


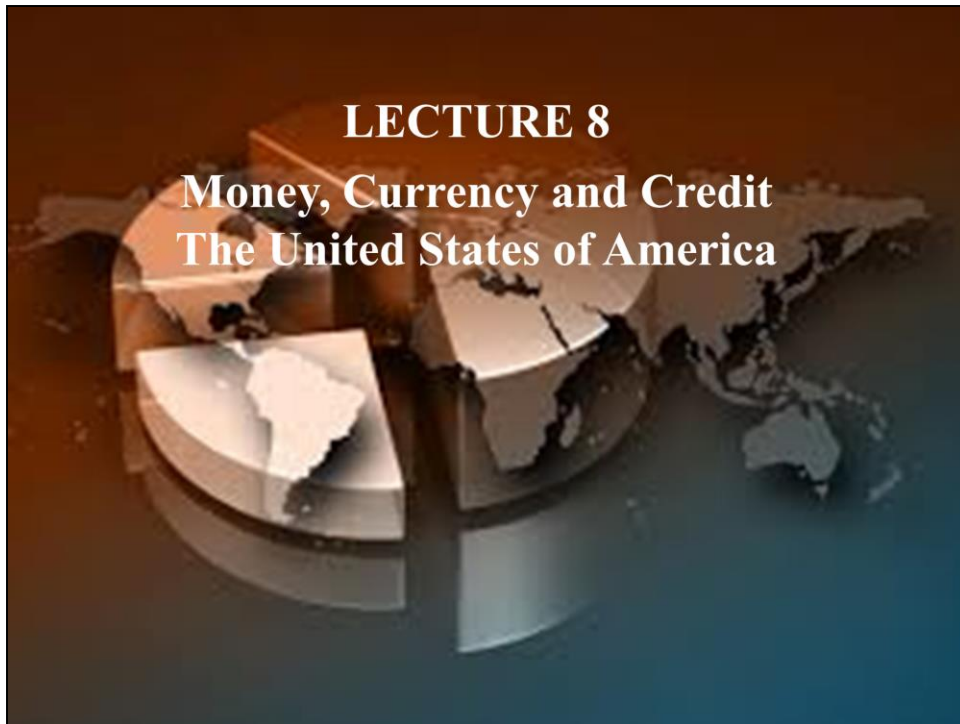
Understanding our Political Economy



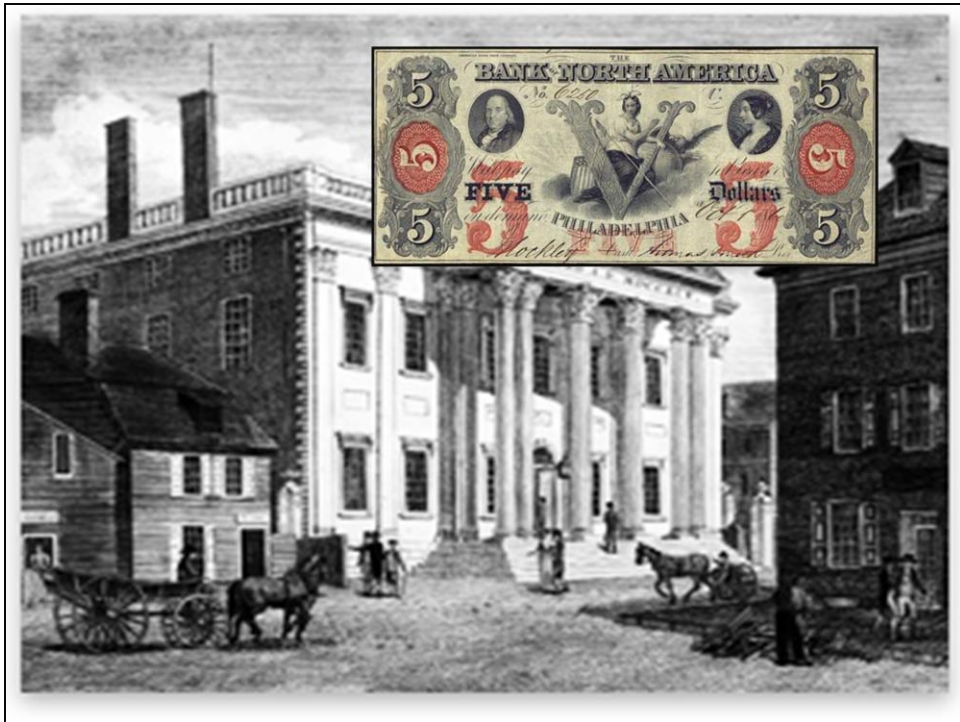
A 3D pie chart with a world map overlay. The pie chart is divided into several segments, with one segment highlighted in a lighter color. The world map is shown in a dark, semi-transparent style, with the continents visible. The background is a gradient of dark blue and brown.

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The experience in the United States of America is worthy of specific examination. There are important lessons to be learned.



Banking came to the newly-formed United States of America in 1781 with the establishment of the Bank of North America.

Robert Morris



The Bank was chartered by the Congress in response to concerns raised by Robert Morris, Superintendent of Finance. The Bank's functions and structure were designed by Alexander Hamilton. The bank was capitalized with loans from the Netherlands and France. In 1785, after the war for independence was over, the Bank's charter was repealed.



In 1791 the *First Bank of the United States* was chartered (for 20 years). The Bank began with a capitalization of \$10 million, \$8 million of which came from private investors responding to the largest initial public offering held to that point in the United States. Importantly, the Bank was authorized to act as the government's fiscal agent.

