2. Cross-examination

When it came my turn to be called before the Finance Committee, I challenged all that had been said up to that point and was practically alone in doing so. As a matter of fact, among witnesses drawn from the business community, only David Stern, editor and publisher of the *Philadelphia Record,* and Ralph Flanders, who was subsequently to become a United States Senator from Vermont, associated themselves with the concept of a deliberately unbalanced budget. But even these two men did not advance a detailed program of action that would make an unbalanced budget meaningful.

What I said was received with astonishment by those who expected all bankers to wear the old school tie, and with relief by the few members of the committee who saw that I wore a Western tie.

In accounting for the depression, I merely repeated the views I had voiced at various places in the intermountain region. The reader will recall my argument as it is expressed in a preceding section. There is therefore no need to state once again the basic reasons why I thought a program of deficit financing was an indispensable prerequisite to recovery in a time of serious depression, while a *balanced* budget or a surplus was mandatory in boom times. But it was one thing to talk that way on my own home ground and quite another thing to repeat it in the intellectual East, where the Baruchs, Taylors, Atterburys, Duffields, Houstons, and Weirs—"with the monotony and persistence of Old Cato"—clamored for a balanced budget, as did the President of the United States. Still, I find some pleasure in noting that if I was a traitor to my own class, I earned that distinction long before Franklin Roosevelt was called one.

Following an analysis of the causes of the depression, I presented a five-point program, in the nature of first-aid measures, along with the outline of a long-range program for economic stability. In the highlights of that program the reader may see in silhouette what later became full-bodied undertakings by the New Deal. Let me add here that ideas similar to those I advanced were being discussed by many other men across the land who were later to play their part on the Washington scene. Yet I was not in touch with those men, nor did they appear before the Finance Committee.

The main points of the first-aid program, with their supporting arguments, were as follows:

Make available as a gift to the states on a per capita basis $500,000,000 to be used during the balance of the year 1933 in assisting adequately to take care of the destitute and unemployed, pending a revival in business.

"We shall either adopt a plan which will meet the problem of unemployment under capitalism, or a plan will be adopted for us which will operate without capitalism," I said. Private charity was exhausted. Practically all our political subdivisions had reached the end of their tax and borrowing resources. It was therefore imperative that the federal government, as the most urgent of all emergency measures, make available *at least* five hundred million dollars for the remainder of 1933 to be prorated among the states. This should be a direct gift, not a loan, and it should be in such amounts that the relief organizations in each state could meet the needs of the unemployed in a more adequate manner than was currently possible.

Though the amount I suggested for relief purposes was picayune in relation to need, even so it provoked an instantaneous objection from some members of the committee, and particularly from Democratic Senators David I. Walsh of Massachusetts and Thomas P. Gore of Oklahoma. Senator Walsh had difficulty in understanding why the separate states—and particularly a wealthy state like New York—could not do the sort of thing the federal government could do.

In reply to his challenge I repeated what I had said for more than two years in Utah: "The individual state is not sovereign. It has no money-creating powers. It cannot call men to war and provide billions for that purpose. It cannot end the depression by the use of public credit on a national scale. The federal government alone can do this. And the longer it waits before it does it, the greater will be its difficulties when it gets around to doing it."

The second of the first-aid measures was this:

Increase the amount of government funds two and a half billion dollars, and more if necessary, for self-liquidating government projects and loans to cities, counties, and states for public works on a liberal basis at a low rate of interest.

I pointed out that during four years of depression everyone, in an effort to protect himself, did what proved to be the wrong thing for the economy as a whole. "The production of wealth and the consumer's ability to buy," I said, "begins with the pay roll and the individual producer of raw material, the agriculturalist. Today we are losing close to three billions per month of national income because of unemployment, and this, in turn, makes it impossible for people to purchase the goods necessary to sustain production. Is there any program of economy and budget-balancing on the part of our government as important as the effort to stop this loss of wealth and the human suffering it entails?"

I suggested that the sum of money the government should appropriate for self-liquidating projects take the form of one billion dollars to be added to the billion and a half dollars already available to the RFC for similar projects; that a separate agency should be established to take over this division from the RFC in such a way as to get money as rapidly as possible into the hands of the consumer.

This conception was to form the basis of the Public Works Administration the next year. But when it was finally brought into being, it seemed, for various reasons, unable to meet the essential specification of speed, which I expressed in the following paragraph from my statement before the Senate Finance Committee:

> Emergency speed, such as was resorted to during the time of war, is necessary for the success of this plan. The self-liquidating plan to date has been utterly ineffective due to the failure to get the funds out because of legal obstacles and the red-tape of administration. In order to obtain speed, I would recommend the appointment of a civilian non-political commission of not to exceed five representatives, leaders in each state, to serve without compensation, whose duty it would be to encourage development of public works and liquidating projects in their respective states as rapidly as possible. Loans should be made on a very liberal basis as to terms of payment and security. The interest rate should not exceed the amount the government is required to pay for its funds, since the purpose of the program is not to make a profit for the government or to discourage the use of these funds. In order to speed up this program a limit of three months from the time of the appointment of the commission in each state should be given in which to file and complete applications; this period of time to be extended, if necessary, by the approval of the President of the United States.

