes, sir.

Mr. MULTER. You and your associates today have been dealing with two distinct though related problems. One is the matter of bank reserves, primarily concerned with commercial credit, and the other consumer and installment credit.

Consumer prices have risen in the last 10 years about 70 percent, while in the same period, consumer credit and installment credit have increased 100 percent; is that not so?

Mr. McCABE. I would have to check the figures. I assume they are correct.

Mr. MULTER. They are taken from your own tables.

Mr. McCABE. Yes, sir; I assume that is correct.

Mr. MULTER. They are taken from charts, on pages 22 and 23 and 70 and 71 of your book of charts. As you restrict credit, you necessarily limit demand, and thereby tend to stabilize prices?

Mr. McCABE. That is right.

Mr. MULTER. And then as the demand decreases or the supply increases, you can lift or curtail your restrictions on credit?

Mr. McCABE. That is correct.

Mr. MULTER. When we talk about installment buying in relation to the necessities of life, is it not true that there are very few of the so-called necessities of life included in consumer credit and installment buying? The greatest part of the items that make up the bulk of your installment credit are such items as automobiles, refrigerators, washing machines, radios, television sets, and such items. You can hardly consider them necessities, much as we would like to have everybody in the country have them.

Mr. EVANS. They are not rent, food and clothing.

Mr. MULTER. Rent, food and clothing are not included.

Mr. EVANS. That is right.

Mr. MULTER. And that is not to be controlled in any way by this regulation?

Mr. McCABE. That is right.

Mr. MULTER. Short-term credit in the main is held by the banks, is it not?

Mr. McCABE. Largely, the bills and certificates are held by the banks and the Federal Reserve System.

Mr. MULTER. And they are mainly dealt in by the banks?

Mr. McCABE. That is right. Some people have them who have excess funds for a short period of time.

Mr. MULTER. Now, this question is addressed to Dr. Thomas. Paper money can hardly be considered irredeemable as long as it can be freely dealt with to pay for services or buy property; is that not right?

Mr. THOMAS. I think that is right. I think that is the important use of money.

Mr. MULTER. It is important to bear in mind whether we use paper money or gold, that if we cannot get the property or the services, whether we want to pay with gold or paper, they have the same value or lack of value, and that as long as you can use your paper money to establish a bank credit, pay for services or buy property, it is not a strictly proper definition to say that paper money is irredeemable.

Mr. THOMAS. That is right.

Mr. MULTER. Mr. McCabe, may I address this question to you as a businessman rather than as an official of the Government? If you were sitting around the directors' table of a business, or with the board of directors of a big business corporation, attempting to determine the price policy your company would put into effect during the next year, and the situation presenting itself was that you had every reasonable expectation that you would sell some \$90,000,000 worth of your products during the coming year, and that you could on that \$90,000,000 product have a gross sales price of \$100,000,000, and if that situation occurred that you make a \$10,000,000 profit and your taxes would be \$7,000,000, leaving you with a net of \$3,000,000. As against that you had a choice of making only a \$5,000,000 profit and paying a \$2,000,000 tax and still having a net of \$3,000,000, which do you think your board would—what policy do you think your board of directors would pursue so far as prices are concerned?

Mr. McCABE. Well, of course, its primary interest would be in the net after taxes.

Mr. MULTER. Yes.

Mr. McCABE. On the face of the proposal as you state it, they would not be so vitally interested in the form of the tax, in the way you have stated it, as in the net of the business after taxes—that is on the hypothetical case you state.

Of course, you would have to have an analysis of the taxes to see to what extent the form of taxes affected the business before the net—that is so far as the future growth of the business is concerned. But, to answer your question, your hypothetical question, their primary concern would be the net after taxes.

Mr. MULTER. And if the net would be the same after taxes, and you had a choice of either paying the high tax because you boosted your price or took the low price, in my example, if your price was \$95,000,000, you would have \$3,000,000 net, and on the other hand if you had this excess-profits tax, and your gross was \$100,000,000, you still would have your \$3,000,000, what would a good business director do under those circumstances? Would they seek the \$100,000,000 price of that or the \$95,000,000 price, having in mind that after you deducted everything you would still have the same net?

Mr. McCABE. Well, I think the average businessman—may I say it this way: It is very difficult to answer a hypothetical case, Congressman. I would have to know a little more about the nature of the tax before I could answer that. But I would say this generally: That if you do a volume of business of a \$100,000,000, or \$90,000,000,

as you have stated it, your primary interest is whether, in the accomplishment of that sales volume during the year, you have constructively done things to help your business in the future.

You want to be sure that you have laid the proper foundation that year for the future growth of business. Therefore, I would want to know a few more factors before I make that decision.

Generally speaking, however, I would say that we would like to do as large a volume of business as possible and get a reasonable return. In that reasonable return we want enough to pay a fair dividend and to put aside a substantial reserve for future growth.

Mr. MULTER. Of course. Primarily my question was directed at this: If you were going to sell your product, and you have your choice of increasing the price and paying away that increased price in taxes, or continuing the same price, you would continue the same price.

Mr. McCABE. There is no question about it. You have stated it more simply now and I agree with that heartily.

Mr. MULTER. In other words, I was directing myself to the question of possible excess-profits tax. If the businessman knew that he could not make an additional profit, a larger profit this year than last year because he would have to give it away by way of excess-profits tax, such a law would tend to keep prices down in those spheres.

Of course, the small man is not affected by that situation. It would simply apply in the case of the larger business corporations.

Mr. McCABE. You come over some day. I would like to discuss taxes with you.

Mr. MULTER. Thank you very much.

Mr. McCABE. Thank you, sir.

Mr. SMITH. Just one word on that matter.

You would take all that the traffic would bear, and that would depend upon your competition and a lot of the other factors, is that not true?

In other words, after all, a firm does not in itself fix prices. It is the market.

Mr. McCABE. That is right, sir.

Mr. SMITH. It is the market that fixes prices.

The committee will adjourn until tomorrow morning at 10 o'clock at which time we will hear Marriner Eccles.

(Whereupon, at 6 p. m., an adjournment was taken until 10 a. m. the following day, Tuesday, August 3, 1948.)

INFLATION CONTROL

TUESDAY, AUGUST 3, 1948

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The Committee reconvened, pursuant to adjournment, at 10 a. m., Hon. Jesse P. Wolcott, chairman, presiding.

Present: Messrs. Wolcott, Smith, Talle, Sundstrom, McMillen, Kilburn, Buffett, Hull, Banta, Spence, Brown, Patman, Folger, and Buchanan.

The CHAIRMAN. The committee will come to order, and we will proceed with the hearings on the inflationary situation.

Mr. PATMAN. Mr. Chairman.

The CHAIRMAN. Mr. Patman.

Mr. PATMAN. Mr. Chairman, the question of State banks is entirely new, that is, the question of placing the Federal Reserve requirements on State banks, and I think the chairman should notify the Federal Deposit Insurance Corporation and other agencies, which can give us the information we will probably need in dealing with this question, to make sure they are available to produce that information when we want it. It occurs to me that the information which has been presented so far is entirely inadequate. Whenever you make the State banks adopt the reserve requirements of the Federal banks, and when it is admitted by Mr. McCabe that the reserve requirements of the States are very much lower than the Federal Reserve requirements, it is likely to cause quite a bit of trouble. It raises a very serious question and problem, so I would like to have more information, if the chairman would notify the people having to do with the State banks.

The CHAIRMAN. I think it raises a very interesting legal question.

May I ask the clerk if the counsel for the Federal Reserve has put a statement into the record yet having to do with that question?

The CLERK. Not yet. They expect to have it ready either this afternoon or tomorrow.

The CHAIRMAN. Well, let us wait and see what he presents.

Mr. PATMAN. That is perfectly all right.

The CHAIRMAN. We have with us this morning, gentlemen, Mr. Eccles, who has appeared before this committee on several occasions and on various matters.

We are very glad to have you, Mr. Eccles. Perhaps it might be interesting, if you have no prepared statement, to give us somewhat of a history of the actions of the administration in relation to inflationary tendencies and related subjects.

**STATEMENT OF MARRINER S. ECCLES, GOVERNOR OF THE
FEDERAL RESERVE BOARD**

Mr. ECCLES. Mr. Chairman and members of the Committee, as Governor of the Federal Reserve Board, and as a past chairman, one who has been with the Federal Reserve Board for nearly 14 years, and as one who has watched very closely the inflationary developments, it is an opportunity and a privilege for me to meet with this committee again.

Everyone, I think, recognized, when this country commenced a large defense program, and later got into the war, that Federal deficits were going to develop on an increasing scale, that the Government's requirements for war purposes were going to utilize a large amount of the materials and labor that normally would be available for the civilian economy, and that the people would be receiving purchasing power from the Government's large and increasing purchases that would exceed the supply of civilian goods and materials available to them, unless taxation was so high that it drew into the Government a sufficient amount to pay for the Government's war program on the basis of a balanced budget. That has never been done, and it was not done in our case.

Taxes were increased to the fullest extent that the public was willing to bear, and that Congress was willing to vote. This left a large residual amount of purchasing power in the hands of the public. That purchasing power came from bank-created money. It came from bank credit which was necessary to finance the Government's deficit.

In order to prevent inflation and maintain stability, this country, within a reasonably short time after the war started, put into effect a full harness of controls, the allocation of scarce materials by the War Production Board, building permits, wage controls, price controls, rationing, export licenses, and excess-profits taxes as well as increased individual income taxes and excise taxes, with the result that we got through the war with a comparatively small inflationary development. I think from 1940 to 1945 the cost of living went up something like 25 percent—which was rather a satisfactory record in view of the fact that the public debt was increased from forty-some-odd billion dollars to over \$270,000,000,000, and that the supply of money—bank deposits and currency—increased more than two and a half times.

It should have been apparent to all that with the public having such a large amount of purchasing power in the guise of bank deposits, currency and Government securities—which was potential purchasing power—and with a backlog demand that had accumulated for all kinds of goods, particularly consumer durable goods and housing, over a period of 5 years, that to take off, as was done in 1945, practically all of the controls, with the exception of price control—which was completely ineffective removed from the other harness of controls—made an inflationary spiral inevitable.

We should not be surprised that there was this inflationary development, but under the circumstances we should be surprised that the inflationary development has not been greater than it is.

The public have not only had what would be considered their current requirements, the requirements that they would have had for the various goods and services had there been no war, but the public, you

must remember, have been trying to buy automobiles, houses, and many other consumer durable goods, and industry has been trying to buy the capital goods that it would normally buy, plus the backlog demand that had accumulated. So that, in effect, you have had an effective demand—and by effective, I mean a demand backed up by purchasing power and easy credit that should take years to fill—the current plus the backlog—which the public have been trying to fill in a period of 2 or 3 years. How can you fill a demand for goods and services that would normally take years to fill in a period of 2 or 3 years, without getting inflation?

You have the example of housing. The cost of housing, since the war ended, has more than doubled. Easy credit for housing, as has been made available by the Federal Government under title VI and under the Veterans' Act, has not necessarily produced more housing. It certainly has produced an inflation in the housing field. I use that merely as an example.

Easy credit certainly has not produced more automobiles or other consumer durable goods. But the demand has been so great in the field of automobiles that possibly it could not have been met even if they had all been sold on a cash basis.

Now, we have been talking about what we are going to do with this inflationary situation every year since the war ended. And up to the present time, it seems to me, there has been practically nothing done to deal with the inflationary pressures which should have been obvious, but there has been quite a good deal done to add to the inflationary pressures that existed when the war ended.

I realize it is difficult to resist the numerous minority pressure groups. Each one wants the benefits of inflation for himself, but he wants the others to pay for them.

The farmer wants a floor under his prices, but he does not want a ceiling.

The real-estate people, the building-materials people, want easy credit so that they can readily dispose of, at inflated prices, the homes and materials they have to sell. But they certainly resist having any excess-profits taxes in order that the Government might recapture some of the profits that are thus made.

Labor has always wanted price control, but they have vigorously resisted wage control.

The bankers want higher interest rates, but they do not want the Federal banking agencies to have increased power over the expansion of credit.

You know the familiar pattern. And now, after 3 years, you have been called together to consider this problem which has been with the Congress constantly, and the American public constantly, and there has been little or no willingness to face up to it, realistically, either by the public or by the Congress, or by the administration.

This situation has gone so far that to stop the inflationary development could well bring about a deflationary development.

You have a great many inflationary forces still in the situation. The supply of money is still expanding through bank credit. Although the Federal Government's fiscal policy, due to a favorable budget situation, has been anti-inflationary, to the extent of about \$14,000,000,000, that has been almost completely nullified by the inflationary effects of a bank-credit expansion of \$12,000,000,000.

A favorable budget picture, which is the most effective anti-inflationary force that could be available to the Government, because it would deal with the basic causes, because it would be reversing the trend that existed during the war, which created the inflation, is no longer available, and there are prospects, next year, of a budgetary deficit which will be increasingly serious if we still have the inflationary situation. I see little hope of securing a budgetary surplus so long as we have an increasing military expenditure with no terminal point, or so long as we have a world-aid program with no terminal point, in such amounts as this Government is now spending, and so long as the cost of maintenance of the veterans' program, interest on the public debt, and other expenditures of the Government that seem impossible to reduce, continue—unless sufficient revenue is made available through taxation to meet the appropriations made by the Congress.

There is not much use talking about controlling inflation unless the fiscal policy calls for a budgetary surplus. Although bank-credit controls are necessary, desirable, and would be useful and effective, they are supplementary to a sound fiscal policy.

It would be impossible, if the country should run into budgetary deficits, to put into effect a restrictive monetary and credit policy.

The purpose of this hearing this morning, as I understand it, is primarily to consider what can be done, particularly in the monetary and credit field, to curb inflationary development. That seems to me to be the most important anti-inflationary proposal in the President's program.

The program taken as a whole seems to me to be more of a political program than an economic one, because there is in the program action called for which would be very inflationary.

The mistake, of course, as I have indicated, was made back in 1945 and early 1946, when the entire harness of controls was prematurely removed, and that includes the removal of excess-profits taxes, which was possibly one of the major mistakes that was made at that time, because that opened the door for a justifiable demand for increased wages.

The American public—and especially those minority groups, minority pressure groups, who were trying to get some advantage for themselves—are primarily, or at least partially, to blame.

What we are interested in at this time, of course, is not so much recrimination. What we are interested in is what can now be done, at this late date, to overcome as far as possible the mistakes of the past.

I do not believe it practical to put back a complete harness of war-time inflationary controls, and I do not believe that to put back some and leave off others would do the job. I do believe that it is too late to avoid a serious deflationary adjustment at some point. The disequilibrium and the distortions have already been created. I do believe that the inflation can go further if nothing is done and a budgetary deficit develops. It can be long postponed, and can be catastrophic in its effects.

I do believe that the sooner inflationary development is stopped, the less serious the adjustment, or the deflationary developments, will be.

I do believe it essential that credit controls of sufficiently broad power and authority, both in the consumer credit and in the bank reserves field, be made available.

That can be, at the moment, the most useful, the most practical, and the most effective.

I do believe that everything within the power of the administration and the Congress should be done to maintain a budgetary surplus.

I do believe that the Federal Government should do everything within its power to encourage the State to postpone every expenditure that it is possible to postpone, and set an example to the States by doing likewise.

I do believe that the Federal Government should not, for what seem to me political reasons, encourage a housing program in excess of the amount of labor and materials available, and encourage further inflation thereby.

I do believe that the Federal Government should do everything within its power to bring down food prices, by encouraging more and not less production.

I do believe that we should—and I may sound naive in this regard—adjourn political considerations, and I say that for both parties, and consider honestly and openly the economic facts of life.

Mr. Chairman and members of the committee, I have spoken, as you observe, off the cuff and from my heart, about this general problem of inflation which you are considering, and I am sure that there are many questions that you may desire to ask, particularly with reference to this matter of bank credit control, as covered in the President's message, and which happens to be in my particular field.

You make like also to consider the question of housing credit, which is also covered in the President's message. The Board has given considerable thought to its inflationary impact.

The CHAIRMAN. Mr. Eccles, you have implied that the President's program might in some respects be inflationary. Do you care to comment generally upon the President's program, generally or specifically, in that respect?

Mr. ECCLES. Well, it is rather involved. I have indicated, Mr. Chairman, that there are many aspects of the program which are inflationary, and others which, of course, are deflationary, and that it thus tends to balance off.

Now, as to getting into each of the specific subjects I must say that I would like to avoid getting into the specific subjects, because it seems to me that the discussion could be endless.

The CHAIRMAN. We are here to discuss the President's program with respect to inflation. You have indicated that the mistake was made when we removed the excess-profits taxes in 1945. The President's first proposal is to recommend that the excess-profits tax be reestablished, in order to provide a Treasury surplus and to provide a brake on inflation. Perhaps you would like to comment on the statement made by Mr. Fred Vinson who at that time was Secretary of the Treasury, in his appearance before the Ways and Means Committee, wherein he said—

clearly the repeal of the excess-profits tax will stimulate production. Today we are starved for new houses, new cars, new radios, and the like. The best offense against the use of our wartime savings to bid up prices on these scarce items is to remove the scarcity. Production and more production is the key. To this end

the elimination of the oppressive influence of the excess-profits tax would make a real contribution.

Mr. ECCLES, I, of course, did not agree with that statement, and I so told Mr. Vinson. I happened to have a very close relationship with him at that time, when he was Secretary of the Treasury and still have a very friendly relationship. I still have a very high regard for him.

The CHAIRMAN. I might say that the committee has a very high regard for him.

Mr. ECCLES. But I did express opposition to it, and I decided to write a memorandum to him giving him my reasons why I thought a mistake was being made, and I wrote him a letter in which I said:

Referring to our brief conversation when you expressed surprise at my opposition to the repeal of the excess-profits tax at that time, I am venturing to enclose a memorandum outlining my reasons for my position.

I have some excerpts from this memorandum here that you might be interested in, for the purpose of getting the other side of this story.

The underlying reasons for maintaining high taxes apply with equal or even greater force during the critical period of postwar because, first, we still face an unbalanced budget. Every dollar of Government expenditures not raised by taxes will have to be borrowed, and, to the extent that banks furnish these funds, new supplies of money will be added to the already enormous accumulation of liquid funds in the hands of the public.

Taxation is the last bulwark against inflationary forces because of the weakening or the removal of other controls such as the War Labor Board exercised over wages, and hence prices, or such as the War Production Board exercised in the construction field with building permits.

The most prudent course, at this juncture, would be to defer tax reductions until such time as the supply is more nearly in balance with demand and we have begun to approach at least a balanced budget.

At this stage we would be wise to err on the side of too much rather than too little revenue. Taxes can always be reduced. Since the basic problem today is one of shortages of goods in relation to demand and purchasing power, a prudent fiscal policy requires that high taxes be maintained in order to reduce the public debt so far as possible.

Not only is the backlog of demand unprecedented, but the supply of money in the hands of prospective buyers is at an all-time high and will be further increased as employment in peacetime occupations occurs.

The situation would be entirely different if we were confronted with a progressive deflation, if inventories were in excess of effective demand. Then the problem would be to create more goods and to give employment, and fiscal policy would call for, first, reducing the taxes in the lower income brackets in order to increase purchasing power.

Any further reduction would benefit primarily those best able to pay. This is particularly true with respect to the repeal of the excess-profits tax. By and large, business and industry, which is in the excess profits, has never been so well off. Never have such vast accumulations of cash and equivalent in Governments been bigger; never have there been bigger earnings after taxes and never have there been such glowing prospects of profits that are to be made in filling the unprecedented backlog of demand from domestic as well as foreign sources.

It is highly significant that expectations of outright repeal of the excess-profits tax are having four adverse effects: It is doing much to lift the stock market; it is drawing into this field speculative funds. It is whetting the appetite of labor for bigger demands, reinforced by strikes. It is inducing corporations in the excess profits group to avoid further sales in the last quarter of this year, because obviously profits after January would go untaxed, so far as excess profits are concerned. It is inviting inventory speculation in anticipation of profits resulting from rising prices.

and so forth.

The argument that business needs a special tax incentive to produce and to employ people at this time is inconsistent with the basic economic facts. The

war demonstrated that if business has orders it will go ahead, producing and furnishing employment notwithstanding high taxes.

Business has never had such a peacetime prospect for orders as it has today because demands, foreign and domestic, are so large and so far in excess of supply. With such intense demand, and the sharp competition for markets, production would go ahead if there was no reduction in the excess-profit taxes.

And I did advocate some reduction at that time.

It cannot be logically held that the removal of this tax will give needed incentives to existing business. As for new business enterprise, its main problem is to obtain the materials and the labor in order to get under way in competition with established industry. Instead of benefiting from repeal of the excess-profits tax, the smaller corporations would lose the advantage of the exemption; and to repeal the excess-profits tax and leave the normal tax as it is would work still further to the advantage of the larger, and to the disadvantage of the smaller, corporations, generally speaking.

The argument is frequently made that the repeal of the excess-profits tax will make no great difference in revenue collections because corporations will pay in dividends to the stockholders what they would otherwise be taxed in excess-profits tax. This would only be true, however, if dividends received were taxable at the same rate and if there was a sufficient effective tax on undistributed earnings to induce corporations to pay them out to individuals instead of retaining them and thus adding to the value of corporate securities,

and so forth.

It seems to me that the record, since the repeal of this tax, has proven that it did not stop inflationary developments by inducing enough further production, as was indicated. Overlooked was this terrific backlog of demand, supported by the very large volume of purchasing power, and the principal effect of this tax was, of course, to take off any pressures that industry might have for raising prices, because, after they got into the excess-profits tax, the benefits of price increases would go largely to the Government. Repeal of the tax, of course, gave them a greater incentive to raise prices because the benefit of the price increases went to them.

It also took away from the corporations a great deal of any resistance to raising wages, and we saw very promptly, with little or no resistance, a first round of wage increases, which was certainly a corollary to the repeal of the excess-profits tax.

We then saw a second round of wage increases, and now we have had a third round.

Of course that is the inflationary cycle. It has been supported by an expanding credit and expanding money supply; so that we have, first, an excessive supply of money and purchasing power in relation to goods and services. That creates an excessive demand, and that brings about a price increase. That brings about increased profits. And, of course, you cannot blame labor, wherever they are able to get increased wages to take care of their increased cost of living, for doing so. And of course they not only, in many instances, got their increased cost of living taken care of, but they got in excess of their increased cost of living.

So that the cycle is: Increased credit, increased prices, increased profits, and increased wages. You have an inflationary cycle. It is not just wages and prices.

I merely indicate here the fact that this tax was removed, I think, prematurely, as were other controls, and that we lacked, in the country, the patience to make haste slowly; to realize that our need for housing and our need for consumer durable goods, our need for expansion of capital facilities, could not be met overnight; that it

could only be met gradually, where our capacity to produce would not only take care of the normal demand but also could gradually build up the backlog demand.

We did not realize that, and we have the result that I have indicated.

The CHAIRMAN. Mr. Eccles, why did we reduce the gold reserves from 35 percent and 40 percent to 25 percent, do you recall?

Mr. ECCLES. I would like before answering that to say just one more word on the question of the excess-profits tax. I am not favoring its reenactment at this time because it would have to be part of a whole program, and I think the question is a very involved one. It would have been an easy matter to continue the tax in force and effect and to have gradually reduced it until it would have been practical to repeal it. But at this late date, to impose an excess-profits tax, the question first arises: On what basis? You have to first determine what is excess; and to determine what is excess you have to determine the formula for deciding the basis upon which to apply it. I will not go into that, but that is a very involved and a very difficult thing to do, and certainly it cannot be done in any short time, in a special session of Congress. I think I, therefore, would not favor its reenactment. I think that our whole tax structure needs to be overhauled—and that is a major job—and that it should not be done piecemeal by an attempt to impose, at this time, an excess-profits tax.

The CHAIRMAN. Do you think the administration made a mistake in taking it off in 1945?

Mr. ECCLES. Well, I just read my letter and excerpts from the memorandum. The date of that was October 20, 1945.

Mr. BUCHANAN. Do you think the Congress made a mistake in reducing taxes this year?

Mr. ECCLES. I do. And I have so stated, publicly, and before committees.

Mr. BUCHANAN. Does the President have the power, at the present time, to check the inflationary spiral? It has often been repeated here that he does have the powers; that the Federal Reserve Board has the powers. Does the President have the powers at the present time?

Mr. ECCLES. I do not think the President has the powers at all. And certainly the Federal Reserve Board does not have the powers.

Mr. PATMAN. If you will pardon me for interrupting, Mr. Chairman, specifically, does the President have the power to increase the rediscount rates of the Federal Reserve banks?

Mr. ECCLES. No; he does not, and I would like——

Mr. PATMAN. He has no such power?

Mr. ECCLES. No.

Mr. PATMAN. And one other question. Does he have the power to prevent the Federal Reserve System from guaranteeing the par value of Government bonds?

Mr. ECCLES. That is a responsibility of the Federal Reserve open market committee. The Federal Reserve System is, of course, a public organization. The Federal Reserve Board is a public body, appointed by the President, for long terms, and confirmed by the Senate. They are not a part of any administration.

Mr. PATMAN. And a member is not subject to removal by the President?

Mr. ECCLES. No, sir; any more than a justice of the court is subject to removal by the President.

The CHAIRMAN. Just a moment——

Mr. ECCLES. I was just going to say that the Federal Reserve Board is an independent body, an agent of the Congress, as shown by the legislative history of the Banking Act of 1935, when Senator Glass insisted that the Secretary of the Treasury, who was formerly the ex officio Chairman of the Board, and the Comptroller of the Currency, who was the head of a bureau of the Treasury, should both be left off the Board that was provided for in that act, for the reason, as I said, that there was too much political pressure exercised, and that he could speak as one who knew, because he had, during his period as Secretary of the Treasury, felt that the Board was unable to exercise its independence in a way that it should be able to exercise it.

Now, it has been indicated, in the press, that the Board is a part of the administration. As I have indicated, it is not a part of any administration. It is expected, of course, to cooperate with, and work with, in every way it can, any administration, and it is supposed to advise with the Congress, and it is required to make its reports to the Congress.

Now, the President does have the responsibility of designating the Chairman of the Board, and the Chairman is looked upon as being the liaison between the President or the administration and the Board or the banking system.

I always considered, while I was Chairman, that it was my responsibility to try to persuade the administration, as far as I could, to go along with the views that the Board might have with reference to the questions upon which the Board had responsibility and to try to maintain a liaison that would maintain a harmonious relationship. Now, I was not demoted. I just was not reappointed as Chairman. That is, of course, as I have said, a privilege of the President. The Chairman is the liaison, and, of necessity, the administration must have a liaison with such an organization as the Federal Reserve System. I just wanted to make clear that relationship and what seems to me the responsibility of the Board, for the record.

Mr. SPENCE. Mr. Chairman.

The CHAIRMAN. Mr. Spence.

Mr. SPENCE. Mr. Eccles, if the controls—price control, allocation, priorities, and rationing—had remained unweakened, and had continued, what effect do you think that would have had upon the conditions which now exist?

Mr. ECCLES. If what?

Mr. SPENCE. If controls had been continued for a longer period, what effect do you think that would have had upon present conditions? You said pressure groups have weakened them. I think that is true. Suppose they had been continued, however, what effect do you think that would have had upon the inflationary conditions that now exist?

Mr. ECCLES. I just do not think you would have the inflation that you now have.

Mr. SPENCE. You think that could have controlled it?

Mr. ECCLES. I do not think there is any question about it. In spite of Canada being so close to us, and being under the pressure and influence of the actions that we have taken, they have not had anything like the inflation that we have had. And that certainly is true of other countries—I am thinking of Australia, for example. Of

course, they are small countries. Great Britain possibly could not have survived without the imposition of the very high tax structure and the very tight controls of every kind. She would have had an inflation such as some of the continental countries have and such as some of the Asiatic countries have. But considering her short supply of goods and the fact that she was in the war from the beginning to the end, and that she had all the monetary inflationary pressures, yet she, through maintaining and keeping controls, has been able to survive and maintain an excellent degree of stability, considering the problem she had. We had no such problem because we had no destruction of our productive capacity. Our productive capacity was greatly increased during the war. Our population was increased. Our manpower was increased. And we are a country of great natural wealth, great facilities for production. So that we had less reason than these other countries, which had much shorter supply, and which did not have within their own borders the resources that we had.

I think we have done an exceedingly poor job in dealing with the inflationary situation, and we could have done a very good job.

Mr. SPENCE. So you think the weakening of the controls is the cause of our present predicament?

Mr. ECCLES. I think the taking off of the entire harness of controls is the cause of our present predicament.

Mr. SPENCE. Do you not recognize that those controls were so weakened that they became ineffective and were allowed to die?

Mr. ECCLES. You are speaking of price control?

Mr. SPENCE. Price control, rationing, and so on.

Mr. ECCLES. Well, that is a very different matter. On the question of the removal of price control, I was in favor of the vetoing of the price-control bill, because I felt that by the summer of 1946 price control was largely encouraging black-market operations and tax evasion, that price controls could not stand alone with the remaining harness of controls taken off, and that the greatest friends of the continuation of price control were the black market operators and the tax evaders, just as the bootleggers were the greatest friends of prohibition. It was a perfectly natural development. So the taking off of price control in the fall of 1946 was certainly overdue.

I think it is perfectly obvious that if you have price control you have to have rationing, and you need allocation of your scarce materials, and you need building permits, you need wage controls, you need export licenses, and tax control. All that was just part of a harness, and to think that this cart could be pulled by a horse without a harness, of course, just does not make sense.

Mr. SPENCE. Do you not think that a large part of that was due to the fact that those controls were so weakened that they did not operate? They operated very well during the war, did they not? They saved the Government billions and billions of dollars in its purchases, and they became so weakened, as you said a while ago, by pressure groups, that they were ineffective at the time they were removed. I do not think they could have been continued, under the circumstances.

Mr. ECCLES. No. This is what happened—and I want to give you the record on that, because they were not weakened by the pressure groups. Naturally the pressure groups were all fighting to get rid of them. The farmers were anxious to get rid of price controls, and labor wage controls, and business excess-profits taxes, there is no ques-

tion about that. But they were doing a good job until they were removed. And this is what happened:

The sudden end of the war in 1945 brought drastic reductions in military procurement. The question of maintaining controls became immediately a major public issue. The policy of the administration on this matter was enumerated on August 18—4 days after the war ended—by Executive Order 9599. The President instructed the Federal agencies to move as rapidly as possible, without endangering the stability of the economy, toward the removal of price, wage, production, and other controls, and toward the restoration of collective bargaining in a free labor market. The day following the surrender of Japan all controls over manpower were dropped, and OPA removed rationing restrictions on gasoline, fuel oil, and all processed foods and heating stoves. Several hundred items were removed from price control within the first hundred days after VJ-day.

On August 21, 1945, the WPB discounted the controlled-material plan—upon which allocations were based—which had become the cornerstone of the War Production controls.

The controlled-material plan was a relatively simple device for dominating the industrial economy by giving WPB complete controls of a few strategic commodities such as steel, copper, lumber, and so forth. A great many control and priority orders were revoked by the end of August, including controls over most metals, except tin, lead, and antimony. Industrial construction restrictions were first eased and then, on August 15, 1945, construction L-14—which was the building permit upon which you determined where your materials were going to be used, whether they were going to go into housing or something else—was revoked by WPB and with it went all limits on new construction.

You had an inflation in that field which is quite fantastic, and you have had scandalous profits made by builders and promoters, who started with little or no capital, and the building industry, such as lumber and other concerns, with excess-profits taxes off, have made profits that certainly would not stand publication.

Before the end of August, we took off controls over transportation and so forth, of all kinds. That may have been all right; I do not know.

The Price Administrator was specifically instructed by the President, on August 18, 1945, to take all necessary steps to assure that the cost of living and the general level of prices would not rise.

However, reconciling labor demands for higher wages and industrial demands for higher prices, and profits, presented difficulties which the stabilization program was in the end entirely unable to solve.

Mr. BROWN. Mr. Eccles, are you making any suggestion as to what we should do now to curb inflation?

Mr. ECCLES. Yes, sir; I did, I think before you came in.

Mr. BROWN. All right. I will read your testimony.

Mr. PATMAN. The only thing I heard you say—

The CHAIRMAN. Very briefly, would you restate what you recommend at the present time?

Mr. ECCLES. What I said at this time is this: It seems to me that credit controls are the simplest, the easiest, and possibly the most effective instruments that could be made available, and yet they are only supplemental to a sound budgetary program which would pro-

vide for a budgetary surplus, or certainly avoid deficits. I indicated that in the field of housing, everything should be done to avoid continuing the inflationary effect of the housing program, because otherwise the credit instruments cannot be very effective, on the one hand, if the Government is stimulating or encouraging an expansion of credit on the other hand, beyond the available supply of building and materials.

The CHAIRMAN. Specifically, would you recommend the passage of S. 866, the Taft-Ellender-Wagner bill, at the present time?

Mr. ECCLES. No; I told the Senate committee the other day that I felt that that would be a very inflationary instrument. I would favor the objectives of that bill as a deflationary program which should be held in abeyance and used to cushion a deflationary development. If you use all the deflationary instruments in an inflationary period, what are you going to have available to cushion a deflation?

I think the expansion of unemployment insurance, the increasing of old-age pensions, are likewise anti-deflationary weapons. Anything that the Government can do to postpone nonessential public works or other expenditures, whatever they may be even though the appropriations may have been authorized should still be done at this time so as to maintain, if possible, a budgetary surplus.

Mr. BUCHANAN. How about the slum-clearance and urban-redevelopment program, under S. 866? Should those programs be begun now?

Mr. ECCLES. I do not think so; no.

Mr. BUCHANAN. The planning of them?

Mr. ECCLES. I think it is all right to do planning now, and I think anything that could be done at this time to get these building codes of the various cities on a rational basis should be done. Anything that can be done in preparation to meet a deflationary situation, should it develop, of course, should be done.

Mr. PATMAN. Mr. Chairman, I would like to ask Mr. Eccles some questions.

Mr. SPENCE. I would like to ask one more question, first.

Do you recommend that the reserve requirements of the State nonmember banks be under control?

Mr. ECCLES. I said the other day that it would be my recommendation that no legislation be passed if the nonmember banks are going to be excluded from this control. The discrimination, at the present time, against the member banks, is already pretty severe. Certainly, if the national banking system is to be maintained and made strong, it should not be put at an additional very great disadvantage as against State banks because the national banks must be members of the system.

Mr. SPENCE. I recognize the dual banking system, but the State bank is a creature of the State, organized under the laws of the State.

Mr. ECCLES. There is nothing proposed in this bill—I should not say the bill—there is nothing in my proposal that nonmember banks should be covered as well as the member banks that I believe to be unconstitutional. I am not a lawyer, but I can give you these as my reasons: The Wagner Labor Relations Act, it was determined by the Supreme Court, covers all banks because they are engaged in interstate commerce.

I understand the Wage and Hour Act likewise covers banks, for the same reason. And certainly there has been no question about the Board's regulation W covering consumer credit. It has always applied to all banks. Regulation U, covering margins on collateral loans, has always applied to all banks.

There has certainly been no discrimination in those fields, and there is nothing unusual in this proposal that the nonmember banks be covered.

The program that the Federal Reserve Board authorized me to present before your committee and before the Taft committee at the last special session of Congress, in November, to consider these problems, covered the nonmember banks.

The program that was submitted on April 13 in response to the President's Economic Report before the Joint Committee on the Economic Report—Mr. Taft's committee—includes the nonmember banks.

There has been unanimity, always, on the part of the Board and of the staff—and, I think, the System—that the nonmember banks should be included in any credit control measure.

The CHAIRMAN. Mr. Eccles, do you think that should prevail in the absence of an emergency?

Mr. ECCLES. Yes, I certainly think it should prevail in the absence of an emergency.

The CHAIRMAN. Regulations T, U, V, and W were promulgated in compliance with powers given to the President under the Trading With the Enemy Act.

Mr. ECCLES. No, no; only W.

The CHAIRMAN. Where do you get T, U, and V?

Mr. ECCLES. T and U were established under the Securities Exchange Act of 1934.

The CHAIRMAN. Could he impose those credit controls now?

Mr. ECCLES. Yes.

The CHAIRMAN. Will you review what T, U, and V were?

Mr. ECCLES. Regulation U is the authority of the Board to impose margin requirements on collateral loans, secured by listed securities, made by banks.

The CHAIRMAN. Is that something in addition to these marginal requirements?

Mr. ECCLES. No, that is part of it. That is the one that covers banks; there is another regulation that covers the brokers.

The CHAIRMAN. Is that T?

Mr. ECCLES. That is T.

The CHAIRMAN. What is V?

Mr. ECCLES. V was under a wartime Executive order that provided for war production loans guaranteed by the Military Establishment, and they were administered by the Federal Reserve System, which acted as the agent for the Army, Navy, and the Maritime Commission in the V-loan program. That has all disappeared with the liquidation of the war.

The CHAIRMAN. In your opinion, if the Federal Reserve is given the authority to increase reserve requirements, by what percentage would they increase them for the different bank categories?

Mr. ECCLES. Well, the proposal is 10 percent.

The CHAIRMAN. I know that. That is the ceiling. What do you think the Board might do with respect to increasing the reserve requirements? Would they raise them 1 percent, 2 percent, 5 percent, 7 percent, or 10 percent?

Mr. ECCLES. That, of course, would be impossible for me to say at this time. As a matter of fact, if the authority existed the effect of the authority itself is perhaps sufficiently important so that use of the power may not be needed, or, at least, it may be needed to a far lesser extent.

The CHAIRMAN. What are the total reserves of all the banks now?

Mr. ECCLES. The reserve requirements, do you mean?

The CHAIRMAN. Total reserves.

Mr. ECCLES. You mean in dollars and cents?

The CHAIRMAN. Yes. What I am trying to get at is how much a 10 percent increase in your authority, if it was used, would increase the reserves.

Mr. ECCLES. Well, this authority would give the Board power to increase the reserves, roughly, something like 11 billion dollars—that is, reserve requirements.

The CHAIRMAN. Twelve billion dollars?

Mr. ECCLES. No, I do not think it is 12 billion dollars. I said around 11 billion dollars.

The CHAIRMAN. In April or May of this year, in your testimony before the Joint Committee on the Economic Report, you said this, in advocating an increase of 10 percent in the reserve requirements for demand deposits and 4 percent for time deposits: That that would give the Federal Reserve System power to increase reserve requirements about 12 billion dollars.

Mr. ECCLES. Yes. Well, I say 11 billion dollars because the statement you have quoted included a power, which the Board had not used, of 4 percent in the case of the central Reserve cities—New York and Chicago. That amounted to about a billion dollars. Five hundred million dollars of that authority has been used.

The reserve requirements of New York and Chicago are now 24 percent. The Board has the authority to increase them another 2 percent.

Mr. SPENCE. Is it not true that the reserve requirements in most State banks are very small?

Mr. ECCLES. The difficulties with the proposal to eliminate the non-member banks are these: I will try to give you some of the objections that I have, and I think this represents the Board's view as well.

State banks, at present, are required to carry only—and it varies by States—10 to 15 percent in reserves in the banks of Reserve cities. That can be carried in cash in their vaults or in balances with the city correspondent, and some States permit them to carry Government or municipal securities.

Mr. BROWN. Right there, Mr. Eccles, suppose the State has a requirement for a certain amount? And suppose the Federal Government comes along and establishes a requirement of another amount? What do we do in those circumstances?

Mr. ECCLES. We do not interfere with that. The State can make any requirement they want.

Mr. BROWN. We never undertook to regulate the reserves of the State banks up to now.

Mr. ECCLES. We do not undertake to regulate the reserves of the State banks even now. All we do is say that in addition to the reserves the State banks are required to carry they must carry an additional amount of 10 percent—the same as member banks—with the Reserve banks of the district.

Mr. BROWN. I do not think your comparison is very good. I do not see how, under the Constitution, you can go ahead and regulate the reserves of State banks. In other words, you would practically control State banks.

Mr. ECCLES. No, there is nothing against the dual banking system in the proposal at all, for the very reason that at the present time possibly 2,000 of the State banks of the country are members of the Federal Reserve System. All of the State banks could be members of the Federal Reserve System and you still would have a dual banking system. This in no way destroys the dual banking system, but it prevents the State system from destroying the national system and the Federal Reserve.

Mr. BROWN. I understand that when you are a member of the Federal Reserve you have to abide by their rules.

Mr. ECCLES. They would not be members at all. They would have locked up, in effect, a reserve equal to 10 percent of their demand deposits, and that could be supervised and policed by the State bank supervisor. So that, so far as the Federal Reserve is concerned, it would have nothing whatever to do with the regulation or the supervision of State nonmember banks, with the exception that whatever requirement they made of the banks in any class of cities which are members of the System would apply also to the nonmember banks in the same cities.

There is no reason why a nonmember bank would join the System—certainly if this additional reserve requirement is imposed on members only. Even today it is practically impossible to get members into the System. There has been practically no growth in membership in the System, because the advantage—especially if you are a bank in a non-Reserve city—of not being a member is great because of the discrimination that is placed upon membership.

For instance, a member bank in a non-Reserve city today must carry 14 percent of its demand deposits in collected funds with the Reserve bank of that district. They must also carry such cash and currency in their vaults—and that is not considered a part of the reserves—as are required.

In the State banks, cash and currency is considered part of the reserve requirement.

A member bank must also, for its own convenience and as necessity to its operation, carry, I would say they average, at least another 10 percent of their deposits in balances in what we call their city correspondent banks so as to enable them to get certain services that the Federal Reserve cannot and does not give them.

