SEARCH FOR A STABLE CURRENCY

IV. Marriner Eccles: The Federal Reserve Board

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MANY factors influence prices. Immediately after V-J Day, American government economists feared that the end of the war would bring a period of unemployment. As they saw it, we needed to create "buying power" to replace the buying power represented by the demands of the war.

Increasing wages seemed to be an obvious way of putting buying power into the hands of the public. But, for the moment, the economists failed to realize that increased wages would be reflected in increased prices. This is particularly true when the demand for goods is great and the supply of money is greater than the supply of goods.

Because World War II was financed in large part by the sale of bonds rather than by increased taxes, the supply of money was great. The excess supply was due to the fact that federal reserve dollars were issued to pay for war goods. After the goods had been used up, the money remained.

After the war was over, goods were scarce and money was plentiful. Naturally, prices increased, and this increase called for the second and third round of wage increases.

> That wide fluctuations in the price level are disastrous is beyond question and determined efforts should be made to prevent such fluctuations as would endanger economic stability . . . the broader objective of maximum sustainable utilization of the Nations' resources cannot be achieved by attempting to maintain a fixed level of prices, and . . . price stability should not be the sole or principal objective of monetary policy.

This paragraph, taken from a statement made to the Senate Committee of Agriculture and Forestry in August, 1937, marks the wide deviation between the theories of Marriner Eccles, on the one hand, and "Coin" Harvey, Irving Fisher and George F. Warren, on the other. All three of the latter were primarily concerned with creating and maintaining a stable price level as a means of stabilizing the national economy. "Coin" Harvey believed that stabilization would result from the addition of silver to the gold basis of the currency. Irving Fisher believed that the dollar could be stabilized by continual adjustment of its gold content in line with the Bureau of Labor Statistics' index numbers. George Warren followed Fisher's line of argument, although he recognized more clearly the importance of other factors in determining price levels.

Like these men, Eccles was and is primarily interested in improving economic stability in the United States. But his basic attitude toward economics is far different, partly because his background has been far different.

Marriner S. Eccles was born on September 9, 1890. His father had arrived in America from Scotland at the age of 14 without any means of support. When he died he left an estate worth several millions of dollars. During his lifetime he had developed exceptionally successful enterprises in the West, and we may assume that the young Eccles lived comfortably.

Marriner Eccles graduated from Brigham Young College in 1909 and following his graduation the young Mormon began to take part in family affairs. After his father's death in 1912, Eccles took charge of these affairs and became a successful businessman and banker. Before he took public office, he had become president of the First Security Corportion, owning and operating 26 banks in Utah and southern Idaho. Eccles was also, according to his biographer, president and treasurer of the Amalgamated Beet Sugar Company, president of the Sego Milk Products Company, president of the Utah Construction Company, president of the Stoddard Lumber

Company and director of two chain retail companies. He was also a member of the governor's executive relief committee and a director of the Salt Lake Branch of the Reconstruction Finance Corporation.

Marriner Eccles first took public office in 1934, when he became assistant to the Secretary of the Treasury. In November, 1934, Franklin D. Roosevelt appointed him a member and Governor of the Federal Reserve Board, following the resignation of Governor Eugene R. Black. On February 1, 1936, Eccles took office as Chairman of the Board of Governors of the Federal Reserve Board.

As Chairman of the Federal Reserve Board under the late President Roosevelt, Eccles gained a reputation as a "New Dealer and advocate of the unusual in banking." The "United States News," noting that he was "as allergic to inflation as to depression," termed Eccles "unorthodox" and noted on more than one occasion that the administration, and particularly the Treasury, was afraid of Eccles' power over the nation's economy.

At least partly because Treasury officials were afraid that Eccles might let the price of government bonds fall, he was replaced as Chairman of the Board on February 6, 1948, and demoted to the rank of Vice Chairman.

