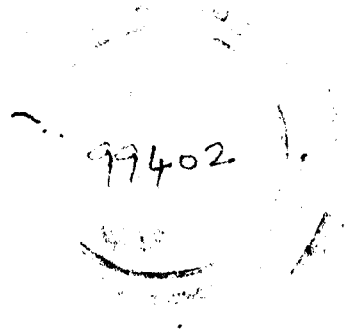


PROCEEDINGS
OF THE
ACADEMY OF POLITICAL SCIENCE

Volume XV
1932-1934

EDITED BY
PARKER THOMAS MOON

THE ACADEMY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY
NEW YORK
1934



COPYRIGHT BY
THE ACADEMY OF POLITICAL SCIENCE

JL
W m 78, N15
N34-15

CONTENTS

	PAGE
No. 1. The Crisis in World Finance and Trade	
I. THE BREAKDOWN IN WORLD TRADE	
<i>Seligman, Edwin R. A.</i>	The Breakdown in World Trade 3
<i>Rogers, James Harvey.</i>	Foreign Credits and International Trade 6
<i>Williams, John H.</i>	The Effect of Currency Depreciation on International Trade 13
<i>Schneider, Franz, Jr.</i>	The Economic Position of the Raw Material Industries 20
<i>Orton, William.</i>	Tariffs and the Movement of Goods 27
<i>Beckhart, B. Haggott.</i>	
<i>Molyneux, Peter.</i>	
<i>Rife, Raleigh.</i>	
<i>Müller, Gardiner H.</i>	
<i>de Garrahl, Charles F.</i>	
<i>Rogers, James Harvey.</i>	
<i>Meeker, Royal.</i>	
<i>Fulton, James A.</i>	
	} Discussion: The Breakdown in World Trade . 33
II. REPARATIONS AND WAR DEBTS	
<i>Houghton, Alanson B.</i>	Reparations and War Debts 51
<i>Altschul, Frank.</i>	The Need for a New Approach to an Old Problem 53
<i>Colby, Bainbridge.</i>	Should War Debts Be Cancelled? 65
<i>Isely, Charles C.</i>	Political Debts of All Nations and Their Relation to Depressed Agriculture 73
<i>Kiep, O. C.</i>	The Basis of German Credit 84
<i>Morgan, Shepard.</i>	The Political Aspects of War Debts and Reparations 94
<i>Wadsworth, Eliot.</i>	
<i>McGuire, Constantine E.</i>	
	} Discussion: Reparations and War Debts 104
III. WORLD ORGANIZATION IN FINANCE AND TRADE	
<i>Cravath, Paul D.</i>	World Organization in Finance and Trade ... 113
<i>Walcott, Frederic C.</i>	How Much Can the Government Help? 115
<i>Stamp, Sir Josiah.</i>	Control or Fate in Economic Affairs 123
	iii

No. 2. Steps Toward Recovery

PAGE

<i>Burgess, W. Randolph.</i>	Introductory Address	141
<i>Chandler, Henry A. E.</i>	Federal Reserve Policy and the Problem of Fugitive Gold	143
<i>Jay, Pierre.</i>	The Structure of the Banking System	151
<i>Brand, Robert H.</i>	International Monetary Problems	162
<i>Douglas, Lewis W.</i>	Economy in Federal Government	172
<i>McAneny, George.</i>	Economy in State and City Government	178
<i>Noyes, Alexander Dana.</i>	Discussion: Monetary and Fiscal Policies	189
<i>Warren, Robert B.</i>		
<i>Adams, Thomas S.</i>	Introductory Remarks	196
<i>Reynolds, Jackson E.</i>	The Railroad Problem	197
<i>Buckland, Edward Grant.</i>	The Problem of Unemployment	207
<i>Wolman, Leo.</i>	The Agricultural Problem	214
<i>Murphy, Frederick E.</i>	Tariffs and Trade Barriers in Relation to International Trade	224
<i>Roorbach, George B.</i>	Discussion: Major Problems of Readjustment	235
<i>Christensen, Chris L.</i>	Introductory Remarks	239
<i>Houghton, Alanson B.</i>	Primary Steps for Banking Reform	240
<i>Lamont, Thomas W.</i>	World Agriculture and Disarmament	251
<i>Astor, Viscount.</i>	Steps Toward Recovery	253
<i>Strawn, Silas H.</i>	Steps Toward Recovery	266
<i>Salter, Sir Arthur.</i>		