As an alternative to the proposed self-liquidating public-works program, and as an alternative that would more quickly meet the emergency, I suggested to the committee that it might consider a modification of a plan that had just been put forward in *Harper's Magazine* by J. M. Daiger.

Daiger urged that the federal government pay to the depositors of the chartered banks that failed the amount of their deposits that were tied up, and thus restore this money to active circulation. He noted that the total of the deposits involved in failures was approximately five billion dollars; that half that sum would probably be recovered; that most of this amount had already been received, either through the receivers of the closed banks, or through advances from other banks, or, more recently, through the Reconstruction Finance Corporation. A bond issue of approximately two and one half billion dollars would be needed to cover the net loss. This, in Daiger's terms, was a "political price," but it was worth paying in order to restore cash, credit, and confidence in the banks.

My own modification of this plan called for its limitation to losses covered by bank failures during the depression—that is, from 1930 on until the necessary legislation became effective. The virtue of the plan was that it would quickly get a large sum of money into circulation and into the hands of those people and communities which were the hardest hit by the effect of bank crashes. It would re-establish confidence in the banks, bring money out of hoarding, tend to raise prices, and thus start the necessary flow of money and credit. All this in turn would greatly increase the value of the assets taken over from the closed banks and facilitate their liquidation, thus reducing the loss in such a venture.

I believed a bank-deposit guarantee law would have to be incorporated in such a refunding measure. Moreover, the law would have to cover all banks, since if any of them were excluded because of their inability to meet certain banking requirements, they would have to close. The exclusion itself would signify their instability, and the depositors would swiftly administer a *coup de grâce* to such an institution. I argued, furthermore, that the stronger banks of the country—which would not need the benefit of such a deposit-insurance law but would get the benefit of wealth-production from the country as a whole—should be required to share a proportionate cost of the plan, thus tending to equalize the burden of loss due to bank failures in the entire financial structure. All of this was incorporated in the Federal Deposit Insurance Corporation when it was established later in the year.

Each bank [I said] should be assessed a necessary percentage of its deposits to provide and maintain an adequate fund to meet losses to depositors. In order not to put a premium on bad banking practices, rules and regulations required for the continuation of the benefits of the fund should be gradually promulgated and enforced over the next few years as business recovers, so that in time a strong banking structure would be developed as a bulwark in future depressions. If banks failed to meet their requirements of eligibility after six month's notice they would be suspended, which would mean their liquidation; the fund would be drawn on to prevent any loss to depositors. In this connection it is my opinion that the banking structure would be greatly strengthened with the passage of the Glass Bill providing for branch banking, thus reducing the cost on the banking structure of maintaining the deposit-guarantee fund.

The third first-aid measure was this:

Adopt the domestic allotment plan, then being contemplated, so as to regulate production and raise prices in agriculture.

In support of this proposal I pointed out that the disequilibrium between the things the farmer sold and those he bought not only had bankrupted him, but had also led to the collapse of commercial enterprises that depended most directly on agriculture. It was therefore essential that this disequilibrium be corrected as a matter of equity and as an important economic device to end the depression. Of the various schemes then being discussed to deal with the farm problem, the domestic allotment plan seemed to me to be the most practical.

The allotment plan [I said] may be a long way from a perfect solution of the problem, but something must be tried. Our progress to date in every field is the result of experimentation, trial, and error. The allotment plan may need to be changed or modified from time to time, but that can be done as experience determines. I believe that some form of the allotment plan is necessary as a permanent measure as long as a tariff policy is in effect in this country. The allotment plan is no more artificial than the tariff, the money system, and all the regulatory operations in the government. Our whole economic system, in the same sense, is artificial and must of necessity continue so unless we revert to a primitive society.

The Agricultural Adjustment Act, which developed later, along with its various amendments, was an outgrowth of discussions that first centered on the allotment plan.

The fourth first-aid measure was directly related to the foregoing one. It was:

Refinance farm mortgages on a long-term basis at a low rate of interest.

The seriousness of the farm-mortgage problem was evidenced by the great difficulties encountered in foreclosing the farm debt. Many foreclosures were prevented by the armed resistance of the farmer's neighbors and friends, or by legislative enactments, in most of the agricultural states, of farm-debt moratoriums. What I proposed to meet this problem involved a grant of authority to the federal land banks to take over mortgages up to the amount of five billion dollars if that sum was necessary. They would stop foreclosures, refinance the farm debt at greatly reduced annual interest and principal payments on the indebtedness, stop a further deflation of farm values and re-establish them, and aid in restoring the credit of the farmer for his essential current requirements.