The career and philosophy of Marriner Eccles are of special interest because his active life has been concerned both with depression in the 1930's and, later, with inflation in the 1940's and 1950's. Much of Eccles' basic philosophy was, however, fashioned during the years of depression. Although he discounted the role played by a stable currency, he recognized that "control over money is a matter of national concern that must be retained by the sovereign power or delegated by it to an agency of its own creation. . . ." He added, also, that "control over the supply of money . . . involved under existing conditions a control over the volume of bank deposits and bank credits."

Nonetheless, Eccles firmly discounted the quantity theory of money, first discussed in this series in the article on Coin Harvey (See *Current History,* February, 1951). According to Banker Eccles, prices cannot be stabilized by regulating the quantity of money in circulation.

> Those who favor such proposals, he wrote in 1939, believe that prices can be raised by increasing the supply of money, that prices can be lowered by reducing the supply of money and that prices can be kept fairly steady by changing the supply of money in the right direction at the right time. They believe that, if prices were kept fairly steady, we would not have booms, depressions, and panics, business would run along on an even keel, and much suffering and hardship would be prevented.
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> Experience has shown, however, that (1) prices cannot be controlled by changes in the amount and cost of money; (2) the Board's [F. R. B.] control of the amount of money is not complete and cannot be made complete; (3) a steady average of prices does not necessarily result in lasting prosperity and (4) a steady level of average prices is not nearly as important to the people as a fair relationship between the prices of the commodities which they produce and those which they must buy.

However, Eccles believed, prices were controlled neither by the amount or the cost of money. This belief is directly contradictory to Harvey's and Fisher's contention that the amount and cost of gold determined fluctuating prices. Currency, Eccles went on to note, does not control prices:

> There was $3,600,000,000 of currency in the hands of the public, outside the banks, in the middle of 1926, and about the same in the middle of 1929, while at the end of 1938 the amount of currency had increased to $5,700,000,000. If prices were governed by the amount of currency, prices would have been about the same in 1929 as in 1926 and would have increased sharply by the end of 1938. The facts are that the average of wholesale prices, expressed in an index number, was 100 in 1926, 95 in 1929 and 77 in 1938.

Of course, Eccles continued, currency is obviously not the principal means used by people in paying for what they buy: "more than nine-tenths of the bills in this country are paid by checks drawn on bank deposits."

> Therefore the deposits that the public holds in banks and can use as a means of paying for what it buys, as well as the currency outside of banks, need to be considered as money. Again the facts show clearly that the volume of money does not control the price level.
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> The amount of money [including demand deposits] therefore, was larger in 1929 than in 1926 and larger in 1938 than in 1929. But what happened to prices? In 1929 they were five per

> cent lower than in 1926, and in 1938 they were 23 per cent lower than in 1926. This proves that factors quite apart from the volume of money, i.e., of currency and deposits together, were influencing the price level.

According to Eccles, those who believe that the quantity of money in circulation influences prices are simply mistaken:

> There have been times when the amount of money and prices have changed together; but usually they have not. When they have moved together, this may have been due to the fact that it takes more money to do the same amount of business when prices are high than when prices are low.

Such a theory is far too simple, the banker believed.

> Whether prices and the volume of money do or do not move together depends on many other conditions, such as weather and the size of harvests, inventions, foreign trade, Government spending, taxes, wages and the general attitude of business.

"Usually," concluded Eccles, "other things have a greater influence on prices than has the amount of money."

"Neither do prices depend on the cost of money," he continued.

> This also has been shown by the experience of the last ten years. The cost of money now is lower than it has ever been at any time for which we have a record. This is true not only of the rate at which the Government can borrow, and of the rate at which large corporations can get money in the money market, but also of the rate charged by banks to their regular customers. . . . During this period when the cost of money was so drastically cut, prices went down by about one-fourth.

IS STABILITY DESIRABLE?

In other words, according to Eccles, stabilization of the price level could not be achieved by manipulating the quantity or the cost of money in circulation. Furthermore, Eccles maintained, a stable price level might not even be desirable.