No. 3. Tariffs and Trade Barriers

I. TRADE BARRIERS IN THE WORLD DEPRESSION

<i>Burgess, W. Randolph.</i>	Introduction	277
<i>Williams, John H.</i>	The United States Tariff and Our International Financial Position	278
<i>Angell, James W.</i>	Exchange Depreciation, Foreign Trade and National Welfare	285
<i>Parker, G. R.</i>	Import Quotas and Other Factors in the Restriction of Trade	297
<i>Dickinson, L. J.</i>	The Relation of the Agricultural Problem to Tariffs	303
<i>Auld, George P.</i>	Discussion: Trade Barriers in the World Depression	311

PAGE

II. PROCEDURE IN TARIFF MAKING

<i>Morgan, Shepard.</i>	Introduction	315
<i>Coulter, John Lee.</i>	The Tariff Commission and the Flexible Clause	317
<i>Rogers, James Grafton.</i>	Reciprocity and the Most-Favored-Nation Clause	328
<i>Day, Edmund E.</i>	Tariff Bargaining	338

III. INTERNATIONAL COLLABORATION

<i>Reynolds, Jackson E.</i>	Introduction	345
<i>Layton, Sir Walter T.</i>	International Cooperation in the Economic Crisis	347
<i>Luther, Hans.</i>	International Cooperation	361

No. 4. Current Problems of Unemployment and Recovery Measures in Operation

I. CURRENT PROBLEMS OF UNEMPLOYMENT AND RECOVERY MEASURES IN OPERATION

<i>Young, Owen D.</i>	Introduction	369
<i>Wolman, Leo.</i>	The Outlook for Unemployment Insurance in the Codes	371
<i>Beveridge, Sir William H.</i>	Lessons for the Present from British Experience with Unemployment	378
<i>King, Stanley.</i>	Unemployment Reserves and Insurance Programs	385
<i>Richberg, Donald R.</i>	Progress under the National Industrial Recovery Act	393
<i>Sloan, George A.</i>	A Necessary Foundation for Stabilized Employment	401
<i>Filene, Edward A.</i>	Discussion: Current Problems of Unemployment and Recovery Measures in Operation	407
<i>Beveridge, Sir William H.</i>		
<i>Marburg, Louis C.</i>		
<i>Sloan, George A.</i>		
<i>Sands, George.</i>		
<i>Richberg, Donald R.</i>		
<i>Honigman, J. Leo.</i>		

II. SCIENTIFIC PROGRESS, THE SHORTER WEEK AND UNEMPLOYMENT

<i>Teagle, Walter C.</i>	The Recovery Program in Operation	412
<i>Butler, Harold B.</i>	Social Aspects of Scientific Progress	419
<i>Slichter, Sumner H.</i>	Implications of the Shorter Hour Movement	431
<i>Harriman, Henry I.</i>	Discussion: Recovery Measures in Operation	444
<i>Hopkins, Harry L.</i>	Unemployment Relief and the Public Works Administration	449

III. LONG-RANGE PLANNING

<i>Swope, Gerard.</i>	Planning and Economic Organization	452
<i>Roper, Daniel C.</i>	Long-Range Planning	459
<i>Steel-Maitland, Sir Arthur.</i>	Long-Range Planning	469

PROCEEDINGS
OF THE
ACADEMY OF POLITICAL SCIENCE

Volume XV

MAY, 1932

[No. 1

THE CRISIS IN WORLD FINANCE
AND TRADE

A SERIES OF ADDRESSES AND PAPERS PRESENTED AT THE SEMI-ANNUAL
MEETING OF THE ACADEMY OF POLITICAL SCIENCE
APRIL 13, 1932

EDITED BY
PARKER THOMAS MOON

THE ACADEMY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY
1932

COPYRIGHT BY
THE ACADEMY OF POLITICAL SCIENCE

CONTENTS

	PAGE
PREFACE	v
I THE BREAKDOWN IN WORLD TRADE	
THE BREAKDOWN IN WORLD TRADE	3
<i>Edwin R. A. Seligman</i>	
FOREIGN CREDITS AND INTERNATIONAL TRADE	6
<i>James Harvey Rogers</i>	
THE EFFECT OF CURRENCY DEPRECIATION ON INTERNATIONAL TRADE	13
<i>John H. Williams</i>	
THE ECONOMIC POSITION OF THE RAW MATERIAL INDUSTRIES	20
<i>Franz Schneider, Jr.</i>	
TARIFFS AND THE MOVEMENT OF GOODS	27
<i>William Orton</i>	
DISCUSSION: THE BREAKDOWN IN WORLD TRADE.	33
<i>B. Haggott Beckhart, Peter Molyneaux, Raleigh Rife, Gardiner H. Miller, Charles F. de Garrahl, James Harvey Rogers, Royal Meeker, James A. Fulton</i>	
II REPARATIONS AND WAR DEBTS	
REPARATIONS AND WAR DEBTS	51
<i>Alanson B. Houghton</i>	
THE NEED FOR A NEW APPROACH TO AN OLD PROBLEM.	53
<i>Frank Altschul</i>	
SHOULD WAR DEBTS BE CANCELLED?	65
<i>Bainbridge Colby</i>	
POLITICAL DEBTS OF ALL NATIONS AND THEIR RELATION TO DEPRESSED AGRICULTURE	73
<i>Charles C. Isely</i>	
THE BASIS OF GERMAN CREDIT	84