I have an enumeration of some of the discrimination that now exists which I would like to read.

A member bank today, for practical operating purposes, has to carry at least, I would say, 25 to 30 percent of its deposits in cash reserves and balances with its city correspondents, whereas the balance that the country bank has with its correspondents for certain services also takes care of its reserve requirement.

Now, if we impose an additional 10 percent on the members and do not apply it to the nonmembers, I would expect a large exodus of the smaller member banks, including the national banks; they would withdraw from the Federal Reserve System because it would be so advantageous to them from an earnings standpoint.

The CHAIRMAN. Mr. Eccles, would it be convenient for you to be back this afternoon?

Mr. ECCLES. Yes.

The CHAIRMAN. I think I should make the statement now that if we can finish with Mr. Eccles this afternoon, Mr. Snyder, Secretary of the Treasury, will be here tomorrow morning, and it is our hope that we may conclude the hearings with Mr. Snyder's testimony and go into executive session tomorrow afternoon.

The committee will recess until 2 o'clock.

(Whereupon, at 12:30 p. m., the committee recessed, to reconvene at 2 p. m. the same day.)

AFTERNOON SESSION

Present: Messrs. Wolcott, Smith, Talle, Sundstrom, McMillen, Kilburn, Buffett, Hull, Banta, Nicholson, Spence, Brown, Patman, Monroney, Folger, Buchanan, and Multer.

Mr. SMITH. The committee will come to order.

I believe Mr. Patman had the witness when we recessed for lunch.

Mr. PATMAN. Mr. Eccles, what caused, more than any one thing, the depression of 1920?

Mr. ECCLES. The inflation of 1919 and 1918.

Mr. PATMAN. That was the greatest contributing factor, was it not?

Mr. ECCLES. Yes, sir. If you had not had the war inflation of 1917, 1918, 1919, and 1920, you would not have had the severe deflation, credit deflation of 1920 and 1921.

Mr. PATMAN. The point I want to ask your opinion on is this: What caused it to start?

Mr. ECCLES. Restrictive credit policy.

Mr. PATMAN. That is right. It caused the banks to call their loans and as soon as the banks called their loans, everything collapsed, is that not correct?

Mr. ECCLES. That is right. But that policy at that time was an extremely drastic policy.

Mr. PATMAN. What was the credit policy which was initiated by the banks at that time which was so rigid, Mr. Eccles?

Mr. ECCLES. You had no open market committee in existence.

Mr. PATMAN. I understand.

Mr. ECCLES. The only instrument of control was the discount rate of the member banks—that was the principal instrument of control. I do not mean the member banks, I mean the Reserve banks.

Mr. PATMAN. It did not work, however, did it?

Mr. ECCLES. Each of the Reserve banks acted separately, upon their own initiative, in that field of Reserve bank credit in their district. There was no uniform, over-all, national credit policy, as there must be today with an open market committee, composed of the Board and five of the presidents, which committee is able to buy and sell in the open market and allocate its purchases and sales to each of the Reserve banks without having to get the consent or approval of each of the Reserve banks. This was put in the Banking Act of 1935.

The discount rates must be approved every 2 weeks and if the Board does not approve of the rates submitted it can determine the rate or the rates on the various types or classes of paper.

In 1920, the member banks were very heavy borrowers from the Reserve banks. The war was largely financed by the customers of the private banks buying Government securities and borrowing to do so from the banks where they did business. They were encouraged to buy and to borrow to buy, and a great deal of the financing was done not by the banks buying the securities directly—I am speaking of the commercial banks now—but by the banks loaning to their customers, and the customers borrowing and putting up the bonds they had purchased as collateral.

Now the banks in turn borrowed from the Reserve bank of their district, whereas in this last war the financing was done by the Open Market Committee purchasing Government securities in the market and thus supplying reserves to the member banks—not the member banks borrowing at all. The effect of it was to supply reserves to the member banks and thereby they were able to stabilize and hold the Government security market on an even basis to finance the entire operation, and it was only through the method which we developed, I think, that it was possible to finance a 200-billion-dollar war debt upon a basis of complete stabilization.

Mr. PATMAN. Do not overlook the point I am trying to bring out, Mr. Eccles. What restrictive policy did the Board put into effect which caused the immediate calling of loans in 1920? In May, was it not?

Mr. ECCLES. Yes, sir. Well, what was done was this—and I think it was done by the Reserve banks. I do not know that the Board disapproved of the policy, but at least the initiation of the restrictive policy I believe was largely made by the Reserve banks of the district, which raised the discount rates. But you can raise the discount rate and still a lot of borrowing may be done. But they put pressure on the banks to pay off —

Mr. PATMAN. Pay the Federal Reserve?

Mr. ECCLES. That is right; pay off the loans they had.

Mr. PATMAN. And that compelled local banks to call upon their customers?

Mr. ECCLES. That is right. That caused the local banks to call upon their customers and it caused a serious credit deflation, because the source of credit was denied or nonexistent. That is not involved at all in this proposal before us now.

Mr. PATMAN. Did they raise the reserve requirements?

Mr. ECCLES. They had no authority to raise the reserve requirements. They had no authority whatsoever. The reserve requirements were fixed in the statute, by the Federal Reserve Act.

Mr. PATMAN. And it was changed in 1935?

Mr. ECCLES. The authority to change came in 1935.

Mr. PATMAN. Now, in 1936, the soldiers of World War I were paid about a billion and a half dollars, on June 15, 1936. The reserve requirements of the banks had not been changed since 1917, I believe, but within about 2 months after the money was paid, the reserve requirements of banks were raised; is that right?

Mr. ECCLES. That is correct.

Mr. PATMAN. Why did you raise the reserve requirements back at that time?

Mr. ECCLES. Because we had a growing speculative development, particularly in inventories. Inventories had grown about \$5,000,000,000. There was a very rapid accumulation of inventories, as prices were rising rather rapidly. That was one of the factors.

Mr. PATMAN. You think that was caused by the payment of that money to the veterans of World War I?

Mr. ECCLES. Well, I think it was a psychological situation. A lot of people felt that the depression was over and now was the time to buy, and there was a lot of forward buying. That tended to help it. There was also, in that year, about a \$4,000,000,000 public works and public relief program, I think, whereas in 1937 you had no veterans' bonus and the social security taxes went into effect and amounted to about a \$2,000,000,000 tax on the public, in excess of the expenditures for relief. So that the entire budget picture was changed very rapidly from a substantial deficit to practically no deficit. I am speaking of a cash deficit.

Mr. PATMAN. Well, we had what was called a recession in 1937, did we not?

Mr. ECCLES. Yes; but if the Board had taken no action at all on the reserves, I am sure it would have made little or no difference, for this reason: That increasing the reserve requirements did not extinguish the excess reserves or raise the interest rates.

Mr. PATMAN. I know, but you raised them three times, Mr. Eccles. You raised them a hundred percent in 1 year.

Mr. ECCLES. That is right; but there was more than enough excess reserve—you see the gold imports had created such a large amount of excess reserves that the interest rate went to zero. The Government was borrowing, in one period, actually, at a negative interest rate on its Treasury bills. The reason for that was there were \$7,000,000,000 of excess reserves in the banking system, with absolutely no opportunity or place for loans or investment.

It was not as though there were a lot of Government bonds available to the banks. The increase in reserve requirements in 1937 did not even sterilize the excess reserves that had already been created by the gold imports that had come in.

Mr. PATMAN. What I cannot understand is why you would, for the first time in 20 years, not only raise the reserve requirements, but double them in 1 year's time.

Mr. ECCLES. We only had authority for 1 year.

Mr. PATMAN. But you doubled them in 1 year?

Mr. ECCLES. That is right.

Mr. PATMAN. Why would you keep on doing it if it had no effect?

Mr. ECCLES. For the very reason that it is not the most flexible instrument. The open market operation is a much more flexible instrument to deal with. Increased reserve requirements have to apply across the board and not to the individual bank. They have to apply generally to a class of banks. Therefore, it is not the most desirable or flexible instrument to use if the open market power is available.

Now, all we could do, toward increasing reserve requirements at that time, was to wipe out to a considerable extent the excess of reserves, so that the open market operation could function and be effective.

I would say as of now that we would not need, nor want, nor desire, the authority to increase reserve requirements if the traditional power and authority that was given to the Reserve System in 1913 could be made effective. We are not asking for additional power. We are asking for a partial substitution of the power that we are unable to use so long as we stand ready to support the public credit, so long as we stand ready to support the long-term 2½-percent rate. That in itself makes the use of the discount rate and the denying of the bank's credit unusable, or ineffective. For this reason the banks do not need, nor are they willing, to borrow today, because they have a portfolio of Government bonds which is equal, for the banks as a whole, to about 50 percent of their total deposits. Those deposits were created when they purchased those Government bonds. That is where they came from. That volume of bonds is about \$65,000-000,000. All the banks need to do is to sell some of those bonds or bills or certificates, and they immediately get funds to take care of their loan expansion.

The Federal Reserve stands there today to support that market, as they are the only residual market. So that the control over credit is in the hands, today, of 15,000 banks, and not in the Federal Reserve authorities. If we could withdraw from the support of the Government market, if we could deny the banks the reserves that they are able to get through the sale of the Government securities that they have, instead of borrowing from the Reserve banks, we would have a sufficient control to absolutely stop the expansion of bank credit, because, as we withdrew from the market, we could then raise the discount rates to such an amount that it would be very, very effective.

Today to raise the discount rate is practically meaningless, except as it may have a psychological effect—because the banks would just sell us the bills and the certificates that they own, the bills yielding about 1 percent, certificates, 1½ percent, with the discount rate being 1½.

In other words, the discount rate is still a little higher. Even with the discount rate as low as 1¼, the total borrowing of the Reserve System is something like \$200,000,000, which is practically nothing.

Now, if we should raise the discount rate to 1½, 1¾, or 2 percent, it would be purely academic. So long as we support the Government short-term rate, that is.

Now, in that connection—and this is all part of the same story—I think that the present Government short-term rate has been in effect too long. I think that the short-term rate should be permitted, by the Treasury, to rise.

There is authority existing today, of course. That is not a matter for Congress. The Federal Reserve has tried to support a short-term rate agreeable to the Treasury, or to persuade them to permit the rate to go up. We were able to persuade the Treasury to permit the short-term rate to go up from ¾ to 1 percent and from 1 percent to 1¼, and thus take the pressure off the long-term 2½-percent rate on Governments which got down to the point of selling at 2.2 percent. But within the last few months the Federal Reserve has been unable to persuade the Treasury to favor the raising of the short-term rate. Therefore, the open market committee has supported the bill and the certificate market at the short-term rate established by the Treasury.

Now, I do not believe that there is any justification for pegging, or supporting the long-term rate at 2½, and also pegging and supporting

a short term rate at 1½, or on bills at 1 percent. I feel—and I know the Federal Reserve people as a whole feel—that we must, so far as we can see it at the present time, and I can give you reasons, if you want them, continue to support the 2½-percent rate.

Mr. PATMAN. The only reason is that it would break every bank in the country if the bonds went much below par, is it not?

Mr. ECCLES. Well, I do not think it would do that.

Mr. PATMAN. It would be possible, however?

Mr. ECCLES. If they had to sell the bonds while they were down, it would certainly impair some of them. But I will mention it in just a minute, if I can, Mr. Congressman, but to try to peg the short-term rate, and hold that down below the point at which it would normally go in a free market in relationship to the 2½-percent rate does not to my way of thinking make very much sense in the present situation. I would certainly feel that if Congress should give to the Board the authority to increase the reserve requirements, as has been proposed by Chairman McCabe when he appeared before this committee yesterday, that they would also favor, as the Federal Reserve does, and I would also hope that the Treasury would favor, permitting the adjustment in the short-term rate to a market rate. Then we would let the discount rate go up.

Now, there may be some people who think that that would create such uncertainty that that will tend to slow up borrowing. I do not think any such thing. I think that the raising of the short-term rate is minor insofar as its monetary effect is concerned, but it is an important part of the overall credit-control mechanism, and I feel that it would not be logical or sensible to increase the reserve requirements of all banks and keep the discount rate down one and a quarter, which would have to be done, and force the short-term rate and continue to hold the short-term rate down to 1½.

Now, aside from its monetary and credit effect, there is a serious question of bank earnings. Especially is that true of the banks in the central Reserve cities and in the Reserve cities. I do not say that that is major, but it is certainly a factor, because all of the commercial paper and business rates are related to that short-term rate.

Their costs have gone up, just like other costs, due to the inflation, very rapidly, and their earnings have dropped very, very fast during the past year. To increase the reserve requirements by 10 percent, which would force them to dispose of 10 percent of their earning assets—their bonds, would affect their earnings quite seriously, and that really is where some of your formidable objections to this bill come in. I feel that as a part of this control, if it is going to be made effective, the short-term rate should be permitted to rise. Failing to permit it to rise, and increasing the reserve requirements and diminishing their reserve assets would put the banks under pressure to go out and seek loans at as high rates as they were able to find, maybe longer term loans, even though it did impair some of their liquidity. We feel that if you should increase this reserve requirement, take away from them that much of their earning assets, that that should be partly overcome by permitting the short-term rate to rise. We would not force it up. It will automatically rise. It cannot go very high if you support the 2½-percent rate. It is not going to create very much uncertainty, so long as you hold the 2½ percent rate, because the range

with which the short-term rate can rise would be within its present $1\frac{1}{2}$ and I would say possibly $1\frac{1}{2}$ percent. That in itself is not a very great rise.

So I do not agree with those who say that is all that is necessary, because it creates so much uncertainty. It cannot create uncertainty so long as you hold the $2\frac{1}{2}$ -percent rate. But if that rate rises, our discount rate rises, in the trend of a credit tightening, and that, in turn, will reflect itself on all other loans and investments. If your dollar is diminishing in price, then, certainly the cost of interest should go up some. The owner of money, the savers, the insurance people, and the investors generally certainly should not be the only ones to suffer to the extent that they have suffered, by holding down the interest rate beyond what seems to be necessary.

Now, getting to the $2\frac{1}{2}$ -percent rate, people say, "Well, why do you not let the $2\frac{1}{2}$ -percent rate go up, so that it will reflect the demand for savings and for investment, so that more people will save and not spend so much? If you let the rate go up, it would be a very important anti-inflationary factor."

Well, to let the $2\frac{1}{2}$ -percent rate go up raises some very, very serious problems, and these are some of the problems that it raises:

In the first place, it would unstabilize the entire Government bond market, and when the public debt represents 60 percent of the entire debt, you are not playing with any small and minor item. You are playing with \$250,000,000,000 of a total debt structure of around \$400,000,000,000. That is not the tail of the dog. That is the dog. If you are going to have stabilization in the Government market, you cannot have the public in a position of complete uncertainty as to how far the price of securities—Government bonds, and, of course other bonds and mortgages—would reflect the price—municipals; they would all reflect the price of a drop—the uncertainty as to what the market value of their assets as well as what the cost of interest was going to be. That is especially true for the reason that the Government has falling due in the next 12 months \$49,000,000,000 of debt—\$49,000,000,000 in 12 months. Another \$46,000,000,000 within the next 5 years. There is close to a hundred billion dollars in 5 years, with \$49,000,000,000 in 1 year.

The job of refunding that much debt is no simple and easy task in a market that is unsupported and unsecured and unstable. How do you price the issues each week and each month that you have to offer to the public? Who is going to buy the issues, and at what price, when they do not know what the price may be after they have bought them? How can you finance long-term or short-term municipals, and corporate and other securities that are falling due every day and every week, and when new money is being raised, when there is no basis upon which to price them?

We have not had any situation such as this before. This is completely unprecedented. And this idea of trying to say what we ought to do because of what has been done, is no more realistic than trying to say, "We are going to fight the Third World War on the basis of the way in which we fought the First World War." And I say that the Federal Reserve Board does not have the authority, as has been claimed by some which they have failed to use, and because of which, if they did use it, this request for new authority would not be necessary. That just is not so, unless we are willing to use the traditional

authority, the power that we have, to withdraw from the important and vital support of the public debt, and raise the discount rate, and deny the banks reserves. Otherwise they would get such reserves as they want. Without more power and authority over the banks, or by withdrawing from support of the Government market—either without one or the other—then, I say that this Federal Reserve System is the greatest engine of inflation that man could contrive, and the limits to which additional money can be created by the will of the banks is fantastic.

Now, we have pointed this problem out over and over since 1945. The Federal Reserve Board has been conscious of this problem during the war, and in our report to the Congress in 1945, the Congress was told that the Board lacked the power to deal with the monetary expansion of credit.

In 1946 we told the Congress.

In 1947, before the Taft committee, on the 25th day of November last year, we told the Joint Committee on the Economic Report the same thing.

On April 13 of this year, I appeared for the Board before the same Taft committee and again told the Congress of the inadequacy of powers to curb bank credit expansion, and you have now had \$12,000,000,000 of bank credit expansion during the past 2 years on top of an inflationary situation, a monetary inflation situation, which even without that \$12,000,000,000 was explosive, and you have nullified, by the bank credit expansion, the entire effect of a favorable fiscal policy in which the Government has taken \$14,000,000,000 more away from the public than they put back.

And I say that that condition is likely to continue. True, during the first quarter of this year, it was deflationary, as I pointed out before this committee and the Taft committee. It was deflationary because during that period there was such a large amount of taxes collected—\$7,000,000,000, practically, in the quarter. That money was used to pay off bank-held debt, and the banks were under heavy pressure during that quarter. It is a time of seasonal decline, too. But in spite of all that pressure, there was still an expansion of total bank credit on balance, and for the first 6 months of this year there has been an expansion of bank credit of, I think, \$1,300,000,000.

There is every indication that with the growth in prices, with the general inflationary situation, there will be now an accelerated bank credit expansion for the rest of this year, adding to the money supply.

Mr. PATMAN. I want to ask you one other question, Mr. Eccles, and I will be through. The charge has been made that the President has the power to check inflation by increasing the rediscount rate of the Federal Reserve banks, and stop the Government's support of the bond market. You covered that in two parts this morning, but I want to ask you whether that is true or false.

Mr. ECCLES. The President has no such authority. The Congress gave that authority to the Federal Reserve Board, on the question of the discount rate. The initiation comes from the banks—from the Reserve banks, but they are required to submit, under the law, discount rates every 2 weeks, and we, therefore, for practical purposes, have the authority to control them because we could refuse to approve them and instruct them to fix a rate.

Mr. PATMAN. And in the support price, the Open Market Committee has the entire power?

Mr. ECCLES. The Open Market Committee has the power and the authority to operate in the open market.

Mr. PATMAN. And the President has no power or authority on either one of these issues?

Mr. ECCLES. No; but the Secretary of the Treasury has the responsibility for raising such money as the Government needs to meet the appropriations made by the Congress that are not covered by taxes. The Treasury likewise has the responsibility of refunding the public debt.

Now, it is true, I suppose, that legally the Open Market Committee could say to the Treasury, "You must price your securities at such and such a price. We will not support the market at the prices that have been outstanding." But, as I brought forth before this committee, the Open Market Committee and the Federal Reserve Board are in favor, with the Treasury—and I think with the great majority of bankers and the public generally—of holding the long-term rate. Now, where there is the difference of opinion is in the question of the short-term rate, and it is hoped that we can negotiate short-term rates that will reflect the market demand for short-term money in relationship to our support of the 2½ percent long-term rate. So the President cannot be charged with responsibility for not using that power, and I said before this committee in December, in answer to questions of Chairman Wolcott, when we were being somewhat criticized for not tightening up and letting the market adjust, as I recall the matter, that I was sure that the Open Market Committee, if the Congress felt that we should withdraw support from the market, if they would want to indicate that and take the responsibility for it, that certainly we would do it. But so far the Open Market Committee has felt that we were choosing what we considered to be the horn of the dilemma which seemed to be more in the public interest to choose.

This matter has all been gone over, and it has been discussed and debated at great length. It seems to me that it is pretty largely a question of trying to have our cake and eat it. The banks, outside of a few of the bigger banks which have nothing but short-term securities—and you must think of that, those who have bills and certificates—of course, when you drop the market, it is not too important to them, because a short-term piece of paper cannot decline much—but outside of the larger banks with bills and certificates, there is not very much support for breaking the two and a half percent rate. The banks, as a whole, are opposed to breaking this rate, the nonmember banks possibly more, if anything, than the members. The banks, as a whole, want to prevent inflation, and yet they do not stop making loans, they are unwilling to have the Federal authorities exercise any control over their reserve situation, they do not want the Board or anyone else to have the powers that have been proposed by the Board as the only means of dealing with this, and they do want the Open Market Committee to stand there and provide them a market for their Government securities when they choose to sell them and without a discount.

Now, I say that is an untenable position for the banking fraternity to take. We cannot deal with this thing and do both. And of

course, the Congress hesitates to give us these powers—and I am not promising too much for them—

Mr. PATMAN. You mean if the powers are granted to you, you are not promising that you can do very much with them?

Mr. ECCLES. Well, not alone, as I indicated this morning.

Mr. PATMAN. You indicated this morning that we would have to balance the budget and have a surplus?

Mr. ECCLES. Yes. I am saying that it is certainly an important factor in the picture.

Mr. PATMAN. That is all I care to ask, Mr. Chairman.

Mr. SMITH. Mr. Eccles, you seem to give the impression that the President does not exercise much power over the policies of the Federal Reserve System. Do you wish to convey that idea?

Mr. ECCLES. Yes, sir. I do not think the President has undertaken at any time, in any way—either President Truman or President Roosevelt—to indicate to the Federal Reserve System what they ought to do, because they had recognized that the Federal Reserve was an agent of Congress.

Mr. SMITH. I mean through the Treasury, principally.

Mr. ECCLES. Well, of course, we have to work very, very closely with the Treasury, because the question of managing a \$250,000,000,000 public debt is an important one, and the Treasury has responsibilities, as we have responsibilities, and there is a divided responsibility, yet there must be complete coordination of the operation.

In most countries the central banking system is owned by the government, and is a mechanism of the treasury. It has little independence. In this country there has been a strong feeling that there should be a political independence on the part of the Federal Reserve System. Yet there must be an effort at a liaison with any government in power. I do not believe that a central banking system can be in a position where, if the Congress appropriates the money, they can then say to the Treasury—which is a part of the Government—"You cannot go out and raise the money except under our dictation, and at such price as we may determine." That is something that just has never been done and I have expressed it in this way: The Reserve, the Open Market Committee, and the Board should have an independence to the extent that they would be expected, as the agent of Congress, to advise with, and to have always their day in court, with an effort at trying to persuade any administration as to what would seem to be, to them, a proper monetary policy, and, I have always gone so far as to say, a proper fiscal policy.

Mr. SMITH. And you would also expect the Federal authority to exercise the same influence over the Federal Reserve; would you not?

Mr. ECCLES. I do not say that they have. But what we try to do is try to advise. Then the question is, if you cannot persuade, and you cannot agree, how far should the central banking authority go in enforcing their will? That is a matter that has not been determined, certainly.

Mr. SMITH. Mr. Eccles, you are supporting the bond market at two and a half percent; is that not a fact?

Mr. ECCLES. We are supporting the long-term market, and all the other bonds in between on a relative basis down to one and one-eighth.

Mr. SMITH. I mean the long-term market. Now, what if the Treasury sets a certain rate? You want that rate to go higher; do you not?

Mr. ECCLES. We have recommended that the short-term rate ought to be permitted gradually to go up.

Mr. SMITH. Why? Just in a few words.

Mr. ECCLES. I will tell you why: For the very reason that we feel that the banks would be more likely to buy short-term Government securities in the market if the rate was a little better, and would be less likely to be out reaching for loans. That is certainly a possibility. We also feel that when the banks come in possession of excess reserves from two sources, over which they are not responsible—one is gold imports, which creates excess reserves, and the other is the purchase, by the Federal Reserve System, of securities from nonbank investors—largely insurance companies, savings banks, and institutions of that sort—noneligible securities, largely, or even eligible securities—when you do that, you create excess reserves in the banking system which they have no control over.

When they get that money as excess reserves, and money idle to them, we would then like them to buy short-term Governments. We would supply the Governments. In other words, we buy the long ones in the market, we buy the gold, and sell the short-term securities, and one sterilizes the other, so that through the sale of the short-term Governments to the banks we sterilize the effect of the gold imports and the purchase of the long-term markets. And if the short-term rate should go up, we think that that might be a factor in getting the banks to be more interested in purchasing the short-term securities.

Mr. SMITH. How much of a factor?

Mr. ECCLES. I cannot say that. I do not think it is major.

Mr. SMITH. It is not major?

Mr. ECCLES. Some of them think it is major. Mr. Sproul, I think, thinks it is major.

Mr. SMITH. You have dwelt on it quite a bit and I just wondered what importance you attach to it.

Mr. ECCLES. Well, it is certainly a corollary to increasing reserve requirements—a very definite corollary to it.

Mr. SMITH. It is that important?

Mr. ECCLES. It is that important, that it certainly should be done as a part of an over-all credit-control program.

Mr. SMITH. No; I said, Do you consider that important?

Mr. ECCLES. Yes; I do.

Mr. SMITH. All right. Now, you said the Treasury did not exercise any power or control over the Federal Reserve policies.

Mr. ECCLES. I did not say they did not exercise it. They exercise a good deal of influence but not statutory authority or power. But they exercise a lot of influence.

Mr. SMITH. No; that has nothing to do with statutory authority or influence. It is inherently a power. If you think that rate ought to be increased because it is affecting your reserves and ability to handle your bond market, that is not a matter of influence at all. So it is true, then, that the Treasury, or the administration through the Treasury, does affect, importantly, the policy, in that particular respect, of the Board of Governors of the Federal Reserve System.

Mr. ECCLES. I said that was minor, and that is the Open Market Committee and not the Board itself.

Mr. SMITH. Mr. Eccles—

Mr. ECCLES. And I will say this for the Treasury—that during my term as Chairman there was not a period in all of last year, and

up until the first part of this year, when the recommendations of the open market committee, with reference to monetary policy, were not accepted. It has only been very recently that the Treasury did not accept the recommendation of the open market committee with reference to the June and the July financing. That is the refunding. So that any responsibility that you may lay upon them in failing to respond applies to that time.

Now, I will say this: There was a period in there, when Mr. Vinson first went in, right after the war and before Mr. Morgenthau went out, that we just could not get them away from an extremely cheap money policy of a buying rate on bills and a special discount rate, and we were very patient, and we finally did get the situation changed, after Mr. Vinson had had an opportunity to become a little more familiar with his job.

He was taking advice from some of the economists in the Treasury who we and the Board think were giving him some very bad advice.

Mr. SMITH. Mr. Eccles, going back to 1936, you sterilized your gold purchases by paying for the gold with Government debentures; is that not correct?

Mr. ECCLES. We sterilized the gold how?

Mr. SMITH. You sterilized your gold imports? What was the year—it was in 1936 that that took place, involving about \$3,000,000,000 of gold?

Mr. ECCLES. As I recall, the bill rate was very, very low, and the Treasury increased the public debt by issuing bills and using the money to sterilize the gold. It was costing them very little. That is right. That was the gold imports that they purchased.

Mr. SMITH. Did that involve the Federal Reserve Bank System in any way at all?

Mr. ECCLES. No; it did not involve them at all, because the gold never got into it.

Mr. SMITH. In other words, you are saying to this committee that that had nothing to do with the credit with which the Federal Reserve System was concerned in its banking operations?

Mr. ECCLES. That was just the same as if it had continued to stay abroad.

Mr. SMITH. And the fact that it did not get into the credit structure had something to do with the Federal Reserve System, did it not?

Mr. ECCLES. Well, if it had come into the System it would have added to the excess reserves, and it would have possibly made for even easier money than it was; and, as I said, the short-term rate was practically zero.

Mr. SMITH. Which, of course, affected the Federal Reserve Banking System. Then why do you come in here and try to lead this committee to believe that the Federal Reserve Banking System is an independent institution, which operates absolutely independently of the Treasury or the executive branch of the Government, when, as a matter of fact, the two are so completely coordinated that there is no possibility of separating them?

Now, the law provides specifically for making—

Mr. ECCLES. It appears that you misunderstood me, Dr. Smith. I answered the question, and then you castigate me for coming in here and saying something that I did not say.

Mr. SMITH. Well, let us get the record straight, because I do not want to do anything of the kind. Did you not say, or did I not under-

stand you to say, that the executive branch of the Government has no power over the Federal Reserve System?

Mr. ECCLES. No statutory power. They have influence.

Mr. SMITH. No statutory power, but they have influence?

Mr. ECCLES. That is right. That is true of every independent agency.

Mr. SMITH. To start with, the President appoints the Chairman, and he appoints all of the governors?

Mr. ECCLES. No; I was not appointed by Mr. Truman. I was appointed by Mr. Roosevelt.

Mr. SMITH. I know; but we are not speaking about one particular President.

Mr. ECCLES. The President does appoint them, that is right, for long terms, and the Senate confirms them, and he designates one of them as Chairman.

Mr. SMITH. So that the Board of Governors of the Federal Reserve System are an integral part of the general political body; is that not true? They are a part of the United States political authority; is that not right?

Mr. ECCLES. That is right; sure they are. As an agent of Congress, they would be that.

Mr. SMITH. Well, we can be a little more specific, because we have the words right before us, "The Board of Governors of the Federal Reserve System is a governmental institution." It is a governmental institution.

Mr. ECCLES. That is right.

Mr. SMITH. If it is a governmental institution, to be sure, the executive department has certain powers and controls over it, whether they are spelled out in a law or whether they are not. You helped to finance the war at the instance and direction of the President of the United States, and you are now handling the securities, bonds, debentures, notes, and so forth, that were issued by the Federal Government, and you have fixed a price at which you are, as you say, stabilizing the bond or security market. That, of course, is in the interest of the Federal Government.

Mr. ECCLES. It is in the interest of the American public.

Mr. SMITH. Well, I am talking about the executive branch of the Government now, because we want to get this thing clear and get the idea out of the minds of the people that the Federal Reserve Banking System is a private institution, because the law says it is not.

Mr. ECCLES. What about the open-market committee? The President does not appoint them, and they are not confirmed by the Senate. Five members of them are Reserve bank presidents selected by a board of directors of 12 banks, the majority of which are elected by the private bankers.

Mr. SMITH. That is true, but there is still a certain amount of control which the Board of Governors of the Federal Reserve has over those 12 banks.

You know what the law is, and we need not go into that at the present time.

Now, Mr. Eccles, I want to ask you this question: How long do you think you can continue to support the bond market, or to manipulate the bond market, or peg the prices of bonds, or rig the Government bond market, until you are forced to come in here and say to us, "We

have got to have a specific law to hold down prices—a rigid price-control law?”

How long is that going to be?

Mr. ECCLES. Let me answer that by asking you a question, because it is not clear just what you mean.

Are you advocating that we withdraw support from the Government bond market and let that seek its level? Is that what you are advocating?

Mr. SMITH. I am not advocating anything, Mr. Eccles. I am just trying to explore the situation to see what is in store for us in the future—where we are headed for.

You do not think you can continue to support this bond market forever without more controls, do you?

Mr. ECCLES. Yes; we can support the bond market for a very long period of time. But I would say this to the Congress, with reference to the bond market; that one of the things—and the most important thing—in the picture that requires our support of the Government bond market is the failure to have a budgetary surplus, because the public expenditures have been increased by congressional appropriations and the taxes have been cut by Congress, and therefore we no longer have a budgetary surplus which, in and of itself, would tend to reduce the public debt and which would be anti-inflationary in the picture, and which would very greatly reduce the necessity for the support of the Government bond market.

It seems to me that the Reserve System, the Board and the open market committee, are put into an almost intolerable position; a position which I must say, at least, is extremely difficult. We could deny the banks reserves upon which credit is expanded by withdrawing or letting the Government bond market seek its own level.

That is one side of the dilemma. And I have indicated rather at length the problem that that would seem to us to create—and I would say that there is unanimity with reference to that subject in the Reserve System. And the other question is that the banks—and up to date the Congress, and, prior to this time, the administration—because last November and last April, when I came before the committees and presented this program and thought that we had the support of the administration in that field, we woke up to find that the administration, and particularly the Treasury—did not support the credit-control program which we abandoned any more than the bankers and the Congress did. So the System has been left with a dilemma here, charged with responsibility and without authority except using an authority that nobody wants us to use.

Mr. SMITH. There again, Mr. Eccles, you admit that the executive branch of the Government has control or affects the Federal Reserve.

Mr. ECCLES. No; upon the Congress. They did not have any effect upon us. We came here and presented the program, even though they opposed it. We came here and presented it.

Now it appears that I was not a proper representative in presenting the program, because I was not redesignated. I thought I was presenting to the Congress—and in that connection I would just like to read into the record, here, something on that subject—I thought we were carrying out a part of the Government's anti-inflationary program.

Mr. SMITH. But, Mr. Eccles, you spoke about the Treasury. The Treasury Department cooperates—

Mr. ECCLES. Well, the Treasury; yes. The Treasury happens to be the agency of the administration that opposed the program for controlling bank reserves.

Mr. SMITH. Of course.

Mr. ECCLES. And they did not offer an alternative. We thought, certainly, that we had the cooperation of the administration, but we were not deterred from pressing it even when we found we did not have the cooperation. And when we came up here again, on the 13th day of April, and presented before the Taft committee our thought with reference to the regulation of credit and the management of the public debt—we thought we were completely in line with the President's statement. When he was asked by Congress what he thought of the program that Eccles had presented before the committee asking for these controls, 2 days after, in the Wall Street Journal there appeared the statement, "Eccles bank credit proposals do not have support of the President"—that was the first I knew of it—"Truman disavows the program, while Snyder declares he did not know what it was about."

Another statement in the Washington Post, on the same date: "Eccles spoke for himself alone, Truman explained."

Now, I spoke entirely for a unanimous Board in presenting that program, and that program that was presented then was identical with the program that is now presented, with the exception that it included nonmember banks. That is the only difference.

Mr. SMITH. Mr. Eccles, it would appear that you are in disagreement with the President on his recommendations, that they would have the effect of still further inflating credit; is that correct?

Mr. ECCLES. Well, I mentioned this morning that it seemed to me that the President's program was more political than it was economic. As I see an economic program to deal with inflation, it should be the type of a program that does not increase purchasing power or increase the money supply but should be the type of a program that certainly tries to hold it in balance or reduces, if anything, the money supply.

Now, certainly that program does not do that. And I would say this for the Republicans' answer: that that, likewise, is a political answer; and, as I said before the committee this morning you cannot meet these economic programs without facing the economic facts of life. And we are where we are because for 3 years since the war ended we have, I think, given too much consideration to the various pressure groups—and nobody, of course, likes to stop inflation for the benefits that they may get, as I said this morning.

A boom is a pleasant sort of a thing for the majority of the people. Unless we face up to the economic aspects of it, why, of course, it is going to continue to run its course, and it can continue to go for an indefinite period if bank credit continues to expand—that is, more money—and budgetary deficits continue to grow.

But to say that we are going to get a bust next week or next month or next year or the following year—you cannot say. The thing can go on for a considerable time. And the dollar can continue to be devalued and devalued and devalued. So that, when a deflation finally does set in, you have wiped out, as has been done in many

countries in the world with which you are familiar, the middle class of people—their savings, their insurance, their pensions. You have wiped out about only half of it now. But you can continue the process until you wipe out that much more. And when the adjustment comes, certainly the debtors then—that have gone into debt in the inflationary period when the dollar was worth little—will be put to a terrific test; and you will get widespread bankruptcy in a deflationary period, and the state will have to intervene.

When that time comes it will have to intervene at levels perhaps even higher than these. That may well be if the deflation goes long enough. You cannot go back to 1940, no matter what; and I do not think that now the economy could stand the deflation that could take you back to 1945. I do not think that is possible now. If this thing continues, and you get a further devaluation, the present levels could look low to you, and they may well be levels below which a deflation could not carry you because of the unemployment and the bankruptcy that deflations create.

I just mention that to point out the seriousness of the inflation that has already been created since the war, and the Federal Reserve Board does not want the responsibility—and is not going to take it because we have time and again sent our reports out.

I have made statement after statement; the Board has made statement after statement to the Congress, to the public and to the Administration—and the record is there.

I am particularly glad, at this time of my demise as chairman, of the opportunity of upholding the record of this Board. It is a voluminous one, and a good one, and I will stand on the record before these committees and before the public.

Mr. SMITH. Mr. Eccles, you are taking this thing very seriously, and I appreciate it. I think it is a very wholesome thing for this committee to realize that a man in your capacity, and with your knowledge of the finances of the Nation, really regards our situation as being critical and dangerous.

I do not suppose I am overemphasizing that, am I?

Mr. ECCLES. I have been pointing out that it was a critical situation that we were developing for a long while.

Mr. SMITH. Now Congress ought to do everything in its power to hold down expenditures, should it not?

Mr. ECCLES. It certainly should.

Mr. SMITH. Even if it is only a dime?

Mr. ECCLES. Absolutely. They should set an example of saving to the public.

Mr. SMITH. All right.

Now the President recommends that we spend some money—quite a sum of money—to build a structure in New York City for the United Nations to house Stalin's agents. I have figured out that the project, under our present system of financing, status of the debt, foreign policy, and so forth, the United States would pay most, if not all, of the cost which would not be \$65,000,000, but could reach twice that figure at the end of 34 years, the period fixed for its repayment.

Do you think it wise for the Congress of the United States to provide that money, particularly at this time?

Mr. ECCLES. Well, I do not want to say whether the providing of that particular money is justified or not. I am not sufficiently familiar with the arguments and with the debates upon the question.

Certainly, no matter what the situation is, the Government, in every period, must spend some money. Now, whether that is some of the money that could be cut out, or whether some other money could be cut out, it seems to me the appropriations committees or the Administration, who are making the suggestion, are better able to judge what the expenditures in the budget should be made for.

I would not want to say that you should cut that money for that building or that you should cut some other particular expenditure. All I am saying is that, in the overall, certainly, if we do not find a way of reducing the budget or increasing the income, we are not going to do very much as an anti-inflationary measure in the fiscal field.

Mr. KILBURN. Will you yield, Dr. Smith?

You said in your statement that the budgetary deficits were increasing?

Mr. ECCLES. No. I did not say that. What I meant to say was that the budgetary surplus was disappearing, and there is every indication that we will run into budgetary deficits. And I went on to mention, this morning, that if we carry out the military expansion program and other obligations that are being discussed—

Mr. KILBURN. There was a budgetary deficit every year up until last year, when the Republican Congress came in.

Mr. ECCLES. No; you had a surplus in 1946. In the fiscal year 1947 you had the biggest surplus the country has ever had—in the fiscal year just ended—but you likewise had a surplus in the fiscal year ending in June of 1946. You had a substantial surplus in the fiscal year ending June 30, 1947, as well as this year.

Mr. SMITH. Mr. Eccles, those of us in Congress, after all, have to use our efforts to cut the budget, and we have got to cut where we can. If you do not care to express yourself on this United Nations tower of Babel, that is all right.

Mr. ECCLES. Well, I will express myself on that. Maybe I should not, without knowing more about it, but at least my first hand feeling is that that is something that could be deferred; that the United Nations seem to be housed in a manner in which they can operate.

Mr. SMITH. Mr. Eccles, you are one of the most forthright and honest persons in the Government with which I have come in contact since I have been in Washington. I have the utmost faith in your integrity.

Mr. ECCLES. Thank you, Dr. Smith.

Mr. NICHOLSON. Yes. But, Dr. Smith, where does it leave us? We are just where we were when we started out.

You are asking us to do one thing, on the one hand, and do something, on the other, that is just exactly the opposite, and I cannot understand it. I cannot understand how it can be done. We either do one thing or nothing. But you ask us to do two things. One, to build houses, for instance.

Mr. ECCLES. Who asks you?

Mr. NICHOLSON. Well, the people who come before this committee.

Mr. ECCLES. I know; but you said "you ask us," as though it was the Federal Reserve or as though it were me.

Mr. NICHOLSON. Well, as I understand it, the Federal Reserve, under the proposition that is before us, wants to take control of the whole banking situation.

Mr. ECCLES. No. We already have certain controls. All we want to do is to have given to us additional authority so as to be able to

put some mild, I would say, restrictions upon the banks of the country insofar as their further credit expansion is concerned.

Mr. NICHOLSON. Are they all member banks?

Mr. ECCLES. No; they are not all member banks.

Mr. NICHOLSON. Do you want to force banks who are not members to become member banks?

Mr. ECCLES. No; we do not.

Mr. NICHOLSON. Or to stop competition?

Mr. ECCLES. No; we do not want to force them in at all.

What we are doing, by this proposal, is to not further expand the discrimination that now exists between the national banks and member banks and nonmember banks—and that discrimination is very substantial.

We started on that this morning when adjournment took place, and I would like to cover that further. I would like to put into the record a list of items of discrimination that already exist and that already weaken the system, and if this further restriction is put on member banks—and the nonmember banks are left free—it will be only adding another discrimination, which is certainly a major one. It is possibly more important than nearly all the others put together, because when you tie up 10 percent of the deposits of one group of banks that already have a much larger percentage of their deposits tied up, because they are members of the System, than nonmembers, then you can readily see that a lot of banks are going to get out of the System. And, to the extent that you leave loopholes in our banking structure, you are unable to make an effective thing out of control and regulation.

It seems to me that at the present time—and the record shows it—the nonmember banks have an earning power of 2.58 and the members 2.01 percent. That already is true because the reserve requirements of members, the amount of cash they have to carry, and the balance which they carry with correspondents are possibly twice those which are carried by the nonmember.

