Marriner S. Eccles, Chairman of the Federal Reserve Board

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> The inherent instability of capitalism may be corrected by conscious and deliberate use of three compensatory instruments, taxation, varying governmental expenditures, and monetary control. *Marriner S. Eccles, 1935*

> Yours was the only revolution on record that entered government by way of a central bank.
> *John Kenneth Galbraith to Eccles, 1976*

On July 29, 1983, the Federal Reserve Building in Washington, D.C. was formally named in honor of Marriner S. Eccles, who served as Governor of the Fed, 1934–36, as Chairman of the Board of Governors, 1936–48, and as member of the Board, 1948–51. While Eccles was honored primarily for his struggle to maintain Federal Reserve independence to conduct monetary policy, his role in introducing "compensatory" monetary and fiscal policies—modern macroeconomic stabilization policies—was undoubtedly of equal importance. In tracing the development of Eccles' macroeconomic philosophy, this study identifies him as one of the earliest American precursors to Keynes, and as the most important figure in the introduction of "Keynesian" economic policies in the United States.

I. Changing Views

> We must acknowledge that progress comes only through toil, economy and thrift, and that these alone are the motive power which creates the enduring structure. *Eccles, 1925*

> The matter of economy is negative, the matter of spending is positive, and we have been doing the negative thing rather than the positive. We have been preaching the negative doctrine.... Our depression was not brought about as a result of extravagance.... The difficulty is that we were not sufficiently extravagant as a nation. We did not consume what we were able to produce. *Eccles, 1932*

In February, 1933, the Finance Committee of the United States heard testimony on the causes and cures of the depression. While farmers argued for remonetization of silver as a means of recovery, and labor spokesmen suggested reduced hours and work weeks, the majority of the 46 prominent Americans who testified were of the opinion that the depression represented the workings of natural economic law, a punishment for the "extravagance" of the 1920's, and that to interfere with the cycle of boom and bust was to invite disaster. Balancing the federal budget in order to "restore confidence" was seen as the only prudent course open to government, a policy reflected in the 1932 political campaign, in which both major parties advocated a balanced budget as the key to economic recovery. In an effort to reduce the deficit,

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Congress had passed in 1932 what was to that point the largest tax increase in U.S. history. Toward the end of the hearing, Eccles was called to testify. Eccles, 43-years-old, was a successful Utah banker and industrialist, a "conservative Republican" whose formal schooling had ended after three years of high school, but whose business acumen had enabled him to bring his commercial and banking interests through the worst years of the depression relatively unscathed.

In his testimony, Eccles identified the cause of the depression as an insufficiency of effective demand, rather than punishment for past extravagances, loss of confidence, or workings of natural law. The cure, Eccles stated, was a restoration of sufficient spending to purchase the quantity of goods which it was possible to produce at full employment. Because the profit motive could be expected to lead individuals, business, and financial institutions to make decisions which would further reduce spending, hence income and employment, the government, motivated not by profits, but by the welfare of the public, must compensate by spending more. "I see no way of correcting this situation except through Government action," Eccles declared (*MSE*, Senate Finance Committee, *Investigations of Economic Problems*, "Statement of M. S. Eccles, President First Security Corporation, Ogden, Utah," February 24, 1933, p. 712). He then proceeded to outline a five-point program of unemployment relief, public works, agricultural allotment, farm mortgage refinancing, and permanent settlement of interallied debts to deal with the immediate problems of the depression. He also proposed a plan for long-run economic stability that included unification of the banking system under the Federal Reserve and the creation of an agency to guarantee bank deposits; tax reform to achieve a more equitable distribution of wealth and purchasing power; passage of national child labor, minimum wage, unemployment insurance, and old-age pension laws; federal agencies to approve all new capital issues offered to the public and all foreign financing, all means of transportation, and all means of communication to insure their operation in the public interest; and a national planning board to coordinate public and private economic activities (see also pp. 712–33). Eccles' testimony was received by the Finance Committee with a mixture of interest, skepticism, disbelief, and outright hostility. Three years later, a cover story in *Time Magazine* evaluated his 1933 proposals in the following terms: "Eccles laid before a Senate committee a plan, which turned out to be nothing less than a detailed blueprint of the New Deal. Only one Eccles suggestion has not materialized—official cancellation of War Debts" (February 10, 1936, p. 60).