	PAGE
THE POLITICAL ASPECTS OF WAR DEBTS AND REPARATIONS.	94
<i>Shepard Morgan</i>	
DISCUSSION: REPARATIONS AND WAR DEBTS.	104
<i>Eliot Wadsworth, Constantine E. McGuire</i>	
III WORLD ORGANIZATION IN FINANCE AND TRADE	
WORLD ORGANIZATION IN FINANCE AND TRADE	113
<i>Paul D. Cravath</i>	
HOW MUCH CAN THE GOVERNMENT HELP?	115
<i>Frederic C. Walcott</i>	
CONTROL OR FATE IN ECONOMIC AFFAIRS	123
<i>Sir Josiah Stamp</i>	

PREFACE

IF the present economic crisis had been confined within the boundaries of any one nation, this volume would not have been needed, for the causes and cure of the business depression would have been discoverable without investigation beyond the national frontier. In fact, however, the depression is world-wide, the crisis international. Our economic malady is not endemic, but epidemic; it has infected every continent and has grown more virulent as it has spread. Any realistic attempt, therefore, to diagnose the disease or to prescribe remedies must take account of the international complications which have made the actual economic disturbance so far-reaching, so severe, so cumulative. It is to these international complications that the Academy of Political Science devoted its Semi-Annual Meeting, of which the present volume is a record containing the papers and addresses in full, together with summaries of the discussion from the floor. This discussion of international aspects of "The Crisis in World Finance and Trade" may well be read in connection with previous numbers of the Academy's PROCEEDINGS in which various local or national aspects of the economic débâcle were studied, notably the issues intitled "Business, Speculation and Money", "Depression and Revival" and "Can Prices, Production and Employment Be Effectively Regulated?".

The Semi-Annual Meeting (Fifty-second Year) of the Academy of Political Science was held at the Hotel Astor in New York City on April 13, 1932. The program was as follows:

PROGRAM*First Session*

Wednesday, April 13, 1932, 10 A. M.
North Ballroom, Hotel Astor

Topic: The Breakdown in World Trade

PROFESSOR E. R. A. SELIGMAN, *Presiding*
Professor Emeritus of Political Economy in Residence,
Columbia University

1. *Foreign Credits and International Trade.*

JAMES HARVEY ROGERS, Professor of Political Economy,
Yale University.

2. *Effects of Currency Depreciation on International Trade.*

JOHN H. WILLIAMS, Professor of Economics, Harvard
University.

3. *The Economic Position of the Raw Materials Industries.*

FRANZ SCHNEIDER, JR., Vice President, Newmont Mining
Corporation, New York, former Financial Editor of
the New York Sun.

4. *Tariffs and Their Effect on the Movement of Goods.*

WILLIAM ORTON, Professor of Economics, Smith College,
Northampton, formerly member British Ministry of
Labor.

5. *Discussion under the ten-minute rule.*

B. HAGGOTT BECKHART, Professor of Banking, Columbia
University.

PETER MOLYNEAUX, Editor and Publisher, *The Texas
Weekly*, Dallas.

Second Session

Wednesday, April 13, 2:15 P. M.
North Ballroom, Hotel Astor

Topic: Reparations and War Debts

The Hon. ALANSON B. HOUGHTON, *Presiding*

Former United States Ambassador to Germany and to Great
Britain and President of the Academy of Political Science

1. *Reparations and War Debts—The Need for a New Approach to
an Old Problem.*

FRANK ALTSCHUL, of the Firm of Lazard Frères, New York.

2. *Should War Debts Be Cancelled?*

The Hon. BAINBRIDGE COLBY, former Secretary of State.

3. *Political Debts of All Nations and Their Relation to Depressed
Agriculture.*

CHARLES C. ISELY, Lumber and Grain Merchant, Dodge
City, Kansas.

4. *The Basis of German Credit.*

DR. O. C. KIEP, German Consul General, New York.