Mr. NICHOLSON. So that the nonmembers can buy this short-term stuff a great deal easier than a member bank can.

Mr. ECCLES. It can. They can make loans.

Mr. NICHOLSON. Yes. And it creates a competition, there, where the nonmember can take up, according to your figures, almost 1 percent of short-term loans.

Mr. ECCLES. But what happens here is that we do not want the banks to expand either their loans or their investments. I mean, we want to curb their loans and investments to the extent that you could increase their reserve requirements, say, 10 percent, and that would take 10 percent of their total deposits. Ten percent of their total deposits would require them to dispose of, to the Federal Reserve, about 20 percent of their Governments.

Now, they are not going to like that; and unless they can get higher rates on what they have left, or on their loans, it will affect their earnings; and that is one of the reasons why we want the short-term rate to go up. But the very fact that the holdings of their Governments have been very substantially reduced, reduces their liquidity and reduces very greatly their desire to expand credit.

Now, I do not believe it would be necessary to put all this power into effect at once. I think the very fact that the Reserve System

could make that apply to all banks means that the banks are going to keep as liquid as they can in order to meet that requirement and they would hesitate to be selling their Governments for the purpose of making loans. So that its effect would be one of restriction—just the very fact that the authority did exist.

If you exclude the nonmember bank you are going to induce national banks—because of the desirability, because of the advantage they get—to get out of the national banking system, and, therefore, you weaken the whole Federal System; and you, in turn, would increase the number of state nonmember banks.

Many of the state banks that are now members of the System will be tempted to withdraw from the System because of the disadvantage, because of the penalty and because of the discrimination imposed on them because they are members of the System. And I have here a whole list of matters—items of discrimination that already exist; and this Congress, or the American public, cannot afford to weaken the Federal Reserve System in any manner.

It does not seem to me to be good judgment to say, on the one hand, that you are going to increase our power and then, on the other, exclude the nonmember banks, so that you weaken it because of the discrimination.

There is nothing unusual in applying it to all banks. And I want to call the committee's attention to a special report that was sent to the Congress on January 1, 1941. That is very important now because of the opposition of the Federal Advisory Council and the opposition of some of the bankers.

This report was sent to the Congress with the unanimous approval of the Board of Governors, the presidents of the 12 reserve banks. This report was sent to the Congress, and in this report it was proposed, among other things—

that Congress provide means for absorbing a large part of the existing excess reserves, which amount to \$7,000,000,000, as well as such additions to these reserves as may occur in the future.

As I indicated a while ago gold imports had been coming in at that time because of the devaluation policy. The Federal Reserve had Governments that they could sell in the open market to absorb the excess reserves, and the net result is the banks had added to their deposits \$7,000,000,000, by the gold imports, and on the opposite side of their ledger, they had \$7,000,000,000 of idle excess reserves, so that the supply of money was so great—excess money—and the demand was so small for credit that the Government was able to borrow on bills at the zero interest rate, and the rates on private credit were exceedingly low. The banks were so much concerned about their solvency and their earnings that they favored, in the council, all of whom are bankers, authority to increase the reserve requirements of all banks to the extent of doubling the then existing authority, which instead of being 10 percent as now proposed by us, would have been approximately 20 percent.

That is what they proposed in order to absorb these excess reserves and get control of the money market and raise the rates.

What happened? The banks still have the effects of that gold inflow invested in Government securities. The banks, when the Government began to finance deficits, immediately had available to them a market for their excesses, and they bought Governments. They

were able to take care of the expansion of the currency. So that as long as the public debt is the size that it is, with the large amount of Governments available, and the demand for credit available, the banks have no excess reserves, they have not had excess reserves for years, and they are never likely to have any excess reserves when there is an opportunity to buy Governments. Those Governments are just the same as excess reserves so far as their liquidity is concerned, or their ability to extend private credit and create additional money supply because they can sell those Government bonds, and they get the reserves with which to extend the credit.

So I say, that they are not consistent—

Mr. NICHOLSON. Well, they could not do it if everybody did it at once, could they?

Mr. ECCLES. They are only going to sell the bonds to the extent that they get demands for loans because they want to get interest on Governments until they can get a better rate on something else. So there is no problem of everybody doing it at once, because it would mean that people were just marketing an interest-bearing Government bond to take a non-interest-bearing, idle deposit, unless they had some other place to put it.

Where you may well get a flood of selling would be if there was an indication of dropping of the market price. Those holding securities, trying to get the best price, thinking in terms of what happened after the last war, when $4\frac{1}{2}$ percent totally tax-free bonds went to 82, you can well imagine what an avalanche of sales might then develop because they would want to try to get the best market, and that is one of the reasons and one of the best reasons why we have to stabilize the market, and why we have to maintain the long-term rate.

Mr. SPENCE. What was the bonded indebtedness of the United States at the time the bonds went to 82?

Mr. ECCLES. Something around 24 to 25 billion dollars. I might ask this question: If Government bonds, totally tax exempt, yielding a rate of $4\frac{1}{2}$ percent, without any support by the Federal Reserve System, could go to 82 or 83, then when our national debt was \$25,000,000,000 only, the query is, where would a $2\frac{1}{2}$ percent fully taxed bond, taxable bond go, if the Federal Reserve withdrew from its support, when there was a debt of \$250,000,000,000?

Mr. SPENCE. I just do not know. But I am just giving you a picture of the relative size of the debt and of the difference in the interest rate.

Mr. TALLE. Mr. Chairman.

The CHAIRMAN. Mr. Talle.

Mr. TALLE. At the outset, Mr. Eccles, I want to thank you for a clear, detailed and well organized presentation.

Mr. ECCLES. Thank you.

Mr. TALLE. There are two points I would like to raise. The first has to do with the nonmember banks. In the event we overlook the question of constitutionality, as to whether there is authority or not—let us waive that for the moment—and assuming that we did enact a law to require the nonmember banks to increase their reserves by the percentage stated, and in the event that those banks chose not to comply, what would be the penalty or the sanction that would be imposed on them for noncompliance?

Mr. ECCLES. I think possibly the same sanction that is imposed upon the member banks for noncompliance. In the case of the member banks, where they are deficient in the reserve, there is a penalty in the form of an interest rate on their deficiency. There is no limit in the statute as to what that penalty can be, as I understand it. They are permitted to average their deposits over a period of a month, in the case of the country bank, and 2 weeks in the case of the Reserve city banks, and 1 week for the central Reserve city banks. This is permitted in order to have the needed reserve requirement every day, these banks would have to carry an excess. Therefore, we permit them to average it over a peak. This would likewise, I assume, and certainly should, apply to the nonmember banks in the same manner. The nonmembers in the Reserve cities and the country banks should be able to average in the same manner as their competitor member banks would average them and the same penalty for deficiencies should apply.

The difference would be that the nonmember banks, we would expect, would be supervised and policed by the State banking commissioners. The Federal Reserve has a very close relationship with the State banking commissioners because we have around 2,000 State banks which are members, and because of that fact we work with them in connection with examinations and regulations, decentralized down to each Federal Reserve district and branch.

We do not duplicate the work of examination. We arrange with them, as a general rule, that they will make one examination and we make the next examination. So that this relationship with the State nonmember banks, through the State banking commissioners, is not a difficult thing to accomplish. As I indicated this morning, we have had a relationship with these nonmember banks in connection with the other regulations that have been given to the board over them.

Mr. TALLE. In the case of a State member bank, would the Federal Reserve System have the right to expel it from membership in the system in the event it did not comply.

Mr. ECCLES. We would not do it for that reason because we would put the reserve penalty on them and that is all that is necessary. They are not going to pay a rate of 4, 5, 6, 7 or 8 percent, for money, if they are getting 3 or 4 percent. They are just not going to pay any such penalty. So there is no question of expelling.

The Reserve System does have a considerable power to expel banks from the system. As to just what those powers are, I am a little hazy.

Mr. TALLE. Could the Federal Reserve Board reach a nonmember bank, influence a nonmember bank indirectly by working through the nonmember banks' correspondent bank which was a member of the Federal Reserve?

Mr. ECCLES. No, you cannot reach them that way. You mean by permitting a nonmember to carry the balances with the correspondent bank?

Mr. TALLE. I was thinking of whether the Federal Reserve Board could work through a national bank, which was large enough to be a profitable correspondent bank for, let us say, a country nonmember bank?

Mr. ECCLES. I do not know how we could in this regard.

Mr. TALLE. It would be a rather devious method, at any rate?

Mr. ECCLES. Yes, sir; the difficulty is that if the country bank carried its balance, its increased requirement, in a correspondent bank, then that correspondent bank in turn would have to carry a reserve against that balance. That is what we call inter-bank balances, and that is one of the processes of pyramiding. One of the best arguments for a unified banking system—and that is what was conceived of in the early days of the Federal Reserve Act—of course, was to get all banks into the Reserve System and to increase the importance of the Reserve System on the basis of par clearance and the facilities of collections. But naturally the reserve city banks and the correspondent banks, those who fought against the Reserve System in the beginning, have continued naturally to resist any action on the part of the Federal Reserve that might tend to reduce the balances that they get from their correspondent banks, upon which they only have to carry 20 or 25 percent reserves.

Therefore, the reserves of a nonmember bank that met the reserve requirements of the State bank commissioner, when they get over to a correspondent bank, those reserves become deposits and that correspondent bank has money to loan, can loan those reserves, except that they must carry against those deposits a certain amount of reserves.

But we are not trying at this time to interfere, any more than is necessary, with the correspondent bank relationship. We are not doing anything to compel membership in the Reserve System. We are merely faced with a problem here of what to do to put some pressures upon the banking system, as a whole, and for it to be effective and not weaken the System, the nonmember banks must be covered.

I mean pressure so as to restrict their credit expansion, to hold it down. There is nothing in this proposal that would bring about or force a credit contraction. It may be too mild. It may be altogether too mild to have very much effect, because if the banks own \$65,000,000,000 of governments, and they could sell \$10,000,000,000, to meet the requirement, they still have a huge potential for credit expansion.

I just wanted to show that this proposal is not very onerous and is not very restrictive, because they would still have, even if they met the increased requirement, the possibility of selling \$10,000,000,000 worth of governments, and would still have \$55,000,000,000 of governments left.

There has been some talk about a compromise then on this bill, and only making it 5 percent. Well, I would say that the 10 percent is still not a very restrictive requirement in itself. Yet I do think that for the present it may be sufficient.

The CHAIRMAN. \$12,000,000,000?

Mr. ECCLES. \$11,000,000,000. As I say, they have got \$65,000,000,000 worth of governments. They could sell the \$11,000,000,000, taking the system as a whole, and have \$55,000,000,000 left. They could sell \$5,000,000,000 of the \$55,000,000,000 and then expand on that; with this increased requirement, it reduces the multiple credit expansion, which is desirable. It would reduce the multiple credit expansion from about 6 to 1 now to about 4½ to 1. Now, every dollar of reserve is the basis for \$6 of credit expansion.

With this requirement every dollar would be a basis of $4\frac{1}{2}$ dollars of credit expansion. That is with the amount that is proposed.

But, as I said, the banking system as a whole will still have an awful lot of governments left, and they could sell \$5,000,000,000 and still get a considerable expansion of credit.

I am not saying that they would do that. I think if you raised the short-term rate, and you had the power to put this 10 percent additional on, that the desire of the banks, under these conditions, would be to try to keep liquid, based on the experience of the thirties, and that might well restrain credit expansion. It certainly would make them extremely selective and very cautious and would put much more restraint on than any voluntary program can or would put upon the banks. I just hope that if anything is going to be given to the board it would not be an amount that would be completely inadequate, because the whole question of the use of this is, as I said, supplementary to other things, but at this time, I believe it is desirable and possibly the most helpful thing that could be done in a hurry to help hold the line.

The CHAIRMAN. Will you yield, Mr. Talle?

Mr. TALLE. I yield to the chairman.

The CHAIRMAN. That brings us right back to this question, as to how you are going to use, immediately—how much of this power you are going to use immediately.

Mr. ECCLES. We may not have to use any, Mr. Chairman. It depends upon whether the banks make that necessary. It depends upon two things: It would depend upon the extent to which we had to buy bank securities from nonbank investors, the extent to which gold flowed in. Those two factors alone will add to excess reserves in the banking system. These excess reserves, if the banks continue to expand credit, should be sterilized by some increase in the reserve requirements to meet that excess that was created, and if the banks then continue to expand credit and sell us governments, we should again raise the reserve requirements to sterilize the effect of such bonds as they sold.

Now I can only say that you would have to use this authority based upon the conditions that would develop, and conditions that would develop after we had such authority may be different from the conditions which exist if we do not have the authority.

The CHAIRMAN. If we gave you 10 percent additional authority, and you put it on tomorrow or the next day, what would be the effect?

Mr. ECCLES. Nobody would think of putting it on in any such a manner, when the banks do not have idle balances. When we increased reserves in 1937 the idle money was already there. They did not have to sell anything to get it or collect a loan to get it. The reserves were there and with all the increase we put on they still had an excess and the short term rate never went above half of 1 percent.

The CHAIRMAN. I have a letter here to the effect that it is going to interfere with respect to reserves. This comes in from the economic adviser of some of this country's leading corporations which have assets of over 75 billions of dollars and he goes on to say this:

Suppose the Congress should give the board power to raise reserve requirements and the board should raise them. Then the commercial banks would either sell Government bonds or call commercial loans. In the first instance the board would either buy the bonds and in so doing raise the reserves of the banks and,

believe it or not, actually negate its previous action, or banks would become insolvent and our new President, Mr. Dewey, as Mr. Hoover, would be a victim of the Reserve Board's stupidity.

If the banks call commercial loans, consumer goods would be sacrificed in the markets, and then production of these goods would decline.

Immediately the demand for industrial equipment and other capital goods would decline, and the country would enter the vale of depression.

It makes me sick to think that we might have to return to such conditions that ultimately would lead us to state capitalism or communism. The imposition of increased reserve requirements would force me to advise these clients to liquidate their holdings of Government bonds and prepare for depression.

Mr. ECCLES. Well, of course, there is nothing new about that letter. We would get plenty of opposition. In the first place, what that fellow says just is not true.

The Reserve System is not going to be so stupid as to overnight increase the reserve requirements of all banks in the country 10 percent, so that they are forced immediately to sell \$11,000,000,000 worth of bonds.

The CHAIRMAN. Let me put this question to you: How much do you think the reserve is apt to be raised in the next 6 to 8 months?

Mr. ECCLES. I could not even guess that for the very reasons that I stated. From the very fact that it was there, the banks would undertake to pursue a credit policy—I know I would if I were a banker—so as to meet that requirement, exactly the same as I would meet it if it were in effect. I would set aside enough of my Governments to say, "Well, now, if they increase reserve requirements, those Governments will be sold, so I cannot count them. That is not part of my liquidity. That is not available for me to dispose for lending," and I would consider my lending policy, and I would consider the credit policy I would pursue on an assumption that I might be required at any time to meet that requirement.

If banks actually do that—certainly nobody wants to take away from the banks earning assets—if they will pursue a policy of a non-general expansion of credit, if they will pursue a policy with the money they have, and the reserves they have received from gold imports, and the money that went into them, from our purchase of nonbank securities, of buying from the Federal Reserve the short-term securities that they held, certainly there would be no necessity or desire to impose a requirement on them that would require them to dispose of earning assets.

But if, on the other hand, they do as they are now doing, and as they have been doing over the past 2 years—taking the year as a whole—expanding their credit and thus increasing the supply of money when we already have an inflationary condition, and a voluntary scheme does not stop them from doing so, it would be up to the Federal Reserve, after getting a raise in the short-term rate, to increase the reserve requirements, slowly, as the conditions warranted.

Now, I am only one member of the Board. I cannot speak for the others. But I am just telling you that is the way I would look at it and, based upon my experience in dealing with these problems—and I have had considerable both as a private banker, over a period of 20 years, and as a Reserve official for 14 years—that is the way I would do it.

The CHAIRMAN. Thank you.

Mr. Talle.

Mr. TALLE. Another question I have in mind, Governor Eccles, has to do with the gold reserve requirements back of Federal Reserve notes and Federal Reserve bank deposits. Historically, they were 40 and 35 percent, respectively, until June of 1945. Of course, I realize certificates have been used in lieu of gold since 1935.

Mr. ECCLES. That is correct.

Mr. TALLE. But the change was made from 40 percent and 35 percent to an even 25 percent for both, in June of 1945. Would it not be desirable to move back to the larger percentages, under present conditions?

Mr. ECCLES. I do not think that would be desirable. I think it would do no immediate good and may well give the public a feeling that it was an anti-inflation action whereas it would not be effective, and it would not do any good for the present.

At the present time the reserve requirements, if they were increased—the gold reserve requirements—if they were increased to 35 and 40, respectively, on currency and bank deposits with the Federal Reserve banks, it would require \$16,069,000,000. The excess of gold now held by all of the Reserve banks is \$5,717,000,000. But, as a practical matter, the excess amount is \$4,642,000,000, because in practice we have found that you cannot get closer than 3 percent to the limit. There is an operating ratio. So that I would say that if we increase the reserve requirements to 35 and 40 percent, you would have \$4,600,000,000 of excess reserves. Therefore, there would be no pressure whatsoever upon the ability of the Reserve banks to expand currency to meet the public demand for currency, or to purchase Government securities in the market, or to make loans to member banks in order to provide reserves.

If the excess amount that I have mentioned disappeared, as it was used up, through an expansion of currency, or if inflation continued, or through an expansion of the purchase of Governments by the Federal Reserve System in the support of the market, then you would be up against this problem: The Federal Reserve System would be entirely unable to help the Government in its refunding operations, would be entirely unable to support the Government market, and we would likewise be unable to meet the increased demand for currency from the member banks whose customers required currency, and we would have to come back to the Congress, as we did before, and say to the Congress: "You must reduce the reserve requirement because if you do not reduce the reserve requirement, the possibility of a collapse in the Government bond market that should eventuate, or our inability to supply the banks with currency, and, in turn, their inability to furnish it to their customers would seriously impair the whole banking system," and I am sure that the Congress would merely reduce the requirement again. But it does not make very much sense, it seems to me, to try to control the expansion and the contraction through the medium of an indirect gold standard. That is really what we are trying to do, and when we say we want to impose that reserve requirement, there is a much more honest and a much more direct way of dealing with the problem. It would amount to this: As the excess reserve got close to the limits, the smart people, the people that understood the restrictions, would immediately say: "Well, the Federal Reserve System Open Market Committee now is limited, in its purchase of Governments. They will not be able to

buy more than another billion dollars or another \$500,000,000. Their limit is there. Or perhaps \$2,000,000,000."

So the big boys, the insurance companies and others, might say, "I think we had better sell our securities to the Federal Reserve System while we know that they are able to support the market," and you may well have enough sale of Governments that they would use the excess reserve they held rapidly, whereas others would not use it at all, but the very fact that it had a limitation, the very limitation itself, could induce a lot of selling of Government bonds, which certainly would be undesirable and unnecessary, and I see no value whatever in changing to that, except if the Congress indirectly wanted to say to the Reserve System, "You shall not support the bond market." Or if they wanted to say, "We are going to put you in a position where you cannot support the public credit."

I say the much more honest way to do that is to say, "Do not support the 2½ percent rate," and the other way is not to vote for appropriations or for tax reductions that create budgetary deficits, but support budgetary surpluses, so that the question of the Government being able to take care of its refunding, can be accomplished without any help from the Reserve System. That is really the direct way of getting at it.

This is a Mr. Spahr idea. I think Mr. Burgess also makes a point of it. I disagree fully and completely with both of them, and although Allan Sproul and I disagree on some things, we agree completely and fully on this issue, and so do all of the economists of the Reserve Board and the economists of the banks and all the presidents. And the people who talk about this one are what I call a few gold standard money cranks.

Mr. TALLE. I recall, when the change was made in 1945, that it was argued by some people in the administration that deflation was just around the corner and that lower reserves would permit a greater expansion of money and credit. This feared deflation did not occur however. Quite the opposite development did occur, and now we are faced with rapidly increasing inflation. Should not then, in line with the administration's theory of 1945, the larger percentages be restored?

Mr. ECCLES. That is fine, but let us bring the public debt down. The idea is you want to go back with these figures but you do not want to go back with the public debt. The action of Congress just recently would indicate that there is no intention of reducing the public debt, and, therefore, it is no time now to change the item. When you reduce the public debt substantially, then you can talk about changing the ratio that was reduced in order to help meet the expansion of the public debt.

There is just one other point I would like to make—and this is a practical operating point—unfortunately, each of the Reserve banks is required to carry gold and Governments against its particular deposits and against its particular issue of currency. That, in one sense, we have 12 central banks. Some day I hope that can be changed. I argued before the appropriate committee of Congress in 1945 that the currency of the various Reserve banks should be interchangeable. We showed that it would save hundreds of thousands of dollars a year in the shipments of currency. We got nowhere. But now the very fact that we have, in 12 separate compartments, currency issues, gold reserve requirements, and Government

bond portfolios, means that some banks may have a deficiency in gold, where others have a large excess.

Now, as a matter of fact, if you should increase reserve requirements—gold reserve requirement, that is—to the 35 percent and the 40 percent, respectively, and we maintained a 3 percent operating margin, as of July 31, there would be 4 banks that would be deficient in gold reserves, even though the 12 banks had an excess of \$4,600,000,-000. That would make it an extremely inconvenient operating job for no useful purpose.

Mr. TALLE. Are the deficits large?

Mr. ECCLES. No; they are not large.

Mr. TALLE. I think for June they amounted to a little over \$105,000,000.

Mr. ECCLES. Well, they are not large. In fact, they are comparatively small. New York, as an example, 1 bank, has almost half of the entire excess. I have here a statement with the arguments on this issue that I would like to put in the record.

The CHAIRMAN. You may put it in the record.

(The document referred to is as follows:)

Restoration of the previous ratio of required gold certificate reserves held by Federal Reserve banks of 40 percent against Federal Reserve notes and 35 percent against Federal Reserve bank deposits has been proposed to your committee as an anti-inflationary measure. This proposal would make no contribution whatever to the fight against inflation. It would not sterilize new acquisitions of gold nor would it give the Federal Reserve System any additional powers to curb inflationary expansion of bank credit.

The present reserve requirements of the Federal Reserve banks stand at a uniform level of 25 percent. Congress established them at this level in consequence of the wartime expansion of currency and Reserve bank credit. The previous requirements of 40 percent against notes and 35 percent against deposits, incorporated in the Federal Reserve Act of 1913, were largely arbitrary.

To restore the prewar levels now would only entail needless operating difficulties for some of the Federal Reserve banks. The combined banks at present hold gold certificates amounting to 50.6 percent of their total note and deposit liabilities, or approximately \$8,000,000,000 in excess of the proposed higher requirements. Thus, they would not prohibit Reserve banks from providing member banks with additional funds on which to base a considerable further expansion of bank credit.

If Reserve banks were to be prevented by this device from issuing currency and member banks were thus unable to supply currency to their customers, it would precipitate the kind of money panic which the Federal Reserve System was created to prevent. Likewise, if the Federal Reserve System, because of an artificial limitation, were unable to supply credit to member banks, the results could well be demoralizing in the Government bond market.

Although the Reserve System as a whole has gold certificate reserves in excess of the proposed higher requirement, there is considerable variation among individual Federal Reserve banks. As a practical operating matter, these banks cannot permit the ratios to go down to the vanishing point and hence require a working margin of at least three percentage points.

If the higher requirement were restored, some Federal Reserve banks would have a substantial deficiency, others would be below or close to the necessary operating margin, while still others would have a large excess.

Reserve banks with a deficiency would be obliged to sell some of their Government securities to or to borrow from Reserve banks which had an excess. The reserve position of the individual Federal Reserve banks is constantly changing with seasonal and other movements of funds in the economy. Therefore, the proposal would entail operating difficulties and constant inconvenience without accomplishing any useful purpose.

Expansion or contraction of Reserve bank credit should be determined by the needs of the economy and not by the amount of gold certificates which Reserve banks happen to have, which in turn is contingent upon international movements of gold.

Likewise, inability to supply credit to member banks would compel the System to withdraw support from the Government securities market and perhaps even to sell securities which it now holds at whatever prices or yields they would bring in the market.

The Reserve banks do not control the amount of currency which the public wishes to hold. It is the depositors of the banks and the recipients of checks who determine the volume of outstanding currency. They create the demand and member banks come to their respective Federal Reserve banks to obtain such amounts of currency as their depositors or others presenting checks may desire to have.

If the Reserve System were unable to meet demands for currency it would jeopardize public confidence and might lead to runs on banks and to hoarding of currency, such as occurred in 1931.

It is already within the System's power to invoke such drastic measures. The System has rejected such a course because of the possible disastrous effects on the entire financial situation of the country.

The proposal would appear to be designed to force the Federal Reserve System to abandon support of the Government securities market and thus bring about sharp increases in interest rates. It is inconceivable that Congress or the public desire either to create a run on the currency or collapse of the bond market. If that were the will of the majority, it should be done openly and frankly and not by indirection.

Excess Gold Certificate Reserves over requirements of 35 percent Gold Certificates against deposits and 40 percent against Federal Reserve Notes, July 31, 1948

[In thousands of dollars]

	Total required reserves (35 and 40 percent)	Excess of gold certificate reserves
Boston.....	894,530	-16,063
New York.....	4,850,294	2,534,050
Philadelphia.....	937,087	75,232
Cleveland.....	1,362,301	152,012
Richmond.....	960,567	112,849
Atlanta.....	830,445	243,525
Chicago.....	2,889,077	1,521,868
St. Louis.....	699,708	-60,623
Minneapolis.....	439,810	51,992
Kansas City.....	708,449	184,123
Dallas.....	579,575	-1,472
San Francisco.....	1,777,952	949,514
Total.....	16,689,793	5,717,008

Mr. ECCLES. I would also like to put in the record the statement of the more important points of discrimination between member and nonmember banks. I will supply that for the record later.

Mr. TALLE. I would like to have that statement inserted in the record, Mr. Chairman.

The CHAIRMAN. Without objection, that will be done.

(The document referred to is as follows:)

SOME OF THE MORE IMPORTANT HANDICAPS UPON MEMBERS OF THE FEDERAL RESERVE SYSTEM AS COMPARED WITH NONMEMBERS

1. Reserve requirements are more onerous for member banks than for non-member banks. Member banks are required to carry certain percentages of their demand and time deposits respectively in noninterest bearing balances with the Federal Reserve banks. Apart from these required reserve balances, member banks have to carry vault cash to meet deposit withdrawals and some balances with correspondent banks, none of which can be counted in fulfillment of statutory reserve requirements. Nonmember bank reserve requirements not only may be lower in amount but may usually consist of vault cash and balances carried with city correspondents, who may render services that are not available at the Federal Reserve banks. In some instances and to some extent reserves of nonmember

banks may be invested in United States Government and other specified securities. To a considerable extent, therefore, nonmember banks receive direct or indirect compensation for a substantial part of the reserves which they are required to carry under State law.

2. Nonmember banks may receive immediate credit for checks cleared through their correspondent banks, whereas credit to member banks for checks cleared through Federal Reserve banks may be deferred from 1 to 3 days for out-of-town items.

3. Member banks are prohibited from charging exchange on checks received from Federal Reserve banks for collection and therefore are deprived of revenue which might otherwise be obtained from this source. Many States permit such charges to be made and there are at least 2,000 State banks that make such charges regularly. Member banks are at a competitive disadvantage particularly as compared with some nonmember banks in their dealings with country bank correspondents because nonmember banks may follow a practice of absorbing exchange charges for their customers, whereas member banks are not permitted to do so.

4. In most States, those having a population of a million or more, a national or State member bank must have a minimum capital of \$500,000 in order to maintain a branch outside the city in which it is located. This is not required of nonmember banks. Even where branches are not involved minimum requirements for capital are frequently less for nonmember banks than for member banks.

5. There are much greater Federal restrictions on investments and loans of national and State member banks than in the case of nonmember banks.

6. There are certain Federal restrictions on holding companies and interlocking directorates which are not applicable where only nonmember banks are involved.

7. Any State nonmember banks is free to choose whether its deposits shall be insured by the Federal Deposit Insurance Corporation and therefore can save the substantial cost of the assessments for such insurance but member banks have no such choice.

Mr. TALLE. In that connection, I would like to ask one question: If you look at total deposits, they are small, are they not, for the nonmember banks?

Mr. ECCLES. That is right, they are a billion and a half, as against about 9 billion dollars.

Mr. TALLE. About 15 percent?

Mr. ECCLES. No, that is the reserves. I have got that right here. All member bank deposits; if you exclude the interbank deposits—that is, the demand and time deposits, not taking into account the interbank deposits—is 110 billion for all member banks. For the nonmember insured banks—and I have not thought of making this cover the uninsured banks, although it could do it, if Congress saw fit—I could not make a good argument for not including them, but they do not amount to much, the only argument being that they are such a small amount—but at the same time there is no economic argument for not including them—would be 19 billion dollars.

The important part about this is that the 19 billion dollars would get larger and the other would get smaller, because you offer every inducement for banks to get out of the System—the State banks that is—and every inducement for the national banks to convert to State banks, and you offer no inducement for them to come in. I, you are going to strengthen the Federal Reserve System and the national banking system, there should be more inducements to come in, and not less inducements, as this would bring about, if you excluded the nonmember banks, that is, this proposed legislation.

Mr. TALLE. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Monroney, do you have any questions?

Mr. MONRONEY. No questions.

The CHAIRMAN. Mr. Folger?

Mr. FOLGER. Mr. Eccles, have you read the committee's bill with reference to title II, dealing with bank reserves? It is a confidential print. I do not know that this is a bill.

The CHAIRMAN. There are merely some technical changes.

Mr. ECCLES. No, I have not read the bill to which you refer.

Mr. FOLGER. It refers entirely to member banks, defining the four categories: Member banks in central Reserve cities, member banks in Reserve cities, member banks not in Reserve or central Reserve cities, and, fourth, all member banks, but no such change—shall have the effect of requiring any such member bank to maintain a reserve balance against its time deposits in an amount equal to more than 10 percent, or a reserve balance against its demand deposits in an amount equal to more than 36 percent thereof, if such bank is in a central Reserve city, 30 percent if it is in a Reserve city, or 24 percent thereof if not in a Reserve or central Reserve city.

What are the figures as they now obtain with respect to these several categories?

Mr. ECCLES. Six percent, time deposits; demand deposits, 14 percent on the banks in non-Reserve cities; 20 percent, banks in Reserve cities; 24 percent, banks in central Reserve cities, which are just two cities, New York and Chicago. There is authority to increase those reserves by another 2 percent.

Mr. FOLGER. That would make it 26 percent?

Mr. ECCLES. That means adding 10 percent to each of those categories. That would make them, instead of 14 for example, 24; instead of 20, 30; instead of 26, 36; and 10 percent on all savings, no matter what the category is in all three categories of banks.

Mr. FOLGER. I noticed, in the chairman's statement, that he refers to his testimony before the Senate committee, and he says:

Since I presented that statement to the Senate committee, the Board has this morning had an opportunity to meet and to discuss the proposed legislation at length. The Board are agreed that the inclusion of the nonmember banks is essential to make the proposed legislation fully effective.

Do you know of that determination by the Board?

Mr. ECCLES. I certainly do. I was responsible for getting that meeting. I will be glad to tell the committee just exactly what the situation was.

Mr. FOLGER. That inquiry is a preface to this question:

That says in order to "make the proposed legislation fully effective." That does not deal particularly with the discrimination that is urged against now—and, I think, properly so—but it would be difficult to make this legislation effective if you did not include the nonmember banks, would it not?

Mr. ECCLES. That is right.

Mr. FOLGER. That would have that effect?

Mr. ECCLES. It would.

Mr. FOLGER. What is done with respect to nonmember banks now with respect to their reserves? Does the Federal Reserve System undertake to influence that?

Mr. ECCLES. Nothing whatever. And, as a whole, they are the ones who have been, in proportion to their size, the greatest extenders of credit. The central Reserve cities—New York and Chicago—in relation to their size have been the smallest extenders of credit and have been more responsive to the need for credit restriction.

Mr. FOLGER. State member banks can withdraw from the System at any time, can they not, by just a mechanical operation?

Mr. ECCLES. Yes, that is their privilege. It is very simple.

Mr. FOLGER. National banks cannot get out?

Mr. ECCLES. Well, national banks cannot get out of the System, but they can get out of the national banking system and into a State system, which would relieve them of this requirement. That is the loophole.

Mr. FOLGER. They would have to convert themselves to State banks?

Mr. ECCLES. That is right.

Mr. FOLGER. And then get out?

Mr. ECCLES. That is right. I would just like to say that I have been in the banking business since 1913. I was president of two banks in 1920. I was the president of a banking organization all during the collapse of the year 1929 and thirties. That organization owned 28 banks, both Reserve city banks and country banks. And I would say this to the committee: If I were in the banking business today and this restriction was imposed upon my bank as a member bank, unless I had a very substantial amount of interbank deposits and I had to have Federal Reserve connection for clearing, and so forth, I would withdraw from the System because I would be able to maintain smaller reserves by a considerable amount than are now required, without the imposition of the increase, and I could put the saving in those reserve requirements, as well as the reserves that I would be carrying with my city bank correspondent, into short-term Governments.

Then this 10 percent that would be imposed upon me as a member—I can likewise put that in Governments. So why would I need membership in the Federal Reserve for borrowing purposes if I had any source of liquidity that I could thus create by getting out of the Reserve System?

Mr. FOLGER. Mr. Eccles, I believe you—and, I think, other witnesses—have indicated that this proposed legislation is just conceived as a supplementary aid to the reduction or minimizing of the inflationary trends or developments that have come about—wholly supplementary to the other things.

Mr. ECCLES. I tried, in my general statement this morning, to make that point. I do not want to underemphasize its importance, and neither do I want it to be overemphasized and have the public or the Congress expect too much and to think that this is by any means a cure-all. I think it is secondary to a sound and proper fiscal policy.

Mr. FOLGER. To many other things that might be done?

Mr. ECCLES. I covered that this morning, Congressman Folger, rather fully, and, if you would excuse me, I would like to avoid the repetition.

Mr. FOLGER. I do not ask you for that. You mentioned the very important fact that the fiscal policy and the budgetary system that we have assure a surplus in the Treasury rather than a deficit.

Mr. ECCLES. During an inflationary period.

Mr. FOLGER. Yes.

Mr. ECCLES. In deflationary periods I am for deficits because you need to put a cushion under the deflation, and the most effective means of putting a cushion under the deflation is public spending and Government deficits.

But unless you have surpluses now, how can you, how are you, in a deflationary period, be in a position to have deficits?

Mr. FOLGER. That thought, I suppose, led you to observe that public spending, in the way of building and other things, is something to be resorted to in a deflationary period and not in a period of inflation.

Mr. ECCLES. Very, very definitely. Unless you use your fiscal, monetary and credit policies as a compensatory mechanism to moderate the inflationary development, and also moderate the deflationary development, I do not see very much hope to avoid the excesses of booms and busts.

Mr. FOLGER. That is all.

Mr. TALLE (acting chairman). Mr. Buffett, do you have a question?

Mr. BUFFETT. Yes. Mr. Eccles, our managed currency venture is running into stormy weather; is that the situation?

Mr. ECCLES. Well, our gold standard ran into stormy weather, as I recall, from 1929 to 1933. But I do not think either the managed currency or the gold standard had anything to do with the creation of the stormy weather.

Mr. BUFFETT. You do not think that the final brake on Government spending in the hands of the producers of the country has any influence on Government spending?

Mr. ECCLES. I do not understand the question.

Mr. BUFFETT. I say, you do not think the decisive brake on public spending in the hands of the producers can exercise a determining influence on Government spending?

Mr. ECCLES. I still do not get your point. Could you put your question again, or put it differently?

Mr. BUFFETT. I will try to rephrase it.

When the producers of a country have some method of protecting themselves against reckless Government spending, then they have an instrument in their hands to restrain inflation, do they not?

Mr. ECCLES. Well, inflation can come from an overexpansion of private credit as well as an overexpansion of public credit. But I will say this: To the extent that you get private credit you usually get a certain amount of production to support the credit—unless you have an inflationary condition—and all that credit does is add to the inflationary pressures. Whereas, in the case of Government spending, Government credit—that is, where they borrow in excess of their tax revenue—you do not get either goods or services available for the consumer to buy.

For instance, European loans or grants do not produce any goods whatever. But they do put pressure upon the goods that we produce.

I am not arguing against the European aid program, but I am merely pointing out an economic fact.

Certainly the worst possible conceivable waste that one can think of are the military expenditures because they certainly are a burden upon our manpower and upon our productive facilities, and they produce nothing available for the consumer to buy. Or any expenditure by Government, for that matter, that is wasteful, that is not absolutely essential in a time of inflation. Now, in a time of deflation, where you have idle men, idle material, Government spending based not upon balanced budgets, but Government spending based upon deficits pumps new purchasing power into the stream and gives employment and production that otherwise may not exist. It is a very different matter under those conditions.

Mr. BUFFETT. Have you ever explored the difficulties of restraining military expenditures in a country where the producer has no way to protect himself against expanding military expenditures? In the gold-standard country he has a method of protecting himself. He can go to the bank and say: "I do not like the way they are running things; I want gold in exchange for paper money."

Mr. ECCLES. That has never been possible, though.

Mr. BUFFETT. It was possible in this country until 1933.

Mr. ECCLES. Oh, no.

Mr. BUFFETT. You mean I could not go to the bank and get gold coins?

Mr. ECCLES. Well, a few people got gold. That was all right. The amount of gold today, in dollars, is based upon the price at which we fix it. We could double the amount of gold in the world in terms of dollars if we said we would pay \$70 an ounce instead of \$35 an ounce. But when the price of gold was \$20.67 an ounce the total amount of gold in the world was about 11 billion dollars. There was over a hundred billion dollars of obligations in this country alone, payable in gold.

Mr. BUFFETT. Why did the people not want the gold at that time? Because the price level was reasonable?

Mr. ECCLES. Surely, that was the reason. But the fact that they could get gold did not keep it stable, because they could get gold, from 1929 to 1933, up to the time of the bank holiday, and the price of gold was \$20.67 an ounce.

The fact that they could get it, and the fact that the price of gold did not change, certainly did not keep the economy stable, and you had a decline, from 1929 to 1933, of a terrific amount, even though you could get gold.

Therefore, I say that the idea that the gold standard keeps your money safe and keeps the economy stable is a myth and a fiction, based upon the historical facts.

Mr. BUFFETT. Well, it has done a better job than any managed currency, as far as I can learn.

Mr. ECCLES. Well, you had a very different world picture before the two world wars. The gold standard worked fairly well, but it was never really a gold standard in the sense that we think of it. It was a sterling standard. Up until the First World War it was the Bank of England that managed the gold standard. We called it an international gold standard. What it really was was an international sterling standard; and sterling, at that time, was the currency of the world in the same way that the dollar is the currency of the world today.

When the war came along and Britain lost its creditor position in the world, they were no longer able to manage the gold standard. They tried to get back on it and were unable to, and what was thought of as a gold standard, but which was a sterling standard, disappeared.

Now you have no chance of getting back to the gold standard in the sense that it would be an international gold standard where gold is freely exchangeable within the various countries and within the country. It will be used, to a certain extent, as an international yardstick; but even at that, it has not proved to be very effective.

Mr. BUFFETT. Then what hope can you offer the bond holder or prospective bond buyer in this country that his bond is not going to

deteriorate as much in the next 30 years as the French bonds and money have deteriorated in the last 30 years?

Mr. ECCLES. I certainly am going to offer him no such prospect, unless the Congress of the United States, in carrying out the monetary and fiscal policy of this country—and that, after all, is where the source is—can create a greater degree of economic stability in the future than we have had in the past.

The stability of the purchasing power of the dollar depends upon the amount of goods and services made available at any given time in relationship to the purchasing power.

Mr. BUFFETT. Have you made any detailed study of the spending pressures that Members of Congress are subject to in good times?

Mr. ECCLES. I have great sympathy for them. I have great sympathy for anyone who has to run for election every 2 years and go out and face his constituents. I realize the problems and the difficulties, and I realize that the pressures are simply tremendous. And it has been due to those pressures, as I pointed out this morning, that the condition of inflation that we now have has been brought about. So I sometimes despair of democracy ever being able to have enough enlightened self-interest—that is, of the people ever having enough enlightened self-interest—to prevent these excesses.

I hope that we might be able to, but certainly our whole history of the past has demonstrated that we are just unable to do it.

Mr. BUFFETT. Well, we have deprived the worker and the producer in this country of a repository of value in which he could have reasonable confidence, have we not?

Mr. ECCLES. Well, we have not deprived him of it. We have never had it. We have never had it in this country or any other country at any time.

Mr. BUFFETT. They have it in Switzerland right now.

Mr. ECCLES. Yes; but I have seen Switzerland when they did not have it, too, when they were on the gold standard.

Mr. BUFFETT. Do you mean that the Swiss peasant who had a small hoard of gold saw that value largely disappear, or be cut in two, and then cut in two again and again?

Mr. ECCLES. Oh, yes; if he wants to sit and hold onto his gold as a means of security, the way matters have turned out, gold has gradually, by devaluation—

Mr. BUFFETT. Wait a minute. He has had the physical gold. You cannot devalue his physical gold holdings.

Mr. ECCLES. That is what I am saying. By the devaluation of gold he has received, in terms of currency, an increase in his money if he wanted to sell that gold. In other words, if the people holding physical gold here could have continued to hold it when this country devalued, instead of having \$20.67 an ounce worth of gold they would have \$35 worth of gold.