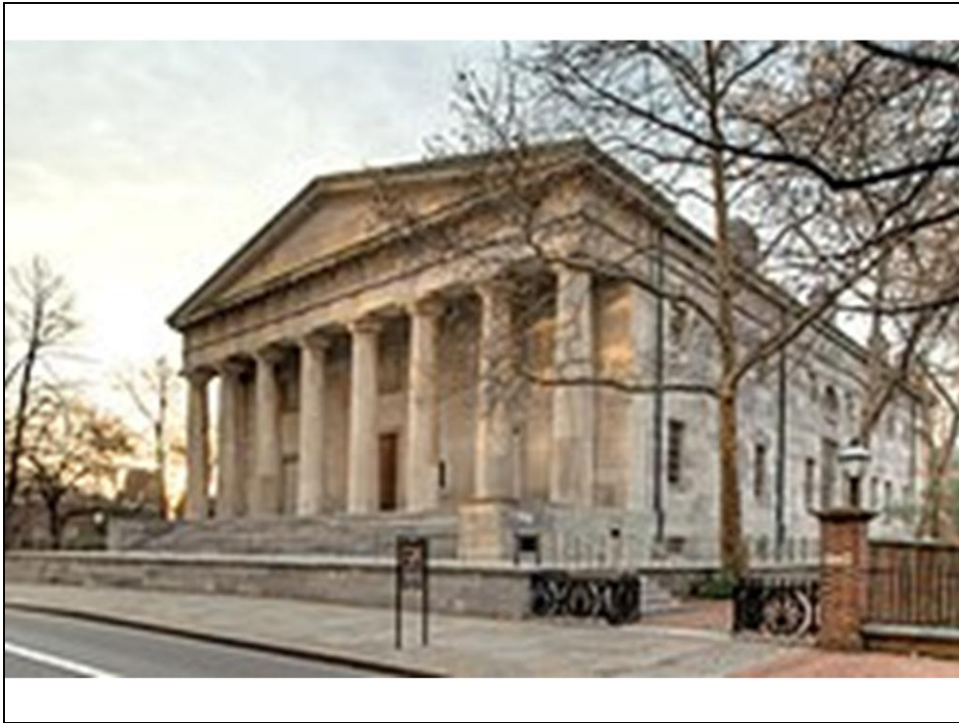


The Bank also functioned as a commercial bank, taking in deposits from the public and making loans to individuals and businesses. The Bank's paper currency entered into circulation primarily by its lending activity. Only the Bank's currency was accepted as payment of federal taxes.

James Swan

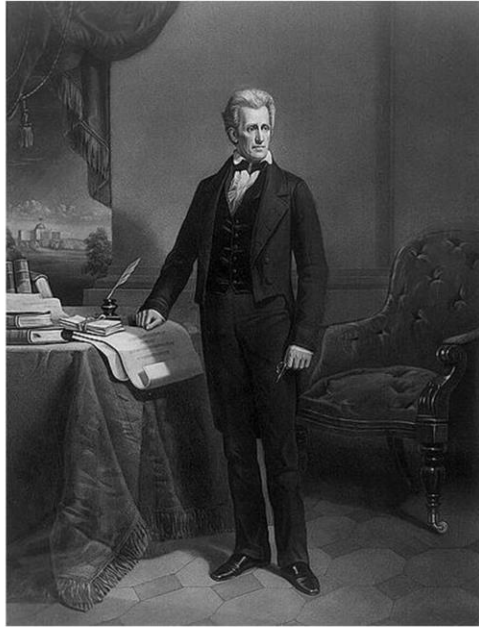


In 1795, the United States government was finally able to settle its debts with the French government, when the Boston-based banker James Swan, acting as an agent for France, negotiated a refinancing of the debt. Swan accepted interest-bearing bonds issued by the U.S. government equal in value to what was owed to the French. He then found investors who purchased shares, using the proceeds to repay the French.



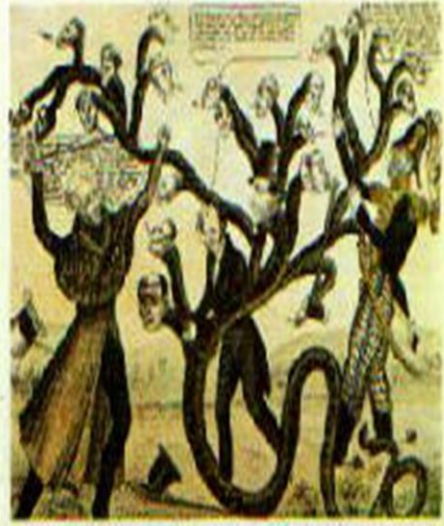
After much debate and several failed attempts by supporters, the Bank's charter was finally issued in February 1816, establishing the **Second Bank of the United States**. Twenty percent of the bank's capital was owned by the federal government. The main branch was on Chestnut Street in Philadelphia, with 25 branch offices scattered around the nation.

Andrew Jackson



The very existence of the Second Bank was perceived by defenders of state sovereignty as an unconstitutional threat. The Supreme Court affirmed its constitutionality in 1819. However, the election of Andrew Jackson to the presidency in 1829 renewed the attack.

Jackson slays the Bank



Jackson ordered all federal deposits removed from the Bank in 1833, and the Bank finally lost its Federal charter in 1836, ceasing operations in 1841. The years to follow were dominated by a decentralized system of state-chartered banks.



People were migrating into the vast North American interior. Currency and credit were desperately needed to meet the needs of the growing economy, and banking interests responded.