5. *The Political Aspects of War Debts and Reparations.*

SHEPARD MORGAN, Vice President, Chase National Bank;
former Finance Director, Office for Reparation Pay-
ments, Berlin.

6. *Discussion under the ten-minute rule.*

The Hon. ELIOT WADSWORTH, former Assistant Secretary
of the Treasury; former Secretary of the World War
Foreign Debt Funding Commission.

CONSTANTINE E. MCGUIRE, Economist, Washington, D. C.

Third Session**Semi-Annual Dinner Meeting**

Wednesday, April 13, 7 P. M.
Grand Ballroom, Hotel Astor

Topic: World Organization in Finance and Trade

PAUL D. CRAVATH, *Presiding*

The Hon. FREDERIC COLLIN WALCOTT

United States Senator from Connecticut, Chairman of the
Sub-Committee to Investigate Operations of the Stock
Exchange.

Sir JOSIAH STAMP, G.B.E., LL.D.

President of the London, Midland and Scottish Railway
Company; a Director of the Bank of England; a Gov-
ernor of the London School of Economics and Political
Science; formerly a British representative on both the
Dawes and Young Reparations Committees.

For the convenience of readers who were unable to attend
the interesting sessions at the Hotel Astor, brief biographical
sketches of the speakers on the program are given here in
alphabetical order.

FRANK ALTSCHUL is a banker and a profound student of
economic and financial conditions. He was born in San Fran-
cisco in 1887. After taking his degree at Yale he rose very
rapidly in the financial world, and is now a member of the
firm of Lazard Frères, bankers, of New York City. Among
the other important financial posts filled by Mr. Altschul only
a few may be mentioned here—member of the Governing
Committee of the New York Stock Exchange, President of the

General American Investors Company and of the Second General American Investors Company, Inc., director and member of the executive committee of the American International Corporation, director of the International Bank of Amsterdam and of several industrial and insurance companies. During the World War he served with the A.E.F. He is a Chevalier of the Legion of Honor and a member of the Cercle Interallié, Les Cent Bibliophiles, and Le Livre Contemporain.

B. HAGGOTT BECKHART is an expert on banking and international finance. He is now Associate Professor of Banking at Columbia University. In 1929 he collaborated with Professor H. Parker Willis in editing an important volume on *Foreign Banking Systems*. He is the author of *The Banking System of Canada* and *The Discount Policy of the Federal Reserve System*.

BAINBRIDGE COLBY, distinguished lawyer and former Secretary of State, was born in St. Louis, graduated from Williams College, studied law at Columbia and at the New York Law School, and began the practice of law in New York City in 1892. He was one of the founders of the Progressive Party in 1912 and was prominent among the leaders of that party. During the World War he served on the United States Shipping Board and the Emergency Fleet Corporation; he was also a member of the American Mission to the Inter-Allied Conference at Paris in November 1917. During the last year of the Wilson Administration he held the post of honor in the Cabinet as Secretary of State, and subsequently he was associated with Woodrow Wilson in the practice of law.

PAUL D. CRAVATH, one of the most eminent of American lawyers, is a native of Ohio and a graduate of Oberlin. He studied the law at Columbia University and was admitted to the bar in 1886. During the World War he was intimately concerned with inter-Allied finance; he represented the United States Treasury on the "House Mission" to the Inter-Allied War Conference at Paris in 1917; and in 1918 he served as advisory counsel of the American Mission to the Inter-Allied Council on War Purchases and Finance, in London and Paris. In recognition of "exceptionally meritorious conduct and

services during the war" he was awarded the D.S.M. by General Pershing.

ALANSON B. HOUGHTON, President of the Academy of Political Science, is Chairman of the Board of the Corning Glass Works. He served in Congress for a time, but resigned in order to represent the United States abroad, first in Berlin as Ambassador to Germany from 1922 to 1925, then in London as Ambassador to Great Britain from 1925 to 1928.

CHARLES C. ISELY is a distinguished citizen of Kansas, a spokesman for the "pig and wheat raiser", and a lumber and grain merchant of Dodge City. In the words of the *Emporia Gazette*, he "is recognized as an independent thinker among other independent minds in the country. He has gained this recognition through the power of a good set of brains. Incidentally he is a candidate for the United States Senate, staggering under the terrible handicap of those same brains."