The total farm-mortgage debt of the United States at that time was somewhere between eight and nine billion dollars. Of this amount, about one and a half billion was held by the Federal land banks, half a billion by joint-stock land banks, and one and three fourths billion by the insurance companies. The balance was held by private mortgage companies, banks, and individuals. It was clear from these figures that any step taken to check the further foreclosure of farm-mortgage indebtedness would indirectly benefit and help maintain the solvency of the farmers' creditors—the banks, insurance companies, implement concerns, and other purveyors of supplies, as well as the counties and states to which the farmer owed huge amounts of delinquent taxes.

This proposal met with an indifferent reception by the Senate Finance Committee. But when the new Administration took office in March 1933, it set up a Farm Credit Administration, backed by sufficient governmental financial resources to finance and refinance the needs of agriculture that were not taken care of by private credit. This included the refunding of all defaulted farm mortgages, livestock loans, and the financing of current agricultural production and of farm co-operatives.

The fifth first-aid measure was this:

Bring about a permanent settlement of the interallied debts on a sound economic basis, the cancellation of the debts being preferred.

These words were no sooner out of my mouth than a member of the Finance Committee leaped up as though I had touched an exposed nerve. "What!" boomed Senator Shortridge of California. "Cancel these debts?" And he kept booming his opposition in various forms after that. In this he voiced the prevailing sentiment that these interallied debts, then wholly or largely in default, should be paid. Yet it seemed to me that so long as we hesitated to face the question of these debts in a realistic manner, we would fail to meet and check whatever influence a lack of foreign trade had on the depression.

I pointed out to the committee that debts between nations could ultimately be paid only in goods, gold, or services or a combination of these three. But the pressure on our foreign debtors to pay their obligations held in this country ran parallel with our restrictive-tariff policies. Since foreign debtors could not sell a sufficient amount of goods to meet their dollar needs, they could pay their obligations only by shipments of gold. Furthermore, since this process led to our acquiring a good part of the world's gold supply, the loss of gold in foreign lands forced many of them off the gold standard and tended to bring about a depreciation of their currencies so that they could produce goods at costs that would offset the effects of our high tariffs. All of this boomeranged on us.

As I told the Finance Committee: "We must either choose between accepting sufficient foreign goods to pay the foreign debts owed this country or we must cancel the debts. This is not a moral problem but a mathematical one."

Despite the views of men like Senator Shortridge, mathematics had the final say after all. These interallied debts have never been paid off. The total amount advanced by our government to European governments for the purposes of the First World War was approximately $10 billion. We have received payments on this indebtedness amounting to $2,750 million, of which $760 million was labeled as payment of principal, and the rest of the amounts received as interest. The large majority of these payments were received before the 1931 moratorium; since 1934 the amounts received have been less than $1 million a year, coming mainly from Finland. Meanwhile some $5 billion of unpaid interest has accumulated, so that the total indebtedness at the time of this writing is in the neighborhood of $15 billion, or a $5 billion increase above the original amount.

The moratorium on interallied debts contracted at the time of the First World War has existed for twenty years, and there is no prospect whatever of collecting the debts. Moreover, the size of these debts is almost of a piggy-bank character in contrast with the huge sums we have advanced and are continuing to advance to foreign nations since those days.

Cancellation of the interallied debt, along with the other measures I advocated before the Finance Committee, did not exhaust the list of things I felt should be done. In themselves they were mere stopgaps and were completely inadequate to deal with the long-range economic problem that faced the country. The larger program, I said to the committee, would require action along these lines:

There must be a unification of our banking system under the supervision of the Federal Reserve System in order more effectively to control our entire money and credit system. High income and inheritance taxes are essential in order to control capital accumulations and to maintain a better balance than the one existing between consumer purchasing power and capital expansion. In other words, productive capacity should not outrun effective consumer demand, and the tax system is a balance wheel for this undertaking. Moreover, there should be national child-labor, minimum-wage, unemployment-insurance, and old-age-pension laws. Any of these laws when left to the states merely create confusion and would not meet the situation nationally unless similar and uniform laws are passed by all states at the same time—which is improbable. As a further measure for economic balance, all new capital issues offered to the public, all foreign financing should receive the approval of an agency of the federal government; this control should extend to all means of transportation and communication so as to insure their operation in the public interest. A national planning board, similar to the industries board during the war, is necessary to the proper co-ordination of public and private activities of the economic world.

Having said this, I caught the next train to New York to keep my appointment with professor Rexford Tugwell at Columbia University. Such personal satisfaction as I gained from this session before the Finance Committee was delayed for two years. In 1935 *Fortune* had occasion to refer to the various aspects of the program I had presented in Washington in February 1933. It went on to say:

"Anyone who will translate the latter suggestions into their present alphabetical symbols and compare the earlier general statements of economics with the economics of the present administration will be forced to conclude that M. S. Eccles of Ogden, Utah, was not only a Mormon but a prophet."