Mr. BUFFETT. And their relative position under today's price level would be unchanged.

Mr. ECCLES. Well, they would be better off. The unfortunate thing is that there is not enough gold in the world—I would not say it is unfortunate, but I would say that it is a fact—that there is not enough gold in the world where everybody can hoard gold as a means of protecting the value of their savings. If everybody did it, it possibly

would not be a protective means at all, because there would be such a surfeit of gold that it would possibly lose its value.

Its value has been due, apparently, to its great scarcity, and it was considered to be the most desirable means as a money base.

I recognize that it was expected to control and stop the inflation of the money supply. The Warren theory, of course, was that in the depression the money supply seemed to be inadequate. We had deflation, and Warren had an idea that if you devalued gold and made it \$35 an ounce, that immediately you would inflate the price. Well, the difficulty is that the public did not own the gold, so that when you devalued they would have something to spend. Therefore the experiment of devaluing the price of gold, so far as inflating or increasing the price level was concerned, proved to be entirely worthless, showing that the price level had little or no relationship to gold.

Mr. BUFFETT. Do you mean that the price level in Switzerland has not been more stable than it has been in France?

Mr. ECCLES. I do not think that is because of gold. I do not think that is because of gold at all.

Mr. BUFFETT. What does cause it?

Mr. ECCLES. Well, I am not sufficiently familiar with the Swiss economy, but I know you have had a very stable price level in other countries, such as New Zealand and Australia—just as stable as in Switzerland—and they have had a managed currency. Not only that, but their central bank has been a Government-held bank practically run by the treasury.

Mr. BUFFETT. Do you think this credit curb will prove effective in stopping inflationary trends at this time?

Mr. ECCLES. I doubt it. I doubt it very much.

Mr. BUFFETT. What would be the next move, then?

Mr. ECCLES. Well, as I said this morning, unless you get a balanced budget, or not only a balanced budget but a budgetary surplus to apply against the reduction of the public debt, while through the credit mechanism you are restraining the expansion of the private debt, you are not likely to stop the inflationary tendencies; it can go on just as long as the Government is willing to pump money into the spending stream through deficits, or as long as banks are willing to expand credit to people and corporations who are willing to borrow.

Mr. BUFFETT. What will happen if the public, one of these days, decides that they have been taken for a ride in buying bonds and then seeing the value if those bonds deteriorate, and they begin to cash their bonds on a large scale?

Mr. ECCLES. That would certainly add to the inflation.

I have pointed out the element of danger where the public loses confidence in the purchasing power of their money. I did that as early as 1944 or 1945.

When the public reaches the point where the Government is not going to protect the purchasing power of its savings, then it might decide to quit saving and start to buying things. I think the public, under all circumstances, has behaved very well, and when you consider the potential inflation and the size of the deposit structure, together with the amount of governments that are almost the equivalent of currency, you realize how much more inflation is possible if the public decided to use the money they have and the government they have in order to buy things.

Mr. BUFFETT. That is one of the reasons I was against the Marshall plan, the British loan, UNRRA, and a number of other experiments. However, I am only in a very small minority. Was the Federal Reserve ever instructed by Congress to support the Government bond market at 101?

Mr. ECCLES. It never was.

Mr. BUFFETT. Does that decision on the part of the Federal Reserve Board itself have a very inflationary influence?

Mr. ECCLES. No; it may well have had the opposite. It may well have stabilized the Government bond market and given the people confidence and stopped all this cashing of Government bonds. There may have been a lot of people and a lot of institutions who would have cashed the bonds and gotten the money; and if they had gotten the money they would have been more likely to spend it than if they had held it in the form of Government bonds.

Mr. BUFFETT. Do you think that that action, plus what you are recommending here now, will lick this inflation?

Mr. ECCLES. No; I have said before that I think a budgetary surplus is far more important, and that by no credit mechanism except of the most severe type, namely, that of possibly withdrawing support from the market and denying the banks reserves, could you get at the root of inflation.

Now, let me add this in connection with the root of the inflation, and I am sorry I did not say something about it this morning:

It is better, of course, always, to deal with causes than effects. Everybody recognizes that direct controls deal only with the effects as a stopgap until you can deal with the causes. We have dealt with the effects of an excess supply of money and credit in relation to goods, by the harness of controls but we ceased to deal with the effects of the inflation before we were prepared to deal with the causes. Even at the present time we certainly have not dealt entirely, by any means, with the causes.

More production—and that, of course, is somewhat of a slow process—is absolutely essential. Ultimately, you must have a supply of goods and services equal to the potential demand. There is always a demand, but I am speaking of potential demand backed up by purchasing power. I do not believe everything has been done that possibly could have been done in the field of production. Certainly strikes by labor curbed a certain amount of production; and it was a mistake, when the war ended, to immediately reduce the workweek from 48 hours to 40, when what we needed was not less work and more money, but what we needed was more work. With more work there is more likelihood of getting more goods and services, more work and more savings. That is what was needed.

Those are the basic things you need to get at.

Now, along with that, we should not have provided the easy housing credit, which was particularly bad to the extent that it effectuated a demand for housing in excess of the supply of labor and materials.

So, to get at the causes, we must reduce in any way we can the supply of purchasing power—taxes is the most important element in that particular picture—we must do everything we can to increase the supply of goods and services available; we must keep credit from expanding.

Mr. BUFFETT. How are we going to keep well-informed people from moving steadily into things and real property when the country is exporting a large amount of its production and, by that exportation, constantly raising the replacement cost of merchandise in this country, so that a man who today buys an automobile or a gas stove or almost any kind of durable goods knows that within 2 years or 4 years or 6 years the price of those goods is going to soar simply because of the great funneling-out process of our raw materials in the way of free exports of our goods.

Mr. ECCLES. Of course, he does not know what is going to happen. If he did, of course, what you say would be true.

Mr. BUFFETT. Do you not think there is a movement like that on now?

Mr. ECCLES. No; it has certainly been a slow movement. Today you even have an excess of certain goods. You have an oversupply, as we know, of certain durable goods and some soft goods. Certainly there is an oversupply of luxury goods, because people have been, as we term it, priced out of the market.

The hopes and expectations of the people are, of course, that prices will not go higher—at least, the prices on things they buy. They would like them to go higher on the things they have to sell. Especially if they have money, or if they have credit and they want to buy, they are hoping that they can get things cheaper later on. That is one reason that the inflation has not been as great as it could be, because there have been a great many people who have deferred the purchase of a car, they have deferred their purchase of a house, and many other things. There have not been enough to do that, however, to reduce inflationary pressures. We may reach a point where enough people will be priced out of the market and will determine that they are just not going to pay inflated prices. If enough of them reach that point so that the supply exceeds the demand, then you will be in for a deflation.

Mr. BUFFETT. What do you think Congress is going to do if that happens?

Mr. ECCLES. Well, of course, if we get into a deflationary period, I think that it is going to run a certain course so as to reduce some of the inflation, but there is a limit to which it can go without wrecking the economy. We found, from 1929 to 1933, that you reach a point where the Government has to intervene on a great scale to save the system. So I would only hope that we would not wait that long. I would hope that if a deflation comes, that we will have a backlog of public housing instead of trying to do it now, and a backlog of private housing, and a backlog demand for public works. We then will have to have some deficit financing, and, whether you like it or not, you will have to reduce taxes, even though it adds to your budgetary deficit, on the great mass of people whose purchasing power would be necessary to sustain your production. We would have to resort to all kinds of crutches. I cannot foresee all of them now, but the further our inflationary situation goes, and the more people get into debt, the more the wealth becomes concentrated again in fewer hands, the greater will be the difficulty of meeting the problem that will develop.

Mr. BUFFETT. Is there any situation more conducive to the real wealth getting into a few hands than a steady deterioration of our

currency that is understood by a small group of people and not understood by the masses?

Mr. ECCLES. Well, I think an inflation certainly helps. There are the speculators who are willing to borrow any amount they can borrow, and take any kind of chances that make the fortunes, and, of course, there have been plenty of fortunes made, which makes anything that ever happened in the past look very insignificant. We were talking about taking all the profits out of war. Of course, we did not do any such thing. There is this difference this time, however: I believe the profit opportunity was much more widely spread than has ever been the case before. The fixed-income groups, white-collar classes, the unorganized workers, have, of course, taken it on the chin, so to speak. The farmers have gotten very much more than their share of the national product, national income, ever since the war started, much more than they were entitled to. That is likewise true of certain business groups. In fact, I would say most business groups have made excessive earnings since the war and particularly since the excess-profits tax was taken off. Certainly some labor groups have profited by the inflation. Their income has gone up substantially more than their increased cost of living.

On the other hand, we also have great groups who have suffered from the inflationary developments.

Mr. BUFFETT. Under our present foreign policy, it seems to me that we have pretty well underwritten the economic wants of the non-Russian world. If that is a correct appraisal, do you think that the present political leaders, and the present Presidential candidates who are pledged with this foreign policy, will come to grips with the roots of inflation?

Mr. ECCLES. Well, there is no question but what the base of our current and expanding inflationary situation is our military and our world-aid program. Without those two programs, we would very soon have a sufficient budgetary surplus, and a sufficient production to meet all of our requirements, all of our demands, and our problem then would more likely be how to prevent a deflation, how to keep purchasing power up.

Mr. BUFFETT. In other words, if it were not for \$575,000,000 or \$600,000,000 worth of goods which we send abroad each month for free, we would be having a surplus and lower price level?

Mr. ECCLES. Well, \$20,000,000,000 of our \$40,000,000,000 budget is in two places, and the reasons for both of those, after all, is the question of the Russians. Until we are realistically willing to face up to that problem, it is pretty difficult to deal with the inflationary picture. Certainly, we cannot continue a preparedness program on a basis of defense that has no terminal point, and continue a foreign-aid program—a global program—that has no terminal point, without ultimately wrecking our economy on the shoals of inflation. We must have a terminal point to both of them, and that terminal point must be brought about through our forcing the conditions of peace before we wreck our economy on the shoals of inflation or on the shoals of a regimentation of controls in an effort to prevent such an inflation. So that means we must find a basis for peace even at the risk of war before it is too late.

Mr. BUFFETT. Do you think we have made any substantial progress in that direction since the end of the war?

Mr. ECCLES. I think the whole world has deteriorated. I think our hopes have come to naught, and I think it is pretty generally recognized that instead of having made the progress that we expected to make when the war ended, there has been a gradual deterioration, and, of course, the whole source of our trouble is Russia. Unless we deal directly and firmly and specifically and soon, with that problem, rather than have an armament race, and then deal with it later on, in a Third World War, it seems to me that this inflationary thing we are talking about is hopeless.

Mr. BUFFETT. It is true, is it not, that in 1945 we were the decisive military, industrial, and political power in the world?

Mr. ECCLES. That is right.

Mr. BUFFETT. Our power in that respect has deteriorated as we have exhausted our strength since that time, and also to the extent that we have diluted the savings of our people by inflation and thus robbed them of the fruits of their labor; that is right?

Mr. ECCLES. That is what happened.

Mr. BUFFETT. I am very much disturbed in this situation in this respect, Mr. Eccles, and I do not see that we are reaching a solution. The longer we temporize with this problem, the longer period of time is provided for those who understand inflation to profit at the expense of the trusting and patriotic citizen who counts on his Government to preserve the value of his savings; is that not correct?

Mr. ECCLES. That is absolutely correct.

Mr. BUFFETT. And if we temporize with this problem, instead of helping him by postponing the climax, we simply add to his ultimate loss?

Mr. ECCLES. That is right.

Mr. BUFFETT. Thank you.

Mr. TALLE. Mr. Buchanan, have you some questions?

Mr. BUCHANAN. No questions.

Mr. TALLE. Mr. Multer.

Mr. MULTER. I agree with you, Mr. Eccles, that our military budget is nonproductive so far as our economy is concerned. You would not, however, reduce that military budget at this time, would you?

Mr. ECCLES. I do not want to get into a discussion of the justification for either the military budget or the world-aid program. I am talking of the economics of the situation, and not the justification. It is a matter that I have some views about, but I do not believe that this is the time or the place to get into the question of our military program or our foreign policy.

Mr. MULTER. I think you might have made some comment about what would happen to the E, F, and G bonds if Government support of the bond market were withdrawn.

Mr. ECCLES. Well, I am glad you mentioned that, because we do have a demand liability in the form of E, F, and G bonds of something like \$53,000,000,000. Certainly any sale of E, F, and G bonds would stop while the long-term interest rate was unsettled and uncertain, and there might be a large cashing in of those securities, because if the interest rate on market securities should go up, which it would if the prices go down, there would be no reason why holders of E, F, and G bonds would not want to either shift to the market bonds—which, of course, in itself, might stabilize the price, except that the Government would have to borrow money to pay off the E, F, and G bonds, in some

form—but the holders of E, F, and G bonds might very well cash in their securities and hold idle cash waiting to see what to do with that money, or they might cash in the bonds and try to spend the money for an automobile or for stocks or any number of things. It would be most unfortunate if the holders of those large savings bonds should start cashing them in on a large scale, which could very well eventuate if you withdrew support from the long-term market bonds.

I am glad you reminded me of that, because that is just another argument supporting the arguments that I have already made for maintaining the present rate of 2½ percent on long-term Government bonds.

Mr. MULTER. Most of those E, F, and G bonds are individually held, are they not?

Mr. ECCLES. Well, there are a lot of the F and G's that are held by corporations and banks and insurance companies.

Mr. MULTER. The surplus you mentioned, the current surplus, for the current year, being the largest the country has ever had, is true from a bookkeeping angle, but if you take into consideration the fact that by legislation this Congress has postponed into 1949 the expenditure of certain moneys already appropriated, the actual surplus would be smaller, would it not? It would be smaller than the 1947 surplus?

Mr. ECCLES. The \$3,000,000,000 that was set aside?

Mr. MULTER. Yes.

Mr. ECCLES. I think the \$7,000,000,000 surplus excludes the \$3,000,000,000. So that if it was not for that, the surplus would have been \$10,000,000,000.

Mr. MULTER. No; I think it would be \$4,000,000,000. If that money which has been appropriated this year—

Mr. ECCLES. In other words, the surplus, from a bookkeeping standpoint, \$4,000,000,000, whereas from a money standpoint it is \$7,000,000,000. So that from an anti-inflation standpoint, it is \$7,000,000,000, although from a bookkeeping standpoint it is \$4,000,000,000.

Mr. MULTER. There was considerable discussion between you and Dr. Smith as to the Federal Reserve System being a governmental agency or an independent agency and whether it is controlled by other agencies. I think the fact is that the Federal Reserve System is the most independent of the governmental agencies in the country, is it not?

Mr. ECCLES. Well, yes; that is certainly true. That is true of the System as a whole, but I would not say that is true of the Board.

Mr. MULTER. You mean the Board submits to outside influence?

Mr. ECCLES. No; I mean that the Board are all appointed by a President.

Mr. MULTER. But their terms of office usually are much longer than the term of office of the appointing official.

Mr. ECCLES. But there are two members whose terms fall due within 4 years, one every 2 years, so you see that is an important political element in the picture. The Chairman and the Vice Chairman are designated by the President, and they, of course, have to meet with and work with all of the other governmental agencies, particularly the Treasury and often, in certain situations, the State Department. The Chairman of the Board is on the National Advis-

ory Council which has to do with the coordination of the foreign economic and credit policies, and so forth. I would not say that they are any more independent than some of the other agencies—that is, the Board. Now, so far as the Federal Reserve banks are concerned, they are. They have maybe too much authority and too much independence. They are elected or appointed by the boards of the banks, the majority of which are elected by the private bankers. And the Board, in Washington, of course, is a supervisory agency, with considerable power to supervise and regulate the operations of those banks. For instance, if Mr. Sproul of the New York bank, comes down—if the Board takes a position in favor of one thing, he can come down and testify, and does right along, against the Board. So you have a degree of independence in the banks that is much greater than in the Board.

Mr. MULTER. The only positive control over the Federal Reserve System is that exercised by congressional legislation?

Mr. ECCLES. That is right. The control, and the responsibility and authority is, in my opinion, too greatly divided and diffused and I am in favor of the study that the Hoover Committee is making on the whole question of reorganization and also the suggested study of the monetary and credit and fiscal problems and organizations of Government as suggested by Mr. Aldrich. I think that we certainly are in great need of reviewing and revamping our present set-up.

Mr. MULTER. One final question: Every time a matter of controls or regulation comes before this committee, we are given the suggestion of socialism and communism. Do you think the Federal Reserve System, in its control of our banking system, smacks of socialism or communism?

Mr. ECCLES. Of course, I can think of a lot of controls which would smack very much more of socialism. I think that any controls that the Federal Reserve System exercises over the system are needed in order to help preserve our private banking and enterprise system. They are necessary to prevent the creation of conditions which might bring on socialism.

Mr. MULTER. Thank you, sir.

Mr. TALLE. Governor Eccles, you have been at work here since 10 o'clock this morning. It is almost 6 o'clock now. We thank you very much. We are very grateful for your testimony.

Mr. ECCLES. Thank you, Mr. Chairman.

Mr. TALLE. The committee will stand adjourned until 10 o'clock tomorrow morning when I understand Secretary of the Treasury Snyder will appear.

(Whereupon, at 5:45 p. m., the committee adjourned, to reconvene at 10 a. m., August 4, 1948.)

INFLATION CONTROL

WEDNESDAY, AUGUST 4, 1948

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee reconvened, pursuant to adjournment, at 10 a. m., Hon. Jesse P. Wolcott, chairman, presiding.

Present: Messrs. Wolcott, Gamble, Smith, Kunkel, Talle, McMillen, Kilburn, Buffett, Hull, Stratton, Scott, Banta, Fletcher, Nicholson, Spence, Brown, Patman, Monroney, Folger, Hays, Buchanan, Boggs, and Multer.

The CHAIRMAN. The committee will come to order. We will proceed with the hearings.

Mr. SPENCE. Mr. Chairman, I understand that the Secretary of the Interior, the Secretary of Commerce, and the Secretary of Agriculture have expressed a desire to be heard.

I feel that the members of the Cabinet who are so closely associated with the various factors which are so important in inflation should be heard.

The CHAIRMAN. Mr. Porter has asked that they be heard, but of course time is of the essence here and whatever should be done should be done as quickly as possible.

This committee is working principally in the field of finance and credit. I understand that they are going to appear before the Senate committee, and I hope that we may be able to close the hearings today after Mr. Snyder has testified.

After Mr. Snyder has testified we will go into executive session.

Mr. MONRONEY. Are we going to close them before we hear the Secretary of Agriculture on the cost of food?

The CHAIRMAN. That is the purpose. We have told Mr. Porter that we would be happy to have the Secretaries file their statements and that they would be made available to all members of the committee.

Mr. MONRONEY. That will not give us a complete coverage of the inflation-control problem—just to work on money instead of some of the other aspects as well.

The CHAIRMAN. As soon as we have concluded the testimony of Secretary Snyder we will go into executive session and take that matter up in executive session.

We have with us this morning the Secretary of the Treasury.

We are very happy to have you proceed, Mr. Snyder.

**STATEMENT OF HON. JOHN W. SNYDER, SECRETARY OF THE
TREASURY**

Secretary SNYDER. Mr. Chairman, I have a prepared statement, and, with your permission, I will read it into the record.

Mr. Chairman and members of the committee, it is a privilege to appear before this committee in support of H. R. 7062. The passage of this bill would strike a major blow against inflation.

The control of inflation is not only one of the most important domestic issues before the country today; it is also of vital significance to our foreign policy. An economic collapse in this country without doubt would prevent the world economic recovery which is essential to lasting world peace. It would further the aims of those who would like to see our foreign policy fail; who do not want world economic recovery.

The President, in his message of July 27, outlined an eight-point program for a concerted attack on the problem of high prices. The Treasury Department is directly concerned with titles I and II of H. R. 7062, which deal, respectively, with the second and third points of the President's program—namely, the regulation of consumer credit and the control of inflationary bank credit.

While these two items are important in the anti-inflationary program, we must keep in mind that they are but segments of the over-all problem and must be treated in their relation to other dominant factors bearing more directly on the cost of living.

Title I would implement the second point of the President's program, which reads as follows:

I recommend that consumer credit controls be restored in order to hold down inflationary credit.

During the war and the immediate postwar period, the extension of consumer credit was controlled by the Board of Governors of the Federal Reserve System, acting in accordance with an Executive order of the President, issued pursuant to the Trading With the Enemy Act.

In June 1947, President Truman quite properly stated that he did not consider that he would be justified in continuing the control of consumer credit longer under the authority of legislation applicable primarily to a wartime emergency, and recommended that Congress pass specific legislation authorizing such control.

Congress acted on this recommendation last summer, but the legislation then enacted extended the authority of the Board of Governors only to November 1, 1947. Since that date, no Federal agency has had statutory authority to control consumer credit.

The Senate passed a bill on December 17 to extend the authority of the Board of Governors to March 15, 1949, but the House of Representatives has not yet taken action. I believe that it is urgent in the national welfare that consumer credit control legislation be enacted as soon as possible.

Total consumer credit outstanding at the end of June reached an all-time peak of \$14,150,000,000. This is an increase of over \$2,000,000,000 since the expiration of control legislation on November 1 of last year.

The increased use of consumer credit in a period of inflationary pressures can only add to those pressures. As we all know, the cur-

tailment of the production of consumer goods during the war period gave rise to a tremendous deferred demand for such goods. And, despite the fact that industrial production since the end of the war has reached the highest level ever attained during peacetime, we have not yet been able to produce enough goods to satisfy this deferred demand. There are still many important shortages of goods. But with production near capacity levels, purchasing power made available by consumer loans can be used only to bid up prices of consumer goods. It cannot call additional goods into existence. It is imperative, therefore, that efforts be made to restrain the demand for scarce goods until supply approaches demand.

It has been urged that the volume of consumer credit, despite its unprecedentedly high level, is lower in proportion to incomes than was the case immediately before the war. This is true, but I do not consider that it is relevant to the immediate problem.

The relevant question now is not how much consumer credit the country can bear, but how little it can do with; since, at the present time, any addition to consumer credit adds to the already strong pressure of inflationary forces. I submit, therefore, that an expansion of consumer credit of the magnitude which has occurred since November 1 is not in the national interest, and that it justified the reimposition, at the present time, of moderate controls on the extension of installment credit, which has accounted for over 80 percent of the total increase in consumer credit since November 1.

At this point, Mr. Chairman, I would like to quote from testimony which I gave to two congressional committees last fall. I do this only to indicate that I have from the beginning urged this type of legislation. I gave this testimony last fall before your committee and before the Joint Committee on the Economic Report:

Anti-inflationary measures which may be taken in the monetary field are of course but a segment of the whole program, and could not, by any means, solve the problem alone. But such steps as can be taken when related to those in other fields will of course be helpful in the over-all solution.

The President is greatly disturbed in regard to price inflation, which threatens our whole economic structure, and he is convinced that the Congress is equally concerned.

The President has laid special emphasis on voluntary actions on the part of businessmen, labor leaders, farmers, and consumers to hold prices down. Intensified efforts will be continued to obtain voluntary restraint. Certain powers are necessary, however, to fortify the voluntary efforts.

The President has suggested that consideration be given to the following monetary measures: (1) That consumer credit controls should be restored and some restraint should be placed on inflationary bank credit; (2) legislation should be provided to prevent excessive speculation on the commodity exchanges; (3) intensified activity in the sale of savings bonds * * *.

As to item 1—restoration of consumer credit controls and restraint on inflationary bank credit—these matters have been discussed by Federal Reserve officials. As to consumer-credit controls, I am in favor of their restoration.

The most effective types of credit control are those which strike at the individual forms of credit extension which are contributing to inflationary pressures. The most important single form of such credit extension at the present time is in consumer credit.

Total consumer credit outstanding at the end of September reached an all-time peak of \$11,400,000,000. At the end of 1945, it amounted to only \$6,600,000,000. Prior to December 1946, total consumer loans outstanding at any one time had never reached the \$10,000,000,000 level.

This increased use of consumer credit in the present period of inflationary pressures can only add to those pressures. As we all know, the curtailment of the production of consumer goods during the war period gave rise to a tremendous

deferred demand for such goods. As we all know, despite the fact that industrial production during 1947 has reached the highest level ever attained during peacetime, we have not yet been able to produce enough goods to satisfy this deferred demand. There still exist many important shortages of goods. But with production near capacity levels, purchasing power made available by consumer loans can be used only to bid up prices of consumers' goods, not to purchase more goods. It is imperative, therefore, that efforts be made to restrain the demand for scarce goods until supply approaches demand.

Money market interest rates form a small part of the total cost of consumer credit, and changes in such rates are almost powerless to limit its extension. It is necessary to cover specifically by regulation such matters as minimum down payments and the maximum periods over which payments may be spread on installment purchases of consumers' goods in order to restrain this type of inflationary credit.

Title II of H. R. 7062 would implement the third point in the President's program. This point reads as follows:

I recommend that the Federal Reserve Board be given greater authority to regulate inflationary bank credit.

The expansion of bank credit, except in the fields of consumer and real-estate financing, has not, in my opinion, been a major contributing force to present inflationary pressures. We must, however, attack the problem of inflation on all fronts.

I have always believed that our chief reliance for the control of inflationary bank credit lies in the good judgment of the individual bankers in the 15,000 banks in the United States. The Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the executive committee of the National Association of Supervisors of State Banks, representing the Federal and State supervisory authorities, have urged bankers to confine the extension of bank credit under existing conditions, as far as possible, to loans that would help production rather than increase consumer demands.

The banks, in general, have been most cooperative. I should like to take this occasion to commend their public spirit, and particularly to commend the American Bankers Association for its program to secure the maximum voluntary curtailment in the extension of bank credit.

But, in the present situation, I think it is clear that prudence requires that additional instruments, to supplement the voluntary action of the bankers, be placed in the hands of the Federal Reserve System.

At this point I would like to quote again from my testimony on inflation control last November:

I would like to point out that I have a positive feeling that the major objective at this time is to maintain the fiscal soundness of the Government and the continued confidence of the public in Government obligations. I feel that the attack on the problem can best be handled by the application of a substantial budget surplus to the reduction of the public debt in the manner which will extinguish an equivalent amount of bank-held Government securities. Since the end of the war, the Treasury has conducted its program of debt management in such a way as to reduce inflationary pressures whenever possible by paying off bank-held securities.

I believe that we have reason to be proud of the manner in which this program has been conducted. The debt has been reduced by about \$26,500,000,000 since the postwar peak reached at the end of February 1946. Not only has the whole of this reduction occurred in bank-held securities, but an additional \$3,500,000,000 of securities have been transferred from bank to nonbank ownership.

In the course of conducting this program, there have been periods when our immediate objective has been to restrain price increases in Government securities, and other periods in which the long-term Government-security market has been supported. The degree of stability which these operations have imparted to the whole high-grade security market has been of major benefit to the business community.

During the heavy tax-collection period of January, February, and March of this year we had a budget surplus of over \$6,000,000,000. Part of this was used to retire debt and part was saved for the lean tax-collection months.

Our present heavy debt, with the resultant addition to the money supply and to the stock of liquid assets, was created, for the most part, as a result of our wartime deficits. These deficits were part of the price of winning the war and were incurred despite an eightfold increase in our tax receipts as compared with the period immediately preceding the war. The debt can be reduced—and the process which attended its creation reversed—only by continuing budget surpluses.

Unfortunately, as a result both of the tax-reduction bill and of the increased-foreign aid and defense expenditures made necessary by the tense international situation, we no longer have a budget surplus at our disposal as a weapon for combating inflationary pressures. In the fiscal-monetary area, we must, therefore, lean to an increasing extent upon other measures for the restriction of bank credit.

The legislation before your committee is born of this necessity. It authorizes the Board of Governors of the Federal Reserve System to increase member bank reserve requirements against demand deposits by 10 percentage points and against time deposits by 4 percentage points. These permissible increases would be in addition to the existing statutory maxima and could be applied flexibly to demand deposits in general or to those in banks in central reserve cities, in reserve cities, or in other places, separately; or to time deposits, as required. The bill provides that these changes in reserve requirements shall not continue in effect beyond June 30, 1950.

Reserve requirements, at the present time, are at their statutory maxima for time deposits in all banks, and for demand deposits in all banks except those in central reserve cities. The present reserve requirement for demand deposits in banks in central reserve cities is 24 percent, as compared with a statutory maximum of 26 percent.

The only remaining authority of the Board of Governors to tighten credit conditions through the medium of increasing reserve requirements applies, therefore, to banks located in central reserve cities. But these banks have shown the least credit expansion, in the recent past, of any class of bank.

It is clear, consequently, that the remaining power of the Board of Governors to increase reserve requirements is not well suited to the nature of the problem which now confronts us.

The proposed legislation would remedy this by providing the Board of Governors with authority to cope with the excessive expansion of bank credit—whenever this may best be done by the required reserve method—in the class of bank where such control seems most needed.

The CHAIRMAN. Mr. Secretary, how would the powers to control installment credit be used?

Secretary SNYDER. I beg your pardon?

The CHAIRMAN. How would the powers to reimpose installment credit be used, if the bill were passed?

Secretary SNYDER. It would be under the supervision of the Federal Reserve Board, and they would direct such imposition of credit controls as were deemed advisable to restrain the excessive use of consumer credit.

The CHAIRMAN. Well, their purpose would be to cut down the volume of consumer credit.

Secretary SNYDER. The purpose would be to cut down the volume of demand for scarce goods. That would be the end effect of it—or the desired effect, at any rate.

The CHAIRMAN. Then, the purpose of it is not to cut down the volume of credit?

Secretary SNYDER. That would be the procedure, but, as I say, the desired effect of that would be to reduce the volume of demand for scarce goods, and not bid up the price when it would not produce any greater volume of goods.

The CHAIRMAN. It was suggested here to us yesterday that at the present time with savings and income, as high as they are, you would not cut down the demand for goods in short supply if you made people pay all cash.

Secretary SNYDER. But you are adding to the cash available an additional amount of credit which is bidding against the limited amount of goods we have available.

The CHAIRMAN. Let us take a person with a thousand dollars worth of E bonds, as an example. Let us assume that he wants to buy an electric refrigerator, let us say. The Federal Reserve has provided that he has to pay 33½ percent down, pay 4 or 5 percent interest, and amortize the debt over a relatively short period of time. Those E bonds that he has in his savings now cannot be monetized, can they?

Secretary SNYDER. They all have a cash value, yes, sir.

The CHAIRMAN. I mean they cannot be pledged for the issuance of Federal Reserve notes.

Secretary SNYDER. No, they cannot be pledged.

The CHAIRMAN. So if he was to take his E bonds, cash them in, and buy the refrigerator, that money would find its way back into the bank system, would it not?

Secretary SNYDER. That is correct, but that was part of the bonds program, to educate people in saving.

The CHAIRMAN. So long as that E bond stays in his possession, that part of the debt cannot be monetized. But if he takes that E bond, cashes it in, and pays cash for his goods, that cash goes back into the bank and that cash can be converted into long-term bonds which can be pledged for Federal Reserve notes; that is right, is it not?

Secretary SNYDER. Yes, that can be done.

The CHAIRMAN. And the man who has no savings, he just does not buy. Do you not think that savings are high enough, and the current incomes of many people are high enough so that the imposition of installment credit controls does not cut down the demand for goods sufficiently so that it would affect prices favorably?

Secretary SNYDER. I think it would have its effect. As I have just stated in my prepared statement, I do not believe that these monetary controls in themselves are the answer to the anti-inflationary

effort. They are just a segment of it, and added to the other efforts that might be made, they would be effective. By themselves alone, I do not think they are going to cure the inflationary forces.

The CHAIRMAN. We have always thought that the reason for consumer credit controls was to cut down the volume of credit. Now, you say its purpose is to cut down the demand.

Secretary SNYDER. No, it cuts the volume of credit, that is true, but its end result is that by not providing the credit, it does actually cut down the demand for scarce goods which, in turn, prevents the increase in prices of those goods.

The CHAIRMAN. In 1947 the volume of consumer credit increased, as I recall, about \$3,000,000,000. I think that on November 1, when controls were taken off, the volume was about \$9,000,000,000. In December and January, when you wanted to restore these controls, you said that the necessity for it was due to the increased volume of consumer credit during 1947. Yet you had consumer credit controls for 10 months of 1947. While consumer credit controls were available, the volume of consumer credit increased \$3,000,000,000. In other words, when you wanted to reimpose these controls, you said the volume of credit controlled, but when you had the power to control the volume of credit, you applied it selectively on only 12 categories of items. That is the point I want to bring out. How are you going to apply these controls? Are you going to apply them across the board, to reduce the volume of credit, or are you going to apply them selectively under the mistaken theory that you can reduce demand for goods in short supply?

Secretary SNYDER. Well, you had the people down here yesterday, Mr. Chairman, whose job it is to implement those controls, and they could better have told you how they intend to use them than I can, because I have no control over them.

The CHAIRMAN. They could not give us very much definite information as to how they would be applied.

Secretary SNYDER. Well, of course, that is one of the problems they will have to meet, if you impose them. They will have the jurisdiction over them.

The CHAIRMAN. If the Congress should give the Federal Reserve the authority to raise reserve requirements, have you, in any of your consultations, been able to determine how much the reserves would be increased under the authority which you would have?

Secretary SNYDER. There has been no definite answer on that to me from the Federal Reserve people, sir. The fact is that they have reached the limit of their powers under the reserve requirement legislation.

The CHAIRMAN. They have reached the limit—

Secretary SNYDER. Except with respect to the 2 percent in the central reserve cities.

The CHAIRMAN. They reached the limit in all but the central reserve cities last year?

Secretary SNYDER. That is correct—earlier than that.

The CHAIRMAN. And the reason why this committee did not act on any bill to increase the reserves—I might say that on several occasions I and other members of the committee suggested that if the administration did not think it had the power to stabilize our economy in the orthodox ways in which it has always been done, we would be

very glad to give consideration to it, and it seems to me that last January and February, when the proposal was made to the Joint Committee on the Economic Report that Mr. Eccles was in favor of secondary reserves, the Treasury was not in favor of secondary reserves, and the controversy was raging between the Treasury and the Federal Reserve as to whether they needed the authority or not, so we decided, I believe, that we would let the Federal Reserve and the Treasury get together on the problem and settle their differences without the embarrassment of hearings before this committee.

Now, I assume that the Treasury and the Federal Reserve are together on their request for an increase in primary reserves.

Secretary SNYDER. Mr. Chairman, as you know, I was never called upon to testify before any committee on that particular subject last year. I was asked the question informally, at one time, as to certain phases of it, but I was never called upon to testify on that particular phase of the program.

The CHAIRMAN. Mr. Eccles said yesterday that he was in favor of these reserves and the Treasury was against them, last February.

Secretary SNYDER. I think that if you will recall, you asked me the question one day, Mr. Chairman, if I thought that this special reserve would accomplish the end for which it was designed, and I said I had my doubts. I believe that is the only statement I ever made in connection with that matter, and I am highly gratified and flattered to think that such a simple statement as that would influence this body. But insofar as any wrangle or fuss, as you referred to, I have never recognized that. I do not think there has been any wrangle or misunderstanding. I read into the record on the Senate side a statement by the Chairman of the Federal Reserve Board, dated December 10, which I will be glad to include in your hearing here if you would like, which states just what I have said, that there was no degree of difference between the Treasury and the Federal Reserve Board.

In order again to clarify the background of the legislative history, I would like to inject here a statement by the Chairman of the Federal Reserve Board on December 10 at the conclusion of the hearings that were conducted at that time:

In view of the fact that some of the press has emphasized a difference in viewpoint between Secretary Snyder and myself in regard to the Board's so-called special reserve proposal, I would like to take this opportunity to clarify the record. I have discussed the matter with the Secretary. The fact is that the area of agreement between us is much more complete than has been represented. Such difference as exists is in evaluating the degree of restraint on inflationary expansion of bank credit that would be exerted by the special reserve requirement. He has expressed to this committee some doubt as to its effectiveness. I am more sanguine about it. We both feel that whether the special reserve is needed at all or whether some stronger measure of restraint may be needed next year depends on factors which cannot be determined in advance with certainty at this time. We are in full agreement:

1. That the most effective anti-inflationary measure has been and should continue to be a vigorous fiscal program to insure the largest possible budgetary surplus consistent with the Government's obligations at home and abroad.

2. That coupled with an intensified savings bond campaign, the program accomplishes two vital purposes. To the extent that savings of the public are invested in savings bonds, spendable funds are taken out of the market place at this time of excessive demand and insufficient supply and can be used to pay off maturing debt held by the banking system. Likewise, a budgetary surplus can be used to reduce bank-held debt. Both measures reverse the process by which the money supply was increased during the war and are effective anti-inflationary influences.

3. That the program which the Treasury and the Open Market Committee have been pursuing during the year has been effective and will continue to exert restraint during the next few months, when the Treasury will continue to have a substantial cash balance that can be used to reduce bank-held public debt.

4. That some additional restraint may be expected as a result of the joint statement of Federal and State bank supervisory authorities cautioning banks against overextension and inflationary lending.

5. That the problem will present a different phase when current debt-payment operations are no longer available. If it appears that other restrictive steps are needed, increased reserve requirements or possibly some stronger measure may be necessary.

6. That this will depend on the course of events and in part upon self-imposed restraint by the banking community, which has gained a broader understanding of the problem as a result of discussions before Congress and in the press.

7. That the Board's proposal is not in any sense a substitute for but a supplement to the fiscal program and direct action on other fronts where inflationary forces are generated but cannot be corrected by monetary and fiscal policy alone.

8. That under present and prospective conditions it is essential to maintain the established 2½-percent rate on long-term marketable Government securities.

9. That restraints should be reinstated on installment credit.

The area of disagreement, therefore, narrows down to whether the special reserve would be appropriate if additional measures prove necessary to limit the now unrestricted access of the banking system to reserves upon which a multiple expansion of bank credit can be built.

The CHAIRMAN. So far as I know, no communication has ever come to this committee from the administration, from the Treasury, or from the Federal Reserve, in the last 2 years, until the President's message, asking for an increase in primary reserves; is that right?

Secretary SNYDER. Well, your records show what you have.

The CHAIRMAN. The record does not show that we have ever received any request from the administration for an increase in primary reserves until the President's message on the 26th of last month.

Secretary SNYDER. Well, of course, it is the primary responsibility of the Federal Reserve System to make those recommendations. The Treasury will appear on any such proposals as it makes. But the Treasury never makes proposals as to the conduct of the affairs of the Federal Reserve bank. As I say, I was never called on to testify on that matter.

The CHAIRMAN. Let us put it this way: If the Federal Reserve is given the power to increase these reserves, what would be your recommendation with respect to the use of that power?

Secretary SNYDER. As to what, sir?

The CHAIRMAN. What would be your recommendation to the Federal Reserve with respect to the use of these powers—the amount to which they would increase their reserves?

Secretary SNYDER. I would make no public recommendation on that, sir. That is their responsibility, and I would like to hear what they have to say about it. I would not make a public recommendation on what they should or should not do.

The CHAIRMAN. It would affect somewhat their program to support the Government bonds, does it not?

Secretary SNYDER. A great number of matters would have to be taken into consideration in making the decision as to where they should move in the imposition of additional reserves.

The CHAIRMAN. There has always been, of course, a very close affiliation between the Treasury and the Federal Reserve. We just assume that you and the Federal Reserve have talked these things over.

Secretary SNYDER. The Federal Reserve and the Treasury Department have worked in very close cooperation ever since I have been in the Treasury Department, and it is my understanding that that situation has occurred all along.

The CHAIRMAN. Now, if the Federal Reserve raised requirements unduly, you might expect banks to sell Governments, would you not?

Secretary SNYDER. It might have a direct bearing, and we would certainly discuss it at great length with them before any such move was made.

The CHAIRMAN. You might expect also, from your experience as a banker, as well as Secretary, that if the rates were too high, the banks would call in a great many of their loans?

Secretary SNYDER. It could result in that, yes, if the banks are overloaned.

The CHAIRMAN. I guess we all agree, then, that the powers should be used very carefully and judiciously.

Secretary SNYDER. Without doubt, they would have to be used with a great deal of careful study.

The CHAIRMAN. Having those things in mind, have you any recommendation as to the amount of the increase in reserves which the Federal Reserve should impose, if this power is given to them?

Secretary SNYDER. I did not understand that, sir.

The CHAIRMAN. I say, having these things in mind, the necessity on the part of the banks, perhaps, to sell Governments, and the necessity on the part of the banks to call loans, having those things in mind, have you any recommendation or any opinion as to the amount of increase in reserves which might be desirable?

Secretary SNYDER. The Board would have to carefully study the area of extension of bank credit by the various groups of banks, under the different classifications—the central reserve cities, the Reserve cities, and so forth, to see where the excessive credit might be extended, and possibly move in the area in which it would be most effective.

The CHAIRMAN. Well, as you say, the power to increase the reserves has been exhausted since last year some time, and we have not been able to get any information from either Mr. McCabe, Mr. Eccles, or Mr. Evans, with respect to the proposed increase or even with respect to what they have in mind with respect to an increase. Yet they are asking for power to increase. For almost a year now, their power to increase reserves has been exhausted, and yet they have made no request to Congress for power to increase the reserves. It seems to me that the whole thing is so nebulous that the Congress finds it difficult to legislate intelligently on the subject.

