

## *Chapter Seven*

### **WAR**

THE events of the war years were so convulsively abnormal that to narrate them in detail would be to overload and distort the story which this book aims to tell. I propose therefore to run through them very rapidly, leaving to the reader's imagination (or memory) the crowded excitements of the period, and concentrating rather on the effects of the war adventure upon the American economy, and particularly upon the processes of economic growth and concentration. These effects were prodigious. When the war and the brief boom and depression which succeeded it were at last over and the country had returned to what President Harding liked to call "normalcy," the scene was very different from what it had been in July, 1914. This chapter will attempt to suggest briefly how some of the major alterations came about.

One warning must be given at once. Drastic as were the effects of the war upon America from the moment when the armies first mobilized in Europe, the reader must not be deceived into supposing that the reform movement petered out at once. It did nothing of the sort.

In so far as it depended upon Theodore Roosevelt and the Progressive Party, to be sure, it did. The election of 1912 had virtually killed the Progressive Party. Woodrow Wilson proceeded to steal their best thunder, and by 1914 Roosevelt gloomily confessed to a friend that in making speeches for the Bull Moose cause he knew he was carrying a dead horse on his shoulders. Roosevelt himself tried to be contented with the inactive life of a man of letters, rushed off in despair to explore the sources of a South American river, returned in shaken health to further dismal inactivity—and then found the joy of battle once more in a cause quite different from that of social justice: the cause of "Americanism" and of preparedness for American participation in the war. The fierce campaign upon which he now entered satisfied his ego by giving him an opportunity to lead an attack upon the administration in power; it suited his temperament by pitting him against Wilson, whose cool caution was hateful to his headlong and belligerent spirit;

it engaged his nationalistic zeal, his boyish enthusiasm for the manly arts of war, his moral ardor; but it did not engage the economic reformer in him. In fact, as a friend of the Allies and an apostle of the Plattsburg movement he found ranged beside him most of the men whom he had once decried as malefactors of great wealth. By 1916 Roosevelt was quite at home in Wall Street. The past was forgotten; these fellows were “good Americans.”

Yet the reform movement went on without him. The Wilson Administration not only pushed through the Clayton Act and the Federal Trade Commission Act but went bravely ahead to enforce them, busily hacking away, year after year, at monopolistic practices and unscrupulous trade methods. It wrote on the statute books the LaFollette Seamen’s Act to improve labor conditions for American sailors; in the Adamson Act it decreed an eight-hour day for railroad employees; after the United States had entered the war it threw its influence behind the principle of collective bargaining and behind liberal labor policies for plants making war materials; and it gave Gompers a place among the advisers of the Council of National Defense. Men like Newton Baker and Brand Whitlock and George Creel, who had been enemies of the political power of big business, now sat in the seats of power. What happened was not that the reformers lost heart or position or that the Wilson Administration lost its liberal complexion, but rather that the war dwarfed every other enterprise, submerged every other issue, distorted the organization of American life, colored every emotion; and that when the war was at last over and the demobilization of men and of enthusiasm had been effected, the national spiritual exhaustion was such that the wish to regulate and control business and finance was thoroughly played out.

## 2

When the armies began to march in Europe at the end of July, 1914, the first effect upon the American economy was a stroke of almost complete financial paralysis. The New York Stock Exchange was closed at once, to remain closed for months; if it had not been, the rush of European investors to convert their American securities into money against the unpredictable emergencies of war financing would have knocked prices down to the bottom, undermined bank loans, and imperiled the whole financial structure.

Frightened hoarding began at once, and a panic worse than that of 1907 might easily have followed if there had not been invoked a half-forgotten monetary measure (passed in 1908 as a result of the lessons of 1907 and known as the Aldrich-Vreeland Act) which permitted banks, in such an emergency, to issue notes based upon non-government securities and commercial paper as well as upon government bonds. The very real danger to American credit was averted only by the bold action of a group of New York bankers, headed by the Morgan forces, in forming a gold pool to meet the requisitions of the outside world. Not for a long time did the disorganized processes of finance come back to anything like a normal equilibrium; for example, not until the first of April, 1915, a full eight months after the invasion of Belgium by the Germans, was it considered safe to open the New York Stock Exchange to unrestricted trading.

The second effect was a partial paralysis of business. Nobody knew how widely the war might spread or what forms it might take, whether exports would reach their destination safely, whether European buyers would be able to pay their bills; foreign trade was violently disrupted, the prices of wheat and cotton and other commodities dropped, citizens were implored to “buy a bale of cotton” to save the South from disaster, business as a whole shrank rapidly, and unemployment spread. The winter of 1914–15 was a very lean winter for America—even for those parts of it in which the war still seemed to most people a remote unreality. There is no more instructive example of the difficulty of business forecasting than the fact that for almost a year after the war broke out, few Americans had any notion of the vast prosperity which it would shortly bring to their country.

