

I. The Moral of the Story

THROUGHOUT A continuous period of service in the government, commencing February 1, 1934, the recurrent and general theme of my economic philosophy has been this:

That in time of depression the government must spend more than it collects so as to stimulate consumer demand and purchasing power sufficiently to match our productive capacity; that in time of high business activity, except in case of all-out war, it must at least balance its cash budget or collect more than it spends, depending on the degree of existing inflationary pressures.

In this conception the government is the compensatory agent for an economy based on principles of private enterprise. It does not compete with private enterprise. But it consciously uses its system of taxation and expenditures, supplemented by monetary and credit policies, for the purpose of maintaining economic stability through maximum production and employment.

The attempt I made to get this conception written into the Banking Act of 1935 ended in failure. But eleven years later I had the satisfaction of seeing it affirmed in the Employment Act of 1946. As I wrote to Senator Robert F. Wagner on June 14, 1945, when the employment bill was being considered by the Senate Banking and Currency Committee:

If this bill or some similar one is enacted, Congress for the first time will have recognized by a formal declaration that the Federal Government has a large measure of responsibility for maintaining a satisfactory level of business activity and employment and that there should be some broad guide and objective formally stated by the Congress to govern governmental acts and policies affecting the Na-

tion's economic life. While this would, of itself, mark a new departure, it would merely be a recognition of the facts (1) that the Congress has step by step authorized the assumption by the Government of numerous responsibilities affecting industry, commerce, agriculture and labor; (2) that the way in which these responsibilities are discharged, the manner in which they are financed, and the timing and direction of various Government expenditures directly affect economic activity and stability; and (3) that, therefore, Government acts and policies need to be co-ordinated and harmonized so that their influence upon the economy may help to sustain and stabilize it at a high expanding level of prosperity.

Still a wide gulf seems always to stand between a statement of principle and its application in day-to-day affairs. This certainly is evident when one views the events of the last five years against the background of the government's avowed intention to maintain economic stability.

In a sense, what happened between V-J day and the start of the Korean war is of a piece with what happened in the depression and in the years of World War II. In all three phases political expediency rather than a detached appraisal of economic realities tended to dictate governmental decisions.

In the depression years a proper fiscal policy called for large planned government deficits, financed primarily by the banking system, with a consequent increase in the supply of money and a reflation of the economy. We needed to discourage savings and to encourage expenditures and credit expansion. We needed to reduce interest rates and to encourage borrowing. We needed to keep taxation down so that the money spent by the government would be added to the spending stream.

Throughout the decade, however, we remained in a state of semidepression because we were not willing to have the government supplement private enterprise with sufficient activity and expenditures to employ our idle manpower and resources. While we had a degree of recovery, it never carried through sufficiently to make any substantial reduction in unemploy-

ment. At no time had we less than from eight to ten million unemployed. Much was done to encourage housing and to stimulate production of capital goods. States and municipalities were subsidized to a large extent by federal outlays for public works. We succeeded in bringing the national income up from some \$40 billion annually at the bottom of the depression to an average of approximately \$70 billion at the end of the decade.

In spite of this, we constantly heard prophecies of inflation, which were never justified. The national income at the end of the decade was still \$10 billion below where it was in 1929, even though there had been a great increase in production and in the size of the labor force. We were never able to take up the large amount of slack that existed throughout the economy. We did not take it up because we did not spend enough. And though we did not spend enough we were told that the doctrine of a compensatory economy was a failure—despite the fact that it had never been tried, except to a mild degree.

The doctrine of a compensatory economy as applied to the war years called for a reversal of the policies that were applicable and should have been more fully used in the depression years. Instead of reducing interest rates to encourage borrowing, we needed to adjust those rates in a way that would encourage savings and investments in government securities to finance war goods rather than stimulate private credit expansion. Instead of a tax structure designed to encourage consumption, we needed one that would recapture for the government a large part of the outlays for the war program and would at the same time reduce the number of dollars that competed for a limited amount of consumer goods and services.

But, once again, the measures required were applied either in a half-hearted way, or too late, or not at all. The charge was nevertheless made that the doctrine of a compensatory economy had failed—though it was never vigorously applied.

In the five-year interval between V-J day and the start of the Korean war—a period of high economic activity—the concept

of a compensatory economy called for a fiscal and monetary policy that would reduce the supply of money and neutralize inflationary pressures. What happened instead now causes dismay in all quarters friendly to us.

Domestically, we are confronted with dangerous inflationary developments that threaten our entire system of democratic capitalism. Instead of having some slack in our economy, we are taut and strained, even before we feel the full effect of a new armament program. This program might have been avoided had we been able to bring about the conditions of peace at a time when we occupied a commanding economic and military position throughout the world.

Our peril on the domestic and international front is very great. Heretofore, for the greater part of American history, our foreign and domestic affairs have lent themselves to separate treatment and emphasis. Men could feel that what happened in either sphere of activity was for the most part self-limiting in its effect. We could know serious domestic difficulties without exposing ourselves to attack by foreign powers. Or again, we could conduct our relations with those powers confident that, whatever happened, the internal structure of American economic and political life would remain unchanged.

But this sort of reassurance is gone. Since the end of the Second World War our domestic affairs are largely controlled and dominated by the international quandary in which we find ourselves. If we fail to stop inflationary forces at home—and not merely postpone their effect—we shall be unable to carry out the military and economic program demanded of us by a rapidly deteriorating world situation. Yet again, if we cannot carry out that program, we shall be brought under the direct line of a Communist attack whose avowed aim is to destroy our economic and political structure.

In my father's day the nations in the Western community could fight each other and at the end of the war, whether victorious or vanquished, retain unchanged the greater part of

their social, economic, and political structure. This was so because most of them subscribed to similar ideas. But in the intervening one hundred years, as the long shadows of the *Communist Manifesto* have encroached on and now overlap the shadows cast by *The Wealth of Nations*, a war between nations takes on the aspect of a revolutionary war in which the vanquished can expect that the whole fabric of its internal life will be replaced by one woven to the wishes of the victor.

In the face of this known risk we have conducted our domestic and foreign affairs in the last five years as though they were self-limiting in their effect; as though a failure in this or that undertaking would cause merely a temporary inconvenience to a few of us instead of a fatal blow to all of us.

The postscripts that follow recount the case history of my own failure and frustration as I tried, in my limited capacity, to influence public thought and governmental policy in the past five years.