After 1816 regulation of banks was left to the states. New banks were subscribed with some specie (i.e., gold coinage), but control over issuance of bank notes was often ineffective. Currency issued by the 700+ state banks was discounted anywhere from 0 to 100 percent based on public confidence in and knowledge of the bank.



Historians disagree on the consequences of this period of minimally-regulated banking. However, some years ago, Alan Greenspan stated in a speech that:

“... more recently, some scholars have suggested that the problems of the free banking period were exaggerated. Retrospective analyses have shown, for example, that losses to bank note holders and bank failures were not out of line with other comparable periods in U.S. banking history.”



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One might naturally raise the issue of whether bank failures and depositor losses have always been high because banks acted not as intermediaries but as money creators.

Edward L. Symons, Jr.



Even so, the story is one filled with many contradictions. One researcher, Edward L. Symons, wrote in 1984:

“In some states, particularly Michigan Where more than forty banks failed before the system was declared unconstitutional, the system is better characterized as a fiasco than a failure.”



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As the United States approached mid-century, the momentum for reform and monetary stability increased. By the onset of the Civil War state banks numbered 1,562.

National Banking Acts of 1863 and 1864

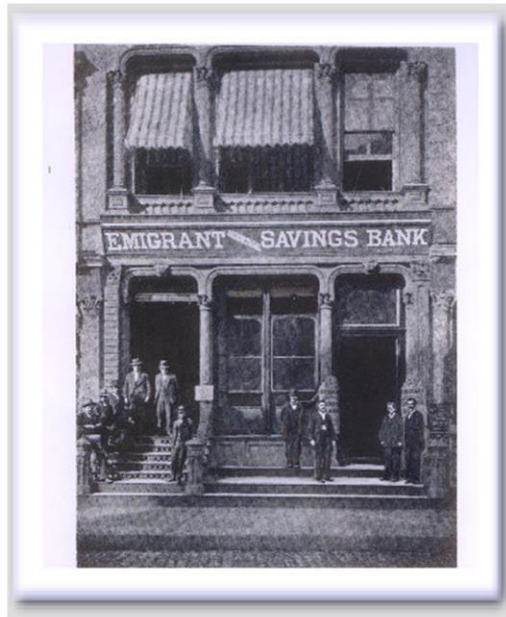


The National Banking Acts of 1863 and 1864 attempted to assert some degree of federal control over the banking system without the formation of another central bank, by creating a system of national banks, a uniform national currency, and an active secondary market for Treasury securities to help finance the Union's war expenses.

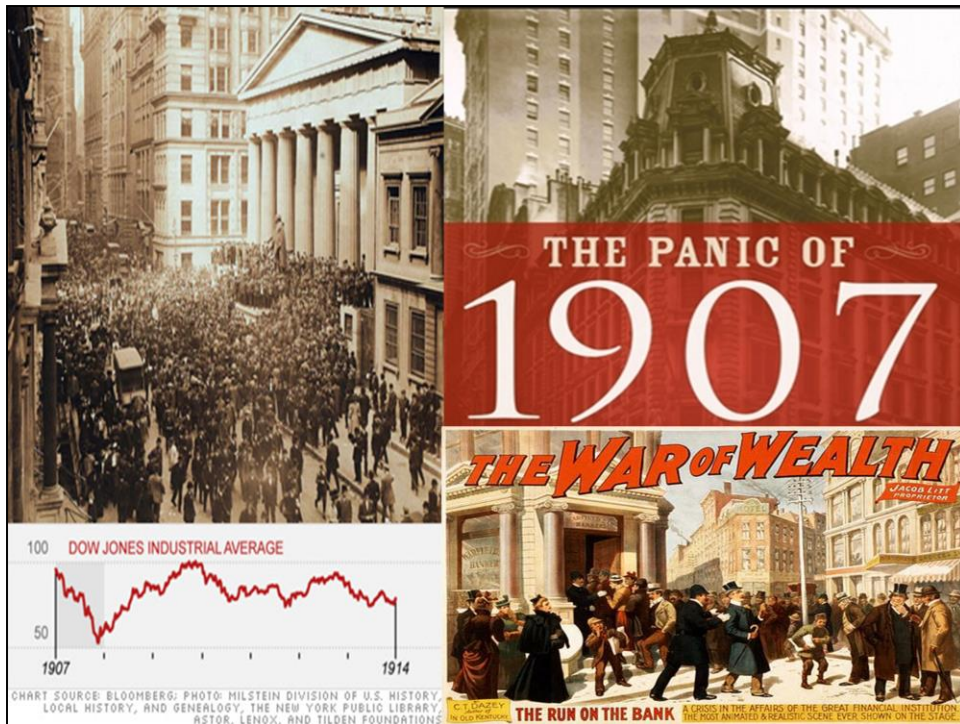
**The number of state-chartered
banks fell to just 325**