When the recovery came, however, toward the middle of 1915, it was sweeping. The largest cause of it, of course, was the discovery of the Allies, and particularly of the British, that they could not hope to win without buying war materials and supplies abroad in quantity. But there were other causes. The world was calling for food and for other products of which the belligerent nations could no longer produce enough to meet the demand. Neutral markets, once dominated by the British or the Germans, were now open to American invasion. The British fleet had virtually cleared the seas of German warships; commerce with the Allies could now be undertaken without much risk. By the autumn of 1915 American factories were roaring, American farmers were closing a profitable season, the tonic effects of

prosperity were stimulating business from coast to coast, and in Wall Street there was already a frenzy of speculation in the “war stocks”; the front pages of the newspapers told the happy story of the broker who in 1914 had staked his all on fifty shares of Electric Boat and was now worth half a million, and of another happy creature who had bought 1,000 shares of Bethlehem Steel at 18 for his baby and now estimated that the baby was worth \$364,000; and the sober *Commercial and Financial Chronicle* felt it necessary to remind its readers that the boom in war stocks was not “based on an enduring condition.”

The expansion of currency and of credit which the war boom invited was greatly facilitated by the Federal Reserve System, now at last in full operation. The creation of this system had come about through a curious combination of forces.

The panic of 1907 had spectacularly displayed the weakness of what was known by courtesy as the American banking system: a collection of national banks (independent of one another except as they were locally organized into clearing-house groups) superimposed upon forty-eight collections of state banks. Not only were the standards of safety imposed by law varied and inadequate (and destined long to remain so) but the individual banks were so independent of one another that there was no way of mobilizing their scattered reserves to meet emergencies in one part of the country or another. Each bank had to sink or swim by itself, aided only by such relief measures as a local clearing house could contrive or as some local leader could impose upon the local banks (as Morgan had done in New York in 1907). The first great need was thus for a practicable device for shifting a part of the scattered reserves here and there in accordance with changing conditions. The second great need was for a more flexible currency: there was no way of providing for a suitable yet controlled expansion of it in times of expanding requirements. The AldrichVreeland Act of 1908, though it was to prove very useful when the war storm broke in 1914, was frankly a measure for panic use only—a stopgap measure to serve until a more elastic system of currency could be devised.

For years after 1907, Senator Aldrich of Rhode Island and various astute bankers such as Paul M. Warburg, impressed by this double need, had been working on plans for a central banking system which could mobilize and hold ready for use a part of the reserves of the individual banks and could also

issue notes based on commercial paper (and thus provide a currency sensitive to the volume of going business). They had labored to convince the slow-moving bankers of the country that such an institution was necessary, and had made some headway. Senator Aldrich finally went so far as to introduce a bill in the Senate in 1912.

The character of the Aldrich Bill, however, may be suggested by the fact that it was written at a secret conclave held at the Jekyll Island Club on the Georgia coast—a favorite playtime haunt of the New York bankers—by a small group of men which included, along with Aldrich and Warburg, two representatives of the dominant financial powers: Harry Davison of the House of Morgan and Frank A. Vanderlip of the National City Bank. Genuine as the wish of these men undoubtedly was to provide a superbank which would truly serve the national need, and adroitly as their proposal was adapted to meeting the shortcomings of the national currency, one could hardly expect that any plan which they drew up would seriously disturb their influence. The plan evolved at Jekyll Island called for a central reserve bank with a board of directors in which the private bankers of the country would have an obvious majority.

At a time when the air was full of talk of a “money trust” such a scheme was obviously impossible. It would be opposed not merely by the adamant conservatism of the average private banker, who distrusted any device which would hamper his individual freedom of action, but also by the fear among Westerners and Southerners and men from the smaller cities generally that a central bank would turn out to be a bank under the control of the powers in Wall Street, and still more potently by the insistence of the reformers upon curbing the financial oligarchy. But when the Wilson Administration came into power in 1913 it made a surprising and very canny move. It took over the Aldrich-Warburg idea and altered it to make it a part of the reform program. The bill which Carter Glass sponsored in Congress and which Woodrow Wilson backed with his commanding influence provided indeed for a superbanking system, but a decentralized one (to meet the jealousy and suspicion of the small cities) which while operated by men chosen by the private bankers (to placate the banking community) would be supervised and regulated by a government board (to prevent Wall Street control). The bill, that is to say, provided for twelve separate regional reserve banks, the directors of which would be chosen by the bankers of these various regions;

but also for a supervisory Federal Reserve Board consisting of the Secretary of the Treasury, the Comptroller of the Currency, and five other men to be appointed by the President.

This masterly compromise won the day. Despite much shaking of heads among the diehards of the financial world, the bill was passed at the end of 1913. The Federal Reserve System was ready to begin operations in November, 1914, only a few months after the outbreak of the war. By the time the war boom gathered headway, late in 1915, the value of the System was already apparent. It did not especially curb the power of Wall Street, but on the other hand it did not accentuate this power. It made such banks as flocked to join it safer, providing indeed as much safety as could be expected in view of the fact that membership was not compulsory and that the legal standards for commercial banking remained varied and lax. And it provided ample currency and credit to meet the growing needs of a nation which had suddenly found itself doing a roaring business.