Secretary SNYDER. I find that in the management of the debt it is a real problem to discuss publicly what we are or are not going to do in reference to interest rates and things of that sort. It makes it a very difficult problem to try to manage the debt under public discussions of that sort, because unfortunately, as Secretary of the Treasury, I can make no statement that is not immediately translated into an intended course of action. I do not know whether that same holds true with the Federal Reserve Board in their reluctance to make statements or not. If they made a statement today that they intended to move into a certain direction, that would be translated into an intent that might immediately have some effect that they would want to study carefully before acting upon such a proposal.

The CHAIRMAN. There seems to be a great deal of controversy, among the members of the Federal Reserve Board, as to Federal Reserve policies. A matter of 3 days ago, the Federal Reserve asked for the authority, in the bill which has been introduced, to increase these reserves only on member banks. The day before yesterday the Federal Reserve Board met and decided it wants this power to apply to all banks, nonmember as well as member banks. In 24 hours they changed a policy which presumably they had been discussing for a year. What is your opinion with respect to whether these increased reserves should be imposed on State nonmember banks?

Secretary SNYDER. Well, I accepted the proposal that was made, as I understood it, which was formulated by the staff of the Federal Reserve Board and was incorporated into the President's message and into the bill supporting that message, and, as I understood, it had the support of the Federal Reserve Board. Of course, that would cover about 80 percent of the outstanding loans and investments in banking today.

The CHAIRMAN. About 85 percent.

Secretary SNYDER. Well, in excess of 80 percent; yes. If 85 percent is the figure, I will accept it, of course. But it is a large part of it. That is what influenced me there. If all banks can be brought under this act constitutionally, why, certainly I would be in favor of it. Definitely there is no intention or desire on my part to hurt the Federal Reserve System or to weaken it in any way. I think we must keep it a very strong System.

The CHAIRMAN. Mr. Spence.

Mr. SPENCE. Mr. Secretary, do you think the control of consumer credit, installment buying, and the increase in the authorized reserves of the banks, will control the present inflationary conditions without resort to other measures?

Secretary SNYDER. I very definitely stated that this was only a small segment of the whole program, and would not, by itself, be too effective. As you recall, I said in my statement:

While these two items are important in the anti-inflationary program, we must keep in mind that they are but segments of the over-all problem and must be treated in their relation to the other dominant factors bearing more directly on the cost of living.

Mr. SPENCE. Would there be any effort to roll back the present consumer credit? Or would there be merely an effort to halt it where it is?

Secretary SNYDER. Well, I do not know if there would be any chance of rolling it back, because it would just be a matter of putting in the regulations covering future credit. It would be pretty difficult to go back and undo an extension of credit which has already been made.

Mr. SPENCE. The Federal Reserve is an agency of Congress, but it is an independent organization so far as the Congress is concerned. Is it not a fact that the powers we delegate to the Federal Reserve are legislative powers and that it is entirely in the discretion of the Federal Reserve as to how they will use those powers?

Secretary SNYDER. I think that is true. You give them certain legislation under which they can act, and leave it up to them to operate.

Mr. SPENCE. There has never been any law or direction as to how those powers shall be used; they are entirely within the discretion

of the Board of Governors of the Federal Reserve System; is that not correct?

Secretary SNYDER. I think that the Congress recognized the fact that they could not be too specific in matters relating to monetary controls and to the management of credit matters, that they could not spell it out too specifically and make it too inflexible. They intended to make a certain degree of flexibility available to the Board in taking actions within its discretion which would be helpful to the over-all problems of fiscal management.

Mr. SPENCE. What other measures would you recommend with reference to the control of inflation besides the reimposition of consumer-credit controls and the increase in bank reserves?

Secretary SNYDER. Well, the President has proposed a number of measures here, and you have had testimony from Mr. Porter on those various items, sir.

Mr. SPENCE. Are you in favor of those measures?

Secretary SNYDER. I think they are necessary to meet a situation of continued inflationary pressures, which might get out of hand. Certainly we have got to take such steps as we can to prevent inflation from getting too firm a grip on the country.

Mr. SPENCE. The inflationary condition is growing worse all the time; is that not true?

Secretary SNYDER. That is the evidence which has been presented; yes.

Mr. SPENCE. I do not think there is any argument on that score. You think that these measures which you have recommended, while they are important segments of the relief proposed, in and of themselves, would not substantially control the conditions which now exist?

Secretary SNYDER. I doubt if alone they would be too effective.

Mr. SPENCE. That is all.

The CHAIRMAN. Mr. Secretary, when you were before this committee last November, I asked you this question—appearing on page 40 of the printed proceedings on the problem of economic stabilization:

Have you had in mind that you would be in favor of giving the Federal Reserve the permanent authority to raise, without limitation, reserve requirements?

Secretary SNYDER. As I understand that proposal, I would not favor it because I do not think it would accomplish the purpose toward which it is aimed.

The CHAIRMAN. Do you think it would be necessary, as a permanent authority, to create what has been termed by Mr. Eccles a secondary reserve?

Secretary SNYDER. Well, I do not want to talk about something with which I am not familiar.

Is your position now the same as it was then?

Secretary SNYDER. My position is exactly the same—this is a different matter which we are discussing here. That was dealing with raising it by considerable volume and under different circumstances, particularly with reference to the Treasury position. At that time we had a surplus that we could depend on in reducing the bank-held debt, and we had a number of other resources to which we could resort, which we have not now within our possession. But this bill which is proposed today is an extension of an orthodox procedure which Congress has approved.

The CHAIRMAN. Let me suggest to you that your objection might have gone to the permanent and unlimited amount of authority which the Federal Reserve would have.

Secretary SNYDER. That is what I say. It was a different proposal than any which is now before us.

The CHAIRMAN. Because it is limited as to date and as to amount?

Secretary SNYDER. Very definitely limited to the date of June 1950.

The CHAIRMAN. Then, you are saying that a 10-percent increase in reserve requirements would do the job?

Secretary SNYDER. Not necessarily. I said it would be a part of the whole program. It is just a matter of keeping pressures on the reserves, and this would give them some latitude within which to do that.

The CHAIRMAN. Understand, we were discussing at that time the 10-point program of the President, similar to that which we are discussing at the present time, and the purpose of it was to control our economy and to prevent prices from going higher. The question at that time, directed to you, was:

Have you had in mind that you would be in favor of giving the Federal Reserve permanent authority to raise, without limitation, the reserve requirements.

Your answer was:

As I understand that proposal, I would not favor it, because I do not think it would accomplish the purpose to which it is aimed.

Now, the purposes, according to the President's statement and the statement of the witnesses with respect to the increased reserve requirements, are the same now as they were then: namely, to give the Federal Reserve more authority to control the volume of bank credit. Why are you in favor of it now when you were not in December?

Secretary SNYDER. That is not the same type of thing. I am not testifying on the same type of proposal.

The CHAIRMAN. I was not referring in my question to the secondary reserves. We go on from there, and I asked you:

Do you think it would be necessary, as a permanent authority, to create what has been termed by Mr. Eccles a secondary reserve?

And in answer to that you say:

Well, I do not want to talk about something with which I am not familiar.

So as a consequence of that, this committee did not go any further, apparently, on this question of raising the reserves.

Secretary SNYDER. Again I say I am flattered that one little statement of mine, two sentences, would have swayed this committee.

The CHAIRMAN. I think we took the attitude that if you were not interested enough to familiarize yourself with it, we surely should not be too enthusiastic about it at the present time.

Mr. Kunkel, do you have any questions?

Mr. KUNKEL. Yes, Mr. Chairman.

Mr. Secretary, if you include the nonmember Reserve banks under this authority, do you not anticipate that that will be a rather severe blow to the dual banking system?

Secretary SNYDER. I do not understand your question. If you included the nonmember banks?

Mr. KUNKEL. Yes, if we included the nonmember banks in this additional power, we are giving the Federal Reserve System over reserves, do you not think that will tend to weaken the dual banking system by inducing more banks to shift over to the Federal Reserve System?

Secretary SNYDER. Well, I do not think that as a temporary measure that it would, frankly. And, as I said before, I want to be sure

that there is a constitutional way of doing it; in other words, that extending requirements over all banks would be done within the constitutional limits. I do not think that any measure of that short a period would have any material effect as to weakening the dual system. I would suggest, if that is to be considered as part of the program, that the president of the National Association of State Bank Supervisors should be heard and allowed to give testimony in connection with the proposal.

Mr. KUNKEL. If you are the head of a nonmember bank, you do not have the certain advantages which are attainable by a rival bank which is a member of the Federal Reserve System; is that not correct?

Secretary SNYDER. There are certain privileges and advantages that a member bank has, in the way of rediscounts, shipment of currency, check collections, and things of that sort.

Mr. KUNKEL. On the other hand, there are certain advantages that you have as a state bank which the member bank does not have?

Secretary SNYDER. That is correct. But the State banks, through their closer relationship with the Federal agencies, are becoming more and more uniform in their requirements and regulations.

Mr. KUNKEL. And they are being regulated by the States?

Secretary SNYDER. Each State has its own banking laws which regulate the State banks operating within that State; that is correct.

Mr. KUNKEL. Now, you being the head of a nonmember bank, have been deprived of all these advantages which you might have obtained. Now, suddenly, in a period of crisis or danger, whatever we might call it, you find that the Federal Government steps in and imposes upon you the same restrictions and the same rules to which the Federal Reserve member banks have voluntarily submitted to by their membership in the Federal Reserve System. I should think if you saw a situation like that arising, and legislation passed which did impose those restrictions on you, that you would have a tendency to say, "Well, from here on in I am going to get into the Federal Reserve System and take the advantages as well as the disadvantages." I believe a great many State bank directors and officials would hold that same view, and therefore, it would tend to weaken the State banking system quite extensively—whether the period were short or whether the period were long. Because no matter how long it might be, it would establish the fact that at any time, at the whim of the Federal Government, you could be subjected to the same disadvantages, assuming it is a disadvantage, to which a Federal Reserve member bank was subjected. Do you not think it would have that tendency?

Secretary SNYDER. I am not too sure that it would.

Mr. KUNKEL. Well, you are not at all sure that it would not, are you?

Secretary SNYDER. I am not certain either way. That is why I would like someone who is well versed in State banking operations to present testimony on that subject, if that is to be included in the bill.

Mr. KUNKEL. From a practical standpoint, if we increase the reserve requirements on the banks, what course of action do you think most of the banks will take, in order to meet those additional reserve requirements?

Secretary SNYDER. The banks have been taking a very careful view of this whole problem of inflationary credit within the past 6 or 8 months. I found, by talking with the examining departments of all

three of our Federal bank-supervisory agencies, that since we have been discussing these problems of inflationary credit, that the bankers are beginning to take a much more careful view of their portfolios and studying them as to the uses of the loans, as to the collateral behind them, and as to the manner of paying off the loans, with a great deal more care. Therefore, I would feel certain that if there were additional reserve requirements imposed, that they would exercise that same careful study in balancing their portfolios.

Mr. KUNKEL. In general, do you not think it is true that, portfolios being what they are generally throughout the country, that they would sell Government bonds?

Secretary SNYDER. There is that probability. But it would be a matter of their studying their portfolios and doing what best suited each bank.

Mr. KUNKEL. When you look at their portfolios, practically every bank in the country is loaded to the gills with Government bonds. If they do sell Government bonds, who is going to buy them?

Secretary SNYDER. We have that problem facing us, without doubt.

Mr. KUNKEL. Well, the Federal Reserve has to buy them; is that not right; in the last analysis?

Secretary SNYDER. If it is necessary to support the long-term rate, we have adopted a policy of that sort, yes.

Mr. KUNKEL. So the net effect would be to transfer the earning power of the bank to the Federal Reserve; would it not? The Federal Reserve would get the interest on the bonds instead of the banks which had them in their portfolios?

Secretary SNYDER. That would be the effect of their purchasing the bonds, yes.

Mr. KUNKEL. And to that extent, Mr. Eccles' proposal for a secondary reserve, which would freeze the assets in the banks, and let the banks retain the earning power, would be as definitely anti-inflationary and at the same time would not hit at the earning power of the banks; is that not correct?

Secretary SNYDER. Would you repeat that, please?

Mr. KUNKEL. Mr. Eccles' proposal, of which the gist is that the banks could set aside a reserve of Government bonds in which they would retain ownership, is that it would increase the reserves and at the same time have the same anti-inflationary effect, but at the same time it would permit the banks to retain the earning power of the bonds, whereas, under the present proposal, assuming that a fair percentage of the banks would increase their reserves through the sale of Government bonds, would shift that earning power from the banks to the Federal Reserve.

Secretary SNYDER. Well, that was limited to the short-term securities.

Mr. KUNKEL. Well, Mr. Eccles limited it to short-term securities. But it would not necessarily have to be limited to short-term securities.

Secretary SNYDER. That is what he proposed.

Mr. KUNKEL. That is what he proposed, but I mean, you could extend that principle and allow long-term Governments just as well as short-term Governments.

Secretary SNYDER. That is a problem we would have to discuss at great length.

Mr. KUNKEL. Now, I want to call your attention to the statement on page 5 of your statement, second paragraph from the bottom of the page, which states:

The debt has been reduced by about \$26,500,000,000 since the postwar peak reached at the end of February 1946.

There was a Victory Loan drive in late 1945, the proceeds of which were 20 billion dollars; is that not correct?

Secretary SNYDER. About 20 billion dollars; that is correct.

Mr. KUNKEL. And then in 1946, the Government had a cash balance of about 26 billion dollars, of which 20 billion dollars was money raised by this sale of Victory bonds in 1945; is that not correct?

Secretary SNYDER. That is correct.

Mr. KUNKEL. So that when you speak of the debt reduction of 26½ billion dollars, what you really did was to collect 20 billion dollars through the sale of bonds, and then pay 20 billion dollars back with an over-all reduction of 6½ billion dollars?

Secretary SNYDER. My reference to that, sir, was to the manner in which it was applied to the reduction, so as not to upset our whole fiscal program. If we had immediately taken that money and paid it off, we would have thrown our whole banking system out of gear right at the time when we were trying to turn around and move toward conversion to peacetime operations. It took very careful handling, taking that amount of money out of the banks. It had to be done in very orderly fashion. That was the point I was bringing out.

Mr. KUNKEL. But the figures I have stated are correct, are they not?

Secretary SNYDER. They are correct; yes, sir.

Mr. KUNKEL. Do you know whether the ratio of increase of consumer credit has been greater during the period since controls were removed than during the equivalent period preceding the removal of controls?

Secretary SNYDER. I can get that for you.

Mr. KUNKEL. I would be glad to have you put that in the record.

(The information referred to is as follows:)

A comparison of the increases in consumer credit before and after the expiration of consumer credit controls should be considered in two parts. On the one hand, installment credit—on which we seek to revive controls—increased by \$1,307,000,000 (or 31.4 percent) during the 8 months prior to November 1, 1947 and \$1,729,000,000 (or 31.6 percent) during the succeeding 8 months through June 30, 1948. At the same time charge accounts, single payment loans and all other consumer credit rose by \$729,000,000 in the 8 months prior to November 1, 1947, and \$365,000,000 in the succeeding 8 months. It is the increase in installment credit, of course, about which we are particularly concerned.

Mr. MULTER. If the gentleman will yield: You will find that information on page 22 of the charts furnished by the Federal Reserve, and you will find that from 1946 to 1948 consumer credit increased 133 percent, while it was fairly static from 1942 to 1946.

Mr. KUNKEL. That does not answer the question I asked, however. I am asking for the increase during the period since controls were removed in comparison with an equal time before controls were removed.

Mr. MULTER. You have that comparison shown.

Mr. KUNKEL. No; we are not speaking about the same period.

The CHAIRMAN. Mr. Brown.

Mr. BROWN. Mr. Secretary, did I understand you to say that you are in favor of increasing the reserve requirements of State nonmember banks?

Secretary SNYDER. I said if it could be done constitutionally under this act.

Mr. BROWN. I know, but I am asking you a question: Are you in favor of it?

Secretary SNYDER. I am in favor of treating all banks in the same fashion; yes, sir.

Mr. BROWN. Why are you just coming out in favor of it now? This is the first time you have ever mentioned it to any committee of Congress.

Secretary SNYDER. I have never even had a chance to testify on this subject before, Mr. Congressman. The only question I was asked was on a certain specific proposal which had been presented.

Mr. BROWN. Suppose we enact this law and require the State banks to increase their reserves, how would you enforce that law?

Secretary SNYDER. That is the problem I have just spoken of. If it could be done constitutionally, all right.

Mr. BROWN. Of course, we can pass it. It might even be within the Constitution. But how would we enforce it? Here is a State bank which derives all of its authority by State charter. How would you enforce it? By criminal punishment? You have no right to go in there and inspect banks. You have no right to send your people in to check up on it. It is a State bank. How would you enforce it; by criminal prosecution or how?

Secretary SNYDER. Well, I was just testifying in support of the legislation to increase the reserve requirements of the Federal Reserve banks. I understand there has been a new element introduced here by the Federal Reserve System itself. I say I have no objection to that if they can do it constitutionally. I am supporting the orthodox increase that is proposed in this bill.

Mr. BROWN. One of my main objections to it is that I do not want the Federal Reserve System to get control of all the State banks of this country against their consent, and this is just one way of doing it. If a State bank wants to become a member of the Federal Reserve it has a right to do so, but I am against any kind of scheme to force a State bank into the Federal Reserve System. I think as long as we have State-chartered banks, it should be left to these banks and the people of those communities to say whether they want a State bank to be controlled by the laws of the State or to be under the control of the Federal Reserve System.

That is all, Mr. Chairman.

The CHAIRMAN. Mr. Talle.

Mr. TALLE. Mr. Secretary, last evening I received a telephone call from the secretary of the Iowa Bankers Association stating that a telegram had been sent to me—which I received this morning. The telegram is signed by Mr. Black, superintendent of banks of the State of Iowa; by Mr. Summerwill, chairman of the Federal legislative committee; by Mr. Blasier, president, and by Mr. Warren, secretary of the Iowa Bankers Association.

I should like to quote a part of the telegram:

The Iowa State Banking Department and the Iowa Bankers Association vigorously oppose any imposition of control over the reserves of Iowa nonmember banks by any Washington authority. We have no opposition to the theory of trying to stop inflation by some statutory authority to increase reserve requirements of banks but to the imposition of any such controls over nonmember banks. Rather, we believe that such controls should remain where they now are—namely, in the hands of the State bank authorities, under laws of the various States. Any other procedure means that the very fundamentals of our State bank system are attacked and being undermined by any such legislation.

That is the problem which I have raised heretofore, under two heads: First, Is there a legal right to impose such restrictions on nonmember banks? And, second, if such restrictions are imposed, What sanctions or penalties could be invoked in the event of noncompliance?

Secretary SNYDER. I raised the same question that you have, Mr. Congressman, by saying if it could be done constitutionally. By that I presume that an appropriate method of enforcement would be included in the bill if it was constitutional.

I gave my testimony on increasing the Federal Reserve requirements of the member banks. The thought of making it cover the State banks was injected here this morning after testimony from the Federal Reserve Board on that yesterday, as I understand it.

I made the statement that if it could be done constitutionally—which would then give the proper legal effect to it—I would certainly have no objection to it. But I would want to be sure that it could be done legally and under the Constitution, with enforceable provisions. What those are, frankly, I cannot testify to because I do not know. I do know about the member banks, however.

Mr. TALLE. In any event, it is an issue that is giving a number of people great concern, and this committee, of course, must take cognizance of the objections raised.

Secretary SNYDER. That is right. That was one of the features of the special reserve proposal about which I had a reservation in the back of my mind. That covered all banks, and would be operated under a Federal statute. I thought it was necessary to iron out all those constitutional questions.

Mr. TALLE. In other words, you felt that that same issue was involved in the matter of setting up secondary reserves, as in this instance?

Secretary SNYDER. It was; yes. But this testimony applies to member banks, and that is what the bill that is now before Congress refers to. It refers to the increase of the reserves of member banks, which is just a projection of an existing statute. When you bring in the question of blanketing all banks under it, it does raise the constitutional question.

Mr. TALLE. That is right.

Secretary SNYDER. That was the reason I proposed, a while ago, that if it is to be done, the State banks ought, through their representative, to be given a hearing on the matter so they might be able to present their views.

Mr. TALLE. I have some figures here, taken from the Federal Reserve Board as a source, and these figures show percentage changes in demand deposits. I find that the comparison is made between December 31, 1947, and June 30, 1948—in other words, the first half of the current year.

Demand deposits are down, for all member banks, by 3½ percent. Nonmember bank deposits are down by 0.6 percent. All commercial bank deposits are down by 4.1 percent. Thus all banks show a decline in demand deposits. When I turn to total deposits, not only demand but time deposits as well, I find, for all member banks, for the same period—December 31, 1947, to June 30, 1948—the deposits of member banks are down by 5.2 percent; of nonmember banks by 0.7 percent; and of all commercial banks, down 5.9 percent.

That decline would indicate something. What would be your analysis of it, Mr. Snyder?

Secretary SNYDER. As to why the drop in deposits?

Mr. TALLE. Yes.

Secretary SNYDER. Over what period was that, again?

Mr. TALLE. December 31, 1947, to June 30, 1948—a 6-month period in the current year.

Secretary SNYDER. The principal reason for that is our debt-reduction program. We took that money out of the banks and applied it on the debt. That was a big factor. Then, of course, the bank loan program is another feature of it. The actual commercial and agricultural loans have been declining this year. It is consumer loans and real estate loans which are continuing to rise.

Mr. TALLE. I would like to turn, for a moment, to consumer credit. These are figures which I have had no opportunity to check, Mr. Secretary. I offer them here, however, in the hope that they can be checked, perhaps by your staff or the staff of the Federal Reserve. This is a statement that has been called to my attention, and all of these figures are quoted as having been derived from reports of the Board of Governors of the Federal Reserve System.

In the final 8 months under regulation W—that would be March through October 1947—installment credit increased from \$4,142,000,000 to \$5,454,000,000. That was an increase of 31.7 percent.

Now, turning to the 8 months for which figures are available since regulation W expired—that is, November 1947 to June 1948, inclusive—installment credit increased from \$5,454,000,000 to \$7,192,000,000. That was an increase of 31.9 percent as against 31.7 percent for the final 8 months under regulation W.

If regulation W had not been lifted but had remained in effect, with the same rate of increase in installment credit assumed, 31.7 percent, installment credit would have increased, in the last 8 months, by \$1,728,000,000. Installment credit actually increased by \$1,738,000,000. Thus the net effect of lifting regulation W cannot have been greater than the difference between these two figures, or the amount of \$9,000,000.

Voluntary control of installment credit has succeeded as well as Government control did in the last 8 months of its existence. "It would be misleading and insincere to reinstate installment credit controls for the purpose of reaching any such inflationary pressure as an item of \$9,000,000."

The final statement is not my conclusion but a conclusion that was stated to me, and I want to test it out.

Secretary SNYDER. What is it you would like us to try to get for you, sir?

Mr. TALLE. If during the last 8 months of regulation W the increase in installment credit was something like 31 percent, and during

the 8 months following the abolition of regulation W the increase in installment credit was 31 percent, with a fractional percent higher—and that fractional percent made a difference of \$9,000,000—are we straining at a gnat in talking about reimposing regulation W if this is all the difference that has occurred?

Secretary SNYDER. Of course, I would have to get the Federal Reserve staff to furnish us with actual records. I do not know, from what you have read there. The figures, in amounts, may possibly be correct. But their application would have to be studied, by the people who are handling these things, from the records.

But we would be pleased to have them address themselves to that, if you would like, sir.

Mr. TALLE. I should like to have these figures checked.

Mr. BUCHANAN. Will you yield for a question, Mr. Talle?

Mr. TALLE. Yes.

Mr. BUCHANAN. Does it necessarily follow that in the next 8 months, beginning with the present time, that will necessarily be the condition—that it will not increase more than \$9,000,000?

Mr. TALLE. No; I am not making any predictions.

Secretary SNYDER. The fact remains that since the war installment credit has gone up by over 5 billion dollars, and the increase is almost as much as total installment credit ever was before the war at the height of consumer-credit operations. So the volume, in dollars, is certainly there. As to how those percentages work out—of course, as it goes up, the dollar value gets much greater than the percentages, as you know. The increase from \$5,000,000,000 to \$6,000,000,000 is low in percentage, but it is an awful lot of dollars. A billion dollars is a lot of dollars to add to the credit field.

As I say, we would have to analyze the figures for you carefully, and I will be glad to ask the Federal Reserve Board to do it or ask our people to get it from them.

Mr. TALLE. There may be a number of things that enter into the picture which careful analysis would bring to light.

Secretary SNYDER. There was one other thing, too, Congressman. The last few months of controls of consumer credit were ineffective because everyone knew that the end was coming, and that you could not start enforcements, so the violations were beginning to accumulate considerably toward the end of controls. That might have had some effect. That would have to be looked into.

Mr. TALLE. It is true that the President had taken controls off many articles, so that there were relatively few left as compared with the original controls; is that not right?

Secretary SNYDER. In an effort not to restrain production; that is correct.

Mr. TALLE. In making this comparison or contrast between 1939 and 1948 we should remember that the population increased by about 10,000,000; so that if we compare present population with the prewar, there is an increase of 10,000,000 people, and we should expect a proportional increase in consumer credit.

Secretary SNYDER. If they have the goods to buy. Maybe the country can support a greater volume than we have now, if we had the goods to sell. But by increasing the credit supply against a limited number of items, it only tends to raise the price and not the volume of production. That is the point I am trying to make.

Mr. TALLE. Of course, that is why there was great pressure after the war—because of the pent-up demand during the war. Naturally it brought on unusual pressure, and it is surprising to me that the figure is not higher when we consider the pent-up demand arising out of the war.

Secretary SNYDER. There is a great demand.

Mr. TALLE. The current figure indicates to me a considerable restraint on the part of the American people.

Secretary SNYDER. I think, Congressman, that our savings program had a great effect on it, too. I think people thought carefully about how they were going to spend their money and what they were going to get for the money they spent. I think that was very effective, from the reports I get.

Mr. TALLE. Do you not think the figures do indicate a reasonable doubt about any unusual increase in installment buying?

Secretary SNYDER. I would have to get them to check the figures from the record, sir. As I say, I do not know just where those figures came from. They may have come from the Federal Reserve Board; I do not know. But, in trying to answer your question, I would like to get the percentages and everything figured right for the record. (See p. 234.)

Mr. KILBURN. Will you yield?

Mr. TALLE. Yes.

Mr. KILBURN. How many bonds has the Federal Reserve bought in the last 3 weeks?

Secretary SNYDER. I do not have those figures here, sir; but I can get them for you.

Here is something that is interesting: On July 28 we actually had fewer Government securities owned by the Federal Reserve banks than when we started to support prices.

Mr. KILBURN. Have you bought any in the last 3 weeks?

Secretary SNYDER. We have been buying bonds.

Mr. KILBURN. How much?

Secretary SNYDER. I will have to get the figure for you. I do not have it in mind.

Mr. KILBURN. Will you put it in the record?

Secretary SNYDER. I will be glad to. But I did want to tell you that the actual portfolio of the Federal Reserve right now is less in volume—in the amount of Government-owned—than it was before we started to support prices.

Mr. TALLE. I repeat; when I consider the record before the war and I consider the pent-up demand arising out of the war, the increase in the national product and the increase in population, I am rather surprised that the growth has not been greater. And I am just wondering how significant, in the whole set-up, consumer credit may be?

Secretary SNYDER. I will try to get the information on consumer credit for you that you ask for—the percentages and what effect it might have on the danger of increasing the inflationary pressures. (See p. 234.)

Mr. TALLE. Now let me offer quickly a statement that was given to me over the telephone last night by a man working in a plant who wants to buy a car.

He said: "If you impose that regulation I cannot possibly buy the car because I cannot afford to pay \$150 a month. I need the car in my work. But if you will permit me to spread the cost over a long period I can get the car that I need on my job."

That is all, Mr. Chairman.

Secretary SNYDER. I have those figures now on the Federal Reserve portfolio, Congressman Kilburn, if you would like to get them.

The total for the last 3 weeks is as follows:

On July 7 the total was \$21,535,000,000—that is the total portfolio.

On July 14 it was \$21,521,000,000. That was a decrease.

For the next week, July 21, it was \$21,326,000,000 a decrease in the total volume held.

Mr. KILBURN. How much?

Secretary SNYDER. \$21,326,000,000 as compared with the previous week of \$21,521,000,000. There was actually a decrease in the total portfolio of the Federal Reserve bank.

Mr. KILBURN. There ought to be, I think.

Secretary SNYDER. Well, you asked me what the purchases were and I am giving you the net results.

Mr. KILBURN. Yes.

Secretary SNYDER. And for the week ending July 28 the portfolio of the Federal Reserve bank was \$21,209,000,000, or a net decrease again; so, actually, while the Federal Reserve Board has been buying bonds, it has also been selling other Government securities and, as a result, the net amount in their portfolio is, over the last 3 weeks in July, less by \$326,000,000.

Mr. KILBURN. Do you not think that a healthy decrease would be three or four billion dollars?

Secretary SNYDER. We would be very happy if it could be; yes.

Mr. KILBURN. Well, that is the test, after all, about whether we are going to have inflation or not—decreasing the amount that you have to buy.

Secretary SNYDER. Well, we could decrease it if we were given a surplus of receipts over expenditures. That is what we are using that surplus for.

Mr. KILBURN. You had that.

Secretary SNYDER. We have already used that up, though. We do not have one to look forward to in the future.

Mr. NICHOLSON. Where is that money?

Secretary SNYDER. Where was it?

Mr. NICHOLSON. Where is the money now—that \$350,000,000?

Secretary SNYDER. I do not understand you, sir.

Mr. NICHOLSON. Well, there is \$350,000,000 left which has not been spent and which is not in circulation. Where is it?

Secretary SNYDER. No; I said that the holding of the Federal Reserve bank in Government securities was that much less, on July 28, than it was 3 weeks earlier. That meant that those securities had either been retired or were taken up by the investment public.

The CHAIRMAN. Mr. Secretary, would it be convenient for you to come back here at 2 o'clock?

Secretary SNYDER. Yes, sir.

The CHAIRMAN. There is a resolution on the floor and we have to go to the floor.

The committee will recess until 2:30, and, after the completion of the testimony of Secretary Snyder, the committee will go into executive session.

(Whereupon, at 12 o'clock noon, the committee recessed, to reconvene at 2:30 p. m. the same day.)

AFTERNOON SESSION

Present: Messrs. Wolcott, Gamble, Smith, Kunkel, Talle, Sundstrom, McMillen, Kilburn, Buffett, Cole, Hull, Scott, Banta, Fletcher, Nicholson, Spence, Brown, Patman, Monroney, Folger, Hays, Rains, Buchanan, Boggs, and Multer.

The CHAIRMAN. The committee will come to order.

We will proceed with the hearings on inflation control.

Mr. Snyder, Mr. Talle was questioning you when we recessed for lunch. Will you proceed, Mr. Talle?

Mr. TALLE. Thank you, Mr. Chairman.

Mr. Secretary, I assume you have something of a problem in managing the Federal debt.

Secretary SNYDER. Yes, sir, it is a problem.

Mr. TALLE. In the event that you could have your own way about it, how would you like to have the Government bonds held? Mostly by individuals?

Secretary SNYDER. That would be the best distribution of the debt, yes, sir.

Mr. TALLE. That would be ideal.

Secretary SNYDER. By nonbank groups, I would say.

Mr. TALLE. Yes, by individuals and nonbank groups.

Secretary SNYDER. Insurance companies, investment funds, and so on.

Mr. TALLE. And held until maturity?

Secretary SNYDER. That would be the ideal way, of course.

Mr. TALLE. Then, it would be easy for you to plan for refunding, and so on?

Secretary SNYDER. That is correct, sir, of course.

Mr. TALLE. I know there has been some selling of bonds. According to my information, bank investors have sold to the Federal Reserve something like \$354,000,000 worth of bonds in the past 3 weeks. Is that correct?

Secretary SNYDER. I can check that figure in a moment.

Mr. TALLE. That is fine.

Secretary SNYDER. That figure is correct, sir, for total Federal Reserve purchases of bonds.

Mr. TALLE. So long as those bonds were held by the nonbank investors, they were not creating any problem, were they?

Secretary SNYDER. That is correct.

Mr. TALLE. There was no pressure on the financial situation at all. However, after \$354,000,000, in a period of 3 weeks, entered the Federal Reserve System, two things happened, I believe: On the one hand, new bank deposits were created, and, on the other, excess reserves?

Secretary SNYDER. That is correct.

Mr. TALLE. That is the sort of thing which makes all the difference in the world between having the bonds held by nonbank investors

and held in the banking system. I am wondering what you could do to make it attractive to the nonbank owners of these bonds to keep them rather than cash them in?

Secretary SNYDER. That is a matter that we are constantly considering, Mr. Congressman, in trying to keep them interested in keeping those bonds in their portfolios.

Mr. TALLE. In the event that it appeared attractive enough to these holders to keep the bonds, the problem we face right now would not be so severe, would it?

Secretary SNYDER. As long as they retained their bonds in their portfolios and continued to buy new bonds, of course, that would be the ideal way from my point of view as Secretary of the Treasury.

Mr. TALLE. And, as these excess reserves increase, it is possible, within the system as a whole, to manufacture new money, actually, demand deposits, by approximately six times; is that right?

Secretary SNYDER. I think there is some such ratio there which is generally used, about six times—something like that.

Mr. TALLE. The way the problem is being approached, then, is that it is proposed to increase the bank reserve requirements and let this thing go on, assuming that nonbank investors continue to sell the bonds, the alternative being making the bonds attractive enough so that they would be held by the nonbank investors?

Secretary SNYDER. Actually, you know, the total Federal Reserve credit was curtailed because the portfolio of the Federal Reserve actually decreased, as I gave the figures this morning. While we have bought some, we have been selling at the same time. The Federal Reserve buys and sells in the market every day. So actually the net portfolio of the Federal Reserve banks has decreased by about \$326,000,000 during the last 3 weeks of July.

Mr. TALLE. You really canceled those bonds, then, with Treasury surplus; is that correct?

Secretary SNYDER. Some of them, and some were sold, too, because the Federal Reserve buys and sells every day. They have not just been buying. They have been buying and selling at the same time.

Mr. TALLE. What is the experience within the banking system when deposits are increased and the excess reserves are also increased? Is it found that additional currency is required by the trade? Has that developed?

Secretary SNYDER. It could occur that way, but not necessarily.

Mr. TALLE. Well, it is really to be expected, is it not, inasmuch as prices go up because of this process?

Secretary SNYDER. It takes more money to handle the transactions, more currency; is that your point?

Mr. TALLE. Yes.

Secretary SNYDER. It takes more currency to handle a \$210,000,000-000 national income than it did when we had a \$40,000,000,000 dollar national income in the early thirties; that is correct, sir.

Mr. TALLE. I raise the question whether it would not be better, at the present time to approach the problem from the point of view of making it attractive to people to hold these bonds, rather than bring them into the banking system and complicating the situation.

Secretary SNYDER. There are certain things to which we can resort to make them attractive, Mr. Congressman. From December 31, 1947, through July 31, nonbank holdings have increased by about a

billion dollars. So they are holding them pretty well. They are not unloading them on net balance.

Mr. TALLE. That means that you are selling more than you are buying?

Secretary SNYDER. That is right.

Mr. TALLE. That is a very good sign. In the event that we impose stringent consumer credit controls—say, installment credit controls—might we not find that the people who otherwise would hold their bonds would cash them in?

Secretary SNYDER. Do you mean banks?

Mr. TALLE. No; nonbank holders of bonds, particularly individuals.

Secretary SNYDER. Our experience with sales and redemptions of E bonds, when consumer credit controls were in effect, was very satisfactory.

The CHAIRMAN. Mr. Monroney.

Mr. MONRONEY. Mr. Snyder, I was pleased to hear you say that the establishment of additional bank reserves and regulation W were only a fraction of the necessary legislation to combat the dangers of inflation. Since you admit that it is only a fractional approach to the whole problem, about what percentage would you say you would valueate this suggestion of credit controls in the over-all program to control inflation?

Secretary SNYDER. I would not attempt to place a percentage figure on it.

Mr. MONRONEY. Would you say it is 5 percent or 10 percent?

Secretary SNYDER. I would not attempt to establish a percentage figure. It would be just part of the whole pattern. How much the problem would be actually affected by this program, unless we had other measures connected with it, I do not know precisely.

Mr. MONRONEY. At any rate, it would be a small fraction of the over-all tools needed to do the job?

Secretary SNYDER. It would be a small part of it, yes.

Mr. MONRONEY. Do you think it will have any effect at all unless other steps are taken, such as some of the other points suggested in the President's program?

Secretary SNYDER. I have my serious doubts as to whether it would be effective enough to really be beneficial.

Mr. MONRONEY. I know that you opposed the very unwise tax reduction that was made by this Congress, and you gave testimony before the Ways and Means Committee in opposition to the tax reduction.

Secretary SNYDER. My purpose was to have a surplus to apply on the debt, and that is a more effective control than any weak device.

Mr. MONRONEY. A far more effective control than we could later come in with; is that correct?

Secretary SNYDER. I think so, yes.

Mr. MONRONEY. And at the time you warned the Congress that that tax reduction would be dangerous and inflationary?

Secretary SNYDER. Yes.

Mr. MONRONEY. And it has proven just as dangerous and inflationary as you said it would be?

Secretary SNYDER. Well, it would have been very beneficial for us to have a surplus.

Mr. MONRONEY. In other words, the accumulation of the surplus not only prevents this additional \$5,000,000,000 from pressing on the supplies, but also would permit you an affirmative weapon with which to cut out of the banking system the highly inflationary credit which existed there?

Secretary SNYDER. That is correct.

Mr. MONRONEY. And you did use that selectively as long as you had the Government surplus, to do it with?

Secretary SNYDER. That is correct.

Mr. MONRONEY. Have you received any communication in the past 2 weeks from Mr. Knutson, the chairman of the Ways and Means Committee of the House?

Secretary SNYDER. Not to date, no, sir.

Mr. MONRONEY. You have received no word whatever from the chairman of the Ways and Means Committee—that would be the taxing committee, under whose jurisdiction any new tax program would have to come?

Secretary SNYDER. I have not heard from him.

Mr. MONRONEY. He is not bothering to communicate with you in any way?

Secretary SNYDER. No.

Mr. MONRONEY. To your knowledge, has the Ways and Means Committee given any notice whatsoever to the President's proposal for an excess-profits tax?

Secretary SNYDER. They have not communicated with me. Now, whether they have with anyone else, I do not know.

Mr. MONRONEY. Well, you are generally the first witness called, and yet they have completely ignored even a study, or the taking of testimony on the subject of correcting the error they made in helping to create this inflationary condition that we now have?

Secretary SNYDER. I have not been requested to appear before the committee.

Mr. MONRONEY. You do not know whether the Secretary of Commerce and the Secretary of Agriculture and the Secretary of the Interior, all of whom, under the proposed program, have a part of the job to do if we are to try to operate again in an effort to hold prices down, whether they are prepared to testify before this committee?

Secretary SNYDER. I am sure that they are. I heard Congressman Spence say that they had requested the privilege of appearing before the committee, so I presume that they are prepared.

Mr. MONRONEY. The point I am getting at is that undoubtedly they have done a considerable amount of work, have they not, in getting ready to testify?

Secretary SNYDER. I am certain they have; yes.

Mr. MONRONEY. Yet this committee is unwilling to spend a little bit of its time to hear that testimony.

Secretary SNYDER. I do not know what the committee has decided to do.

Mr. MONRONEY. Well, apparently so. Do you think it is possible to have any effective bill that would not do more than what is being proposed under the credit restrictions?

Secretary SNYDER. You mean in this bill here?

Mr. MONRONEY. Yes.

Secretary SNYDER. Well, referring to this particular bill on which I was testifying, I feel that that is not adequate in and of itself to do the job.

Mr. MONRONEY. You are referring now to the extension of regulation W and the increasing of the reserve requirements?

Secretary SNYDER. That is correct.

Mr. MONRONEY. Do you have a copy of the proposed bill before you?

Secretary SNYDER. The new bill?

Mr. MONRONEY. Yes.

Secretary SNYDER. No; I have not seen this bill.

Mr. MONRONEY. On the typewritten first page, under section 2, paragraph (b), it reads:

The first sentence of the fourth paragraph of section 16 of the Federal Reserve Act, as amended, is amended by striking out "25 percent" and inserting, in lieu thereof, "40 percent."

Secretary SNYDER. What does that refer to?

Mr. MONRONEY. That is what I am trying to find out.

Secretary SNYDER. Is that in connection with the gold reserve requirements of the Federal Reserve banks? It probably refers to an increase in the gold reserve requirements.

Mr. MONRONEY. Of the central bank?

Secretary SNYDER. Of the Federal Reserve banks; yes.

Mr. MONRONEY. Which ones: The member banks or the central Federal Reserve banks?

Secretary SNYDER. The 12 Federal Reserve banks.

Mr. MONRONEY. Well, the 12 Federal Reserve banks?

Secretary SNYDER. That is right.

Mr. MONRONEY. What I am trying to get at, and the point I am concerned with, is will moving up of this reserve requirement from 25 to 40 percent be restrictive of the open-market operations by the Federal Reserve banks?

Secretary SNYDER. This will have absolutely no mechanical effect at all, because they are operating at 51 percent now.

Mr. MONRONEY. Only some of them, though, in the big centers, as I recall it, are dangerously close to the 40 percent, which, because they operate in various sections, would not make it possible for some of your larger central banks —

Secretary SNYDER. We are not talking about the bank reserves now, we are talking about the gold reserves that must be behind the extension of credit. Is that not what we are talking about?