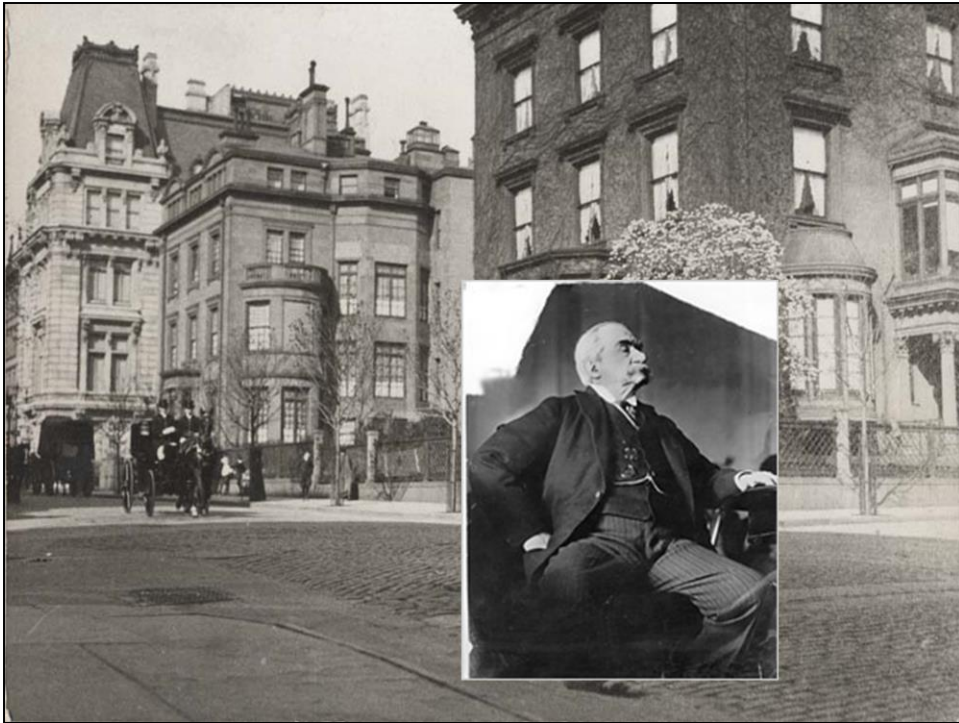
The result was that by 1870 there were 1,638 national banks and only 325 state banks.



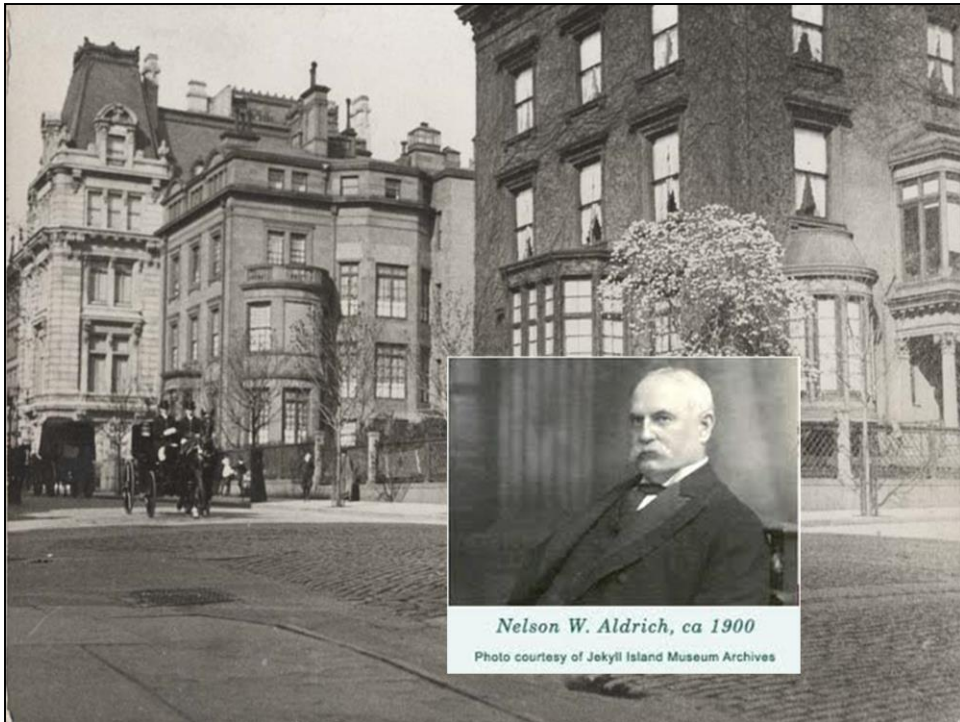
Surviving state banks responded by offering customers checking accounts as a substitute for banknotes. As a result, by 1890 only ten percent of the nation's money supply was in the form of currency. Combined with lower capital and reserve requirements, as well as the ease with which states issued banking charters, state banks again became the dominant banking structure by the late 1880's.



The banking system limped along until the Wall Street Panic of 1907. Speculative bubbles in the real estate and the stock markets burst. Several long-standing New York banks failed. The unemployment rate reached 20 percent in the fall of 1907. Millions lost their deposits as thousands of banks collapsed across the nation.



The panic ended only after J.P. Morgan intervened. Morgan, personally, made temporary loans to key New York banks and other financial institutions.



In 1908, Senator Nelson W. Aldrich established and chaired a commission to investigate the crisis and propose future solutions.



Woodrow Wilson won the Democratic party's nomination for President in 1912, defeating Theodore Roosevelt who ran as a Progressive. In his acceptance speech Wilson warned against the "money trusts," and advised that:

**“ ... a concentration of
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After taking office, Wilson signed legislation to reform the nation's currency system. The Federal Reserve System was the result.



Despite Woodrow Wilson's stated desires, the bankers ensured the new Federal Reserve System operated as a regulated private system and not as a government agency. The Federal Reserve Act established a system of eight to twelve mostly autonomous regional Reserve Banks that would be owned by commercial banks and whose actions would be coordinated by a committee appointed by the President.