DR. O. C. KIEP, German Consul General in New York City, was born in Scotland, and received his education partly in Glasgow, partly in London, partly in Germany. He holds the degree of LL.B. from the University of London as well as that of D. Jur. from the University of Leipzig. After serving with distinction in the World War, he entered the German diplomatic service and attended the chief international conferences—Versailles, Genoa, London, Locarno, Geneva—from 1919 to 1926. He had charge of the press bureau at the Foreign Office for a time. From 1927 to 1931 he was Counselor of the German Embassy at Washington, and in 1931 he accepted the post of Consul General in New York.

CONSTANTINE E. MCGUIRE, keen student of international economic problems, had just returned, shortly before the Academy meeting, from a sojourn in Europe, where he had been engaged in study of the economic situation and in conferences with experts and officials. Among Dr. McGuire's numerous publications, the volume on *Germany's Capacity to Pay* (of which he was joint author with Dr. Moulton) and the subsequent book on *Italy's Economic Position* are most pertinent to the subject which he discussed at the Semi-Annual Meeting, viz., "Reparations and War Debts".

PETER MOLYNEAUX is an eloquent spokesman for the Southern cotton-grower. Born in New Orleans, grandson of a Confederate soldier, he has spent his life in Louisiana and Texas. For nine years he was chief editorial writer of the Fort Worth *Star-Telegram*. He is now editor and publisher of *The Texas Weekly*.

SHEPARD MORGAN is Vice-President of the Chase National Bank. In the period of the Dawes Plan Mr. Morgan served in Berlin as Economic Adviser to the Transfer Committee and later as Finance Director, Office for Reparation Payments. He went to Paris at the instance of the Chairman of the Committee of Experts in 1929 and drafted the sections of the Young Plan dealing with the Bank for International Settlements, which, after consideration by the appropriate subcommittee, the main committee adopted in its report. He later participated in the final work on the Statutes of the Bank at Baden-Baden and The Hague.

WILLIAM ORTON was born in England and educated at Cambridge. During the World War he served with the British army in Gallipoli, in Egypt, in France; he was wounded in the Battle of the Somme. After the war he resumed his studies, taking degrees at Cambridge and at the University of London, and serving at the same time as staff officer of the industrial relations department in the Ministry of Labour. He was called to this country in 1922 to fill the chair of economics at Smith College. He has written a book on *Labor in Transition* and has contributed numerous articles to periodicals. His article on "The Meaning of the Gold Crisis" in the February *Atlantic Monthly* has been widely read and commented upon.

JAMES HARVEY ROGERS is the author of a recent and challenging volume, *America Weighs Her Gold*. He had taught economics at the University of Missouri only a year when his academic career was interrupted by the World War. After the war, resigning his commission in the army, he returned to teaching at Missouri, then at Cornell, then at Missouri again, and, since 1930, at Yale, as Professor of Economics. In his books on *Stock Speculation and the Money*

Market (1927), *The Process of Inflation in France* (1929), and *America Weighs Her Gold* (1931), and in his section on "Foreign Markets and Foreign Credits" in the *Report on Recent Economic Changes*, he has made significant contributions to the special study of money, credits, inflation, and their effect on trade.

FRANZ SCHNEIDER, JR., Vice President of the Newmont Mining Corporation, is well known as a financial writer. He was financial editor of the New York *Evening Post* from 1920 to 1925, and subsequently of the New York *Sun*. He has been connected also with the American International Corporation and the National Securities Company. During the World War he was attached to the General Staff with the rank of major.

EDWIN R. A. SELIGMAN, former McVickar Professor of Political Economy at Columbia University and now Professor Emeritus in Residence, presided at the Morning Session. Although he has laid aside the burden of academic duties, Professor Seligman has not retired into well-deserved inactivity. Very recently he published a new volume (with the collaboration of R. H. Love) on *Price Cutting and Price Maintenance*. Volume by volume the monumental *Encyclopaedia of the Social Sciences*, of which he is Editor-in-Chief, continues to appear. A complete list of the public and academic services he has rendered, of the honorary degrees and decorations he has received, and of his published works would fill twenty pages or more. His *Essays on Taxation* have gone through ten editions, his *Principles of Economics*, twelve editions, and at least nine of his books have been translated into foreign languages.