Mr. MONRONEY. I am trying to find out what we are talking about, because I do not have a copy of the act before me, and I have just been given this.

Secretary SNYDER. Well, I have just seen this for the first time.

The CHAIRMAN. I think Mr. Eccles testified yesterday that the restoration of the 40-percent reserves created a condition where one or two of the Federal Reserve banks did not have sufficient gold to meet that reserve. I think he said there was a question of some hundred million dollars. And they had to sell some bonds to some of the other banks to get gold.

Mr. MONRONEY. Would that restrict their open-market operations in any way?

The CHAIRMAN. No; it would not.

Secretary SNYDER. But on this subject, this is the first time I have seen this proposal, but I would like to state here that I would like to oppose this provision. It is already 51 percent, so it would not have any mechanical effect.

Mr. GAMBLE. That 51 percent you speak of is voluntary, Mr. Snyder.

Secretary SNYDER. That is under the present operation, with the 25-percent requirement.

Mr. GAMBLE. The 25 percent is the mandatory requirement and they have the right to go up, and the 51 percent comes in because they have voluntarily gone up to it?

Secretary SNYDER. That is right—the present situation.

Mr. GAMBLE. Thank you.

Secretary SNYDER. But the thing that concerns me more is its possible effect eventually on operations of the open-market committee. If it is raised to this 40 percent, it could have a bearing on the open-market committee's operations.

Mr. MONRONEY. That is what I was wondering. Perhaps you have enough cushion now, but the country knows that you have that capacity to make effective your open-market operations because you have got ample funds that you can go ahead and support the Government bond market with, because you can go clear down to 25 if you have to, so no group of people is going to try to raid governments to try and overload the Federal Reserve to get them over-committed to where they have to get out of the bond-support business.

Secretary SNYDER. That is exactly right, and we would like to keep that cushion in there.

Mr. MONRONEY. That is right.

Secretary SNYDER. It would have no immediate effect, but it could have a long-range effect.

Mr. MONRONEY. That is right, you have destroyed the cushion which they have to operate on if you raise that to 40 percent; have you not?

Secretary SNYDER. That is right.

Mr. MONRONEY. And without this, they are now operating at 51 percent, and perhaps if no one makes a blunder and raises the amount too much by law, the successful operation of the open-market committee can be assured. But it could actually jeopardize the par value and the present going interest rate of governments, if it were raised arbitrarily at this time. It would have absolutely no effect, would it, on consumer credit in any way?

Secretary SNYDER. I do not see how it could, immediately. It might have a long-range effect on the debt-management problem.

Mr. MONRONEY. But it would not have any effect on the ability of a member bank to make a loan to anybody for building a race track or a juke joint or anything else?

Secretary SNYDER. It would not affect that at all.

Mr. MONRONEY. It has absolutely no effect on an individual borrower from a bank?

Secretary SNYDER. That is right.

Mr. MONRONEY. But it could perhaps have an effect on the Government's ability to maintain this terrific financing job—\$50,000,000,000, I believe, in the next year—that must be refinanced in the market?

Secretary SNYDER. That is correct.

Mr. MONRONEY. And you are destroying the weapon that the Government has of holding its bonds at par and preserving the 2½ percent interest?

Secretary SNYDER. That is right, sir.

Mr. NICHOLSON. Mr. Secretary, you are against this bill; are you not?

Secretary SNYDER. I have not had a chance to read the bill, Mr. Congressman. This is the first time I have seen it, and we have just had a chance to look at that one paragraph. But that one paragraph I would oppose; yes.

Mr. NICHOLSON. Well, if you are against one paragraph, you are against the bill; is that not right?

Secretary SNYDER. I have not read the rest of the bill and that is a broad statement, but certainly that feature of it I would be opposed to.

Mr. SMITH. A bill has everything in it. That is the trouble with us.

Secretary SNYDER. Not ever having seen it before, I cannot say.

Mr. SMITH. Bills come in here.

Secretary SNYDER. You are asking me to testify on a bill I have never seen before.

Mr. SMITH. I am not asking you to. I asked if you were opposed to it and you said "No."

Mr. Secretary, in substance you are telling this committee not to do anything to limit your power to inflate; is that right?

Secretary SNYDER. Not to do anything to limit our power to manage the debt.

Mr. SMITH. Which, of course, involves the matter of inflation. In other words, the pegging of bond markets is distinctly an inflationary process; is it not?

Secretary SNYDER. Does this committee want to pass a regulation that forbids us to support the bond market?

Mr. SMITH. That question has been put to me by previous witnesses for the President's program when I asked them the same question.

Secretary SNYDER. Well, you are posing that question to me, and I certainly want to know what your feeling is about it.

Mr. SMITH. I am simply trying to explore the situation and as I understand it, you, and as I understood Mr. Eccles, and as I understood Mr. McCabe, all of you have taken the position that you do not want this committee to do anything which would prevent the power of the Government to inflate at will.

Secretary SNYDER. I personally do not want this committee—if you would give any weight to my feelings in the matter, and I hope you would give me the same weight that you did on a mere doubt that I had in the past—not to limit the power of the Treasury Department to manage this debt. This might seriously handicap us in the future.

Mr. SMITH. Is the pegging of bond prices inflationary or is it not inflationary?

Secretary SNYDER. In this time we are in, the degree between inflationary and noninflationary pressures is pretty closely defined. Certainly we have other things to take into consideration when we have a condition such as this debt to manage. We have to use every possible recourse that we have to try to keep it under control.

Mr. SMITH. Is the effect of pegging Government securities, in the manner in which you are now doing, to raise or to lower the value of the price of credit?

Secretary SNYDER. What I would like to do would be to have an ample surplus each year to apply against that debt and reduce it and that would counteract the problem.

Mr. SMITH. That is not answering my question. Will you answer my question?

Secretary SNYDER. I tried to answer your question in the best way I could, sir.

Mr. SMITH. Let me ask you again: Is the effect of the policy that is now being pursued by the Federal Reserve System, to peg the price of Government securities, to raise or to lower the interest rate on money and credit?

Secretary SNYDER. Mr. Congressman, the area within which the Treasury can move in the interest field is rather limited. If we move the average interest rate by as much as one-half of 1 percent, the cost is something like \$1,250,000,000 in taxes to meet that problem. So we have got to take a great deal into consideration. We have got these refinancing operations to take care of. If we do not carefully consider the position of our market on those bonds, we may find it extremely difficult to meet those refinancing operations when they come up.

This morning I was trying to touch on that very point of what we are doing to try to lessen those pressures. We extinguished 26½ billion dollars of bank-held debt by pay-offs and we transferred from bank-held to non-bank-held, 3½ billion dollars. All of which is working toward the end to which we are applying our discussion. We are trying to remove those inflationary pressures in the bank-held debt.

Mr. SMITH. Mr. Secretary, is the effect of pegging bond prices to make money easier or tighter?

Secretary SNYDER. It is the purpose of that to maintain our ability to manage the debt and to meet our refinancing.

Mr. SMITH. Well, it makes it possible for people who hold bonds to sell them to the Government and get money and spend it, does it not?

Secretary SNYDER. Would you want to change that so you could not sell your bonds?

Mr. SMITH. I am not the witness here. I am exploring the field. You men come in here and you tell us you want to control inflation. I am simply trying to find out whether you really mean what you say. You are asking for the power to manipulate Government security prices, in such a manner as to make credit easier, and to provide a greater volume of money, because there can be no other effect when you go into the market to buy bonds, but to supply an additional amount of money and credit. Is that not true?

Secretary SNYDER. If the Congress wants to direct us to remove our support prices from the bonds, it is within their scope to do it.

Mr. SMITH. I see that you do not care to answer the question. It is a fact that you men are coming in here and asking for more power to create inflation. That is exactly what you are asking, Mr. Snyder.

Mr. MONRONEY. Mr. Snyder, is it not a fact that the most inflationary thing that could hit the country would be for Government bonds to drop from a hundred percent down to about eighty?

Secretary SNYDER. It would be the most disastrous thing that could happen.

Mr. MONRONEY. And would it not amount, the way so many E bonds and other bonds are pegged, on an immediately cashable basis to a run on the Treasury on the Treasury and a recycling of the whole public debt into higher and higher interest rates, and then you really would have your 5- and 10-cent dollars?

Secretary SNYDER. Our operation, as you will recall—managing the debt is not simply a matter of supporting bond prices. We have sold bonds to keep the prices of bonds from going up at one time. It is a matter of stabilizing bond prices. Sometimes we have to sell bonds to hold the price down; and other times we are supporting them to keep them from dropping below the 2½ percent rate.

Mr. MONRONEY. It is a big job with a \$250,000,000,000 debt and with \$50,000,000,000 to refinance this year, is it not?

Secretary SNYDER. It is a difficult thing, yes, sir.

Mr. NICHOLSON. The answer is, if you have faith in your Government the bonds are good, but if you have not, they are not any good; is that not the answer?

Mr. MONRONEY. Faith in the purchasing power of the money.

Mr. NICHOLSON. It is not faith in the purchasing power of the money, as I see it, after sitting on this committee for a year. You have to have faith in the Government, and if you do not have it your bonds are not any good anyway. Am I right or am I wrong?

Secretary SNYDER. Well, I happen to have faith in the Government and I think we are going to work this problem out, sir.

Mr. NICHOLSON. That is right.

Mr. SMITH. Mr. Snyder, the question was asked you of Mr. Monroney, if you would let bond prices drop, whether that would not be inflationary. You answered the question by saying it would be disastrous. Would you answer the question directly, whether that would be inflationary or deflationary?

Secretary SNYDER. Well, there is no question but what it could be inflationary.

Mr. SMITH. Would be which?

Secretary SNYDER. The immediate step might be inflationary but the end result would be a disastrous deflation.

Mr. SMITH. Why do you say the immediate effect would be inflation?

Secretary SNYDER. It would build up prices in other fields.

Mr. SMITH. Well, explain that.

Secretary SNYDER. Well, the people would liberate their money from Government bonds. If they take their money out of Government bonds and put it in other things, they would be bidding up prices of other things.

Mr. SMITH. But generally there would be a drop; is that not true?

Secretary SNYDER. Over the long range there would be a disastrous drop; yes, sir. We are just as interested, Congressman, in avoiding a disastrous deflation as we are in not creating inflation. We have the double problem always before us. It is not a clear-cut problem. Right now the inflationary pressures are greater so we are having to address ourselves to that angle. At the same time we have to bear in mind the effect that deflation would have, or what deflation could do to us.

Mr. SMITH. Do not misunderstand me, Mr. Snyder, I am not holding you responsible for these things, because you have come into this picture at a late hour, but we would like to have the facts brought before this committee so that we may know whether or not the purpose

of pegging Government securities is to prevent inflation, or create it. Is not the prime purpose of pegging these prices of Governments to prevent deflation?

Secretary SNYDER. The prime purpose of it is to stabilize the market for Government bonds.

Mr. SMITH. Well, you call it stabilization. I am merely considering the factors that are involved in the stabilization process. I speak of deflation and inflation, and those are the factors that are involved in what we are considering at the present time. You and the other proponents of this bill have come in here and said to this committee, "What we want is unlimited power to inflate and unlimited power to deflate." That is exactly what you have asked for.

Mr. FLETCHER. Mr. Secretary, what would be the effect if the bond price, instead of being pegged at 101, was allowed to find a level of, say, par? After all, they were sold at par, were they not, Mr. Secretary?

Secretary SNYDER. Some bonds; yes, sir.

Mr. FLETCHER. These E bonds, these 2½-percent bonds were all sold at par?

Secretary SNYDER. Yes, sir; that is true on our marketable bonds; as you know a \$100 E bond sells for \$75 and matures at par.

Mr. FLETCHER. So when the price is pegged at 101, the people who purchased them have a profit, is that not right?

Secretary SNYDER. Well, the pegged price is a little bit less than that.

Mr. FLETCHER. So why not let them go to par or 99, let us say?

Secretary SNYDER. We have come right on down close to the 2½ percent rate. We have demonstrated just what you are talking about. We have let it down.

Mr. FLETCHER. I know, but why not let it down some more? Why give these people who bought these bonds a capital profit? They bought them for the interest rate.

Secretary SNYDER. Well, it is pretty close to the 2½ percent rate.

Mr. FLETCHER. Well, it is pretty close, but they would still be all right if you let them go to 100 or 99. There would not be this easy profit that some of these people have been making. I have never been able to understand why you did not let them go to 99 or 100.

Secretary SNYDER. Some of them are at par and a quarter and some are at par.

Mr. FLETCHER. Then they have been dropping right along?

Secretary SNYDER. We have kept bringing it closer to the 2½-percent rate.

Mr. FLETCHER. Do you think it might be advisable to even allow it to find a little lower level?

Secretary SNYDER. I think we are definitely committed to a support of the 2½-percent rate.

Mr. FLETCHER. At par?

Secretary SNYDER. The 2½-percent rate, whatever that works out, for the long terms.

Mr. FLETCHER. Thank you very much. Excuse me, Dr. Smith.

Mr. SMITH. That is all right.

Mr. KUNKEL. Mr. Snyder, you are supporting also the price of short-term Government, are you not?

Secretary SNYDER. The short terms are put out at different rates; yes; the bills at about 1 percent and the certificates at 1½.

Mr. KUNKEL. And that is also in the nature of an easy-money operation, is it not?

Secretary SNYDER. Well, as you know, we have gradually been stepping up the rate to meet the market situation.

Mr. KUNKEL. You went up about last July, did you not, from $\frac{7}{8}$ up to $1\frac{1}{8}$?

Secretary SNYDER. We have made several steps in advancing the rate on the short-terms; yes, sir.

Mr. KUNKEL. If you let the short-terms go up a little more, would it not have a deflationary effect?

Secretary SNYDER. Mr. Congressman, that is a debt-management problem that I will be glad to discuss in executive session. I just do not think you want me to make suggestions here, because, as Secretary of the Treasury, any statement I make will be translated into a course of action that I might take. Do not forget, I am dealing with a public market, and the remarks that I make can have an effect one way or the other. I do not want to withhold any information from this committee, but I prefer, if we are going into that discussion, to do it in executive session.

Mr. KUNKEL. Well, inasmuch as it has nothing to do with your course of action, it is inflationary to keep the level on short-term Governments down to $1\frac{1}{8}$, is it not?

Secretary SNYDER. Well, it all depends on the market operations as to what we should do.

Mr. KUNKEL. I did not say what you should do. You have that fact to take into account. But the fact that you are supporting them is an inflationary element in the market, is it not, an easy-money element?

Secretary SNYDER. We have a problem that we have to face.

Mr. KUNKEL. I am not talking about all the other problems of debt management, involved in your debt management, which may outweigh the easy-money consideration involved in this particular operation, but taking this in and of itself and putting it to one side and forgetting about the rest of the world and just answering the specific question, supporting them at $1\frac{1}{8}$ is an easy-money operation, is it not?

Secretary SNYDER. We have recognized the problem that you face—

Mr. KUNKEL. Why do you not answer the question? I have shoved all your general policy questions over to one side.

Secretary SNYDER. I say we have demonstrated that we recognize that problem because we have been advancing the rates.

Mr. KUNKEL. All right, then you can just say "Yes." That is another definitely easy-money phase, that, if you could reconcile it with the other problems in your field, would be another corrective measure which could be taken and could have been taken?

Secretary SNYDER. We have been taking those steps, sir, right along.

Mr. KUNKEL. Would you outline just briefly what the effect of increasing the short-term rate would be on the bank investment in long-term Governments?

Secretary SNYDER. I am going to ask the chairman to excuse me except in executive session from discussing money rates here, please. I will be glad to discuss them in executive session at any length.

The CHAIRMAN. I do not think the Secretary should be required to make public statements on matters which affect those things.

Mr. KUNKEL. I cannot imagine a more positive statement than the one to the effect that you would support the Government bond market at 2½ percent rate. That is all.

The CHAIRMAN. Mr. Spence.

Mr. SPENCE. Mr. Snyder, when we had 2½ percent bonds the debt of the Nation was \$21,000,000,000 to \$23,000,000,000. When those bonds went to 80 percent, where do you think these 2½-percent bonds, which are taxable as against the others which were nontaxable, if not supported by the Federal Reserve, would go to now when the national debt is \$250,000,000,000?

Secretary SNYDER. I would be greatly concerned as to what would happen if we just turned loose the support of the bond market.

Mr. SPENCE. Does the support of the bond market not have a psychological effect upon the holders of the bond very similar to the effect of the Federal Deposit Insurance Corporation on depositors in banks? It gives them a confidence which makes them retain their bonds. Otherwise they would probably put them on the market, and nobody can tell how low they would go; is that not true?

Secretary SNYDER. I think that is true; yes, sir. There would be constant doubt as to just what the level would be.

Mr. SPENCE. How essential is it to maintaining the credit of the Government?

Secretary SNYDER. From my point of view it is the most essential thing to do right now, to maintain confidence in the Government's monetary operations.

Mr. SPENCE. If that confidence were destroyed the inflationary conditions would certainly be very much worse and one can hardly foresee what would happen. I think that is the very basis of the whole thing. Whether the support of the bond market is inflationary or not, it must be continued.

Mr. BROWN. I think by all means we should hold these bonds at par. Any suggestion you have to make to this committee in order to help you do that, I think this committee would like to have, because I think that is the most important thing. We should hold these bonds at least at par. I think you are doing a good job on this line.

Secretary SNYDER. Thank you.

The CHAIRMAN. I suppose there is a difference between holding bonds at par. You have to take into consideration the terms of dollars and the terms of purchase at par. I can see a situation where if we continue inflation for the purpose of maintaining your bonds at par, and the value of your dollar goes down 20 percent, there is not too much difference between that and letting your bonds go down to 80.

Mr. McMILLEN. Mr. Secretary, I received two telegrams yesterday, and a letter today from the secretary of the Illinois Bankers Association, having to do with this problem of reserves, and so much interest is shown in this letter that he poses a number of questions that he wants me to ask you. Perhaps I can conserve time by asking you five or six questions having to do with the same principles, after which I wish you would discuss it and answer it, if you will, for the Illinois Bankers Association.

First, hog prices are now \$31 per hundredweight. In what way are the legal reserves of banks responsible for this price?

Prime steers are well over \$41, as are all other live animals proportionately, which are delivered to our stockyards. While these food animals are going up, each

week grain futures, including all cereals, are going down. What effect, if any, has the legal bank reserve, either on the increase in animals or the decrease in grains? After all, what we are mostly interested in is how much it costs you and me to buy food and other necessities for living.

Recently several of the automobile manufacturers announced increases of 8 percent on the wholesale prices of automobiles. Did or did not the present reserve requirements influence these increases?

The steel companies have announced several increases in the prices of finished steel. What effect, if any, has the legal reserve of banks on these increases?

The third round of wage increases is now in process. Do bank reserves have anything to do with that?

Building costs have gone up to the point where an ordinary house has practically out-priced its market. Did the legal bank reserves cause this?

They involve all of the same principles, I believe, and I wish you would discuss that for the benefit of my constituent.

I know if Mr. Stratton were here he would want to join in these questions, being from Illinois himself.

Secretary SNYDER. If you will let us have your letter, we will try to give you a studious reply to it.

Mr. McMILLEN. You will have to speak louder.

Secretary SNYDER. I say if you will let us have that letter we will try to prepare a studious reply to it. That involves quite a broad field.

Mr. McMILLEN. Will you make it a matter of record in the proceedings here?

Secretary SNYDER. Yes, sir, we will try to prepare a letter for you insofar as we are in a position to do so.

Mr. McMILLEN. Could you not at this time give an answer to the general question?

Secretary SNYDER. Those are very carefully thought out questions and I would like to apply the same time, in preparing the answers, that was applied or taken to prepare the inquiries.

(Additional information supplied by Secretary Snyder follows:)

As I stated in my testimony, the Treasury Department is directly concerned with only two titles of the bill under consideration by this committee, namely, those which deal with the regulation of consumer credit and with the control of inflationary bank credit. I stated further that:

* * * While these two items are important in the anti-inflationary program, we must keep in mind that they are but segments of the over-all problem and must be treated in their relation to other dominant factors bearing more directly on the cost-of-living.

As you may recall, I also stated that:

* * * The expansion of bank credit, except in the fields of consumer and real estate financing, has not, in my opinion, been a major contributing force to present inflationary pressures. We must, however, attack the problem of inflation on all fronts.

and—
* * * prudence requires that additional instruments * * * be placed in the hands of the Federal Reserve System.

But again I should like to remind you that, as I stated in my testimony on inflation control last November and again in my prepared testimony this morning, it is my opinion that in the fiscal-monetary area this inflation problem can best be handled through the application of a substantial budget surplus to the reduction of the public debt in such a manner as to retire bank-held Government securities. Doing this reduces the total loans and investments of banks, it reduces the money supply, and it reduces the amount of consumer incomes available for expenditures. It constitutes a powerful attack upon the inflation problem. But, in the absence of a budget surplus, we must make the best use we can of other instruments.

Mr. McMILLEN. He asks another question here, which I think is quite germane and should be answered by you, and he specifically mentions you, along with Mr. Eccles:

If legal reserves are increased, what would they do, as a responsible bank manager investing bank funds, if Mr. Snyder or Mr. Eccles, for instance, were responsible for the operation of a bank, and out of that operation had to meet the pay roll, the cost of supplies, the other operating expenses, including taxes and dividends, and a reasonable reserve for losses, and were suddenly confronted with the necessity of reducing their loans and investments by 10 percent? Would they not first sell their Governments in order to effect that reduction? If they did sell their Governments, who would buy them? Wouldn't the answer be the Federal Reserve banks? If the Federal Reserve banks bought these Governments on the market, how would they pay for them? Would they not pay for them out of new money which they would print? And would not that, therefore, inflate the currency outstanding and completely reverse the process of anti-inflation at which they are aiming?

Secretary SNYDER. Mr. Congressman, as a former active banker I know that the earnings of the banks are important. I know that it is important for banks to constantly observe their earnings ratio because they have to pay dividends and maintain the operation of their banks. But that problem is not facing us right now because bank earnings are rising. So there is latitude within which they can consider their portfolios. Perhaps for some banks it would be difficult, but then we can never do anything that suits everybody across the board.

Since the Federal Reserve Board has no more latitude in which to raise the reserves, I think it is appropriate that we give them some area in which they can manage their reserve requirement charge, as given them by Congress.

Mr. McMILLEN. Well, if these banks did ask the Federal Reserve to purchase Government bonds, where would the Federal Reserve get the money for the purchasing of those bonds?

Secretary SNYDER. If that happens, why, of course they have to take it out of their operations by crediting the particular bank's reserve account.

Mr. McMILLEN. In other words, they would have to ask the Government to print more money in order to meet the demand for sale of those bonds; is that right?

Secretary SNYDER. If it took actual currency. That does not always take place.

Mr. McMILLEN. That would be inflationary, would it not?

Secretary SNYDER. But I say that that does not always follow.

Mr. McMILLEN. Well, as I say—

Mr. KILBURN. You cannot just print the money in the Federal Reserve.

Secretary SNYDER. Oh, no; there must be gold backing.

Mr. NICHOLSON. They have to stand back of it.

Mr. KILBURN. I know. They have to have a gold reserve back of the money in order to print it; is that not right?

Secretary SNYDER. That is right.

Mr. McMILLEN. Now, Mr. Snyder, I would like to ask you, on my own behalf, this question: You are familiar with the legislative program requested by the President of the present Congress and of the Congress coming in in January, are you not?

Secretary SNYDER. Yes, sir.

Mr. McMILLEN. You are familiar, of course, with the Taft-Ellender-Wagner housing bill. Do you think that if that bill were enacted

into law, and the terms were fulfilled, that that would or would not be inflationary?

Secretary SNYDER. It has been testified right along that it would be inflationary. There is no question about that. But then there is the other problem of providing the houses. You have to balance one against the other.

Mr. McMILLIN. But it would be inflationary. That is the question.

Secretary SNYDER. The Congress has to consider that and decide whether or not the inflationary action should be offset by other considerations, which are equally or more vital.

Mr. McMILLIN. My question is not what are the merits of that bill. I am just getting your opinion as to whether or not the act itself is inflationary. That is true of all of the some 12 or 13 or 14 pieces of legislation that the President requested Congress to enact into law in his message of a week ago Tuesday; is that not true, Mr. Snyder?

Secretary SNYDER. There is—

Mr. McMILLIN. How about the bill commonly known as the educational bill requiring \$300,000,000 of credit and money to be furnished by the Government now and additional amounts from year to year hereafter? Is that inflationary or not?

Secretary SNYDER. There is an element of inflation in many of those bills, of course. But then you have to measure that against the other benefits—whether they are urgent enough to require meeting those problems.

Mr. McMILLEN. How do you feel about the minimum wage law, wherein Mr. Truman asked Congress to raise that minimum to at least 75 cents an hour? Is that inflationary or not?

Secretary SNYDER. Mr. Congressman, I am in general support of the President's message, and, if there are inflationary portions in it, there is an offsetting reason for it that more than offsets that.

Mr. McMILLEN. Well, I am going through these requests of the President and asking you a plain question; not whether or not you favor the entire program because the President asked for it, but whether or not, in your opinion, as a banker and an expert in finance, these particular pieces of legislation are or are not inflationary—just generally. Are they or are they not inflationary?

Secretary SNYDER. Some of them are and some of them are not.

Mr. McMILLEN. Well, the first three I have mentioned are, are they not, Mr. Snyder?

Secretary SNYDER. They could have an element of inflation

Mr. McMILLEN. The President further suggests that old age retirement benefits, which are now \$39 a month—and for women with two children \$49 a month—be increased at least 50 percent. The enactment of such a law as that is inflationary, is it not, Mr. Snyder?

Secretary SNYDER. Right at this time any expenditure by Government can be considered inflationary, Mr. Congressman.

Mr. McMILLEN. What do you think about appropriations for the United Nations building up in New York?

Secretary SNYDER. As I understand it, that is a loan that would eventually be repaid.

Mr. McMILLEN. That is inflationary. Even if it is a loan, that is Government credit, is it not, Mr. Snyder; that is being furnished; and that contributes to inflation, does it not?

Secretary SNYDER. It certainly is a matter involving a bid against materials and labor. But, as I say, any expenditure of Government is inflationary. The salaries paid to us who work for Government are inflationary. The handsome salary that I receive as a Cabinet officer is inflationary. And the salaries paid to you Congressmen is inflationary because the Government is providing you with money to spend for things.

So, if we get right down to that narrow field, we are going to find that any money the Government spends can be called inflationary.

Mr. NICHOLSON. Will you yield?

Mr. KILBURN. He means that any new expenditures are inflationary; not your salary or mine.

Secretary SNYDER. No. What I am saying is that, whether it is new or old, if the Government is spending it can be considered inflationary.

Mr. KILBURN. But what he is getting at is that the expenditures of the Government involved in the new proposals are inflationary.

Secretary SNYDER. Some of them may be and some not.

Mr. KILBURN. What is that?

Secretary SNYDER. Some could be and some could not be, sir.

Mr. KILBURN. Well, you have been kind enough to answer with respect to several of the bills. There are a good many others here. The President has requested the special session to provide funds for a steam plant in Tennessee.

Secretary SNYDER. Congressman, now I cannot hear you.

Mr. KILBURN. The President requests of the special session to pass legislation providing for a steam plant down at Johnsonville, Tenn., and other electric power plants over the country. If that legislation is passed and those plants are built, now, would that or would that not be inflationary?

Secretary SNYDER. In the long run it might be very anti-inflationary, if it provided the source of power for more production. So that has to be given consideration.

Mr. KILBURN. This inflation, Mr. Snyder, is an immediate serious problem. Assuming that tomorrow we passed that bill requiring millions of dollars of credit and money to be furnished by the Government to build that plant and other plants, would or would not that be inflationary?

Mr. RAINS. Will the gentleman yield to me for a question?

Mr. McMILLEN. Not just now; I am sorry.

Secretary SNYDER. We cannot just completely go one way or the other. We have got to balance one problem against the other as we go along and do the best we can to try to meet this transition period.

Mr. KUNKEL. We are really going completely both ways if we follow the President's message, Mr. Snyder.

Mr. McMILLEN. Mr. Snyder, the President also recommends some adjustment, or the ironing out of some inequities which he has described, which would require additional raises in salaries of Federal employees. If that was carried out now, would that be inflationary or not?

Secretary SNYDER. I will let you answer that. You have had more recent experiences with raises than I have, Mr. Congressman.

Mr. McMILLEN. Now, Mr. Snyder, you are in a position to answer these questions.

I want you to help me because we are up here working on this together.

I want your opinion on this subject. I have respect for your judgment, and I think you should answer the questions as I ask them.

Would that be inflationary?

Secretary SNYDER. I have answered every one of these, Mr. Congressman. I have said that all Government spending can be considered inflationary, and I think I have covered all those questions for you.

Mr. McMILLEN. Furthermore, the President requests the Congress coming in in January—which is only a few months away—to enact legislation for a comprehensive health program based on health insurance and a universal training program, a National Science Foundation and approval of the St. Lawrence waterway.

In themselves they would require billions and billions of credit and money to be furnished by the Government. Do you think the enactment of those proposals into law and the carrying out of their terms would or would not be inflationary?

Secretary SNYDER. He asked, along with those things, for a Federal surplus, too, which would offset them.

Mr. McMILLEN. Well, let us take them all together and let us assume, as it is reasonable to assume, that if all of this legislation that Mr. Truman requests were passed it would require tens of billions of dollars of money and credit to be furnished by the Government to carry out the terms of that legislation. If that came to pass within the next few months, would it or would it not be inflationary?

Secretary SNYDER. It all depends on how our economy is moving along. It could be a sustaining element in preventing inflation.

Mr. RAINS. Mr. Secretary, on the Republican platform at Philadelphia there were these same matters of housing that my friend is asking about and numbers of other items of expenditures in the Federal Government. If the Republicans spent that money next January, would that be inflationary also?

Secretary SNYDER. The same answer applies either way, Mr. Congressman.

Mr. RAINS. Going back to that Johnsonville steam plant, I happen to hail from that section and I happen to know that we are within one and a half percent of the top amount of power that TVA can generate. If it closes down the plants in that area—and especially the great aluminum plants out of which we hope to get aluminum to build our 70-group Air Force—would that be wise simply because the spending of a few million dollars would be inflationary?

Secretary SNYDER. I have made the statement that if that particular project is for providing for greater production, it would be anti-inflationary.

Mr. NICHOLSON. Mr. Chairman, can those questions not be taken up in executive session? I think we are wasting time here.

Mr. PATMAN. Mr. Chairman, I want to ask a few questions.

The CHAIRMAN. Are you through, Mr. McMillen?

Mr. McMILLEN. Yes, sir.

The CHAIRMAN. Mr. Patman.

Mr. PATMAN. I am greatly concerned about the raising of the gold requirements behind Federal Reserve notes from 25 to 40 percent. If that will seriously affect the open-market operations to the extent

that it will possibly be necessary to suspend support prices on Government bonds, I think it would be a devastating step for this Congress to take.

Do you think it would be a very serious matter if we were to pass a provision like that?

Secretary SNYDER. I so stated a while ago.

Mr. PATMAN. I am sorry; I was not here. The reason I am asking you the question is that I know there is a lot of sentiment in this Congress to do away with support prices on Government bonds and to let them seek their level. I think it would be one of the most disastrous things which could possibly face our country—for the same reason that we had such a condition after the other war, when bonds went down to 75 cents, as you well recall.

This time it was contemplated that we would not permit bonds to go down. I know when the Ways and Means Committee was considering war financing, before the war, I appeared before the committee in support of a program that would prevent that very thing, and I was assured by the members of the committee that that committee—the Ways and Means Committee—would do everything within their power to prevent that disaster occurring again.

It was going to be the policy of the Government always to keep those bonds above par, and to assure the people that they would be above par—and so far they have done that.

Now, if we go back on that—what we might call an implied promise and a recognized promise by congressional leaders of that time—after people bought bonds on the strength of that fact, and if the word were to get out that support prices are likely to be done away with, I do not know what might happen in this country, because the people would begin to run to the banks, run to the Treasury, and they would begin to cash their bonds.

I can see in that one of the most disastrous things, or possibly the most disastrous thing, that is proposed in this whole program.

How long could you support the market with a 40-percent requirement? How much, in bonds, could the Federal Reserve buy through the open market operations, and how much could they buy if it remained at 25 percent? Do you know?

Secretary SNYDER. I cannot tell you offhand.

The CHAIRMAN. May I answer that?

Mr. PATMAN. I wish you would.

The CHAIRMAN. Mr. Eccles testified that there would still be \$4,600,000,000 of excess gold reserves if reserves were restored to the 35- and 40-percent levels. Now, using a 35-percent reserve on Federal Reserve deposit liability, the \$4,600,000,000 of excess gold would permit deposits of \$12,100,000,000. This \$12,100,000,000 of Federal Reserve bank deposits could be the base of the credit expansion of \$50,000,000,000 due to the fractional reserve system on which the system operates. We could still expand our credit base by \$50,000,000,000.

Mr. PATMAN. Does the chairman have in mind forcing a condition whereby we might have to remove support prices at any time in the future?

The CHAIRMAN. No. Your gold imports are increasing; your gold purchases are increasing right along; there isn't anything possible that could happen to cut it down to 40 percent.

They have 51 percent now. And we have this almost \$5,000,000,000 in excess reserves and a possible credit expansion of \$50,000,000,000. We do not want to put ourselves in the position of whistling in the dark or justifying practices that are not based on facts.

The psychological effect alone of restoring these gold reserves would have a very wholesome stabilizing influence on the public generally. That is the point. And they have got so far to go before they could possibly be affected, and it is so far in the future that we cannot see how it could happen.

They were reduced from 40 percent on notes and 35 percent on deposits, to 25 percent to meet in part an anticipated postwar depression which did not materialize. The sensible thing to do, if we are going to stabilize, is to reverse these processes and by this action, at any rate, indicate that it is the policy of Government to stabilize and not to continue a loose-money policy. That is all we claim for it.

Mr. PATMAN. May I ask the chairman another question, which will have a lot to do about my feeling about this thing?

If the chairman believes that this provision, if enacted into law, would seriously affect the Open Market Committee in its support-price program, the chairman would be opposed to that, I am sure.

The CHAIRMAN. I am not so sure. I think that I would consider that, of course, as a factor. But I am not so sure that I am wedded to the support of Government bonds at a particular figure. They are up above par at the present time. If it is stabilizing to let them go down to par, then I think we should let them go down to par. They were supported at par and one for a long time. Now they are down to par and a quarter. I do not see any particular reason why we should not let them go down to par. Surely we could not be charged with bad faith.

Mr. PATMAN. Oh, I do not object to that.

The CHAIRMAN. But I think we should do everything—even reduce Government bonds to par—if, by doing so, we can inspire stabilization influences. That is all we can do, in this committee and this Congress, to inspire stabilization influences. That is all we hope to do.

I do not think that anybody is recommending that the powers which the Federal Reserve and the Treasury and the President have at the present time would be used in such a manner as to bring on a depression, although I am firmly of the belief that the powers which the President and the Federal Reserve and Treasury have at the present time could be used in such a manner as to bring on a depression or anything short of a depression, which means stabilization.

I think Congress owes it to the people to show that the Government is in favor of stabilizing; that we do not want to accept as a matter of policy that we have got to continue with inflation to support the Government debt.

Now, if we have got to continue inflation to support the Government debt, then we should be courageous enough to say so and let the people know that the high prices are incident to supporting the Government debt. I do not think that the administration, at least, wants to admit that, although there are some indications that the administration is put in a position where that is what they are doing.

Whether the policy should be to continue inflation, to continue high prices to support the Government debt, is a question of policy

that we will not have the time to develop fully and decide at this session, but I do think that we should give the people to understand that we want to initiate here all the influencing factors possible through which we might stabilize our economy and bring prices down, if we can, in an orthodox way.

Secretary SNYDER. Mr. Chairman, I would like to point out that the history of the management of the public debt, certainly within my own knowledge as Secretary of the Treasury, has certainly been toward constructive lines of stabilization of the debt without any inflationary intentions.

Mr. PATMAN. That is all, Mr. Chairman.

Mr. NICHOLSON. I just want to say this one thing: If we stabilize these things—and I think that is what every Member of Congress wants to do—can we do it under the present law? What we want to do is pay our honest debts. Is that inflationary?

Secretary SNYDER. That is what I want us to do, by giving the Treasury a surplus with which to pay the debts.

Mr. NICHOLSON. Yes, but you have already paid \$7,000,000,000 this year to cut the country's debt down; have you not?

Secretary SNYDER. That is correct. But then we still have a pretty big debt. We have got to pay some more next year and the next year.

Mr. NICHOLSON. But you do not have to do it today; do you?

Secretary SNYDER. No, but we have to do it the next year and the following year, as long as we are prosperous and can afford it.

Mr. NICHOLSON. How does every man run his family? Do they pay their debts off the first year?

Secretary SNYDER. We are not going to pay this debt off in 1 year.

Mr. NICHOLSON. I understand that. But we have been called here in special session to do this today, and we cannot do it today. We have got a bill here to build houses. Then we have got a bill to stop people from buying something to put into the houses; have we not, Mr. Snyder?

Secretary SNYDER. No, because you cannot buy more than is available to buy. What we are attempting to do is to keep them from bidding up prices on what is available for purchase. That is the purpose of it, as I understand it.

Mr. NICHOLSON. No, the Government is coming in and saying: "We are going to build houses for people." Is that not right?

Secretary SNYDER. I think that is a bipartisan program, as I understand it. Both parties are pledged to doing it. I do not know whether it is the Government or who it is, but I think everybody is agreed that the housing shortage is a problem.

Mr. FLETCHER. May I interrupt for a correction there? I think if you will read that platform carefully you will see that the Government is not pledged to build public housing, only where the States and the local Governors are unable to do it or where private enterprise has failed. There is quite a distinction between the Democratic and the Republican platform on housing.

Secretary SNYDER. But it all goes to the same end, taking materials and labor to accomplish it.

Mr. FLETCHER. That is true. But he was drawing the distinction of the Government doing this job and you said both parties are pledged to that program, and I wanted that distinction made clear.

Mr. MULTER. The distinction, Mr. Fletcher, is very slim. They are both pledged to the same thing.

Mr. FLETCHER. If you will read it, you will find it is quite different.

Mr. NICHOLSON. No, Mr. Fletcher. Mr. Snyder is talking about bonds and money and saying that we have obligated ourselves, and some of us have gone deeply into debt, to buy these bonds. I do not see that it is inflationary, so long as we have confidence in the Government. We cannot let them stay there for 10 years and then go in and get them. Or, we can say, "Well, we do not have the money now; we will give it to you 10 years from now." Is that not about the kind of proposition we have?

Secretary SNYDER. We have got to maintain the confidence in the Government monetary operations; yes.

Mr. NICHOLSON. And you do that by taxation; do you not?

Secretary SNYDER. That is correct.

Mr. NICHOLSON. You have to set up a background for these things?

Secretary SNYDER. That is right.

Mr. NICHOLSON. That is right. And who is kicking about it? Are you, Mr. Snyder?

Secretary SNYDER. I am certainly not kicking about supplying a surplus with which to pay that debt.

Mr. NICHOLSON. Through the years have we not given you \$7,000,000,000 with which to cut down some of it—to pay the interest and the principal? Have we not done that?

Secretary SNYDER. And I have used it for that purpose.

Mr. NICHOLSON. And we are going to keep on doing it; are we not?

Secretary SNYDER. I hope so.

Mr. NICHOLSON. But we do not have to do it today, like—I do not say you said so, but somebody said it has to be done today. I do not believe it.

The CHAIRMAN. Mr. Folger.

Mr. FOLGER. Thank you, Mr. Chairman.

Mr. Snyder, I will not ask you any questions about the matter of restoring the 35 and 40 percent gold reserves by the Federal Reserve banks, except to read this and see if the circumstances have substantially changed.

At the time the changes were made, in 1935, from 40 to 25 percent, this observation was made in the report:

The growth of Federal Reserve note circulation has been a part of the general expansion of currency which has accompanied war activity in every country in the world. The expansion of both notes and deposits has reflected growth in Government war expenditures, enlargement of national money income and advancement of pay rolls, and trade at higher prices. So long as the Federal Reserve banks continue to do their part, as they surely must, to assist the Treasury in Government financing and in maintaining stable conditions in the market for United States Government securities, these banks cannot be restricted by an arbitrary reserve ratio.

Now, in your opinion, does that logic hold good under present circumstances?

Secretary SNYDER. Certainly we have the same problem today. In order to carry out this debt operation, and with our level of economy where it is today—with a national income of around \$210,000,000,000—we still have a serious problem.

Mr. FOLGER. Then there is this:

While the reserve ratio for all of the Federal Reserve banks combined is at present a little above 47 percent, that is considerably above the legal minimum.

Individual Reserve banks have ratios that are much nearer to the low point required by law.

Now, I am alarmed about this other part of the bill. And that is the proposal to raise the reserve requirements of member banks—that is, members of the Federal Reserve System, which is composed of national banks—all together, none of them being exempt, and such State banks as may become members by voluntary action. At any time State member banks can withdraw; the national banks cannot withdraw.

I was very much interested in what Mr. McMillen read as to the questions asked and the suggestions made in the letter by a banker to the effect that what he would have to do would be to sell his Governments, and they would go back to the Federal Reserve in its support of the Government securities and in the open market operations.