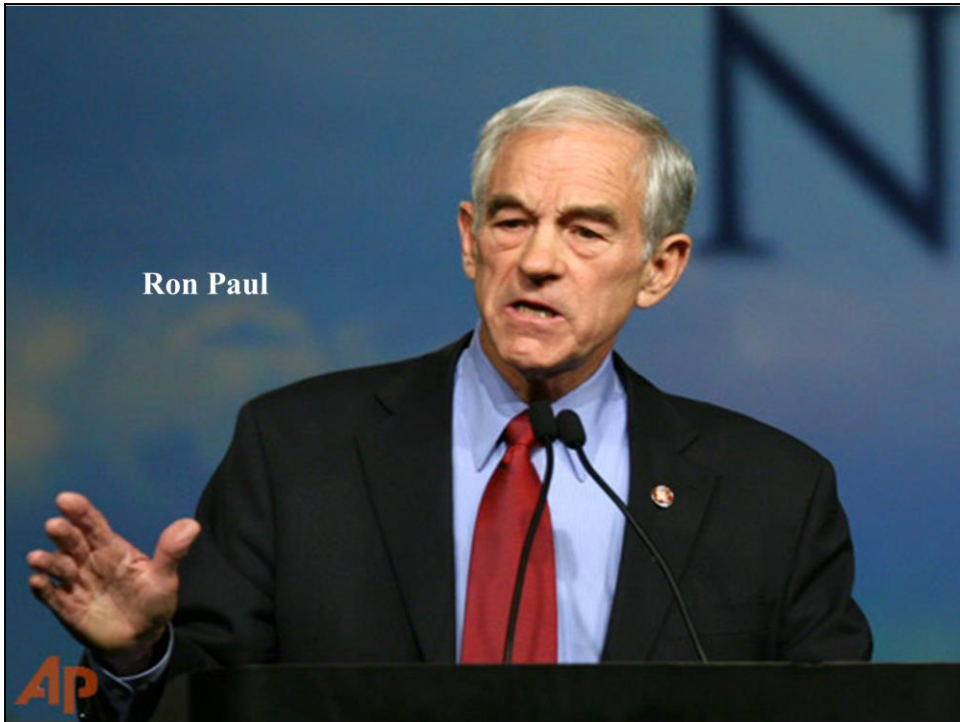


From inception, the Federal Reserve System had its harsh critics, including at the time Congressman Charles Lindberg, who argued:

“The Act establishes the most gigantic trust on earth. When the President signs this Bill, the invisible government of the monetary power will be legalized. ...The greatest crime of the ages is perpetuated by this banking and currency bill.”



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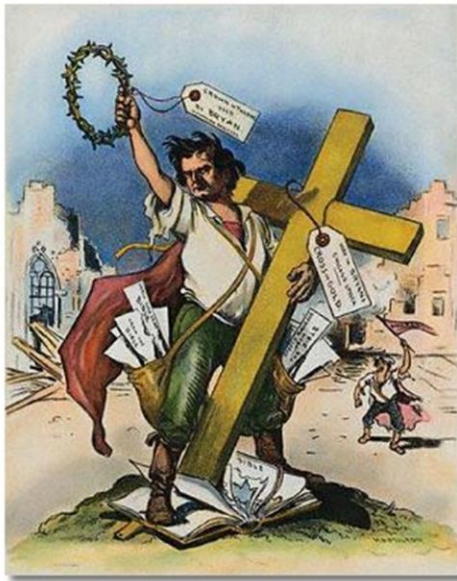
In recent decades, U.S. Representative Ron Paul of Texas has called for its dissolution, writing:

“Since the creation of the Federal Reserve, middle and working-class Americans have been victimized by a boom-and-bust monetary policy. In addition, most Americans have suffered a steadily eroding purchasing power because of the Federal Reserve's inflationary policies. This represents a real, if hidden, tax imposed on the American people.”



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Argument is ongoing over whether the Board of Governors of the Federal Reserve System has too much or too little power, or whether its very existence causes monetary instability.



The battle between silver and gold interests came to a head with William Jennings Bryan's "Cross of Gold" campaign.

Legislation passed in 1873 embraced the *gold standard* and demonetized silver. Mining interests and “westerners” unsuccessfully fought against this measure. Enter the Democrat William Jennings Bryan onto the stage.

William Jennings Bryan



And, in Bryan the westerners found their champion.



Bryan called for bimetallism. Campaigning for the Presidency in 1896, Bryan delivered his famous “No Cross of Gold” speech, in which he declared:

**“...if protection has slain its
thousands, the gold
standard has slain its tens of
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A major part of the debate over reform is whether the issuance of currency should be fully privatized or made the responsibility of government.



Stephen Zarlenga

Stephen Zarlenga, who founded the American Monetary Institute in 1996, extensively researched the history of money and banking and credit. In a speech he delivered in 2004, he brought up the problem created by mainstream economists:

"One reason economists have failed mankind so badly is their poor methodology – an over-reliance on theoretical reasoning. Alexander Del Mar the world's greatest monetary historian noted: *'As a rule economists...don't take the trouble to study the history of money; it is much easier to imagine it and to deduce the principles of this imaginary knowledge.'*"



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Stephen Zarlenga believed we should:

Nationalize the Federal Reserve System

Reconstitute the Fed within the U.S. Treasury, to become a fourth branch of government