> The principal difficulty with a stable price level as the objective of economic policy is that it is not in itself a satisfactory indicator of a continuously smooth working of the economic machine. There have been periods in the past when the price level was stable and nevertheless there were developing numerous maladjustments which led to an economic collapse. For example, from the latter part of 1927 to the latter part of 1929 the index of wholesale prices showed little change, but other events were threatening economic stability. Prices and activity on the stock market were rising rapidly and brokers' loans grew at an unprecedented rate. Construction of office and apartment buildings was being promoted with a view to quick profits at a rate that endangered the long-time outlook in the building industry. Loans were being made for enterprises abroad without careful investigation of credit risks, and business activity was increasing, partly as a result of speculative developments, to a level that could not be sustained. The use of the commodity price level as a guide to credit policy in these circumstances would have been entirely unsatisfactory. There is no assurance that it would be satisfactory in the future.

". . . Furthermore," he continued:

> In periods of rapid advance disparities between prices of different groups of commodities generally become more pronounced and yet, both from the point of view of justice and of economic stability, the most important thing in regard to prices is the maintenance of proper relationships between prices of different commodities that are exchanged for each other.

In 1938, a bill was considered by Congress providing for government ownership of the Federal Reserve Banks, and making it one of the duties of the Federal Reserve Board "to stabilize and maintain a dollar of uniform purchasing power for the purpose of assuming the kind of dollar which a generation hence will have the same purchasing power and debt-paying power. . . ."

This Eccles and his fellow-members on the Board opposed wholeheartedly. In a statement at hearings of the Committee on Banking and Currency of the House of Representatives, Eccles pointed out that:

> No matter what the Federal Reserve does in the future, and no matter what it has done in the past, it will always be on the spot. . . . You have in the country your debtor and your creditor classes. Your debtor classes as a general rule want inflation, so that they can pay debts with cheaper dollars, and your creditor class wants the opposite, and neither of them is ever thoroughly satisfied with the purchasing power of the dollar.

Eccles saw the danger of deflation during the 1930's and he also at that time foresaw the danger of inflation. Speaking at a bankers' meeting in 1936, he declared that:

> It is just as important to bankers that deflation be prevented as it is that inflation be prevented. . . . Deflation, if anything, is more destructive to bankers than inflation. They are twin evils, and both should be prevented, if possible. . . . If we expect to maintain stability or reasonable stability of business, we must find ways and means of maintaining a more uniform flow or velocity than we have had in the past.

What, asked Eccles at that time, is the reason for deflation? Reasoning from findings of the Brookings Institution, he noted:

> As to income distribution and its results, we found . . . the proceeds of the nation's productive effort going in disproportionate and increasing measure to a small percentage of the population—in 1929 as much as 23 per cent of the national income to one per cent of the people. We found the unsatisfied wants—needs according to any good social standard—of the 92 per cent of all families who are now below the level of $5,000 annual income, sufficient to absorb the product of all our unused capacity under present conditions of productivity and still demand much more from such unexplored potentialities as might hereafter be opened up.
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> We found the incomes of the rich going in large proportion to savings and these savings strongly augmented by others impounded at the source by corporations through the practice of accumulating corporate surplus. These savings . . . we found spilling over into less fruitful or positively harmful uses.

Eccles concludes these observations:

> Thus, we begin to discern the answer to our question whether the basic defect in our economic system, not discovered in the technical processes of production, is to be found in the ways in which we conduct the distribution of income. The answer is affirmative: this is the place at which we do find basic maladjustments.

And this maladjustment, Eccles believed, could not be overcome merely by stabilizing prices. Full employment for labor, he felt, would be a much more helpful step. Eccles' attitude toward labor, and labor's role in economic stability, is often misunderstood. In an address to Harvard Business School Alumni in 1939, Eccles declared that:

". . . our greatest domestic problem—the major task before the nation—is to find productive employment for all of our people capable of working who are now unable to find employment."