Marriner Stoddard Eccles was the eldest son of the second wife of David Eccles, Utah's first native millionaire. David Eccles, who had been illiterate when he emigrated from Scotland to Utah at the age of fourteen, left an estate appraised at more than $7 million when he died in 1912 (see Leonard Arrington, 1975). Marriner Eccles' success in consolidating and managing his father's estate has been documented in Eccles' autobiography, edited by Sidney Hyman (1951).

In addition to wealth, Eccles inherited from his father a set of beliefs about the proper roles of individuals and government in the functioning of the economic system. In the automatically functioning, self-adjusting, capitalist economy, the role of government should be limited to "maintaining confidence" through strict budget-balancing, while the greatest benefit would be received by those individuals who worked hard, practiced strict economy, and invested prudently (Hyman, 1951, pp. 4–5, 21, 37, 51). "We must acknowledge," Eccles told Utah bankers in 1925, "that progress comes only through toil, economy and thrift, and that these alone are the motive power which creates the enduring structure" (*MSE*, written address, June 1925, p. 3). As the crash of 1929 deepened into prolonged depression, Eccles was forced to reevaluate his thinking. Early in 1931, he recalls, "I saw for the first time that though I'd been active in the world of finance and production for seventeen years and knew its techniques, I knew less than nothing about its economic and social effects. The discovery of my ignorance, however, did not by itself lead anywhere.... As an individual I felt myself helpless to do anything" (Hyman 1951, pp. 54–55). Eccles had run aground on the shoals of macroeconomics.

The reformulation of his thinking was reflected in his public addresses. In a speech to bankers in the spring of 1931, Eccles said, "The modern system by which society supplies its wants...is a wonderfully effective organization when in balance..., but if anything happens to throw it out of balance it is possible to have millions of people unable to buy the products of others because they cannot sell their own" (*MSE*, written address, March 26, 1931, pp. 5–6). Eccles had by this point rejected the idea of the automatic restoration of economic prosperity through the workings of the invisible hand of narrow self-interest. He had discovered the fallacy of composition, and had concluded that "intelligent and courageous" open-market purchases by the Fed could have averted the drastic deflation which followed the crash. He had also concluded that underconsumption, not overproduction, was the basic cause of the depression (see also pp. 4–5, 7–8).

During the period 1931–33, Eccles developed and expanded the underconsumption theory, and by 1933 had arrived at the essential framework of Keynesian analysis and policy. The evolution in his thinking can be identified in his public addresses of 1932 and 1933. In a 1932 speech, Eccles declared, "Our depression was not brought about as a result of extravagance.... The difficulty is that we were not sufficiently extravagant as a nation. We did not consume what we were able to produce" (*MSE*, written address, June 17, 1932, pp. 2–3). Eccles mentioned the fallacy of composition problem and the futility and perversity of government efforts to balance the budget, which could only lead to further unemployment. "Just to the extent that unemployment increases," said Eccles, "just to that extent are you going to find it more impossible to...balance any budget" (p. 4). Popular theories of causes of the depression were dismissed: "These are not acts of God, they are mistakes of man" (p. 6). Traditional theories of economic recovery were also discarded. "The theory of hard work and thrift as a means of pulling us out is unsound economically. True hard work means more production, but thrift and economy mean less consumption.... Now for the solution to our problem," said Eccles, "How are you going to put these people back to work? There is only one agency in my opinion that can turn the cycle upward and that is the Government. ...[T]he Government, if it is worthy of the support...of its citizens, must so regulate, through its power of taxation, through its power over the control of money and credit,...the economic structure so as to give men...the opportunity to work" (see pp. 5–6).

Eccles had further refined his ideas by 1933. On economic recovery through spontaneous revival of investment, he said, "The assumption of spontaneous revival through new investment has always rested on the fallacious belief that people and banks will not indefinitely hold money in idleness" (*MSE*, written address, October 27, 1933, p. 3). On the notion that a shortage of currency in circulation was prolonging the depression, Eccles stated, "There is no shortage of currency in circulation.... The need is not for more money, but for more spending" (see pp. 5, 2). To the view that recovery was dependent on the establishment of "sound money," Eccles commented,

> For the past two years or more we have had the painfully sound dollar measured by its purchasing power in terms of goods and services. The sounder it got the further prices fell and the more unemployment increased. Had the policy of economy and budget balancing on the part of the Government continued, it would have soon been so sound that all of our credit institutions would have been closed, there would have been no bank money and all of the people would have been starving to death with an abundance of everything for everybody, or at least the willingness and power to produce it.
> [See pp. 10–11]

Self-interest cannot be relied upon to create recovery, Eccles told the Finance Committee, since "if we leave our 'rugged individual' to follow his own interest under these conditions he does precisely the wrong thing" (*MSE*, Senate Finance Committee, *Investigations*, February 24, 1933, p. 719). The decline in spending and investment since 1929 "could have been prevented by action of the Government which is the only agency which could continue spending money without regard for profit.... Financial fuel is piled up —The Government, and not the bankers, must apply the torch. Motives of public welfare must lead us out of the present depression as greed and war have led the world out of past depressions," Eccles said (*MSE*, written address, October 27, 1933, pp. 2, 4).