### 3

When old Pierpont Morgan died, men had wondered whether the supremacy of the banking house which he had built would come to an end. If character were the secret of financial influence, as the old man had argued at the Pujo inquiry, perhaps the great days of the Morgan house were over; for J. P. Morgan the younger, who now at the age of forty-five became the senior partner, had given no evidence of any such colossal personal force as his father had radiated. He was an attractive young man, by reputation solid and reliable; he inherited his father's patrician spirit and tastes, his father's scorn of the common herd, and his father's blinding temper; but his capacity for personal leadership had not been tested. He was surrounded by exceptionally able partners; Harry Davison in particular, a protégé of George F. Baker's who had had a leading part in the organization of the Bankers Trust Company, was looked to as a rising power in the Street. But the question of the future influence of the firm remained open, and all the more so because the Clayton Act soon forced the members to resign as directors of the commercial banks on whose boards they sat, and in deference to public opinion they resigned also from thirty of the directorships which they held in business concerns. These resignations had but a slight effect upon their

influence, for as already noted in the previous chapter of this book the number of directorships which a firm held was by no means a measure of its power; nevertheless the move added to the uncertainty with which the future of the House was surrounded. This uncertainty was not completely dispelled for two years.

The war boom of 1915 and 1916 dispelled it, however, and conclusively.

The House of Morgan had always been closely tied to England. Morgan the Elder had received his early training in his father's American banking house in London. He had spent much time at his splendid house in Prince's Gate. He had been accepted by the leading financiers of England as a kindred if somewhat overmastering spirit. Morgan the Younger was likewise sympathetic with the English. The House had a branch in Paris, too, and a long record of close association with French as well as British bankers. These facts, together with the enthusiasm of the partners for the Allied cause—"Our firm had never for one moment been neutral," wrote Lamont later; "we didn't know how to be"—and with the supreme position which the firm occupied in American finance, bore rich fruit in 1915.

As a result of the diplomatic suggestions of the ever-alert Davison, who spent weeks in conference with British officials in London, the British government made J. P. Morgan & Co. its purchasing agent in the United States. The French government also decided to coordinate its American purchases through the Morgan office. And both governments made the House of Morgan their fiscal agent in the United States, entrusting them at the outset with the staggering task of selling to American investors a half-billion issue of Anglo-French bonds, the largest issue of securities ever floated in the country.

The position which the firm came to occupy in the American economy as a result of its successful exercise of the double function of purchasing agent and money-raising agent was as extraordinary as it was unprecedented. The Allied purchases of munitions and war materials of all sorts were growing and soon became enormous: they were the chief stimulant of the new prosperity of 1915 and 1916. The only way in which trade between the United States on the one hand and England and France on the other hand could be balanced while such vast exports were going on was by a combination of three simultaneous processes: first, the importation into America of over a billion dollars' worth of gold; second, the gradual sale to

American investors, through the stock exchanges, of foreign-owned American securities to the extent of a billion and a half dollars (the selling of which, incidentally, was also entrusted to the Morgan firm); and third, the borrowing by England and France of over a billion dollars more. I say borrowing—but the money was all spent in the United States. It was taken in from American investors under the name of the Allied governments, and it was handed out to American manufacturers, also under the name of the Allied governments, in payment for munitions and supplies. And both the taking in and the handing out were managed by the House of Morgan!

To be more specific: J. P. Morgan & Co. organized the syndicates which borrowed the money for the Allies—huge syndicates, the first one of which, to distribute the Anglo-French bond issue of 1915, consisted of several hundred banks and investment houses, sixty of them in New York alone. And through a special department headed by Edward R. Stettinius (who soon became a Morgan partner) the firm also apportioned the British and French orders among steel mills and powder plants and tool works and the numerous other plants all over the country which darkened the sky with their smoke as they fed the slaughter in Europe. No such direct economic power had ever been exercised by a single group of men in all American history.

As to the effect of all this activity upon the neutral position of the United States, it might be mentioned here that on August 15, 1914, when the war was hardly a fortnight old, Secretary Bryan had written to the House of Morgan: “In the judgment of this Government, loans by American bankers to any foreign nation which is at war are inconsistent with the true spirit of neutrality”; but that this virtual prohibition was later permitted to lapse. The stimulating effect of war orders upon American business and the quickly rising sympathy of Americans—especially in the East—for the Allied cause, were too strong to permit it to stand. There is little question that the extent to which American economic fortunes were staked upon an Allied victory proved a strong factor in aligning the United States with the Allies.