SIR JOSIAH STAMP is preëminent as an economist and at the same time as a practical man of affairs. As a Director of the Bank of England, as Chairman of the London, Midland and Scottish Railway, as former Secretary and Director of Nobel Industries, Ltd. and as Director of Imperial Chemical Industries, he has played a conspicuous rôle in the actual conduct of business in Great Britain. He has likewise rendered very distinguished public service in the domain where government and

economics overlap. He was one of the British representatives on the international committee which drafted the Dawes Plan and also on the committee which subsequently devised the Young Plan, and he has served on an impressive number of official committees concerned with British economic and financial problems. He and Professor Seligman were colleagues on the League's committee of experts on double taxation. Sir Josiah has managed to combine his business and public responsibilities with a brilliant academic career, which began at London University and pursued its way through honors and prizes to a place in the Senate of London University (1924-1926), vice-chairmanship of the London School of Economics, governorship of several colleges, presidency (1930-1932) of the Royal Statistical Society, chairmanship of the Rockefeller Social Science Advisory Committee, and many other posts of distinction. Among his numerous writings are volumes on *The Wealth and Income of the Chief Powers* (1919), *Fundamental Principles of Taxation* (1921), *Wealth and Taxable Capacity* (1922), *The Financial Aftermath of War* (1931), *Internationalism* (1931), *Papers on Gold and the Price Level* (1931), *Taxation during the War* (1932).

ELIOT WADSWORTH was a member of the firm of Stone and Webster, electrical engineers, from 1907 to 1916. During the next decade he served the American Red Cross as Vice-Chairman of the Central Committee, later as national treasurer. He was also Assistant Secretary of the United States Treasury, 1921-1925, and Secretary of the World War Foreign Debt Funding Commission during the years when the inter-Allied debt agreements were being made. He represented the United States at Paris in 1923 in negotiations for the settlement of the cost of the American Army of Occupation.

FREDERIC COLLIN WALCOTT was a successful investment banker and a director or officer of numerous corporations, when the World War began. While America was still neutral he engaged in Belgian and Polish Relief work. From 1917 to 1919 he was a member of the United States Food Administration. Retiring in 1922 from an active business career, he presently interested himself in Connecticut politics, serving two terms in the state Senate. In 1928 Connecticut elected

him to the United States Senate. He has recently served as chairman of the Senate's subcommittee to investigate operations on the New York Stock Exchange.

JOHN H. WILLIAMS has taught economics at Harvard since 1921, with the exception of a year spent in Italy as Westinghouse Exchange Professor. His volume on Argentine commercial and currency problems, some years ago, was awarded the Wells prize. In 1919 he inaugurated the important series of *Annual Studies of the Balance of Payments of the United States*. He is one of the leading experts on international gold movements.

The Academy is deeply indebted to the distinguished speakers who took part in the Semi-Annual Meeting and to the Program Committee, a list of whose members is given below.

COMMITTEE ON PROGRAM AND ARRANGEMENTS

NICHOLAS MURRAY BUTLER, *Chairman*

MISS ETHEL WARNER, *Director*

WINTHROP W. ALDRICH	SAM A. LEWISOHN
FRANK ALTSCHUL	SAMUEL McCUNE LINDSAY
B. H. BECKHART	ROBERT M. MACIVER
WILLIS H. BOOTH	R. C. MCCREA
DONALDSON BROWN	GEORGE O. MAY
W. RANDOLPH BURGESS	OGDEN L. MILLS
J. HERBERT CASE	PARKER T. MOON
JOSEPH P. CHAMBERLAIN	SHEPARD MORGAN
FREDERIC R. COUDERT	THOMAS I. PARKINSON
JOHN W. DAVIS	GEORGE A. PLIMPTON
STEPHEN P. DUGGAN	WILLIAM L. RANSOM
EDWIN F. GAY	JACKSON E. REYNOLDS
JEROME D. GREENE	E. R. A. SELIGMAN
GEORGE L. HARRISON	FRANCIS H. SISSON
ALANSON B. HOUGHTON	JOHN THOMAS SMITH
PIERRE JAY	THOMAS J. WATSON
THOMAS W. LAMONT	LOUIS WILEY
	OWEN D. YOUNG

PART I
THE BREAKDOWN IN WORLD TRADE

THE BREAKDOWN IN WORLD TRADE¹

EDWIN R. A. SELIGMAN

McVickar Professor Emeritus of Political Economy in Residence
Columbia University

IN these introductory remarks I desire to call attention to one or two significant points. We are not discussing today the causes or the real meaning of the present depression, but whatever reasons we assign, there are certain definite implications which are of importance to us today.

Apart from the more general explanation of crises and depressions, which is psychological in character and which has to deal with the inevitable ups and downs in human emotions, there are two possible frontal attacks upon the problem. Since we are dealing with a depression or a change in the price level, we can approach the problem from the point of view either of the commodity in which prices are measured, or of the commodities the prices of which are measured.

Those theorists who explain the present troubles in terms of money, that is of currency in the widest sense, are concerned with so increasing the supply, whether of gold or of credit, as to check the further deflation of prices. Those, on the other hand, who approach the problem from the point of view of the things measured rather than of the measure, are equally concerned in trying to devise some adjustment, some equilibrium in the forces of production and consumption.