Now, I would like to have it understood that I am highly favorable to the dual banking system. I do not want anything done that would injure nonmember State banks or any other State banks. But, at the same time, I am fearful that if you make a discrimination such as this proposal makes—and the bill does not say anything about nonmember banks, and I seriously doubt if it can—you will drive out of the Federal Reserve System the State members. And that will really result in the national banks, sooner or later—if this is to obtain—leaving the System themselves, which they can do by certain procedures, and getting out from under the enlarged restrictions.

Is there not great danger in that—the member banks withdrawing, the State member banks, and the national banks changing to State charters?

Secretary SNYDER. The national banking system and the Federal Reserve System have grown up under that very problem. When the Congress set up the Federal Reserve System and set up the requirements for member banks, that gave them that same problem then. That system has grown up under that very situation which you are mentioning now, and the States, gradually have brought their requirements closer to those of the Federal Reserve. But that is the way the Federal Reserve banking system grew up.

Mr. FOLGER. That may have gone on pretty well most of the time, but the observation was made by one of the witnesses who have testified here that the member banks were getting a little bit tired of being restricted and that to have a discrimination between member banks and nonmember banks, in raising the reserve requirement, would add more fuel to the fire.

And the Board of Governors of the Federal Reserve had a meeting in Washington, from which they came back and said this:

Since I presented that statement to the Senate committee, the Board has this morning had an opportunity to meet and to discuss the proposed legislation at length. The board is agreed that the inclusion of the nonmember banks is essential to make the proposed legislation fully effective. I have also been in touch with several of the presidents of the Federal Reserve banks, and others. There is strong concurrence with the statement that it would be very unfair to single out member banks to carry the additional reserves to combat this inflationary situation. This is particularly true of the presidents from those districts where there are large numbers of nonmember banks, which would be given a competitive advantage as against member banks. It might result in a serious loss of membership—

and so forth.

That is the finding of the Board of Governors of the Federal Reserve System, concurred in by the presidents of several of the Federal Reserve banks. That was done after the matter was presented to the Senate and no doubt occurred from fear that this thing was a dangerous proposition.

It is not fanciful, to find that these banks will either sell their Governments or surrender their charters or change from a national bank to a State bank if these continued restriction and requirements are pyramided, as this seems to do in part.

Now, the question I want to ask you is: Do you entertain the fears that the Board has set out here in the testimony of its Chairman and to which he called special attention after their meeting one day this week? Do you share that fear? What will become of the Federal Reserve System?

Secretary SNYDER. Well, I, of course, have to bow to the judgment of the people more directly concerned in the Federal Reserve Board. They are living with that problem every day. But it does not appear to me that there would be a great exodus from membership in the Federal Reserve System by the application of this short-term legislation here, and that there are more advantages of belonging to the System than would be offset by the suggested increase in reserve requirements.

Mr. FOLGER. This has been referred to——

Secretary SNYDER. Although I did say, if you will recall, this morning, that if a constitutional way can be found to blanket them all under the program, why, that certainly would not meet with any opposition from me.

Mr. FOLGER. And then it has been acknowledged that this in itself is almost an inconsequential step, in a great program that probably has been otherwise neglected, toward preventing the further spread of inflation or minimizing it—an inconsequential thing and not too much to be expected of it.

Secretary SNYDER. It is a small thing in a large program.

Mr. FOLGER. Now I want to read to you what Mr. Eccles, the former Chairman of the Federal Reserve Board, said:

I would just like to say that I have been in the banking business since 1913. I was president of two banks in 1920. I was the president of a banking organization all during the collapse in the years 1929 and 1930. That organization owned 28 banks, both Reserve city banks and country banks, and I would say this to the committee: If I was in the banking business today and this restriction was imposed upon my bank as a member bank, unless I had a very substantial amount of interbank deposits and I had to have Federal Reserve connections for clearing, and so forth, I would withdraw from the System because I would be able to maintain smaller reserves by a considerable amount than are now required, without the imposition of this increase, and I could put the saving in those reserve requirements, as well as the reserves that I would be carrying with my city bank correspondent, into short-term Governments. Then this 10 percent that would be imposed upon me as a member—I can likewise put that in Governments. So why would I need membership in the Federal Reserve for borrowing purposes if I had any source of liquidity that I could thus create by getting out of the Reserve System?

That is how he considers it. He is a member of the Board. He said he was present at the meeting that was held when the attitude of the Board was changed from its position taken before the other body particularly to meet this situation and to point out this great danger.

Is it not a little far-fetched that we should risk such consequences as those to get the little benefit that we might hope for, in an anti-inflation movement, by raising these requirements to these banks all over the country? Is it not a little far-fetched to insist on that with the danger that is facing us, as pointed out by the Board and by Mr. Eccles in his testimony?

Speaking about this other matter, I do not know too much about it. I do not know what the situation is with respect to 35 percent and 40 percent and gold requirements, but this seems to me to be a plain statement of fact, concurred in by the Board, and it makes me very uneasy.

I am not here to advocate the imposition of this increased requirement upon nonmember banks. I seriously doubt if Congress could do it. But even if they could, I am not seeking to do that. I would like to maintain the same good working arrangements which have obtained in the dual banking system right along. But, on the other hand, if this action is potentially able to drive from the Federal Reserve System the banks that are members, because they are discriminated against or because they can do better in another field does that not present a very serious proposition for all of us?

Secretary SNYDER. Are you asking me a question?

Mr. FOLGER. Yes, sir. Does that not present a very serious proposition for all of us?

Secretary SNYDER. Of course I have great respect for the statement just read, made by the Federal Reserve Board—

Mr. FOLGER. It must be important if the Board has to have a special meeting to deal with it.

Secretary SNYDER. But I do not think that it is quite as all-out as that; that a bank would withdraw quickly on that account. There is some prestige due to being a member of the Federal Reserve System or else 85 percent of the assets in the banking system would not belong to the members of the Federal Reserve. It is evident that there must be other elements there. But I am not arguing the point because I am in perfect accord with blanketing them all in, if it can be done constitutionally. So I am not arguing against you. I am in favor of blanketing them all under the provision if it can be done under the Constitution.

Mr. FOLGER. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Buffett.

Mr. BUFFETT. Mr. Secretary, do you believe that credit controls contained in the administration bill will effectively restrain business expansion?

Secretary SNYDER. I do not know just what you mean by "business expansion." Our business is pretty well expanded right now. We are right up to full employment; we are right up to the utilization of about all the available raw materials that we can produce right now. So it is a matter of our business operating pretty close to the limit, under the present circumstances.

Mr. BUFFETT. Will those controls operate as enough of a damper on the pressure for goods and services to restrain any further rise in the general price level?

Secretary SNYDER. The best evidence you can get on that is from those who would implement those controls and control them in their fields. I think that would be the best evidence, sir.

Mr. BUFFETT. I am trying to get your view of this situation.

Do you think that the credit controls contained in this bill—or curbs on credit—will, in the hands of the Federal Reserve Board, enable them to restrain further rises in the general price level?

Secretary SNYDER. I think they could, yes, serve as a part of a program to bring that restraint about.

Mr. BUFFETT. You then believe that we should enact the entire program as contained in the Administration bill; is that correct?

Secretary SNYDER. I have supported that by a statement; yes, sir.

Mr. BUFFETT. Do you think that that bill, with its various provisions, gets at the root causes of inflation?

Secretary SNYDER. It gets at a great many of them.

Mr. BUFFETT. What are one or two of those?

Secretary SNYDER. By providing controls against further expansion of inflationary forces.

Mr. BUFFETT. As long as the Government supports two-and-a-half-percent credit in the Government bond market, easy credit is going to prevail for municipalities, States, corporations, and everybody else who wants money; is that not right?

Secretary SNYDER. I think I talked at great length on that, Mr. Congressman, and stated that it is my sincere belief that we must support the two-and-a-half-percent rate. And I believe that sincerely, sir. It is important to the maintenance of confidence in our Government finances that we support that rate.

Mr. BUFFETT. The problem that I run into in that connection, Mr. Secretary, is the statement by well-informed people that, so long as you support those bonds at par or above, there will be no effective curb on business expansion, and that for that reason any action of that kind simply temporizes with the real problem.

Secretary SNYDER. Mr. Congressman, I have found no one who had the responsibility of debt management, either through legislation or through administration, who is willing to say that he would recommend removal of the support of the Government bond market.

There are some folks outside, who have no responsibility and probably might not be directly affected, who don't feel that way. But anyone who is directly responsible, through legislation or through administration, has not recommended removal of support, to my knowledge; at least, I have not yet heard anyone come out and say that we ought to stop supporting the Government bond market.

Mr. BUFFETT. There is another side of this problem which puzzles me, Mr. Secretary: Which is the worst for the ordinary citizen of this country who has his trust in Government bonds—for that market to receive a shock, we will say—which would happen if those bonds sold below par and the general inflation in our present situation were somewhat lessened—or to have the Government support the bonds at par or above par and have inflation go on and the value of his bonds, in terms of purchasing power, deteriorate the way it has in other countries?

Secretary SNYDER. Mr. Congressman, it is not anywhere near as simple as that. It is not the direct owner of the bond that is influenced by this. It is the insurance company, the bank, the investment trust, the place where you have deposits, the places where you have your insurance policies, the places where you have your legacies invested. All those have a bearing on this problem about which we are talking today.

It is not just a matter of letting the bond market drop a point or two points, or any points, that is affected. It runs through the whole texture of our monetary system and our economy.

Mr. BUFFETT. I understand that, and I recognize that you are up against an extremely complex problem. What I am trying to determine in my own mind is whether there are any genuine brakes on this inflationary process in this country or whether we are simply going to, from time to time, pass measures that might act as a psychological influence on less-well-informed people and cause them to have confidence that the well-informed do not have, and, because of that situation, that the less-well-informed might be taken advantage of by those who know what is going on.

Secretary SNYDER. But this management of the public debt does take care of the less-informed as well as the informed because the man who has his deposits in a bank, or who has that and an insurance policy, may not be informed on money matters and know how to handle his bond account, but he has put his money into something that is important to him—and he is one of the less-informed. We have to give very careful consideration to that.

You have asked if there is any brake that we can put on there. Yes; in these prosperous times we can keep our revenue program up to where there is a budget surplus, where we can be reducing that debt and helping to meet this inflationary bank credit problem by paying off those bank-held securities.

Mr. BUFFETT. Well, it is too involved a problem to discuss with you at this late hour, so I will not go any further into that except to ask you this one question: Is there anything in the administration bill to restrain or cut back the inflationary pressures caused by our overseas spending program?

Secretary SNYDER. That was a matter that was carefully discussed in Congress at the time that measure was before Congress, and all of those elements were taken into consideration when the Congress passed the authorization for that foreign defense spending. When I say "foreign defense" I am covering both the military program and the ECA program because I consider all of that as part of our national defense. It actually is. Before those measures were passed, of course, they were carefully considered by the Congress as to their effects and purpose.

Mr. BUFFETT. Well, it seems that the Congress did not anticipate the inflationary pressures accurately at that time.

Secretary SNYDER. Well, I am not going to question the wisdom of the Congress. But they did have those matters before them at the time they were discussing those proposals.

Mr. BUFFETT. They did not evaluate them correctly, or at least they were not evaluated correctly, or we would not have the problem today growing worse.

Secretary SNYDER. Well, at least, in this period, we have to apply ourselves in the best fashion we can to meeting the problems as they came up.

Mr. BUFFETT. Do you think that we would be troubled with these inflationary prices today if we had no overseas spending program, or if our overseas spending program were considerably less than it is at the present time?

Secretary SNYDER. I think the evidence that was given at the time took that into consideration—that if we did not have that spending, there would be less inflationary pressures. That was discussed openly at the time of the passing of the legislation.

Mr. BUFFETT. I do not believe the American people were ever accurately or effectively apprised of the inflation burden that those programs would place on its back.

Secretary SNYDER. But that is another one of those matters which I think we would have passed whether there was an inflationary angle to it or not. I think we did do it realizing the inflationary aspects of it, because it was so important to the future of our country that we took that measured handicap that might be involved in passing the legislation.

Mr. BUFFETT. Certainly the people were not told when that measure was passed that they were going to be placed under the Office of Price Administration again, were they?

Secretary SNYDER. Well, it was certainly openly discussed in hearings just such as we are having here—the implication of it.

Mr. BUFFETT. Well, I do not recall it.

Secretary SNYDER. I attended many of those, sir, so I do recall it. I was sitting in a chair before the committee and we discussed it at great length.

Mr. BUFFETT. Do you know of any responsible administration official who said that if the Marshall plan was passed that we would have to go back under the Office of Price Administration?

Secretary SNYDER. I do not suppose they said exactly that. But they did concede the inflationary aspects of the spending.

Mr. BUFFETT. It is clear to me that if they saw that regimentation ahead, they did not disclose it. If they did not see it, then, they did not properly evaluate the inflationary impact of the foreign program.

Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Hays.

Mr. HAYS. I have one short question, Mr. Secretary. One of the country's leading bankers complained yesterday that there was little control of speculative loans. I wondered just what might be done about that. The powers are rather inadequate at present, according to his comment, and it seemed to me that Congress might appropriately consider some measures to put some restraints on loans that are obviously speculative. Have you had occasion to study that feature of the inflation problem?

Secretary SNYDER. I have not. Except that has come up from time to time, as one of the segments of the problem of restraint. The Secretary of Agriculture could tell you more about that. You are speaking of the commodity markets?

Mr. HAYS. No, not necessarily. Of course, that would be one type.

Secretary SNYDER. Are you speaking of stocks and bonds?

Mr. HAYS. Yes.

Secretary SNYDER. Oh, we have a very strong regulation there. It is a 75-percent-cash requirement there, a 75-percent margin on loans for trading in the market. Is that what you are talking about?

Mr. HAYS. This comment I am referring to did not specify.

Secretary SNYDER. He must have been thinking of the commodity markets.

Mr. HAYS. That would be included, but there would be other types of speculative loans, I suppose, to which he had reference. I was just wondering to what extent that complicated the picture.

Secretary SNYDER. If he is referring to commodities, that, of course, has been discussed on a number of occasions. But if he was referring to the stock market, and operations of that sort, I think we have the most unusual situation, where many stocks are being sold at four and five times their earnings. There is certainly not an inflationary trend in the stock market.

Mr. HAYS. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Buchanan.

Mr. BUCHANAN. Mr. Secretary, in section 2 (b) there is a provision to which you object. Will you restate it again?

Secretary SNYDER. The raising of the gold reserve requirements from 25 to 35 and 40 percent.

Mr. BUCHANAN. Yes.

Secretary SNYDER. Yes.

Mr. BUCHANAN. The gold reserves at the present time are about 11.3 billion dollars; is that approximately correct?

Secretary SNYDER. You mean our total gold reserves?

Mr. BUCHANAN. Yes.

Secretary SNYDER. Close to \$23,000,000,000. Our operating ratio is now 51, so that is perhaps the figure you have in mind.

Mr. BUCHANAN. Yes. That gives you how many billion dollars in order to support the Government bond market? Do you multiply that by a ratio of 4 to 1, approximately?

Secretary SNYDER. I would like Dr. Haas to answer these questions.

Mr. BUCHANAN. I would like to go into detail on this.

Dr. HAAS. Chairman Wolcott had some figures that he got from the Federal Reserve Board. I have not calculated it, but he gave some figures just a few minutes ago.

Mr. BUCHANAN. Is about \$45,000,000,000 the approximate amount?

The CHAIRMAN. \$50,000,000,000.

Mr. BUCHANAN. That is the amount you now have in order to protect the Government bond market; is that correct?

Dr. HAAS. That is assumed.

Mr. BUCHANAN. Now, if the reserves were increased from 25 to 40 percent, that will cut down that amount, and by how much?

Dr. HAAS. I did not get your question.

Mr. BUCHANAN. If the reserves are increased from 25 to 40 percent, that will reduce the gold-reserve support; will it not?

Dr. HAAS. It will cut down the cushion; the amount available.

Mr. BUCHANAN. Cut down the total amount available for the protection of the Government bond market.

Dr. HAAS. And for a possible expansion of the currency, and so forth. Currency expansion was one of the reasons they gave for having the ratio reduced some time ago.

Mr. BUCHANAN. In other words, you really are destroying the elasticity, and reducing the amount available to cushion any shock on the Government bond market.

Dr. HAAS. Not only on the Government bond market, but to meet any emergency which is required.

Mr. BUCHANAN. What would happen now, supposedly, if we were to effect this into legislation? What would be its immediate effect,

say, within weeks or a month? Would it not be apt to cause a break in the Government bond market?

Dr. HAAS. That is difficult to predict. It might. The market would wonder why it was enacted.

Mr. BUCHANAN. It certainly would leave a soft spot there which would not be available to cushion any drain that might occur in the bond market, by reducing the amount available to cushion it.

Dr. HAAS. Yes; that would be obvious.

Mr. BUCHANAN. What good can this do at this time, to tighten up the elasticity?

Secretary SNYDER. I feel that it would have no immediate effect other than I can see there might be some remote psychological effect. But I think that the problem would far outweigh any benefit that could possibly be conceived. I think it would handicap us considerably at this time in managing the debt—

Mr. BUCHANAN. In other words, you would be content to—

Secretary SNYDER. —and maintaining the confidence in Government credit.

Mr. BUCHANAN. —maintain the status quo as is, rather than tinkering with any device such as this?

Secretary SNYDER. Well, this particular item; yes.

Mr. BUCHANAN. That is all.

The CHAIRMAN. Mr. Boggs.

Mr. BOGGS. No questions.

Mr. SMITH. Mr. Chairman.

The CHAIRMAN. Dr. Smith.

Mr. SMITH. Just one more point, Mr. Secretary. I understand you to say that the figure which Mr. Wolcott gave, if this change were made to 40 percent, that there would not be an expansion possibly there of \$50,000,000,000 worth of credit.

Secretary SNYDER. What was that, sir?

Mr. SMITH. What effect would this have on your credit expansion possibility if the 40 percent and 35 percent provisions as proposed were adopted?

Secretary SNYDER. That was the question that I asked the technician to answer.

Mr. SMITH. Did I understand you to answer Mr. Buchanan to the effect that we now have sufficient excess gold reserves to permit \$50,000,000,000 of credit expansion, and that if this change were made it would reduce that amount?

Secretary SNYDER. What was your statement?

Dr. HAAS. I did not give any estimate. The chairman made a calculation. I did not make any calculation.

Secretary SNYDER. We were just referring to the chairman's figures that were given him yesterday. Is that not the case, Mr. Chairman?

The CHAIRMAN. Yes, I think I was commenting upon the statement Mr. Eccles made yesterday.

Secretary SNYDER. We do not have that.

Mr. SMITH. If this change were made, you would have approximately 4.6 billion dollars of excess gold reserves?

Secretary SNYDER. Well, these figures were worked out—

Mr. SMITH. Assuming that is correct, how much credit expansion can you produce on the basis of 4.6 billion dollars?

Dr. HAAS. On the basis of this proposed legislation, I have not read the bill, is it 40 percent?

Mr. SMITH. 40 and 35 percent.

Dr. HAAS. It is difficult to make an estimate. Something between that.

Mr. SMITH. Let us take 40 percent. How much currency could you issue on the basis of that amount of gold? That is a simple question. Two and a half times 4.6?

Dr. HAAS. That is right.

Mr. SMITH. And how much credit can you expand on that basis?

Dr. HAAS. Well, it depends on which bank it goes into and where it is located. Some people take a figure of 6.

Mr. SMITH. Five or six?

Dr. HAAS. Yes.

Mr. SMITH. You would still have approximately 57 to 69 billion dollars of credit expansion power, if this change were made. That is a fact, is it not?

Secretary SNYDER. I am not answering any questions on that, sir, because I have not had a chance to go into it.

Mr. SMITH. I am assuming that the gentleman in the rear, I do not know his name, is answering for the Federal Reserve.

Secretary SNYDER. No. Dr. Haas is not answering—

Mr. SMITH. I meant the Treasury.

Secretary SNYDER. We have no figures at all. That is why I hesitate to try to formulate answers.

Mr. SMITH. Now, Mr. Snyder, how much Treasury gold is there?

Secretary SNYDER. Are you speaking of this \$23,000,000,000 that we have in the Treasury?

Mr. SMITH. Have you any Treasury gold that is not covered in the Federal Reserve banks by gold certificates?

Secretary SNYDER. The total amount, covering all gold, in the Treasury and in the Federal and everywhere else, in the Government, \$23,678,000,000, as of August 2.

Mr. SMITH. Is it possible for the Federal Reserve System to avail itself of more gold certificates on the basis of the gold which the Treasury is holding, in excess of that which is already covered by gold certificates?

Secretary SNYDER. I did not quite get your question.

Mr. SMITH. You have here a total of \$22,000,000,000 as of June 23, \$22,261,000,000 of gold certificates.

Secretary SNYDER. Well, the Federal cannot issue more certificates against that particular gold.

Mr. SMITH. That is right. Can any more gold certificates be issued against the gold, excess gold, which you hold, the other billion?

Secretary SNYDER. There is about a billion there, yes.

Mr. SMITH. Another billion three hundred million?

Secretary SNYDER. That is about right.

Mr. SMITH. And you could convert that into gold certificates, could you not?

Secretary SNYDER. That is correct.

Mr. SMITH. Very well. Now, you have \$1,300,000,000 multiplied by $2\frac{1}{2}$, multiplied by 5 or 6, which would give you at least an additional \$16,000,000,000 of possible currency credit expansion; is that not true?

Secretary SNYDER. Credit expansion.

Mr. SMITH. How in the world could the raising of these gold reserves, as proposed, affect your position to meet your credit needs? How could it hamper your credit needs?

Secretary SNYDER. It might not hamper it today, Mr. Congressman.

Mr. SMITH. With at least 57 billion dollars of potential credit in the hands of the Federal Reserve banks, after the change was made, and the possibility of adding to that another \$16,000,000,000, or a total of \$73,000,000,000—you are not saying to this committee that the passage of this bill would, in the least bit, affect your credit expansion power, are you?

Secretary SNYDER. It might not tomorrow or the next day, but for the long range, I do not think this is any time to be changing that provision.

Mr. SMITH. How about until we come back for the next session, in 6 months?

Secretary SNYDER. Well, why include it right at this time? Why not wait until you get back at that time to consider it?

Mr. SMITH. No. I am assuming that we pass this measure. Do you think anything serious could happen to hamper you in managing the Federal debt, or doing anything else you want to do?

Secretary SNYDER. Do you think that anything of value would come of doing it between now and that time?

Mr. SMITH. I mean does this hamper the operations of the Federal Reserve System, in any way?

Secretary SNYDER. It might not have any immediate effect, but I am concerned about the long range.

Mr. SMITH. Let us say in the next 6 months.

Secretary SNYDER. Are you stating that you will take it out if there is any effect there?

Mr. SMITH. Pardon?

Secretary SNYDER. Are you stating that if you pass this, that you will reverse it in 6 months?

Mr. SMITH. No, I am not saying we will reverse it.

Secretary SNYDER. Well, then, let us not put it in.

Mr. SMITH. But we will come back here, and then, if anything were to take place, which indicated that the reserve requirements ought to be lowered, they could then be lowered, could they not? So nothing is going to happen here in the next 6 months; is that not correct, Mr. Snyder? Is it not, Mr. Snyder, just a little ridiculous for the Secretary of the Treasury of the United States to come up here and testify that the small increase in reserves provided for by this bill might hamper the operations of the Federal Reserve?

Secretary SNYDER. No, I do not think it is ridiculous, Mr. Congressman, and neither would you if you were sitting in my seat of responsibility.

Mr. MONRONEY. I might add that the Federal Reserve is scared to death of this.

The CHAIRMAN. Just a minute. Let us have order. The Secretary apparently wants to make a statement.

Secretary SNYDER. I made my statement. I deny the ridiculousness of my making that statement, because I have the responsibility as Secretary of the Treasury of managing that debt and the problem is a serious one to me.

Mr. BOGGS. Mr. Chairman.

The CHAIRMAN. Mr. Boggs.

Mr. BOGGS. I passed a moment ago and I would like to ask a few questions on this matter.

I am still unable to understand exactly what the implication of this proposal is. I have been informed that the Federal Reserve System is very much concerned about it. The statement has been made—I do not know how authentic it is—that it is entirely possible that the adoption of this proposal would actually affect the stability of Government bonds. Is that possible?

Secretary SNYDER. It could easily be possible, and we are offering no testimony as to the reserves or anything until we have had a chance to present them in a studied fashion.

Mr. BOGGS. Why could it easily be possible?

Secretary SNYDER. As to our support program?

Mr. BOGGS. Yes.

Secretary SNYDER. It all depends on the amount of bonds that are turned in for redemption.

Mr. BOGGS. So that the adoption of this proposal, without more serious consideration and with Congress going home immediately after it is done, could, in the interval between now and January, actually depreciate the Government bond market?

Secretary SNYDER. We feel like it might be a serious problem, yes.

Mr. BOGGS. One of your representatives here said that this cushion or this elasticity was also needed in other emergencies. What type of emergencies might arise where that would be so?

Dr. HAAS. The two most general ones are an outflow of currency, if there is a need for additional currency. That absorbs the gold reserves also. Or, if you export gold, gold actually going out of the country. Those are contingencies that might happen. At the moment, it is not a problem, but next month it might be, or in the next several months it might be. Nobody knows.

Secretary SNYDER. And it is not just a matter of this particular bond market today, but it affects our refinancing as we go along.

Mr. BOGGS. Exactly. Is it not also likely that this might have quite an adverse psychological effect, if nothing else, and is it not conceivable that a large number of people and corporations might suddenly flood the market with these bonds?

Secretary SNYDER. The psychology works both ways. I think that the psychology that would endanger our management of the debt is greater in its effect than the psychology that would improve the stability.

Mr. BOGGS. What possible helpful psychology could arise from the enactment of this bill?

Secretary SNYDER. Well, the chairman advanced that awhile ago as to the psychology of our stabilizing and tightening up.

Mr. BOGGS. Do you agree with that theory?

Secretary SNYDER. I do not, no, because I do not know how far that psychology would go. The other psychology might more than offset it.

Mr. BOGGS. At best, it is a mere theory, is it not?

Secretary SNYDER. Psychology is always a theory. It is not an exact science.

Mr. BOGGS. But it is not improbable, or, let me put it this way, it is not impossible that the enactment of this provision without further study, and without further testimony from the Federal Reserve people, or from others, might actually depreciate the Government bond market and make the management of the debt very difficult?

Secretary SNYDER. I have expressed my concern about it.

Mr. BOGGS. Thank you.

Mr. MONRONEY. Will you yield?

Mr. BOGGS. Surely.

Mr. MONRONEY. If we now have in the Federal Reserve 11.3 billion dollars of actual gold reserves to support the bond market which can be committed in the open-market operations and if that is expandable four times, as has been said here, that would give you \$45,200,000,000 to support the bond market with, would it not?

Secretary SNYDER. Well, those are figures that you are working out there.

Mr. MONRONEY. Assuming that you can expand the gold four times.

Secretary SNYDER. I presume the Federal has testified on these matters.

Mr. MONRONEY. But if you cut the gold reserve down by this bill to 4.5, we will say, which I think that is the figure the chairman has used, and that is expandable two and a half times, as this provides, you get a 10 to 12 billion dollar figure, so you drop from \$45,000,000,000 to about 10 or 12 billion dollars in the resources behind the open-market operations. This 450 percent reduction might be a signal to those who were concerned about the value of Government bonds that it might be wise to cash them in to the Federal Reserve now. Remember, you are faced with \$50,000,000,000 of refinancing. It certainly would mean a much higher interest rate that the Government would have to pay on the debt, instead of the present 2½ percent policy.

Secretary SNYDER. It presents a very great problem to the management of the debt.

Mr. MONRONEY. I certainly think the problem is great enough not to be called ridiculous by a member of the committee.

Secretary SNYDER. I thought so, too.

The CHAIRMAN. Thank you very much, Mr. Secretary.

Secretary SNYDER. Thank you, Mr. Chairman.

The CHAIRMAN. We are very glad to have your testimony.

There has been received a communication from Mr. Paul Porter, the Special Assistant to the President to coordinate the President's program. We told Mr. Porter that we would be very glad to have the Secretary of Commerce, Secretary of the Interior, and Secretary of Agriculture present statements, and, without objection, as soon as they arrive, they will be inserted in the record.

(The documents referred to above have not been supplied for inclusion in the record.)

Mr. MONRONEY. Are we not going to have them appear in person, Mr. Chairman?

The CHAIRMAN. No.

Mr. BOGGS. Mr. Chairman, I have a telegram I would like to read for the record.

The CHAIRMAN. Just a moment.

I also have a companion statement to one which was put in before the Senate committee by Joseph M. Dodge, president of the American Bankers Association. Without objection, that will be inserted in the record.

(The document referred to is as follows:)

THE AMERICAN BANKERS ASSOCIATION,
THE DETROIT BANK,
Detroit 31, Mich., August 4, 1948.

In re H. R. 7062.

HON. JESSE P. WOLCOTT,
House of Representatives, Washington, D. C.

DEAR JESSE: There is attached hereto a statement which I have prepared on the above bill on behalf of the American Bankers Association.

It will be greatly appreciated if you will arrange to have this statement inserted in the official hearings on H. R. 7062.

Yours sincerely,

JOSEPH M. DODGE, *President.*

STATEMENT BY JOSEPH M. DODGE, PRESIDENT OF THE AMERICAN BANKERS ASSOCIATION, TO THE BANKING AND CURRENCY COMMITTEE OF THE UNITED STATES HOUSE OF REPRESENTATIVES, AUGUST 4, 1948

In H. R. 7062, which is before you for consideration, there are two proposals which are of particular interest to the banking business and to the members of the American Bankers Association.

One is the regulation of consumer credit referred to in title I and the other is the increase of bank reserves referred to in title II. I intend to direct my comments to these.

The American Bankers Association has long recognized the dangers of the present inflationary situation and the importance of avoiding an excessive expansion of bank credit. The association's program of voluntary credit control and anti-inflation action was designed to meet those dangers.

The program was presented and put into effect on January 5 of this year—7 months ago. It began with a series of 13 pilot meetings in the key cities of the country. At these meetings the program was presented to representative bankers of each area of the country. The pilot meetings were supplemented by hundreds of additional meetings held by the bankers associations of every State, whose officers accepted the responsibility of carrying the message to the individual banks. The activity was of tremendous scope. On my own part it involved 6 months of time and 35,000 miles of almost continuous travel, all for the purpose of carrying out this program and emphasizing its importance to the bankers of the country.

I can testify to the acceptance and cooperation of the State bankers' associations and the thousands of individual member banks. The evidence of their cooperation is apparent in the results in the first 6 months of this year.

Since the normal spring and early summer meeting period of the State bankers' associations has come to a close, we have supplemented this activity with a communication addressed to the chairman of the board and to the president of each bank, under date of July 29. The communication further emphasizes the need aggressively to continue the anti-inflation program. You have already received copies of this folder, which reproduces a covering letter from myself to the officers and directors of the member banks of the American Bankers Association, a letter dated July 2 from Secretary Snyder to me, and my reply to it dated July 7. I think it is important to mention that this material was prepared before the introduction of this bill, as a further step in carrying out our anti-inflation policy.

Immediately after the end of the war we engaged in a program to provide the credit necessary for reconversion and for the stimulation of peacetime production. However, when it became apparent that the inflationary situation was not well in hand we voluntarily embarked on this program to emphasize the need for selection and restriction in the extension of credit and the stimulation of savings. We urged the banks to scrutinize credit carefully, to restrict its use to loans that stimulate immediate production, to avoid increasing the pressures on consumption, to restrict its use to sound and necessary purposes, to avoid speculation, and in general to hold the obligations of borrowers well within their capacities to pay. We asked the banks to use every effort to encourage the public to invest in Treas-

ury savings bonds and to increase savings-deposit accounts. We emphasized the need for these actions in our meetings, through speeches, and in other forms of publicity. This was a reversal of the program that we had been engaged in, and I emphasize it because we took the voluntary method of cooperative action to meet a national problem. This program demonstrated a type of flexibility much more appropriate to the American philosophy than arbitrary controls of any nature.

It is evident that the voluntary credit-control program has been effective and successful. The increase in bank loans in the first 6 months of 1948 was largely in the consumer credit and mortgage fields. Commercial, industrial, and agricultural loans actually were reduced about \$300,000,000 as compared with the end of 1947. In the last 6 months of 1947, loans increased at a rate of about \$10,000,000,000 a year. In the first 6 months of 1948 it was at a rate of about \$3,400,000,000 a year, or roughly one-third of the rate prevailing in the last half of 1947.

Mortgage loans, backed by Government guaranties, contributed substantially to the loan increase which has taken place. This is largely the result of a Government policy of easy mortgage credit. The increase in consumer installment credit for durable consumer goods goes along with increasing production and new construction. New homes must be equipped and furnished.

Bank deposits have not been increasing. They have been declining. Bank deposits have declined about \$4,000,000,000 since January 1. That of itself tends to restrain lending activity. The effect has been to induce still another element of caution in bank lending. The increase in total loans has been offset by an even greater decline in investments. Thus there has been no increase in total bank credit outstanding, but an actual decrease.

A comparison of the increase in total bank loans, using the prewar year 1940 as a base, shows that the ratio of increase in total loans is less than that of the rise in the cost of living, wholesale commodity prices, or the gross national income.

On the subject of regulating consumer credit, which is referred to in title I of the bill, it should be observed that installment sales credit only would be controlled. This proposal apparently attacks only 25 percent of the problem. Installment sales credit represents less than \$3,500,000,000 of the present \$14,000,000,000 total of consumer credit. That \$3,500,000,000 includes FHA title I loans, which are Government-sponsored credit.

It should also be pointed out that if consumer credit installment sales are restricted by the proposed regulation, manufacturers or distributors may finance such sales by the use of regular commercial credit. A contraction of consumer credit may thus increase the use of regular commercial credit.

Most consumer durable goods, with the notable exception of automobiles, are now in relatively adequate supply. The reimposition of regulations on consumer credit would have a tendency to give preference to those who can meet the larger down payments required. The less fortunate individual, whose need is as great and who is worthy of credit, may be deprived of the article he wants.

The banks of the country now use conservative installment credit terms, such as those suggested by the American Bankers Association, which approximate the terms which prevailed under regulation W. A return to regulation W will not result in terms appreciably different than those now being used by the banks. For that reason we have no serious objection to this proposal if the Congress believes it should be enacted.

Whatever loose credit of this type there may be is extended outside of the banks. As was pointed out earlier, the proposal is limited to an effect on about 25 percent of what is commonly referred to as consumer credit. It is our view that if it is intended to use this regulatory approach to consumer credit as an anti-inflation act, it should cover the whole field of consumer credit.

There is no evidence, and I believe no testimony has been submitted, which indicates that the use of bank credit has been an important factor in creating the present inflationary situation or that there is any current excessive expansion of loans. The proposals and the discussions of the problem of curtailing credit have been based on a possible inflationary increase in the use of bank credit and assumptions about what could happen, not on the facts as they are today.

To meet these assumptions about what could happen, the proposal is made in title II that the Federal Reserve Board be given authority to increase reserves against demand deposits of member banks by 10 percent thereof, and time deposits by 4 percent thereof. I am not sure everyone understands exactly what this means. I have seen references to an increase of 10 percent and further assumptions that this means an increase of 10 percent in existing reserves. This

percentage refers to deposits, and means an increase in reserves of 10 percent of total demand deposits. It should be emphasized and clearly understood that the proposal for increased reserves as it affects demand deposits means an increase of 70 percent (viz, from 14 to 24 percent in country banks, 50 percent (viz, 20 to 30 percent) in Reserve city banks, and 40 percent (viz, 26 to 36) in central Reserve city banks.

It has been estimated that if put into effect these increased reserves will immobilize some 10 or 11 billion dollars of the assets of the banks. This cannot by any means be called a moderate increase. It is a drastic proposal which, if put into effect will affect banks and borrowers alike, and could seriously affect the economy itself.

The argument may be made that while authority is given to do this, it may not necessarily be immediately exercised. As a matter of fact, mere passage of such a law creating the authority to invoke these drastic increases in bank reserves puts every bank on notice that these powers may be used. It makes it necessary for banks to modify their investment policies, in anticipation that the powers may be used, almost as if the powers actually were fully in effect. This is true because it is inevitable that these powers will be used and these extra reserve requirements put into effect at the time when banks are least able to meet the requirements. Sound bank management requires anticipation of such an action. I believe Mr. Eccles has affirmed this by testifying that every bank would have to keep itself in position to meet these reserve requirements. In principle, legislative authorization of any such increased reserve requirements, even though only in the form of authority, might well have the same effect as if they were immediately fully imposed.

Another point in connection with the proposal to increase bank reserves is that it applies only to member banks of the Federal Reserve System. There has been testimony to the effect that if enacted this proposal should be made to apply to all banks, whether member or nonmember banks.

There have been questions raised as to whether this increased reserve proposal can be legally applied to nonmember banks. Up to this time, State laws have controlled the reserve requirements for State nonmember banks.

If the proposal is amended to make it apply to all banks, regardless of whether or not they are members of the Federal Reserve System, such a step would be an encroachment on the principle of dual banking, and an invasion of the rights of the States and the State banks they charter and supervise. In effect, the reserve requirements imposed by State law and regulation would be nullified, and in their place would be substituted the requirements dictated by a governmental agency in Washington.

For the foregoing reasons the association is opposed to the inclusion of non-member banks under this proposal.

There are several major questions about the proposal for additional reserve requirements which need careful consideration.

The first is the question as to whether these increased reserves are necessary, and particularly whether they are necessary now. In this connection, certain facts should be pointed out: First, the voluntary credit-control program of the American Bankers Association is being actively continued and has already produced results; second, the Federal Reserve and the Treasury already have powers which are adequate to meet not only the present situation but also any situation which could arise between now and the time the next regular session of Congress convenes. The short-term rate on Government securities can be further increased, and there has been some discussion of such a step. The rediscount rate can be further increased. Moreover, there is also the power to sell Government securities now held in trust funds or by the Federal Reserve.

There remains a 2-percent increase which can be made in the reserve requirements of the central Reserve cities. However, it has been said that the final 2-percent increase in New York and Chicago has not been necessary.

There was action taken along these lines in December and January. This had a salutary, cautionary effect.

Under section 301 of the Federal Reserve Act, the Federal Reserve Board is charged with the responsibility of obtaining necessary information on the use of credit and controlling the proper use of credit. With that authority, the Federal Reserve Board is given the right to refuse rediscount privileges to member banks under appropriate circumstances. This could be made the means of any necessary disciplinary action.

The Federal Reserve System and its 12 Federal Reserve banks constitute a source of natural leadership, information, and power to control the use of credit at

the local and individual bank level, without the enactment of new laws. What the American Bankers Association has been able to do in a voluntary and cooperative program is an example of what could have been done under the leadership of the Federal Reserve System, had the System been willing to accept and use that principle rather than to ask for additional powers.

We emphasize that the Federal Reserve Board and the Treasury already have sufficient powers and that the granting of any additional powers, particularly powers as drastic as those proposed, should be given only on specific evidences of what increases are needed now and before the next regular session of Congress, why they are needed, and what effect they will have on the credit structure and the economy of the country.

The second major question concerning the new reserve proposal is whether or not it will be effective.

With banks holding large amounts of Government securities and the Federal Reserve ready to absorb them, it is not apparent how increased reserve requirements can reduce reserves available for loans. The banks can sell Government securities in order to acquire those reserves.

This proposal would not apply to other sources of credit or to direct and indirect Government lending agencies. The proposal aims to restrict only the credit activities of member banks and leaves all other types of lenders free to continue lending as they are doing now.

This proposal can be nullified by other inflationary acts or other causes of inflation outside the banking system.

The powers granted in this proposal will not reduce prices or the cost of living unless used so extensively that they result in denying needed credit to productive business, thus pulling down both employment and production.

The third major question is whether or not this proposal has any elements of danger in it. The proposal is an action which hits member banks equally, regardless of their individual loan and investment positions. It tends to freeze the banking system uniformly, regardless of varying local credit needs.

Credit has two aspects: One relates to consumption, and the other to production. The use of credit follows prices and business volume. Someone has to ask for credit before it is granted. Its use is based on the need for it. If business activity is to be continued at the present volume and at present high price levels, there will be a continuing need for a correspondingly large use of credit.

We must be careful not to contribute to an economic reversal so freely prophesied and wished for by the Soviets. We must be sure that the cure proposed does not bring a reaction worse than the disease. Credit on a national basis is a delicate mechanism. Rude handling can produce disastrous chain reactions.

Reference has already been made to the fact that if this proposal is enacted the banks will be put on notice to prepare for the full imposition of the requirements. We do not know what the future has in store for us. At the beginning of 1947 everyone was convinced a recession was imminent. Now, we have inflation, and everyone seems convinced that more inflation is inevitable. We cannot afford to take any action which may prove to be the spark that sets off a drastic reversal.

This proposal is an emergency action. It is proposed before an emergency session of Congress. Such an action, taken in haste and under the emotional stresses and strains of the present situation, may not be as well thought out as it should be.

We oppose the proposal to give the Federal Reserve power to increase bank reserve requirements because there is no evidence that it is immediately necessary or warranted; because it is not directed at the fundamental causes of inflation; because it includes elements of danger to the economy; because it is an emergency action taken under unusual political and emotional circumstances; because it is an action in a single limited area of the inflation problem; because the proposal has such broad implications that it needs further extensive study as to its possible effects; because it is an unnecessary addition to the regulatory powers of a governmental agency; and because adequate, unused powers already exist.