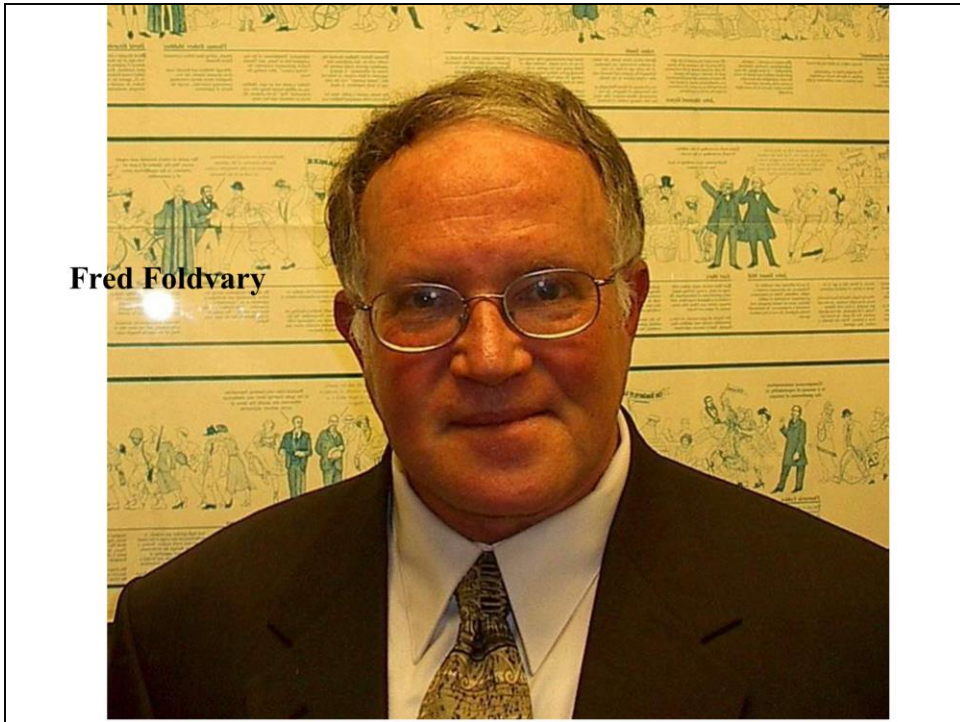
Restrict the creation of money to the Federal government



(a) Nationalize the Federal Reserve System; (b) Reconstitute the Fed within the US Treasury, to eventually evolve into a fourth branch of government, on a par with the executive, judicial and legislative branches; and (c) Restrict the creation of money to the Federal government. This last recommended reform is one that Henry George would certainly have supported.



At the opposite end of the reform spectrum is the proposal to once again permit “free banking.” Any banking entity could issue its own banknotes. Market forces would be relied upon to control the supply of banknotes and the quantity and form of reserves required to meet demands for specie by depositors. Reserves would be in the form of gold, silver or possibly other scarce commodities with a stable value.



Fred Foldvary, who taught economics at Santa Clara University, believed free banking would work very efficiently and with little corruption. He wrote as follows:

“... The artificial increase in money supply can be halted permanently by implementing free banking. Without a central bank and a national currency imposed on the economy, inflation of the money supply beyond the growth of the economy is no longer feasible, since there is no longer a monopoly of the money supply.”



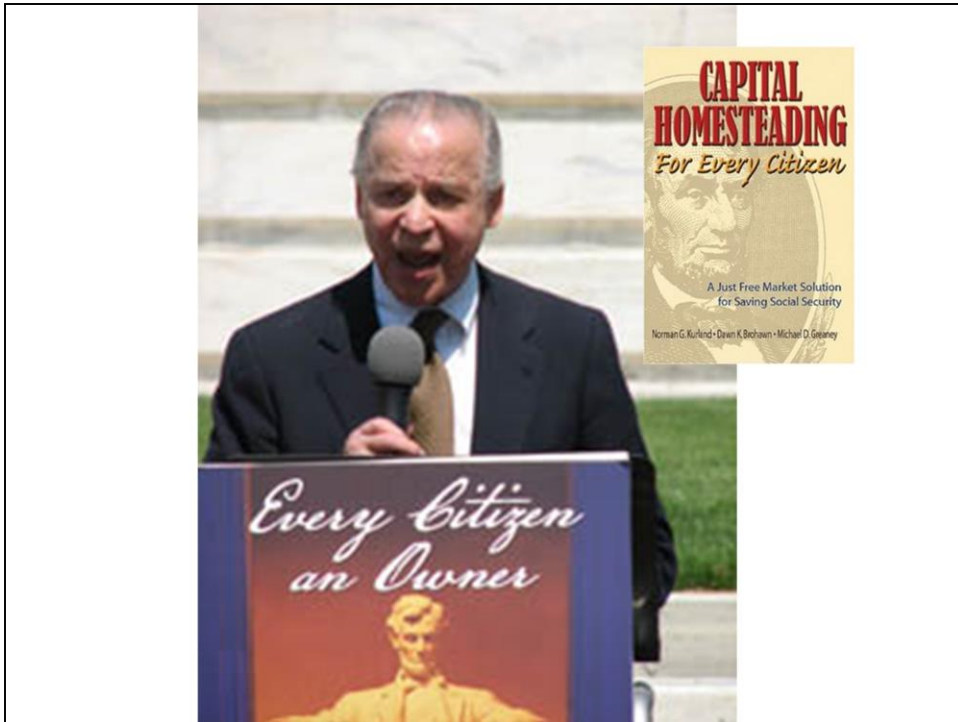
From: The Science of Economics, Chapter 12

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Norman Kurland



And, a somewhat different approach was advocated by the Center for Economic and Social Justice, a Washington, DC-based organization headed by Norman Kurland, who was a long-time associate of and collaborator with Louis Kelso, the person most responsible for legislation creating Employee Stock Ownership Plans.