II. Compensatory Economics

> The government must be looked upon as a compensatory agency in this economy to do just the opposite of what private business and individuals do. The latter are necessarily motivated by the desire for profit. The former must be motivated by social obligation.
>
> *Eccles, 1936*

By the mid-1930's, Eccles' compensatory policy recommendations were based on a sophisticated macroeconomic analysis which covered the consumption function; the multiplier; a distinction between the relative sizes of the government expenditure and transfer-tax multipliers; leakages and injections; causes of inflation; liquidity trap; velocity; the transmission mechanism of monetary influences; the Phillips curve relationship; the relationships among wage increases, productivity increases, and inflation; the role of inflationary and deflationary expectations; income and wealth distribution effects; the coordination of monetary, fiscal, and incomes policies; and the interrelationships between domestic stabilization policies and international movements of goods and capital. While he was not interested in the construction of a formal model, all of the elements of Keynesian analysis, with the possible exception of the accelerator, may be found in his speeches, letters, and memos.

All policies which came under Eccles' scrutiny were examined for stabilization implications. As an example, Eccles felt that Social Security taxation should be deliberately controlled in a countercyclical fashion, with increases in rates during booms and reductions during depressions. Taxation in general should be used mainly as a means of redistributing income from wealthy individuals and corporations to low- and middle-class consumers who had, Eccles believed, higher marginal propensities to consume. He said in 1933,

> The fundamental economic plans, when they are finally established, will of necessity center in the distribution of purchasing power and in the allocation of income between investment and expenditure.... They will involve relief of taxation that rests on the consumer... [and] the establishment of heavy income taxes especially in upper brackets. They will involve heavy taxation of undistributed corporate surplus, to force corporate income into dividends and taxes. [p. 7]

A good summary statement on compensatory policy was delivered by Eccles in 1935, when he declared his hope that "the inherent instability of capitalism may be corrected by conscious and deliberate use of three compensatory instruments, taxation, varying governmental expenditures, and monetary control.... It should be evident by now," he said, "that simple maxims and rules of thumb are not sufficient" (*MSE*, written address, February 16, 1935, pp. 21–22).

Eccles saw in the instability of capitalism the seeds of destruction; in compensatory policy he saw the mechanism of salvation.

> If we regard capitalism simply as a particular economic organization of society, our defense of, or attack on, that organization must be directed toward its effectiveness—its ability to satisfy in an adequate and equitable fashion the material needs of mankind. If it cannot be defended on these grounds it is doomed.... Private enterprise today is on trial solely because it is not producing the goods it has the capacity to produce and because it is not providing a more equitable distribution of the goods it is producing. [pp. 2–3]

The major threat to capitalism, Eccles believed, lay in the creation of a large group of unemployed. "These people no longer have any stake in preserving our present economy. They have nothing to lose. And if this condition persists...neither you nor I will have anything to lose" (pp. 2–3). "You have got to take care of the unemployed," he told the Finance Committee, "or you are going to have a revolution in this country" (*MSE*, Finance Committee, February 24, 1933, p. 733).

III. Influences

> My own viewpoint has sometimes been erroneously identified with that of Mr. Keynes, doubtless to his embarrassment. *Eccles, 1939*