At the same meeting, the banker re-iterated his sympathy for labor:

> I fully realize the importance both from the social and the economic point of view of having continuous employment of labor at as high a real wage as the national income will permit. . . . But the first requirement for a satisfactory labor policy is responsible and not conflicting leadership of labor itself. Furthermore, wage advances must in general correspond to and be paid out of increased productivity of labor. It is obvious from an economic point of view that there is no other continuous source out of which increased labor costs can be met.

LABOR POLICIES

Eccles then attacked, as he had before, the "monopolistic advantages and practices of certain minority labor groups. . . ."

Two years before, in 1937, Eccles had warned of the danger of raising wages and shortening hours as a means of ending the depression, because this policy would result in limiting or reducing production.

> Wage increases and shorter hours are justified and wholly desirable when they result from increasing production per capita and represent a better distribution of the profits of industry. When they retard and restrict production and cause price inflation, they result in throwing the buying power of the various groups in the entire economy out of balance, working a particular hardship upon agriculture, the unorganized workers, the recipients of fixed incomes and all consumers. The upward spiral of wages and prices into inflationary price levels can be as disastrous as the downward spiral of deflation.

Eccles did not spare big business, however, in his search for factors which unbalanced the economy. In his 1939 speech to Harvard Business School Alumni, he declared:

> The policies of many of our large industries to meet a decline in demand by radical curtailment of output, while leaving prices at high levels, results in accentuating depressions. . . . Better planning of production and price

> policies by business concerns with reference to more than the short-time garnering of profits would do much to reduce violent fluctuations in business.

The tendency of monopolies to restrict production and to keep prices high was attacked by Marriner Eccles on more than one occasion.

Throughout, Eccles seems to be impressed with something that approaches a "fair" or "just" value for money. He attacks monopoly either of business or of labor if monopolistic practices are used to increase wages or prices while decreasing output.

This, of course, is based on the importance of money as a medium of exchange. From it, Eccles must inevitably get into a theory of value. But at present economists do not want to tamper with prices based on any "theory of value."

As Eccles points out, we try to maintain the status quo. As soon as we try to upset the status quo, we must have a reason for our action. It is of little avail for one group (labor) to attack another (industry) if the inevitable answer is "you are doing the same thing."

As Eccles also brings out, farmers want to see "parity" maintained. Manufacturers want greater profits. Labor wants more wages. The government wants to help all of them. But all this results in high and higher prices.

Eccles grapples with this dilemma in very general terms:

> In order to provide for the maximum possible elasticity in our economy so that there will be no obstructions to the income flow, we must find means of controlling monopolistic and other uneconomic practices both by industry and by labor.

Full employment and better planning of production were two of the means through which Eccles felt that depression could be combated. Believing that "economic stability rather than price stability should be the general objective of public policy," Eccles called attention to other major policies of the Government "which influence business activity, including particularly policies with respect to taxation, expenditures, lending, foreign trade, agriculture and labor."

> The process of everyone getting out of debt, of course, means deflation. We have never had an expansion of business activity except with an expansion of debt. Our whole capitalistic system is built upon a system of debit-creditor relationship, and if everyone proceeded on the theory of getting out of debt and having a rainy day reserve to meet a depression, our insurance companies would certainly have no place to loan the insurance premiums that are paid in to them. . . . In a business recession debt is extinguished. That is what tends to create the recession.

It is interesting to study Eccles' statements of the 1930's and compare them with his policies in the 1940's. Even during the depression, as we noted above, Eccles warned against inflation as a "twin danger." In a recent article in "Fortune," Eccles has described inflation:

> Inflation is a grave injustice and a serious danger to our free economy. It injures most the aged, the pensioners, the widows and the disabled, the most helpless members of our society. It diminishes the desire to work, to save and to plan for the future. It causes unrest and dissension among the people and thereby weakens our productivity and hence our defense effort. It imperils the existence of the very system that all of our efforts are designed to protect.