As to the manner in which the men at the corner of Broad and Wall Streets exercised their power, Lamont’s figures in his life of Davison are illuminating: “The final record as to the British contracts showed that, of the hundreds of different concerns dealt with, there were only eleven in which the Morgan partners held any interest; and the largest interest they held in any one of those eleven did not exceed three per cent of the shares. In the case of



the French, the percentage was even more trifling.” The British government, hearing rumors of favoritism in the letting of the contracts, sent over an investigator but could find no basis for criticism. The firm made a practice of notifying the British or French government, in advance, of their precise interest in any firm to which they considered giving an order. Some of the profits made by munition-makers were immense—but the House of Morgan believed in profits.

The prestige of the firm rose to new heights. Morgan the Senior was gone, but the institution that he had set up was now mightier than ever.

#### 4

The twenty months or so between the beginning of the war boom in 1915 and the entry of America into the war in early 1917 were a time of furious activity—business booming, credit expanding; prices rising, wage increases being granted—or, if not granted, being demanded and struck for by workmen; profits leaping; the farmers enjoying the best times they had ever known; the stock market making fortunes in Wall Street. It was also a time of furious emotions. From the day that the *Lusitania* was sunk till the day that Wilson read his war message to Congress—all through the long months when the celebrated Wilson correspondence with Germany was indeterminately proceeding, and Roosevelt and the patriots of the National Security League and the Plattsburgers were shouting for preparedness, and Hughes was running against Wilson for the Presidency—the one great question which hung over the country was “Will America go to war?” and the answers given to it were hot with passion. As the months went by, gradually the war thrust other issues and other interests into the background; and when, on the last day of January, 1917, Germany announced her intention to engage in unrestricted submarine warfare, it became clear that America herself was to be sucked into the maelstrom and that the concentration of the country upon war-making activities was to become furious and transforming.

What happened during the succeeding twenty-one months need not be detailed here: the decision of an anxious and depressed Wilson to call for a declaration of war and for a policy of conscription; the raising of an army of over three and a half million men, two million of whom were sent to Europe; the lethal campaign of 1918, in which American troops fought in the blood

and filth and anguish of the trenches and aided the French and British to turn back the German tide; the tumult and shouting at home, the tramp of soldiers' feet on American pavements, the flags hung along the streets, the Hoover food-saving campaign, the frenzy of Liberty Loan campaigns and Red Cross campaigns and United War Work campaigns, the converging upon Washington of the dollar-a-year men; the fury and rapture of the war spirit, the unworldly idealism of the Wilson war messages; the long, long casualty lists, with all that they meant to broken families; and at last, the wild rejoicing of the first Armistice Day. For the purposes of this narrative, all that concerns us is the effect of this strange interlude upon the American economy. It was an effect multifold and significant.

In the first place, industrial production was still further expanded. It had to be expanded because Washington was calling insistently not only for men but for guns, shells, uniforms, cantonments, airplanes, trucks, rolling stock, ships, and other supplies in endless variety, to be delivered in quantity and at the earliest conceivable moment. This huge demand was superimposed upon a continuing demand for munitions and supplies for the Allies. In view of the shortage of men and of raw materials and transportation facilities, this inevitably meant cutting down on the production of things not needed for the winning of the war. It meant converting plants from peace-time uses to those of the emergency. In view of the utter derangement of supply and demand (for demand was imperative and almost unlimited), it meant regulating prices. Hence the creation of the War Industries Board, with its almost dictatorial power to decide to what uses the industrial machinery of the country might be applied; hence the Railroad Administration, which took over the roads and operated them as one huge system, giving priority to troops and to necessary supplies; hence the Food Administration and the Fuel Administration and other sources of inevitable interference with rugged American individualism.

During those twenty-one months the center of economic control moved definitely from New York to Washington. Wall Street became almost an outlying province. The House of Morgan was busy with many things, among them the difficult stabilization of British exchange; but it was shorn of its previous power. Morgan himself was not called upon by the Administration for any war service. Stettinius became an Assistant Secretary of War. Vanderlip of the National City Bank managed a war-savings campaign for the Treasury Department. Other bankers were drawn into the huge Liberty

Loan organization. In every bank and corporation office there were now vacant places as men went off to the training camps, to France, to dollar-a-year service in Washington. In the drama of economic concentration through financial control, these months were an intermission, strange and exciting.

Wealth was not conscripted though life was, and in some cases wealth made a good thing out of the disaster. Despite the contempt with which the country regarded “profiteering” and despite the efforts of the government to set prices at fair levels, it must be admitted that the vast volume of war orders, the increasing efficiency of production, and the fallibility of governmental officials combined to permit some very high profits. The biggest concerns which made war materials did not, on the average, fare quite as richly as during the boom of 1915 and 1916 when they had been making munitions at the behest of the House of Morgan, but this was partly because of drastic charges for depreciation and heavy excess-profits taxes—and it must be recalled that 1915 and 1916 had been altogether extraordinary years for such concerns. All things considered, they fared very well even after the United States went into the war.