> I know of no professors whose writings have influenced me. *Eccles, 1949*

Eccles' contention that he arrived at his economic philosophy without having read Keynes (see Hyman, 1951, pp. 131–32) is accepted by his biographers (see Hyman, 1976, p. 128; Dean May, 1981, pp. 53, 58–59; Herbert Stein, 1969, p. 148). He had, in fact, read *something* by Keynes, as he quoted Keynes in 1933 on the difficulty of gaining public acceptance of deficit spending except in wartime (*MSE*, written address, October 27, 1933, p. 8). By this time, however, Eccles' ideas were already well-formulated, and he was actively searching for evidence and confirmation, such as he had found in the writings of Foster and Catchings (Hyman, 1976, pp. 93–94). With this minor exception, Eccles had apparently read nothing by Keynes before he came to Washington as Assistant to Treasury Secretary Morgenthau in 1934. His later exposure to Keynes' works was also limited. As Lauchlin Currie, Eccles' first and most important economic advisor recalls, "[Eccles] never read Keynes' *General Theory*, and he accepted the Keynesian arguments, when I summarized them [in a written review prepared for Eccles in November 1936], as a matter of course. Nothing new!" (Currie to author, letter, August 24, 1983). Eccles claimed to be innocent of any academic influences. "I know of no professors whose writings have influenced me," he stated in 1949 (*MSE*, Eccles to William Merrill, letter, September 22, 1949). The use of the word "professors" is instructive, as Eccles went on to identify eight individuals with whom he worked at the Fed who might "have possibly had some influence on my thinking." Among those were some, Lauchlin Currie, Alvin Hansen, and Richard Musgrave, who had been and/or would be "professors." Musgrave contends that "economists undoubtedly influenced [Eccles'] thinking,...." His discussion of public debt in particular strongly reflects Hansen's position" (Musgrave to author, letter, September 22, 1983). These influences apparently came through the working relationship, rather than through "academic" writings. Evsey Domar recalls that Eccles never came to the Federal Reserve Seminar, which was established during the war with Keynes being the first speaker. "Somehow," Domar writes, "I have the impression that he did not care much for academic economists" (Domar to author, letter, July 6, 1983). Likewise, states Milton Friedman, "the academic world was not influenced by Eccles" (Friedman to author, letter, July 22, 1983). The academic world, however, was very much aware of Eccles' analysis and policy, as is indicated by his correspondence with many prominent economists. Irving Fisher, then Professor Emeritus at Yale, was one with whom Eccles had correspondence on several occasions. Although Fisher had written a very favorable three-part essay on Eccles' views in 1935 (*MSE*, Irving Fisher, "The Mind of Mr. Eccles," 1935, ms.), Eccles did not always agree with Fisher's views. In 1938, for example, Eccles, in a draft reply for Franklin Delano Roosevelt's signature, pointed out the flaws in a plan strongly urged on the president by Fisher to bring about economic recovery by monetizing the float. In submitting the draft, Eccles commented on such plans pressed on the president, and concluded, "I am returning also, with a suggested reply as you requested, the correspondence from Professor Irving Fisher, who is much more intelligent but certainly misled on this point" (*MSE*, Eccles to M. H. McIntyre, letter, June 2, 1938). "If he felt he was right," recalls Currie, "he was not in the slightest impressed by 'authority' to the contrary" (Currie to author, letter, August 24, 1983). This characteristic was evident in his belief, contrary to the opinions and advice of his economists, that the war would be followed by inflation, not deflation.

Quite aside from any influences from economists to which Eccles might have been subjected during the early 1930's or later, the fact remains that he came to a view of the workings of the macroeconomy which was practically unthinkable for one from his background. Eccles attributed the advanced nature of his thinking to the fact that he was a country banker and had not attended college (Stein, p. 485, fn. 47). Currie's explanation is to suggest that "he was what in biology is called a mutation!" (Currie to author, letter, August 24, 1983). Perhaps Eccles' Mormon background preconditioned him to see a role for government in economic planning and a stabilization. Mormon economic policy during the nineteenth century was characterized by strong central direction and control, and Mormon economic institutions blended principles of self-reliance and cooperation.

Whatever the explanation for the evolution of Eccles' ideas on macroeconomic policy, his was a remarkable intellectual accomplishment, and one which has had lasting impact. Musgrave, Eccles' personal assistant from 1944 to 1948, considers Eccles as "a great figure in a crucial period of our history... an extraordinary figure, with a great deal of insight and courage. ... It is easy," writes Musgrave, "to belittle theoretical qualities in a man of action such as Eccles; yet which academic, other than Keynes, was as important in implementing a modern view of macro policy into actual policy measures?" (Musgrave to author, letter, September 22, 1983). Friedman does not exempt even Keynes from the assessment when he states, "I believe [Eccles] played a far greater role in the development of what came later to be called Keynesian policies than did Keynes or any of his disciples" (Friedman to author, letter, July 22, 1983).

Eccles was a paradox: a developer of economic theories who expressed an intense dislike of "theory" and categorically denied being an economist; a "conservative Republican businessman-banker" who served a Democratic president and delighted in pointing out logical flaws and backwardness in the thinking of bankers and businessmen; and a defender of the free-enterprise market economy who believed that only significant government intervention in the economy could save the system.

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