The point of present importance is that irrespective of the school to which one may belong, the problem has been translated from a local or national to a worldwide or international sphere. So many things have happened in the past few decades that the old monetary theory which predicated a restoration of the equilibrium of prices through the semi-automatic action of gold, has now become much more complicated. Things now happen which did not occur in any such degree in

¹ Presiding officer's introductory remarks at the opening of the First Session.—Ed.

former generations. The international flow of funds has become far more widespread. The influence, not alone of these long-term loans but of the short-term credits and transfers, has shown itself most intensively, especially in recent years. As a result, all the other factors, upon which it is needless to dilate here, have become so involved that it is hopeless, even in the minds of those who propose to solve the problem by a managed currency, even to think of the situation in terms of a national management. In fact the very first steps in the direction of an international management have been taken, —faltering and timid steps it is true—at Basel.

But those also who share the second point of view, and who think that we can secure a restoration of equilibrium by adjusting the forces of production and consumption, now realize that the problem is one which far transcends any local or national effort.

I do not for a moment wish to belittle the importance of setting one's own house in order, as we are trying belatedly to do with our attempt to balance the budget, and liquefy our credit. But I do wish to point out that all these plans will be fruitless unless they involve the acceptance of the international point of view—international planning as over and against any futile national planning.

This means that what we need today is a new Adam Smith, or, if you will, another Grotius. In the Middle Ages the writers who dealt with economics at all discussed the situation from the point of view of the individual. His chances of salvation were inevitably connected with just prices, with usury and so forth. The mercantilists were the first to reach the conception of national wealth, the welfare of the community as something more important than the welfare of the individual. Then came Adam Smith with his immortal work entitled *The Wealth of Nations*,—not "The Wealth of The Nation," but *The Wealth of Nations*. He first sounded the keynote of the new explanation. But Adam Smith's work was essentially destructive. It was an attempt primarily to show the shortcomings of the mercantilists. What we need today is a new, a constructive Adam Smith, who will lay the real foundations and point out the real meaning of "The Wealth of Nations," as a unified concept.

Now whatever you do, whether you are an advocate of the monetary or of the commodity interpretation of depression and prices, it is plain that any national or local effort at once reflects itself in a change of international trade, in an alteration in the conditions of exports and imports, whether of gold or of commodities. The very first step therefore in any effort to understand the present, has to deal with this problem of international trading. It is for this reason that we begin our discussion today with "The Breakdown in World Trade."

FOREIGN CREDITS AND INTERNATIONAL TRADE

JAMES HARVEY ROGERS

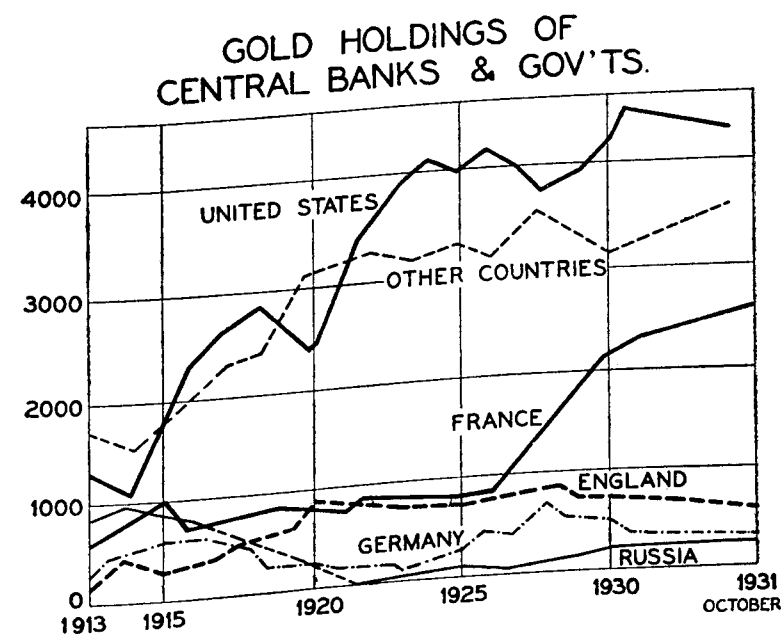
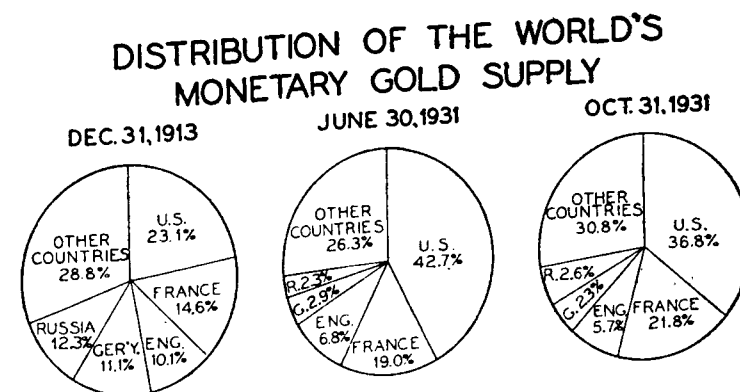
Sterling Professor of Political Economy, Yale University