For example: the net income of the duPont powder concern (after amortization but before interest on bonds) had been only a little over 5½ millions in the dire year 1914. In 1915 it had jumped to 57 millions, in 1916 to 82 millions. In 1917 and 1918, when the United States itself was calling for duPont explosives, it dropped back—but only to 49 and 43 millions respectively. Bethlehem Steel was another great munition-maker. Its earnings (after depreciation and fixed charges) had been a little over 5½ millions in 1914, had risen in 1915 to 17 millions and in 1916 to 43 millions, and fell back in 1917 and 1918 only to 27 millions and 15 millions respectively.

As for the United States Steel Corporation, its changing fortunes may be expressed in earnings per share on the common stock. In 1913 these earnings had been \$11.02. In the bad year, 1914, they had dropped below zero (the corporation not quite earning its preferred dividend). In 1915 they had recovered to \$9.96. In 1916 they had gone up to the remarkable figure of \$48.46. In 1917 the decline was only to \$39.15; and in 1918, to \$22.09. An average war-time profit of somewhere in the neighborhood of thirty dollars a share on Steel Corporation common stock! (To see such a figure in its full perspective one must recall the origin of those common shares, as recounted in the first chapter of this book.)

It might be added that accountants reporting to the Director General of Railroads subsequently gave—rightly or wrongly—much larger figures for the Steel Corporation. Adding to the net earnings, as reported by the company, various items which, they claimed, were “improperly deducted in the corporation’s statements: Interest on bonds, etc., of subsidiary companies; inventory profits, intercompany; sinking funds on subsidiary bonds; and excess depreciation,” they arrived at “adjusted earnings” totaling over eleven hundred million dollars in two years (1917 and 1918). Amateur statisticians may be interested to figure how this two-year total would compare with the total pay of all the soldiers in the A.E.F.

Large profits permitted the payment of very large dividends. Let us glance for a moment at the record of these same three companies, all of them big makers of munitions or war supplies. Bethlehem Steel paid \$22.50 per share in 1917 and also declared a 200 per cent stock dividend; in addition, it offered its shareholders an opportunity to subscribe for further new stock at par; in 1918 the company handed out \$10 a share on both the old and the new stock, thus giving shareholders the equivalent of \$30 a share on their original investment. (Bethlehem’s president, Eugene G. Grace, received bonuses of over a million and a half for 1917 and over a million and a third for 1918!) The Steel Corporation paid \$16.75 per share in 1917 (of which one dollar was intended to be passed on to the Red Cross) and \$16 per share in 1918. And as for duPont, perhaps the most striking testimony as to this corporation’s endurance of the hardships of war is to be found in a passage from its annual report for the year 1918, in which I take the liberty of italicizing one clause:

“... 1915–1918, the total dividends on the common stock of E. I. duPont de Nemours Powder Company and on the exchanged securities of E. I. duPont de Nemours & Company have amounted to 458 per cent on the par value of the original stock. *It is difficult to imagine a more satisfactory result, especially in view of the fact that the liquidation of the balance of the military powder investment as it stands today cannot materially alter the conditions above described.*”

There were companies whose rate of profit was even higher than this. For instance, according to figures published in the Nye report in 1935, the Calumet & Hecla Mining Company made 800 per cent on its capital stock in 1917; the Utah Copper Company, 200 per cent. Some other concerns, one

must remember, did not make money on their war orders; some sustained heavy losses by reason of expanding their plants in 1918 and finding their contracts canceled at the close of the war and their new equipment useless. Nevertheless that passage from the duPont report has a peculiar significance. Perhaps it had best be forgotten by those who write inscriptions for soldiers' monuments.

Another result of the war—and this, of course, must be borne in mind in weighing the figures given above—was that prices rose rapidly. By the time of the Armistice the cost of living had climbed 61 ½ per cent above where it had been in July, 1914. The wage-level likewise climbed; in fact, in some vital war-time occupations the shortage of labor caused it to rise to remarkable heights—till the wearing of silk shirts by shipyard employees became a matter of common talk. The shortage of labor (combined with the halting of immigration) also made it easier for workmen to organize and impose demands; the government was conciliatory, partly because of its liberal sympathy with labor and partly because of the need for maintaining enthusiastic and uninterrupted production; therefore there was a rapid growth in the membership of labor organizations of all sorts, conservative and radical: the total union membership rose steadily toward its postwar peak of over five millions. Labor wanted a place in the sun: was not the war being fought for democracy? Not until the war was over did the government withdraw its protecting hand and permit this new offensive on the part of the workmen to meet an equally determined offensive on the part of unreconstructed employers who preferred what they ingeniously called the “American plan”—meaning no traffic whatever with labor organizers.