We are all concerned with the general problem of inflation and high prices. There is no easy answer or easy way to meet the problem. There is no single act which will correct it. There is nothing that can be done that will be painless. There have been many years of excessive Government spending, Government deficits, and Government-sponsored easy money. These have brought us to our present difficulties. If the problem is to be corrected, these policies must be reversed. What is needed is a consistent anti-inflationary Government policy. The basic answer to our inflationary problem is to so conduct our fiscal affairs

that we insure budget surpluses which, appropriately used, can provide the necessary anti-inflationary effect.

The CHAIRMAN. When Mr. Eccles was on the stand the question of the constitutionality of applying these reserve requirements to non-member banks was brought up and we asked him to prepare a brief statement on that point. That has been submitted and, without objection, it will be inserted in the record.

Mr. BUCHANAN. What is the gist of the statement?

The CHAIRMAN. He is contending, and cites cases in support of his contention, that it is constitutional to apply the reserve requirements of member banks to nonmember banks. The opinion is prepared by George B. Vest, general counsel of the Federal Reserve Board.

(The statement above referred to appears at p. 124.)

Mr. BOGGS. Mr. Chairman.

The CHAIRMAN. Mr. Boggs.

Mr. BOGGS. I have a telegram addressed to me which I would like to read. It is from A. F. Whitney—

Mr. KILBURN. Do you have to read it?

The CHAIRMAN. We all have it.

Without objection, it will be placed in the record.

Mr. BOGGS. Well, it is just a telegram.

Mr. KILBURN. We will give you credit for it.

Mr. BOGGS. I would like to proceed, if I may.

The CHAIRMAN. Proceed.

Mr. BOGGS. It is a telegram from the Brotherhood of Railway Trainmen stating that Mr. Whitney requested 10 minutes to testify before this committee, and stating that he was denied the opportunity to testify.

The CHAIRMAN. I might say that there were several other witnesses who have attended these hearings and who have communicated with us, who would have liked to appear, but it does not seem to be feasible to continue with the hearings any longer.

Are there any other members who have communications that they would like to insert?

Mr. HAYS. I would like permission to insert in the record a copy of a telegram from one of my bankers.

The CHAIRMAN. Without objection, that will be done.

(The document referred to follows:)

Hon. BROOKS HAYS,

Member, Banking and Currency Committee:

After careful and deliberate consideration of the proposed increase of reserves that commercial banks must carry in the Federal Reserve banks, we are firmly of the opinion that such a move will bring about a credit panic, the result of which would be a great curtailing of production of manufactured goods and products of all kinds, thus creating additional scarcity that of necessity would result in further price increases. It is our further belief that the Government bond market would be seriously affected if this power is given the Board of Governors of the Federal Reserve System. Credit is not the basis of the present inflation. Which rests upon continued Government spending and the price of wages and materials that go into manufactured goods. The curtailment of credit at this time would seriously affect the movement of crops which farmers depend upon for their prosperity, which is now at our door.

This demand of the administration is so drastic, with such potential bad effects upon the economy of the country, we sincerely request you use all the influence at your command to have matter deferred for further intensive study.

NATHAN ADAMS,
Chairman of the Board, First National Bank in Dallas.

J. C. TENISON,
President, Dallas National Bank.

The CHAIRMAN. The committee will go into executive session. (Whereupon, at 5 p. m., Wednesday, August 4, 1948, the committee went into executive session.)

(The following statements were submitted for inclusion in the record:)

(Inserted into record at request of Gov. R. M. Evans:)

Congressman Wolcott quoted a statement to the following effect: "According to the 1948 consumer credit survey of the University of Michigan, published a month ago, 9,000,000 family units are now using this form of credit, against between eighteen and twenty million family units using it just before the war."

This statement appears to have come from a press release of July 14 given out by the American Bankers Association. It is not strictly correct in four respects: (1) The figure of between eighteen and twenty million family units using consumer credit just before the war was not taken from the Consumer Finance Survey but from some other source. (2) The 1947 figure of 9,000,000 does not cover all units. It refers only to purchasers of certain selected durable goods on installment sale credit; that is, credit obtained from vendors. It does not include purchases of other types of goods on installment credit, nor does it include installment borrowings directly from banks or other cash-lending agencies. (3) The 9,000,000 figure also refers to spending units rather than family units. (4) The 9,000,000 figure relates to units which obtained credit during 1947, a group that may be different from the units which "used" it, depending on how "use" is defined.

On the basis of families rather than spending units, and making allowance for some duplication as a result of a family obtaining more than one form of installment credit, the 1947 figure might be close to sixteen or seventeen million families, but this would be in terms of families obtaining credit.

STATEMENT OF HON. WILLIAM J. MILLER, A REPRESENTATIVE IN CONGRESS
FROM THE FIRST DISTRICT OF CONNECTICUT

Mr. Chairman and members of the House Banking and Currency Committee, as a former member of this important committee I hesitate to ask you for time to present a few thoughts on the subject matter before you, namely anti-inflation legislation. It is only because I know how honestly you strive to get all possible information or suggestions that I impose on your time today.

Like every other Member of the Congress I am concerned about inflation and the resulting high cost of living. I have told my constituents that if the mere passing of a law would reduce prices or guarantee the building of rental housing for low-income groups, it would have been passed long ago. Each one of us would love to come up with a solution of these difficult economic problems. We don't, however, want to bring about a condition wherein the cure would be worse than the disease.

Deflation out of control is as bad if not worse than inflation. It wouldn't take many wrong steps to bring about a complete collapse of our whole domestic economy. The removal of one key support could bring about such a price recession that thousands of small businesses would be thrown into bankruptcy.

I have recently heard several people argue that the law of supply and demand will not work in time of war nor in the present postwar period. I believe the law of supply and demand is working but it is working to our disadvantage. Actually we have too great a demand and too small a quantity of many basic commodities. That added to the fact that we have too much currency in circulation has naturally brought about high prices. The Constitution places on the Congress the right to issue and regulate all of our currency. I believe we should at this time give serious consideration to ways and means of withdrawing from circulation a great deal of the money that was issued during the war period.

In spite of the tremendous increase in production of farm commodities we have not been able to get production enough to bring prices down. With domestic demands at an all time high plus the commitments we have made to ship foodstuffs abroad, we now face a situation where it seems to me we must impose some controls, controls that the American people would not accept during a normal peacetime period. I do not want to see the old OPA restored with its ration boards, ration books, and thousands of Federal employees running all over the country.

The President seems to think that he can do something helpful with limited price control. I for one am willing to give the President the power he asks for in his special message of July 27. If the fear expressed by those who are opposed to granting these powers to the President should materialize between now and next January and black markets reappear or the supply of foodstuffs should be reduced, we can deal with that situation next January or, if the situation justifies it, we can reconvene the Congress shortly after the November elections. The President's program could not do any irreparable damage between now and next January.

We all know that between 1933 and 1938 Congress passed many bills for the sole purpose of raising prices, particularly the price of farm commodities. The record indicates that prices reacted very slowly to the legislation passed during that period but over a period of years the legislation passed in the early years of the Roosevelt administration did bring about higher prices. Much of that legislation is still on our statute books and should now be repealed. As far as I personally am concerned I am willing to stay right here in Washington until the end of the year if there is any possible legislation that will lower the present high cost of living.

Some of our colleagues have expressed surprise that so many of the younger GI's have been alining themselves with either the Communist Party or the Wallace party. That does not surprise me. I am really surprised that more of them haven't swung to the left. Take the case of a young GI now 24 years of age. His first vivid recollection was the onset of the depression that started in 1929. Shortly thereafter his father lost his job. Months or possibly years of CWA, WPA, direct relief from his local government, private relief, etc., followed. By 1941 conditions looked brighter for him. He got a job. Then came the war and his life was further upset. He served anywhere from 1 to 5 years in the Army or Navy. He is finally discharged and comes home with high hopes and a greater appreciation of his own country. He wants to get married and start his own family but he can't find a rent at a price he can afford to pay. Is it any wonder that he may at times ask if this American system and our democratic form of government is all he had thought it would be? These young GI's now look to us to do something, anything that will make it possible for them to find decent housing, to earn enough so that they can pay for the necessities of life and save a little besides. These men are loyal citizens. They will be patient but many of them are naturally becoming very restless.

As for the balance of the President's program, I am definitely opposed to considering such legislation as the Federal aid for education bill, expanded social security, huge rivers and harbors projects, or the St. Lawrence seaway, all of which will cost hundreds of millions of dollars. Throughout the Eightieth Congress I have consistently voted against all new projects not of an emergency nature that would involve the expenditure of large sums of money. Much of the proposed legislation is meritorious and at a later date after we have reduced the inflation pressure should be considered by Congress.

Today, however, our No. 1 task is to check inflation and bring about an orderly reduction in the cost of living. We can't check inflation by adding fuel to the fires of inflation as recommended by President Truman.

In closing may I urge this committee when it reports out an anti-inflation bill to specifically call the attention of the country to the provisions of the anti-inflation bill passed by this Congress last November. I find very few of my constituents are familiar with section 6 of that bill.

You will recall that that section provided that whenever the President shall determine that there is or threatens to be a critical shortage of any raw material, commodity, or product which jeopardizes the health or safety of the people of the United States or its national security or welfare and there is no prospect that such critical shortage may soon be remedied by an increase in the available supply without additional governmental action, he may prepare proposed measures for conserving such raw material, commodity, or product which he shall submit to the Congress in the following form:

(1) A statement of the circumstances which, in the President's judgment, require the proposed conservation measures. (And I might add here that price control and allocations would certainly be considered conservation measures.)

(2) A detailed procedure for the administration of the proposed measures including the additional budget and additional personnel required for their enforcement.

(3) The proposed degree of curtailment in current and prospective use of each such raw material, commodity, or product, and

(4) A complete record of the factual evidence upon which his recommendations are based.

The section then provides that when the President sends that information to Congress the Joint Committee on the Economic Report shall within 15 days conduct public hearings thereon and shall make such recommendations to the Congress for legislative action as in its judgment the recommendations of the President and any additional information disclosed in the public hearings may require.

If at any time between January and June while the Eightieth Congress was in session the President had carried out the provisions of that section of our anti-inflation law, we would have been in a position to pass the necessary legislation. Even though the present emergency was urgent enough to justify the calling of a special session of Congress, the President evidently does not think that our critical shortages and resulting high prices justify his carrying out the provisions of the 1947 Anti-Inflation Act.

It is certainly unfortunate that we haven't been able to secure the cooperation of those in the executive branch of our Government at a time when we face these terrific and unusual economic problems.

IS SOCIALISM UN-AMERICAN?

(Testimony submitted to the House Banking and Currency Committee on the anti-inflation program, special session, 80th Cong., August 5, 1948, by Alden A. Potter)

When and if we must choose between fools and rascals in public office, assuming that we know the difference, we'd do well to choose the rascals. Even in politics a successful parasite never kills its host. For its own sake it rather stimulates and often protects a host which might otherwise succumb for lack of competence in its own protective devices.

Wise legislators must, therefore, expect to frame policies that are foolproof as well as rascalproof. They must guard against dupes, particularly in the current conflict with communism, rather than venal spies; that is the plain lesson of our postwar disillusionments. It is, then, drawing a red herring across the trail of Communist infiltration to criticize, as some writers of reactionary predilections are doing, the House Committee on Un-American Activities for uncovering innocent as well as venal "weak links" in the public service. These writers seem to think the committee should, to quote one of them, be "bringing into the open the full pattern," not of dangerous infiltration, but only of sheer disloyalty.

It is certainly not the business of Congress to prepare evidence for grand-jury indictments. Congress is employed to frame, not to enforce, laws. To tend this business is to uncover, not venality, but folly in our laws and their administration so that they may be changed by new legislation or revision of old. The really valuable lesson for Congress to glean from the Bentley and other similar cases of Communist "espionage," is that legislation directed against, and so congressional investigation of, disloyalty, is not what is needed. Communist affiliations are largely prompted by highly altruistic motives. This is what makes them so dangerously subversive; for when conscience and patriotism clash not everyone will say, "My country, right or wrong."

Indeed, where basic issues are concerned, a political loyalty which goes against moral convictions cannot be justified. That is why we can rightly sing the praises of refugees from tyranny and make it a national policy to afford a haven for political fugitives. That is why it is also vital for this or any other nation to seek out the beam in its own eye. In the present instance this means seeking the reasons for the belief in communism among so many of those leaders of fuzzy thought in America who were so aptly criticized by Herbert Hoover at Philadelphia. There seem to be powerful reasons for conscientious objection to a war with communism—reasons that are not just a matter of fear or of political conspiracy.

Those reasons are most unfortunately obscured by defining communism without any reference to socialism, as "a system by which one small group seeks to rule the world." The educational campaign of the Committee on Un-American Activities against the ideas which are creating such cases as that of Dr. May in Canada gets off on the wrong foot with such a definition, which is entered as the very first statement in the committee pamphlet on One Hundred Things You Should Know About Communism in the U. S. A. What is needed is to educate, not the uneducated, but the educators. While none of them have ever advocated "a system by which one small group seeks to rule the world," many a professor has advocated, and is now advocating, communism as defined in the dictionary: "A system of social organization in which goods are held in common—the opposite of the system of private property."

World rule by one small group is precisely not the Communist ideal, even though such rule be the objective of the political organization which is playing up altruistic ideals to justify such an expedient. Similarly the inflationary implications, pointed out by Governor Eccles in these hearings, of government by pressure groups, is the excuse for the police-state expedient of dictated prices. This suggests the paradox so often noted in this connection, of an interim of dictatorship to preserve freedom—of a socialistic transition period as requisite for the survival of free enterprise.

As for the communistic ideal, it is defended by a leading American moralist and churchman because it envisions, not rule by a small group, but no rule at all. It projects a withering away of the state as soon as freedom from want is at last attained and the common man can consume according to need and devote himself to spiritual rather than material welfare (if he chooses so to do). Forgetting the Christian injunction not to seek, first, material welfare, this pseudo-spiritual equation seems to put the material cart before the moral horse: Abundance equals low prices equals economic welfare equals political and moral freedom. For material welfare is begotten by freedom, not freedom by material welfare.

Communism is also unblushingly advocated, even to the point of saying that Christians must be materialists and proposing a U. S. S. R. of the world, by Prof. Joseph Needham, Director of the Science Section of UNESCO in the United Nations (serving under Julian Huxley). His name appears inside the cover of the current number of the American journal, *Philosophy of Science*, as one of the board of editorial advisers. Is it a mere coincidence that this issue carries an article by a professor (Lewis S. Feuer) of Vassar, Elizabeth Bentley's alma mater, which bases its anticapitalistic conclusions on the dogma that "the uncontested advantage of a Socialist economy is that it can travel at ordinary speeds" in "controlling the workings of the economy to assure the stable basis of life for all"? "The capitalist economy," he says, by contrast cannot serve such a universal well-being in the masses because of a basic "contradiction" or "dependence on the law: Innovate or decline. There is, of course, a third alternative: War * * * But unless the capitalist world proposes to lead men into an era of endless wars, it would do well to put aside militarist solutions to its economic problems."

How naively, by implying the impossibility of any other solution, the professor places the blame for all future war on capitalism. Capitalism, he opines pontifically, cannot boondoggle investment but must find useful (profitable) outlets for savings; failing which it must turn to war or else "decline" (into a "bust"). But socialism, it seems, can waste its substance ad lib and so avoid war as a way to rid the economy of the "surplus value" millstone that sinks the "capitalist world."

Not even capitalism, however, can now lead men into an era of endless wars; that "era" began long before employment at wages had even been thought of. The job of capitalism is to lead men out of this era of endless wars that began when what property there was belonged to quarreling communes (typically socialistic factions) who had never heard of profit as the reason for the failure of their society to attain freedom from want and so permanent peace. They had no one to tell them that they should assert their right to a chicken in every pot and two cars in every garage as the material basis for the life of liberty that was worth fighting for. So they just fought selfishly, without benefit of clergy or of Vassar.

The trouble is that these cases of perverted ideas are not isolated instances of an infiltration of "foreign ideologies" through disloyal conspiracies. As noted by Mr. Hoover these fuzzy notions are part and parcel of our own thinking. If it be true, that we do, indeed, find a "weak link" in the present Director of the Bureau of Standards, whose name appears alongside that of Professor Needham on the board of advisers for *Philosophy of Science*, where would we find a scientist of adequate technical training who would not also be a weak link? The magazine's board is a roster of our most distinguished, and equally muddled, scientists.

Indeed, a candid few are recognizing the muddle. Says Prof. Eli Ginsberg, Columbia economist, writing in *Science*, on his own field of Social Science and the Established Order: "The currently available body of theory, facts, and techniques is inadequate to cope satisfactorily with current problems. Only the new, the different, the unconventional, hold promise. Yet the system operates to place the greatest hurdles in the path of the emergence of the new. * * * The burden of the evidence is clear. For a variety of reasons the university environment exercises a most restrictive influence on the development of the social sciences."

If this be reminiscent of the Hoover critique of current academic thought, it is also highly pertinent to the observation of Governor Eccles, during these hearings, that the situation we face in dealing with the central fact of current social conditions, namely inflation, is "unprecedented" and cannot be dealt with traditionally. In the final analysis mathematical theory is the heart of man's monetary methods. And what is the status of mathematical theory? In the current (August) number of the *Scientific Monthly*, Professor Court, of Oklahoma, with a doctor's degree in physical and mathematical science from the University of Ghent, says:

"That unshakably solid rock of classical logic (has) simply slipped away from under the mathematical edifice, and the whole structure is now 'on the rocks.' As mathematicians put it, their science is at present passing through a 'crisis.' It has been in this state, roughly, since the beginning of the present century. What connection, if any, is there between this crisis and the social and political turmoil in the throes of which suffering mankind has been laboring during the same period of time?"

While, he says, "mathematics is not going to the dogs," still the theory of cardinal numbers is open to sweeping revision; and the cardinal way is the way numbers are used in the price system where they are added and subtracted and otherwise computed as if they were fully "commensurable"—as if every monetary unit were the same yesterday, today, and forever. A correct cardinal theory is certain to dispose, once and for all, of the "Paradox of a Metal Standard," to quote the title of Prof. Anatol Murad's book on this problem as related to money and prices. It will give conclusive support to Governor Eccles' indication of the illusions related to the idea that money can be a "standard of value" chosen from among commodities with the "market" expressing only a subjective ordering of values (ordinal numbers) without any fixed point of reference or unit such as the "gold standard" (correctly) contends for and attempts (unsuccessfully) to establish.

Without this essential revision of basic theory, we shall find that Barnum, not Lincoln, was right, and that gold-brick suckers are a norm. All the people—even the intelligentsia—can be fooled (self-deceived) all the time. We are hardly happy unless we are being duped. And this has become a human, not just an American, failing. Even the Russians, or Marxists, seeking to avoid the "opiate of the people" in some forms of "religion," have naively fallen for the very same folly in but a slightly different guise. By alining themselves with Utopian hopes of freedom from want for everyone everywhere, they are deceiving themselves with the same old notion of a Providence that is kind and only man—the other man—is vile in acting the part of a dog in the manger.

A brotherhood of man is not a peculiarly Christian ideal. What was new, and still is novel, in the Gospel of Christ, was the idea, not of altruism, but of truth as the basis of a civilized society where peace and good will are a result, not a cause, of understanding. The Christian gospel leads, not to reconciliation between good and evil, but to intolerance of evil and so to crucifixion. The torture of Golgotha was traceable, not to tortured morals and bigoted intolerance, but to false doctrines that cannot be tolerated. "They know not what they do." Moral transgressors are fools, not rascals. The "gospel truth" was and is a plea for intelligence and against preaching an altruism that no one can practice—a false doctrine that only paves the way to hypocrisy and the road to serfdom.

Christianity, in conflict with oriental mysticism, has actually paved the road to science; and science, once its handmaiden of mathematics is cleansed, must finally remove the personal equation (and incidental witch hunting) from social solutions. Material, hereditary, biological considerations are basic to life but not to the problem of developing methods for getting along together in an industrial civilization where strength of mind, rather than of body, begets survival through a process of competitively choosing values that will promote life—which gold will not do. A sweating brow, not a bending back, knows value and so rejects the Marxian (and Marx was a "gold bug") theory that value is produced by and equated to the cost of production in terms of labor ("labor-hour productivity").

Christianity—science—tells freedom that its security lies in truth, its peril in hypocrisy. It says that liberty's undoing is not the love of wealth, but the love of money—the failure to know enough to render unto Caesar that which is Caesar's (which is not wealth) and unto God that which is God's (which is not money).

FREEDOM IS MONETARY

In effect, what Governor Eccles said in answer to a committee question (from Mr. Multer) was that that government which governs least and best—which is not totalitarian and paternalistic—is that which can and does control its money supply effectively. That is obviously what our Government is not able to do, in part because of divided authority in the dual (State and Federal) banking system. The attempt to impose additional reserve requirements on State (non-member) banks by the Federal authorities, seems doubtful from the angle of enforcement. Section 10, article I, of the Constitution must have been intended to make the chartering of State banks to "emit bills of credit," prohibited to the States themselves, unconstitutional. But no way of enforcing this provision has as yet been attempted except the prohibitive tax on State bank notes imposed by Federal law during the "wildcat" period in banking following the Civil War.

This provision was written into the Constitution with the experience of "shin plasters" during earlier times in mind—essentially divided authority in issuing money competitively among the Colonies finally broke down a system that had worked very well in some Colonies, Maryland for example, on a paper basis for a long time. Since Federal control was validated over any form of issue, by the legal tender decisions, the prohibition of States, or for that matter any authority other than the Federal Government itself, to issue money of any kind under criminal penalty—and this must include the creation of clearing houses which afford monetary utility to bank credit expanded against "reserves"—must assuredly be constitutional.

What the existing monetary system is attempting to do is to make bankers serve two masters—their own legitimate profit in expanding credit through loans and investments, and the directly conflicting public interest (which is the proper business of Government and not of businessmen) which under present inflationary conditions requires contracting of the very same loans and investments. Banking must, by existing laws, throttle business enterprises, by methods which are also inherently discriminatory and certain to favor big business already established, for the sake of fulfilling what is a properly and exclusively Government function, namely restricting the money supply. Is it true that these functions cannot be separated and so kept out of conflict? Must we have a Government debt which, as Chairman Wolcott asks, must be supported by continuing inflation? Is human intelligence really incapable of resolving so elemental a problem?

There is, in fact, an almost inevitable movement emerging from this economic paradox into a separation of the business of money control from banking, that is, lending of money. We are moving, not toward the heretofore typical out-running of the system of partial reserves by bank loans and investments with resulting and literal bankruptcy leaving only cash with which to do business because of the Gargantuan public debt we are moving toward an accelerating cashing of the debt and an inflation in terms of cash which must lead to a monetary redistribution similar to that recently carried out in Germany and periodically employed in Russian monetary revisions for controlling inflation. A super-abundant cash can become so worthless than not even paper can be circulated. But before this happens and barter is all that is left to trade, no government can endure which does not cut money supply in order to restore its utility, by redistribution.

We hear talk of "supporting" the 2½-percent rate on long-term bonds. But the movement is accelerating out of long term into either no market for bonds or a short-term refinancing of the debt in the banks, with the rates higher so that banks can live on the interest and yet be compelled, by an enforced "secondary" reserve, to carry the public debt while doing business with the commercial world at spiraling rates of interest, with a separate reserve system, the whole being tied into foreign conditions by the illusory "support" of the gold reserve and the Bretton Woods Fund and Bank. That this is illusory is becoming progressively evident, for as Governor Eccles points out, the prewar, 1914 "gold standard" was really not gold but sterling and (contrary to the fleeting hope expressed by Under Secretary Clayton at the ITO conference held by the Chamber of Commerce in June) cannot be restored.

A POSITIVE PROGRAM

At a time when social justice is the basis for so widespread an appeal favoring communism, there is a healthfully corrective element in these hearings wherein official witnesses are so deeply engrossed with the trees in monetary affairs that they cannot see the forest, in Chairman Wolcott's concern for the justice of proposed arrangements, that is, in his protest that the procedure is widely discriminatory.

The essence of the task of framing a system of free competition is that the part played by government shall not be discriminatory. It must, accordingly, be noted that within the framework of a competitive system (and no other is humanly possible), no procedure that allows administrative discretion in the vital sphere of money can fail to be discriminatory in the final analysis. There must inevitably be some few "insiders" able to take advantage, if they will, of the very probity of those charged with such duties. The greater the integrity of the principals, the more valuable must be the position of the sycophants of such a regime.

This raises the question of devising some basis for formula control over monetary action, to remove discretion. With Government debt removed as Thomas Jefferson advocated (even to the extent of a constitutional amendment to prohibit all Government debt), this becomes simply a matter of holding banking strictly to the use of saved funds borrowed and loaned competitively (from savers to spenders), and relying, as suggested clearly by Lauehlin Currie in his Harvard monograph on "The Supply and Control of Money in the United States," on a budgetary gap for the control of money supply. This has been the basic concept of Keynesian fiscal ideas, but in them a vital factor is ignored; for the gap must, for the sake of competitive free enterprise in the private sector, be developed, not as suggested by Governor Eccles and Keynesians generally, by deficit spending in public works, leaf raking, etc., but by lowering taxes automatically (and reducing spending as far as possible) so that whatever the community can afford to spend under the conditions of available resources, is spent by private initiative and not by pyramiding public activities—including the "endless wars" suggested by Professor Feuer of Vaasar.

Once such a formula is in operation the so-called "timing" problem would be eliminated. The effect of changes up or down in price level would be imposed at once by the knowledge, on the part of the taxpayer, that he would have less—or normally more—to spend than his normal tax rate would leave him. The critical event would not be administrative decisions, nor yet the actual collection of the quarterly tax payment. It would be the movement of price levels as set forth by the statutory control formula. The more the Government spends, the heavier the tax burden as soon as the market, which must be left wholly free and unpegged by the Government, responds with high prices to the increased money supply and the diversion of productive into unproductive activity.

The vital fact is that public spending is inflationary only if it is not balanced by taxation; correlatively, taxation is not deflationary if the money is re-spent. The current system of tying the public budget into "compensatory fiscal policies" for the control of bank credit inflation implies the highly impractical and unethical proposition of preventing inflation by drawing on taxation for money to be loaned and invested by the private banking system. That taxes may not be currently collected, but can be politically postponed by debt, only saddles the community with a political choice of evils as between inflation and paying the "debt." Such procedure develops a complicated set of confusions in administrative "discretion" that not even the experts, let alone the voting public and its representatives in Congress, can understand or successfully operate. Only a system that every literate citizen can understand can promote business stability under free institutions. No such system is being suggested by anyone in public life.

What should be done now instead of Paul Porter's prescription of police state methods to control prices—symptoms—rather than money supply as the cause of inflation (coupled with the President's program of vain attempts to keep incomes of the needy abreast of inflation by pyramiding pensions, subsidies to housing, etc., in the guise of "loans") is to stop trying to pretend that the Government owes anything to the banks even while setting up special "reserves" by law which are nothing but a permit to draw a subsidy in the guise of "interest." Let the banks, now that they can and should, sink or swim in private business depending on savings only as a source of funds.

Let the Government finish the job, begun by the Federal Reserve Act, of taking over the clearing system completely and, by assuming the liabilities of the banks to demand depositors which were created by war debts, simply cancel out all Government bonds in bank portfolios against this assumption of their

obligations to depositors, requiring also other collateral (without taking over the income) to cover a later progressive liquidation of any difference between the demand obligations assumed and the bonds surrendered.

This procedure would freeze the sum total of demand deposits and stop further inflation at once without collapsing the whole money and price structure like a house of cards. The budget would be relieved of unwarranted interest payments and, because of the requirement of a continuing discharge of Government bonds to the extent of all demand deposits, would afford a continuing market for the bonds held outside the banks, thus securing insurance and similar funds from collapse. By direct compensation for the service rendered, the existing banking personnel and equipment could be kept in service—to the extent required by the clearing system for checking accounts—by Government payments covered, as in the postal service, by service charges (for checks and accounts instead of for stamps).

Such a simple formula system, with its automatic balance, can afford a pattern of competitive private enterprise which can maintain any pace required by circumstances, using innovations to their best economic advantage and not according to bureaucratic decisions paid for, as under socialism, by taxes instead of by profits (and losses). It insures optimum, not maximum, productivity over the long, not short, period, provided only that public control over the use of resources be developed by competitive arrangements tempered by wise conservation policies in a setting of private property so established that the operator will not be living from hand to mouth but will have an enduring personal stake in conserving his holdings.

PRESIDENTIAL POLITICS

The President now says "it is obvious that we cannot rely solely on more production to curb high prices"; but back in the days when he was talking about the dangers of a police state he was himself telling us that we might expect to overmatch the extent of war production by postwar expansion. This had been the rather Utopian implication of the report to the President (F. D. R.) by Vannevar Bush entitled "Science the Endless Frontier." Fulfillment of the New Deal promises of freedom from want for everyone everywhere was just around the corner of the development of atomic energy through compulsory licensing of patents, and was part and parcel of the plea that OPA needed only a temporary continuance while reconstruction got under way and supply was given a chance to catch up with demand. (Obviously, the terminus would be considerably postponed by the longer period required to catch up with money supply—"demand"—at lower prices.)

But this idea of supply filling demand and stopping prices has not been merely a fond hope of the OPAians. It has been dignified also by statistical analyses of money supply and price movements allegedly showing that we need only prevent further expansion of credit to assure a check on inflation since the rise in prices has now, with the help of full employment of men and resources in unprecedented productivity, caught up with the money supply. This conclusion has been developed by the statistical device of "smoothing out" the variations in the graphs showing the relation between money supply and price. It is thus discovered that over many years there has been an apparent trend toward using more money for a given price and trade level.

Admittedly, however, the rate of using money is slower in depression than in boom; and this is the heart of the problem which we now face with a money supply already so large that, with a speeding up of turn-over in the vicious circle of rising prices, it could become the basis of inflation even aside from further credit inflation in either the public or private sector of deficit financing through the commercial banks. The price level has "caught up" only on the assumption that the public will not develop a fear of holding money and start spending it faster, and then get to cashing their savings bonds. These bonds are not involved in bank reserves, but they hang like a sword of Damocles over the money supply since they are cashable on demand.

FARM VERSUS CITY

There can be some hope of clearer thinking once we have abandoned the idea, as President Truman has now done, that more and more production is the answer to inflation. That idea simply reverses the little-pig-killing fallacy which alleged that less and less production was the answer to deflation and depression. The prospect of bounteous crops this year bears no threat of depression, primarily

because of the influence of the public debt. This would be true even though we had no laws underwriting a so-called parity floor for prices on farm crops. Farm prices benefit automatically from inflation. True, they may be hard to sustain temporarily in the face of an oversupply induced, supposedly, by Government guaranties. But such a result will spell trouble for only a limited sector and for a limited time; if they sag a bit prices will rebound to produce the typical effect of inflation in providing the farmer with enough money income to care for what he needs to buy without selling all he can produce.

The economy as a whole cannot compete with itself and "price itself out of the market" to the point of raising prices beyond what anyone will buy. In food supplies, as a whole, no buyers' strike is possible. In inflation the urban trader always gets too little, not too much, and so fails to bring the rural trader into the market often enough to clear his production. Prices in the farm sector do not therefore collapse, for there is no pressure to sell as there is on the urban side. The spur to produce and sell is shifted from country to city by inflation. Back in the thirties farmers were struggling in vain to produce and sell more to get enough money to cover debt payments and necessary purchases. But now the pressure for a rising cost of living in the city will increase regardless of any so-called controls over prices, or even because of them should they be instituted, since they can only add fuel to the fire of excessive money supply by removing the already lessened incentive to produce and sell food supplies.

To put a ceiling over farm prices would have an effect which the floor already provided cannot offset. This is because the temporary stimulus to production has been far less due to the presence of a floor than to the absence of a ceiling on prices under the fleeting circumstance that there was a postwar backlog of needs to be filled by farm purchases of industrial products. This demand will not endure indefinitely. With farm mortgages largely paid off so that they no longer serve to force farm deliveries, shortage of food supplies under price ceilings must impel the urban majority to seek some other politically coercive measures to bring about more ample supplies.

It was this kind of a situation which led, in Russia, to the liquidation of the kulaks—their starvation and seizure of their lands. This was an evil and not too effective effort to remedy the conditions induced by the attempt of the urban proletariat to issue money (or credit, if you please), into their state-owned industries without incurring the result of having the rural population refuse to accept the money in trade. Obviously, a system which prevents the use of money for buying property and does not offer industrial products on an adequate scale, would not make money very useful to rural people.

Slavery and starvation are implicit in such a state of monetary impotence with its implication of a bitter class struggle engendering emotions likely to incite national and racial conflicts. Under these conditions of world-wide uncontrolled inflation and lack of competent monetary institutions, those who are agitating for a step into world government through an internationally organized police power are promoting, not world peace through law and order under free institutions, but only world tyranny.

NEW DEAL EVASION OF MONETARY PROBLEM

It needs to be observed that the inadequacy and incompetence of the President's program can be traced to deliberate evasion of the monetary problems of modern society during the whole period of Democratic control. This characteristically socialistic attitude toward money appeared in everything the New Deal administration did from the day in 1933 when President Roosevelt said, in his inaugural address, that the money changers were unscrupulous in proposing only the lending of more money. How scrupulously those unscrupulous proposals were followed by their Presidential critic is a matter of record; witness the deliberately un-Jeffersonian erection of public debt as an antideflation measure.

It required an expansion of that scheme into a huge war debt to make it work in the only way it ever could have worked, that is, by oversaturating the economy with money. A deadly lag in recovery, never fully accomplished, was inevitable because all the money added to the income stream entered by way of nonproductive Government spending, and had to be continually reappropriated. It was called, at first, pump priming; but when it failed to prime the private pump, capital was said to be "on strike." The continued emergency began to call for "public investments" and we heard references to "that old laissez faire notion" implying that private enterprise was passé.

The simple truth is that the same additions to money supply, had they been left in the taxpayers' hands and so spent in the private sector, would have been

respond automatically, doubtless with unduly inflationary results under the existing system of bank credit expansion and the gold-purchase policy. It does make a lot of difference how, as well as whether and when, money goes into circulation. The mere quantity of money, though it can by no means be ignored, is not conclusive (unless it be averaged over a long period of time) as a determinant of price levels. This is not to say that quantitative controls could not, by a formula method of management, be made to serve as a sufficiently competent determinant of open-market agricultural prices in a moving annual average which would ignore any purely seasonal influence of supply on prices. It is to say that the practice of expanding and contracting the supply of money through bank loans and investments cannot be put under any effective control without producing the perilous swing from boom into bust which is falsely attributed by our "liberals" to the capitalistic system of private property and free, competitive enterprise.

This "liberal" delusion, be it reiterated, can be traced to a studied indifference to the monetary factor in price problems. There was the statement of Leon Henderson in initiating the TNEC studies at the opening hearing in 1938, that the money question would be severely ignored. A column of criticism printed in the New York Times failed to change his mind or that of Chairman O'Mahoney. Nor did the wartime inflation of money supply change the "liberal" minds which enacted and set out to administer the Employment Act of 1946, through the nonmonetary wisdom of such a statement as that of Chairman Nourse of the Council of Economic Advisors who said in a New York speech just as he took office:

"During the process of legislative consideration and redrafting, the Congress definitely turned its back upon any single type of remedy and specifically upon money magic as a means of getting out of the artificial conditions of wartime business on to a sustained basis of efficient and prosperous peacetime operation."

MONEY IS A WORLD PROBLEM

Well, the Congress that turned its back on "money magic" was turned out in its turn by ballot and was a lame-duck organization even as Dr. Nourse spoke. The reign of Senator Wagner over the Banking and Currency Committee, during which he spent his time on "liberal" labor magic, was ended. We now have Congressman Buffett and Senator Tobey developing the proposals for a new Monetary Commission offered by the son of Senator Aldrich who developed the Commission from whose work the Federal Reserve Act, now clearly obsolete, resulted. If that law was, as charged by its critics, a sell-out of reform to privilege, that was only because of its resemblance to monetary "reform" in general in failing to provide for any real control of inflation and deflation. No current proposals indicate any better results. So the one thing which should have been pressed for enactment by the special session was not even suggested by the President, namely, the setting up of a commission for immediate and intensive study of a social problem which has far outrun the material gains of a period of rapid technological development. Let such a commission seek out, not great minds, but new ideas, to resolve this quandary of modern life.

Granting that the problem of stabilization, even in peace, is clementarily monetary, and that peace depends upon economic stability, it is nonetheless true that the problem of monetary inflation is not susceptible of solution while war and an ERP are playing against a budgetary balance. With the public debt already in jeopardy, the calling of a special session to agitate the question was, at best, ill-advised in view of the extreme confusion of thought for which no one, least of all the "liberal" coterie, or a Congress harried and overworked even when not facing an election, is able to offer any solution.

No reasonable solution for inflation can be entirely domestic in action, as seems to be assumed by the President's program of legislation. Our "bipartisan," foreign and our domestic policies are in dire conflict, if the London Economist is to be believed in its opinion that "it seems overwhelmingly probable that the dollar shortage will last for a generation to come." That "shortage" now rests, as it did not while sterling was the world's currency, on a continual American source of European subsidies such as have kept England's record in price "control" so much better than our own. Following the other war and during the New Deal our "loan" and gold purchase policies were not, formally at least, doing more than maintain the sterling area intact. But today the dollar is the world's currency and its foreign exchange value depends upon what it will bring abroad—which is almost entirely what "Uncle Sap" is giving away. At any time that policy is stopped, say to save us from a wild domestic inflation, a large sum of

dollars now hoarded and in use abroad are likely to return and require a better system of sterilization to avoid inflation than is available today. Without sterling to take their place, however, a heavy demand for gold abroad could, if our sale of gold at \$35 is continued, eat away our 20,000-ton "reserve" and precipitate, by the enacted provision requiring a limitation of reserves on a 40-percent-gold basis, the kind of deflation which was precipitated by the "gold standard" requirement in 1921.

If we hope ever to terminate our European subsidies, we shall have to abandon the "international gold standard" and the "supporting" Bretton Woods agreements completely. As so cogently indicated by the London Economist, the dollar cannot be maintained as a world currency without constant maintenance of the Marshall plan contributions to keep it in circulation. The real problem before human society is the establishment of a world currency sustained by world government—which is impossible as long as the current "central banking" processes are not abandoned for purely governmental control of money supply.

STATEMENT ON INFLATION TO HOUSE COMMITTEE ON BANKING AND CURRENCY
BY PEOPLE'S LOBBY, INC., WASHINGTON, D. C., BENJAMIN C. MARSH,
SECRETARY

Since most of party platforms are repromises of past promises, direct or implied, this Congress need not feel it a moral obligation to put off till the next Congress, what this Congress should have done, before this year's conventions.

The President's anti-inflation program is a step in the right direction, but not enough.

The rearmament program, and to a much lesser extent the European reconstruction program, will so expand the demand for most heavy goods and many consumer goods as to pour kerosene on inflation flames.

The full effects will not appear till next year, but must be anticipated by action now.

The theory that high prices are necessary to pay off the national debt doesn't hold, unless excess-profits taxes are restored.

July's Economic Indicators, issued by the Joint Committee on the Economic Report, shows that corporate dividend payments in 1939 were \$3,800,000,000, and in the first quarter of this year at the annual rate of \$7,500,000,000; while undistributed profits were in 1939 only \$1,200,000,000 and in the first quarter of this year at the rate of \$12,200,000,000—or over 10 times as much.

Even if most of this \$12,200,000,000 of undistributed profits were taken in taxation, it would mean consumers, not stockholders, paid the taxes in higher prices.

America has reached the safe limit of trying to raise the dollar income of people to meet the extortions of profiteering, though a minimum wage of at least 65 cents an hour is necessary.

The immediate job of Congress is to end the causes of inflation, starting with speculation in land and in other natural resources, and stop tinkering with the inevitable results of known causes.

Inflation has already imposed a capital levy of about 40 percent since 1939, in reducing the rapidly diminishing savings of people with small incomes and small savings.

Progression is an essential feature of fair taxation as attested in our income and estate taxes, but the capital levy of inflation is regressive, instead of progressive.

There is a patent irony in our insistence that European nations included in that recovery program, should cooperate and utilize their own resources, as well as our help, to raise the standard of living of all the peoples involved, while we permit the lowest paid people in America—millions of whom cannot increase their dollar income; to be exploited in a planless brutal orgy of profiteering.

A Congress which can't or won't stop inflation is not worthy of reelection.

In addition to the President's antiinflation program we urge that this Congress:

1. Levy a tax of 1 percent upon the value of all land exclusive of improvements therein, and thereon, with a small exemption to exclude little home and farm owners.

2. Reestablish price fixing and rationing for all essential goods, at once, and create a Government Marketing Corporation empowered to buy farm products and sell them here, utilizing farmers' and consumers' cooperatives, to prevent black markets.

A current Gallup poll reports that excluding farmers, the national median cost of food and milk per family is today \$25 per week compared with \$11 in August 1942.

Many families are eating better, but not that much better.

These measures, with those the President recommends, will tide the Nation till next year.

The next Congress will have to face the fact that we cannot meet the world situation, and play our part in it—without public ownership of all natural resources, natural monopolies and basic industries, to be operated by technicians and production engineers, under an over-all plan for America.

The billions of dollars spent in advertising by press, radio, and television give the lie to the claim our present economic system can provide either plenty or security.

They can be attained only by an economic system directed to those ends, not to scarcity, profits, and world domination.

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