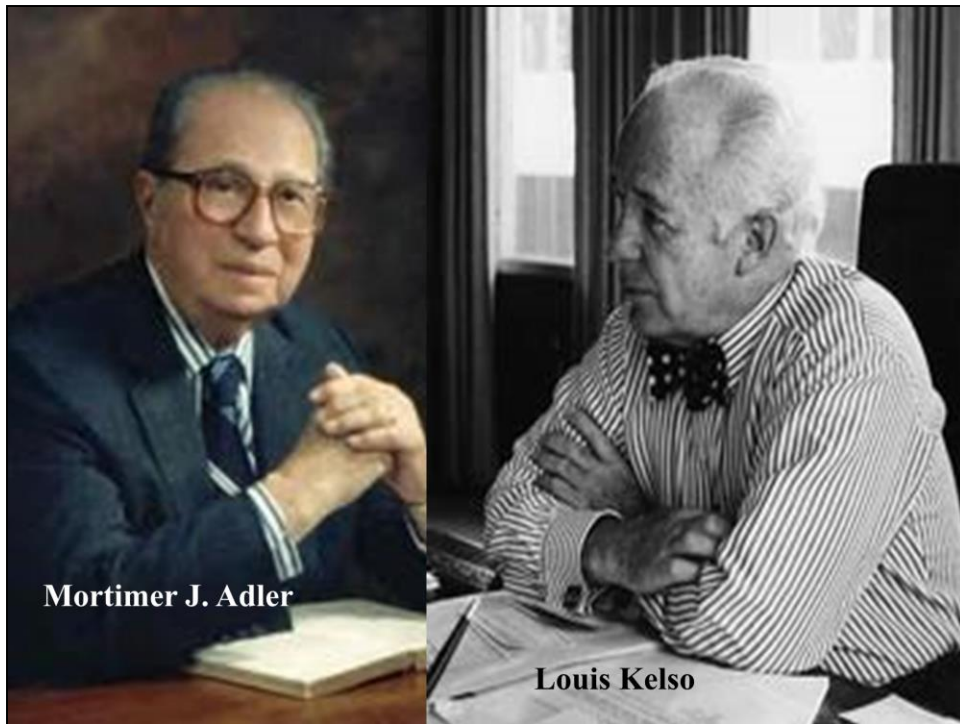


What Kurland and others advocated is a society where every person derives income from the ownership of shares of stock. To make this a reality, his organization lobbied for passage of a Capital Homestead Act, which he described as follows:

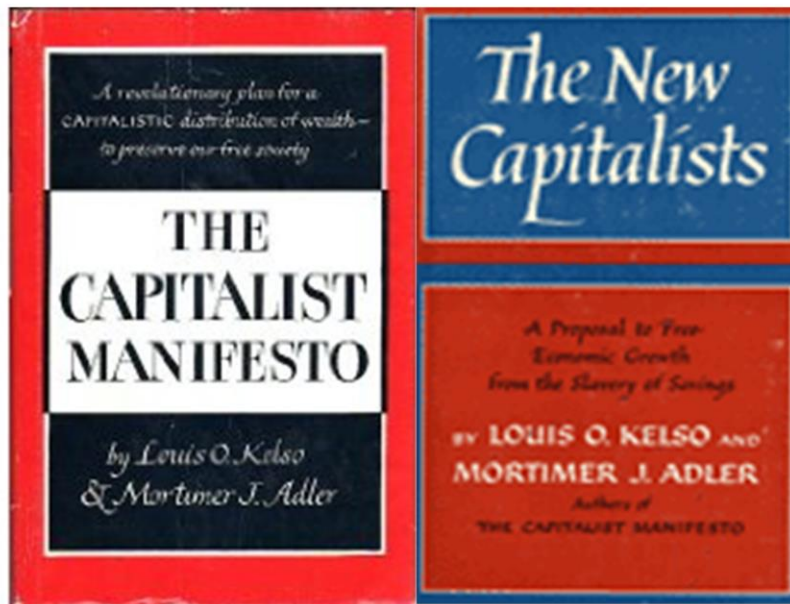
“The Capital Homestead Act's central focus is the democratization of capital (productive) credit. By universalizing citizen access to direct capital ownership through access to interest-free productive credit, it would close the power and opportunity gap between today's haves and have-nots, without taking away property from today's owners.”



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Back in the late 1950s, the philosopher Mortimer J. Adler teamed up with attorney Louis Kelso to write a sharp critique of the American economic system. In two books -- *The Capitalist Manifesto* and *The New Capitalists* -- they developed their program of universal capitalism.



In the preface to *The Capitalist Manifesto*, Mortimer Adler explains that the ideas on economics are those developed by Louis Kelso, but which he came to embrace. His primary concern had been on how to preserve and nurture democracy. He wrote:

“In the twenty years or more in which I have been developing a theory of democracy as the only perfectly just form of government, I slowly came to realize that political democracy cannot flourish under all economic conditions. ...”