Another class whose rising fortunes during the war were to have significant after-effects was the farm population. The demand for food was huge. The cry of “Food will win the war” echoed through the country. Prices rose to unprecedented heights. In the spring of 1917, for instance, wheat leaped to \$3.45 a bushel; and the price of \$2.20 which was shortly afterward fixed by the government, though it looked low by comparison, was a very high figure beside the normal peace-time level. At this price of \$2.20 the government offered to take all the wheat that could be grown. The demand for other staples was likewise intense. Hence a great increase in the acreage planted, an increase in the use of farm machinery, and the beginning of a boom in farm lands which was to collapse a few years later, with paralyzing

effects upon an unhappy farming class.

The government's financial program for the prosecution of the war also left its marks upon the American economy. To reduce to the simplest possible terms the immense problem to which this program was the answer, the situation was this:—

First, the Allies had to be financed—no longer, of course, through private operations conducted by the House of Morgan, but through direct extensions of government credit—to the extent of no less than eight billion dollars. And second, to pay and equip and supply the American forces and pay the other costs of American participation required another twenty-four billions. Thus the total cost of the war to the United States was over thirty-two billion dollars—a staggering sum. (As Noyes points out, it was more than ten times the cost of the Civil War to the Union!) How could such an incredible amount of money be raised?

Despite the insistence of a large group of representative economists that the country must pay as it went, in order to avoid inflation, only about a third of the sum was raised by taxation—chiefly by great increases in the income taxes (with surtaxes running up to 65 per cent for the wealthy) and by excess-profits taxes. In other words, some of the money was collected by diligently taking away a part of the winnings of the fortunate corporations and of those who were fattening upon their dividends.

The remaining two-thirds had to be raised by borrowing on an unprecedented scale in five war loan campaigns. Yes, one may say, but how did the American people have so much to lend? One answer is the profits above mentioned. Another is that corporations purchased bonds with their surplus earnings. Another is that men and women sold other securities: the stock-market, which had boomed during 1915 and 1916, showed strikingly the effects of such selling while America was in the war. A fourth answer lies in the extraordinary breadth of the Liberty Loan campaigns, which tapped the savings and surplus earnings of men and women who had never before invested in securities of any sort. A fifth answer is that people borrowed from the banks to buy bonds—in other words, that they bought them out of anticipated earnings: a process which added greatly to the already large volume of credit outstanding and sharply accentuated the generally inflationary effect of the war upon the American financial system.

The Liberty Loan campaigns—ingeniously contrived, intricately

organized, and advertised with an altogether unprecedented patriotic ballyhoo—were successful. The war was financed to a finish. We emerged from it the strongest and by all odds the richest nation in the world. But we also emerged from it with our public debt not two or three or four times larger than it had been when Wilson called upon Congress to declare war, but *twenty times larger*. Furthermore, we emerged from it with the Allied governments owing us upwards of eight billion dollars—a debt which was to cause endless trouble. And although it was pleasant to reflect that we were now a creditor nation, this fact, too, was to cause us trouble, because we did not quite know how to play our new economic rôle.

One more word as to the significance of these figures. It might aptly be said that during 1915 and 1916 the House of Morgan had been engaged in conducting a huge public-works campaign—raising the money for it, placing the orders for it—and that in 1917 and 1918 the Government took over this task on a much enlarged scale. From the point of view of “scarcity economics” this campaign was devoid of one embarrassing result which conservatives discern in public-works campaigns in peace time: it did not “compete with private business” by producing useful goods which would remain to satisfy the population and limit their desire to buy. What it produced was conveniently useless except for purposes of destruction, and much was promptly blown sky-high. But inflation it did produce on a gigantic scale. Those who distrust governments which run into debt in order to feed the hungry should reflect that in less than two years the American government went over twenty billion dollars into debt and other governments went other billions into debt—with consequences which plague us to this day—not to feed the hungry, but to kill and maim and destroy. There is no surer engine of inflation than war.

When the Armistice was signed and the guns ceased firing along the Western front—on November 11, 1918—there was wild jubilation everywhere. After the anxieties and horrors of war, the prospect of a return to the ways of peace seemed incredibly happy. But sober financiers and economists faced the future with some disquiet. War contracts were at an end; a powerful stimulant to prosperity was now suddenly to be removed.

Three and a half million Americans were about to strip off their uniforms and look for jobs. The governments of the world were bowed down with debts. Many other wars had been followed by long periods of economic exhaustion, and surely Europe, if not America, must be exhausted now.

The events of 1919 and 1920, however, took a strange and unexpected turn. For a few months there was an anxious pause as business tried to adjust itself to altered and confusing circumstances; then there began, not a decline, but a furious boom.

So many cross-currents of economic tendency and of emotion were running during those years of demobilization that it is difficult, even at this late date, to present a clear interpretation of the forces that made this boom, gave it its peculiar qualities, and then destroyed it. Yet the attempt must be made, for here again the forces proved to have long-term consequences.