INFLATIONARY DANGERS

As Chairman of the Board of Governors of the Federal Reserve Board, Eccles began to publicize his views on the inflationary danger shortly after the end of the war. In June of 1947, he was disturbed by the rise in the volume of consumer credit to a record level well over $10,000,000,000. True, he recommended the end of temporary controls on installment credit, but this recommendation was based on his belief that such controls should not "rest indefinitely in peacetime on emergency or war powers after the Congress has had ample opportunity to consider the subject." He asked for permanent controls of installment credit from Congress, instead.

By October of that same year, it was reported that bankers were under official pressure to tighten up on lending, and Eccles once again was the principal advocate of this policy. At this time Eccles noted once again the expansion of loans and investments of commercial banks (at a rate equal to $10,000,000,000) and called attention to the end of controls on consumer credit on November 1. Speaking of credit expansion, Eccles warned:

> . . . if this should continue it would provide an inflationary force more than double the anti-inflationary effect of the prospective surplus in the federal budget. . . . It would equal the inflationary impact of the unprecedented surplus of exports over imports in this country's foreign trade during recent months.

Eccles believed at this time that the roots of the post-war inflation lay in the money supply and credit policy of the federal government, especially easy loans for housing, excessive government spending, and too small a Treasury surplus. He wanted Congress to give the Federal Reserve Board the power to require member banks to set up "special reserves," to reduce their ability to expand loans.

Because of Eccles' bold attack on government fiscal policy and his tremendous influence over the members of the Board, the Treasury feared that Eccles might let the price of government bonds drop below face value. Since 1942, the Board has been under committment by the Treasury to peg the price of federal securities in the market by buying in the market whenever necessary. Largely because Eccles opposed this policy, he was replaced as Chairman of the Board by Thomas B. McCabe in February, 1948, but although he was demoted to the post of vice chairman, he did not resign.

In 1948, this "stormy figure of the New Deal" began to warn even more frankly of trouble ahead, declaring that "bust we must." During that year, the Federal Reserve Board pegged the price of government securities and pumped out money to feed the inflation. Eccles declared promptly that the Federal Reserve Board had become "simply an engine of inflation."

In the article Eccles wrote for "Fortune" in November, 1950, he attacked the system which forces the F.R.B. to supply reserves "at the will of the market."

> If the Federal Reserve had complete freedom in its open market operations, it could refrain from buying securities during inflationary periods and let prices decline until the market is self-supporting.

This the government is not willing to do because of the "huge size and cost of carrying the public debt," and the "difficult refunding problem when there are widely fluctuating interest rates."

Although Eccles did not believe, in 1934, that decreased purchasing power was responsible for the depression, he does believe, today, that "the amount of money available is excessive."

> There is no limit to the amount of money that can be created by the banking system, but there are limits to our productive facilities and our labor supply, which can be only slowly increased and which at present are being used to near capacity.

To this extent at least, Eccles today is coming around to a belief in the quantity theory of money. We seem to have created enough paper money so that this fact alone is a major factor in our continually rising prices.

To protect the dollar today, according to Eccles, the government must institute a spartan tax program, providing for a "pay as you go" financing of present preparedness plans. In addition, he would like to see the Federal Reserve Board empowered to set higher interest rates if it considers such action necessary. This is at the root of Eccles' controversy with Secretary Snyder of the Treasury and with administration fiscal policy in general.

THE DOLLAR PROBLEM

Eccles, however, takes a broader view of the dollar problem than merely the domestic one. The dollar problem, he believes, is not only an American problem, but a European problem as well, and in the long run our economy cannot be stabilized without taking this into account. Actually, Eccles notes, we face several dilemmas. Internationally, we preach the virtues of free economy; domestically, we contradict this.

At home, for example, we are ready to distort the meaning of "full employment" to maintain the status quo, that is, "to guarantee that all firms now in existence and every worker employed by those firms must be kept doing what they are now doing."

Eccles calls attention to the "propping up" going on in all sectors of our economy: agri-