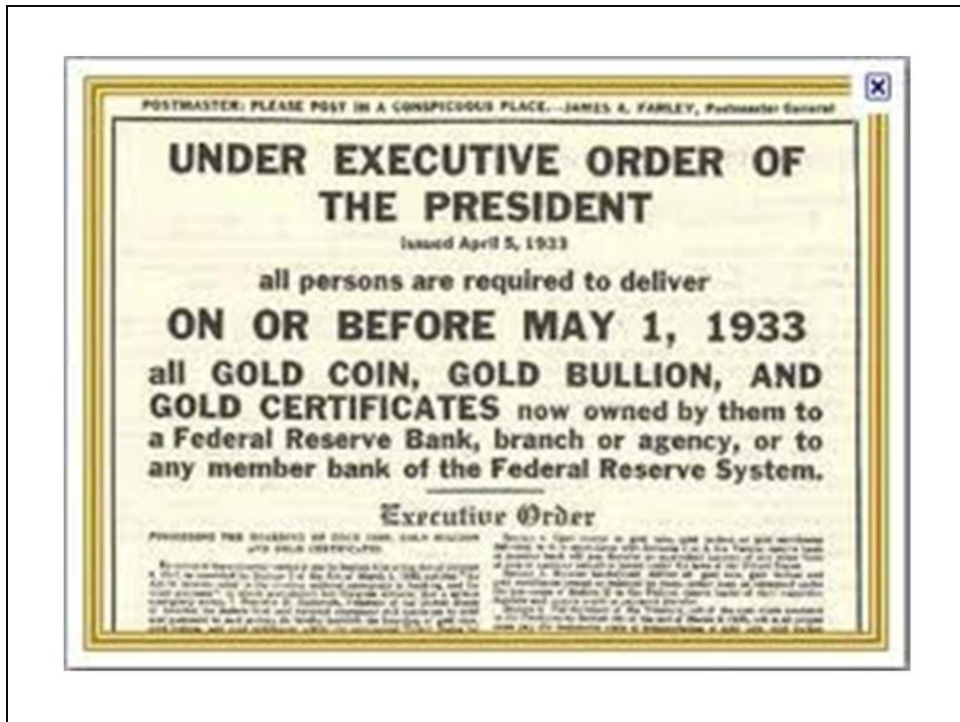


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One way for government to try to stabilize its economy is to exert direct control over the monetary system. In 1933, the United States government took the dramatic step of closing down the gold market and ending its commitment to redeem gold certificates.



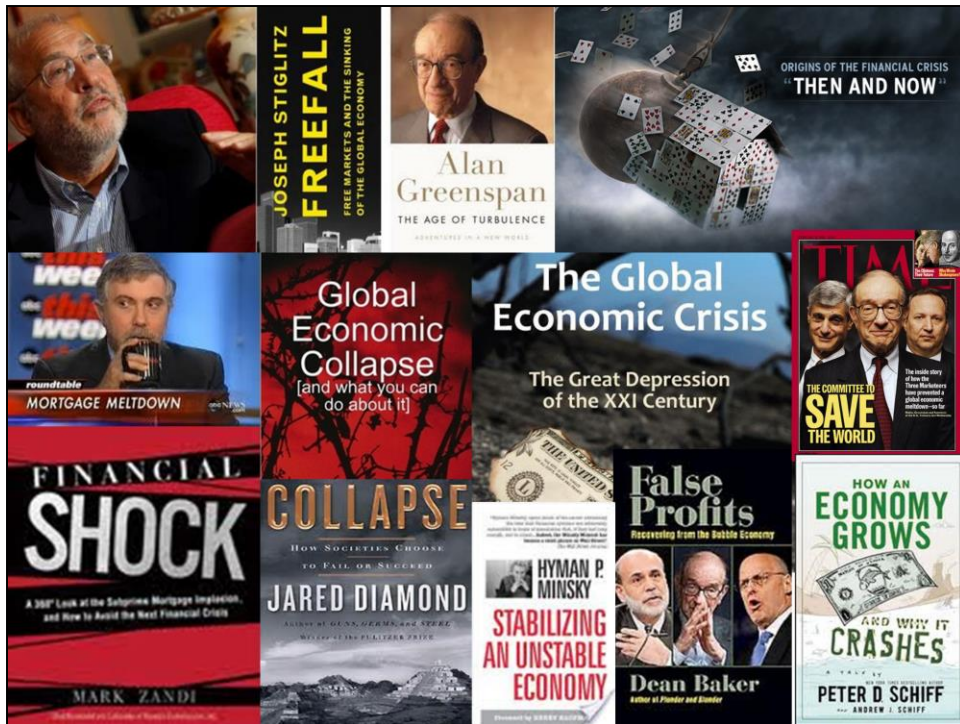
Which leads us into a discussion of the causes of economic recessions and depressions. Monetary reformers have focused on the roles played by money, banking and credit. However, as we will soon discuss, Henry George concluded the causes were even more basic.



A fundamental question is whether that portion of the economy engaged in financial transactions adds to the production of actual wealth or merely results in its redistribution. Is there a loser for every winner?



Beginning in the 1970s, political leaders in the United States and their economic advisers committed the nation to a long process of deregulation of the financial services sector and a reliance on supposed competitive forces to discipline the activities of individual players.



Now that the global economy is poised to experience yet another systemic failure (forecasted to occur in 2026 by those who have studied the cyclical history of land and property markets), an almost endless list of analysts have offered their interpretation of what happened and why.



The widespread fraud that characterized the subprime mortgage loan business of the late 1990s and early 2000s became apparent when borrowers failed to make even the first payment due on their loans. The nation's property markets had again overheated and then crashed. They were credit-fueled and speculation driven. The Federal Reserve's response was textbook: do all that could be done to convince investors and potential buyers that property prices would recover and climb to new heights. Reducing mortgage interest rates to less than 3 percent did the trick.



And, here is the perfect metaphor for where this has brought us!

END OF LECTURE 8