To begin with some of the economic factors: It was quite true that Europe was groaning with debt. But for a time she continued to live on borrowed money. For example, she went right on purchasing from America on credit—not materials of war, but materials of reconstruction. (In the year after the Armistice the Allied debts to America made a further growth from a little over eight billions to more than nine and a half billions.) In the second place, a considerable part of the world had gone for a long time without the necessities of normal life and was in a mood to buy them wherever they could be bought—for a time at least. It was these two factors which set the 1919 boom in motion; there was a sudden jump in American exports during the months when the peace commissioners were laboring at Paris, and this jump in exports sounded the note for an advance.

The emotional factors in the 1919 boom were complex. In the first place, the war had been conducted under a pressure of terrific enthusiasm; this enthusiasm did not disappear at once, but was at first transferred to other causes and enterprises, taking strangely varied forms. It brought about, for example, the ratification of the suffrage amendment—and the prohibition amendment. It sent Wilson to Paris to try to establish a League of Nations which would end war once and for all. It led thousands of Americans to dream of the establishment of a socialized economic order, to endorse the Plumb plan for permanent government ownership of the railroads, to back the demands of labor for a larger share in the fruits of industry. It led business men and financiers to entertain extravagant hopes of making the United



States a nation pre-eminent in foreign trade. And it also led labor to feel that now its day had come. American workmen had had an unprecedented bargaining power during the war, they were better organized than ever before, having secured at last a toehold even in the steel industry; they saw labor parties rising to power in Europe and the proletariat even winning its way to dictatorship in Russia; and they forgot, perhaps, that when the troops were fully absorbed into the working population the bargaining power of labor would be diminished. Suffragists, drys, Wilsonian peace-lovers, radicals, exporters, labor leaders—all of them, in 1919, resolved in their varied ways to carry to a conclusion the “lessons taught by the war.”

Another emotional factor—which likewise took various forms—was a very natural desire to be rid of the constraints and duties of war-time. Among many business men it took the form of an intense resolve to get away from government regulation and red tape, to throw off the burden of high taxes, to cease what they considered a dangerous and economically unsound truckling to labor. They wanted independence again. They wanted to be running things again. Some of them wanted to speculate again. Again, among many workmen this same revulsion against restraint took the form of a feeling that now they could strike and not be called unpatriotic—and that they would do it and get what was due them.

Finally, there was the growing mood of disillusionment—the gradual spread of a feeling that the high resolves of war time had been too high, that the Wilson program was a lovely pipe-dream, that Utopia was a long, long distance away, and that in the meantime you might as well decide what you wanted and grab it, for this was the way of the world. Slowly disillusionment began to tarnish the remnants of war-time enthusiasm, and to transmute the desire for independence into ruthlessness and greed.

The result of these interworking forces in 1919 was a brief and utterly undisciplined boom in business, combined with a bitter conflict between labor and capital. When American foreign trade began to pick up in the spring of 1919, business men regained their confidence and proceeded to make the most of the new prosperity. There was wild speculation in commodities, which lifted prices sky-high; there was speculation in stocks, an intemperate expansion of exports, and in general a sharp inflation. This boom was punctuated by a series of grim strikes: a great steel strike, a coal strike, even a police strike in Boston. The employers (particularly men like

Gary, whose refusal to recognize labor unions had the full support of the masters of Wall Street) held fast, and fought the unions with the aid of company police, espionage, government injunctions, and a great deal of patriotic flag-waving to convince the public that they were defending the American order—"American principles of liberty" was Morgan's phrase—against Bolshevism. Meanwhile the crazy purchasing of goods against a supposed world shortage continued apace—until the spring of 1920, when the inevitable and long-postponed collapse began. Even after it had begun, the speculators of Wall Street continued to sport with the shares of Baldwin Locomotive and Mexican Petroleum and Crucible Steel, and there was a spectacular corner in the shares of the Stutz automobile company.

The collapse which began in 1920 continued for considerably over a year, and the damage it did was widespread. South American and Cuban buyers of American goods canceled their contracts, and the export bubble was punctured. A widespread buyers' strike against high retail prices took effect, and down came prices, fast and far; there was a dismal writing-down of inventories for American business concerns in 1921. Down came farm prices in particular, bringing with them real estate values in the formerly rich farm lands and ruining a great number of little banks which had been formed during the war and the succeeding year or two. Down came steel operations to eighteen per cent of capacity. And down came the hopes of union labor too. Adverse economic conditions, combined with post-war disillusionment and with that curious distortion of patriotism into a frightened Toryism which I have described at length in *Only Yesterday*, broke up the labor offensive and restored to the managers of American industry their former independence.

## 6

With the depression of 1921 the war period of American finance and economics may be said to have closed. As the recovery began, in 1922, the abnormal influences of the war had in some degree worked themselves out; things had begun to approach a normal balance. Let us pause for a moment and take stock of what these eight years had done to change the economic scene and prepare the way for a new era.

1. They had greatly stimulated industrial production and efficiency; had intensified the use of machinery; had developed new industries and had

matured others (such as the automobile industry).

2. They had perhaps interrupted somewhat the process of concentration—but an increasing number of mergers of banks and industrial companies showed that the trend was still toward concentration and that the process was ready for thorough-going resumption. (For instance, the railroads were now back in private hands, and in the Esch-Cummins Act Congress had actually given permission for their consolidation into large systems, if this could be managed to the satisfaction of the Interstate Commerce Commission.) Furthermore, the passage of the Webb-Pomerene Act in 1918, which permitted corporations to combine forces for foreign trade purposes, inevitably had opened the way toward combinations for domestic trade purposes. Not that this Act allowed companies to agree on domestic prices and other domestic policies. This was still forbidden. But if a group of managers are permitted to meet and fix prices on exports, it is very easy for them to discuss domestic prices too without anyone's being the wiser. Another breach had been made in the Sherman Act's wall of defense against monopoly.

3. The national debt had become enormously larger. Not only that, but the expansion of governmental functions which had begun during the pre-war reform period (under the impulse to regulate business and provide services to the public) had continued during and after the war, the result being that the yearly expenditures of the Federal government had jumped from about three-quarters of a billion dollars in 1915 to over six billion dollars (including interest on the national debt) in 1920, and that the expenditures of state and local governments had similarly multiplied. Apparently there was no escape from the principle that as the trend toward centralization continued, so must the trend toward growth of governmental functions and of taxes continue.

4. Meanwhile there still remained the Allied debts to the United States; and as Europe was still prostrated, there remained a tendency toward a lop-sided balance of trade. Since the United States did not see fit to lower its tariff and thus permit Europe to pay its debts (and balance its purchases from the United States) in goods, the only way of achieving a balance was the dangerous method of lending the necessary money to Europe. This, in effect, was what we had done during the war, and the results had been very persuasive. Yet it was a strange method to adopt for permanent use, and there was some question how long it could be resorted to without trouble.

5. The inflationary effect of the war had geared American business to a new price level; even the collapse of 1920–21 did not bring prices down to anywhere near the level of 1914.

6. American agriculture was very sick, with little prospect of recovery. Its booming export business had gone, never to return on a large scale; for other countries were resuming production of wheat and other staples, and there was new competition from South America. The drop in farm prices had undermined permanently the values of farm property and farm mortgages, and thus had reduced a part of the country to comparative poverty.

7. American finance, however, was doing very well. New York had become the most powerful financial capital in the world. The Federal Reserve System had come through the war with flying colors; and its mobile reserves had been so effective in preventing a serious money crisis in 1921 that bankers began to believe that the System offered an automatic guaranty against another panic. This confidence in the System, coupled with a confidence born of America's new financial pre-eminence in the world, was tending to relax that eternal financial vigilance which is the price of security: to make men think that a good System of reserves could atone for loose and inadequate banking standards.

8. The Liberty Loan campaigns had done much to form among Americans the habit of investing. The big war-time profits of many corporations and the stock market booms of 1915–16 and 1919–20 had played a supporting part in developing this habit. The result was a remarkable increase in the number of stockholders of American corporations: the total number of book stockholders in thirty-one large corporations more than doubled between 1913 and 1923; and according to the estimates of H. T. Warshaw, the total number of book stockholders in all corporations must have almost doubled. The Liberty Loan campaigns had also taught business men that you could accomplish almost anything through a publicity campaign. Both facts were to prove important: the first, in pulling hundreds of thousands of people into the stock market and preparing the way for new methods of corporate control and aggrandizement; the second, in preparing the way for public-relations counsel and other masters of the art of whitewashing.

9. And finally—the war and its aftermath had left the American people in a state of spiritual exhaustion. The reform impulse was at last moribund. The fear of the trusts, and especially of a money trust, was almost forgotten—it

seemed like last year's nightmare. The frenzy of war-time was gone; the millennial hopes of war-time had turned to dust and ashes. Trying to improve things seemed a wearisome and futile occupation. Let us go back to business and get rich and forget all that, said the American people in effect.

They repudiated Wilson and all the ideas for which he had stood, and in 1920 they elected Warren Gamaliel Harding, an amiable and second-rate man who could, they thought, be trusted not to cause business any trouble. Harding wore a McKinley carnation in his buttonhole; and business men, recalling vaguely the dear dead days of McKinley—when the promoters were making millions, and Mark Hanna kept the government at Washington in its place, and the reformers had not begun their impertinent attacks upon American prosperity—felt that the “normalcy” which Harding promised was all that their hearts could desire.

Normalcy. Back to the good old days. Hands off business. Those were the mottoes which appealed to the tired business men of the post-war years.

But it was impossible to go back to the good old days. The world had changed. The industrial order had changed. The financiers and corporation lawyers had been developing new devices to perpetuate and extend their sphere of power. Now that the brakes were removed, the process of concentration was to proceed in strange new ways and to unforeseen ends—as we shall see.