It will not be my purpose, in spite of the charts which you have before you this morning, to go into an elaborate statistical study of the effect of foreign credits on international trade. That I have attempted in the past without very gratifying results. All that I found in making the direct comparisons was a very general sort of conclusion. Certainly we know that when direct investments by Americans in foreign countries are made, for example when one of our copper companies buys properties and begins to operate in some of the South American countries, the investment normally leads to exports, from this country, of mining machinery and what not.

I did find a very poorly defined relationship likewise between our export of capital or our export of all credits, and our favorable balance of trade. There is some slight connection between the two, apparently; but, as I say, it is not these rather general results that I plan to talk about today.

There is a very much more important relationship between international credits and foreign trade which I shall attempt to emphasize, and I think it ties up so completely with the extraordinary gold situation which we have at the present time, that I shall talk about the three together. That brings us then to the chart of gold holdings (page 7). The discs at the top of the chart represent the distribution of the monetary gold supplies of the world on three different dates, the first being December 31, 1913 (marking the end of the last full pre-war year, before the war effected the redistribution of the gold); the second date is June 30, 1931, and the final disc represents the situation on October 31, 1931. Since that time there has been a slight redistribution, but not a very great one. The point that I wish to make with regard to this chart is this: You notice, of course, that the part held by the United States and France together at the end of October, 1931, represents

[6]



[7]

almost two-thirds of the total gold stock of the world. The same was true on June 30, 1931. Notice, however, that on December 31, 1913, the distribution was very different indeed, the United States and France having about one-third of the total at that time as against two-thirds at the later date. At the earlier date England had a much larger share than at the later date. The fact is that her holdings were reduced from 10.1 per cent to 5.7 per cent, and those of Germany very much more.

In connection with this maldistribution of the world's monetary gold supplies, let me call attention to the fact that while there is a difference of opinion among the gold mining engineers as to the prospect of new gold supplies coming out of the ground, and while in recent months we have had a most extraordinary discovery in the way of a gold mine—that is, in India, where the inhabitants have disgorged a great quantity of gold quite unexpectedly—nevertheless, there seems to be no immediate promise of relieving the gold situation by a sufficient production of new gold.

Let us face the situation which many countries have had to confront in recent years because of a relative gold shortage. Since I am dealing primarily with international credits, I will take up very briefly the situation existing in England and in Germany prior to the crises of 1931.

In the summer of 1931 it became known gradually in this country and in various other parts of the world that the holdings of short-term credits in the London market were very much above the total gold holdings of the Bank of England. As a matter of fact just before the crisis in September it became known that such holdings of short-term credits by the French banks were more than all of the gold in the Bank of England; and at one time it was clear that the holdings of short-term credits in the London market by the Bank of France alone were more than all of the gold in the Bank of England. Bearing in mind that these short-term credits can be very largely withdrawn, literally over night, one can appreciate the position of the officials of the Bank of England when that situation became more and more generally known abroad.

The situation in Germany was very much worse. Prior to the German crisis of last summer it appeared that the foreign

short-term credits held in the Berlin market were five to six times the total gold holdings in the German Reichsbank. Under such circumstances, and with the depression conditions growing more and more serious all over the world, uncertainty developed as to the final payment of these credits. The critical situation soon made its appearance.

Similar conditions existed in a good many other countries. When I say similar, I mean similar generally, though different in many respects.

The question is, what does a country do when it finds itself in an embarrassing position, because of uncomfortably small gold supply?

In the past the ready corrective has been the adoption of credit policies, primarily by the central bank, destined to tighten rates in the monetary center of the country threatened. In London, for example, money rates would have been raised under ordinary circumstances, and continually raised until funds were attracted from abroad to take advantage of the higher rates in that market.

In the recent period rates in London were tightened relatively to rates in other parts of the world, but as uncertainty developed it soon became clear that it would be impossible to tighten them much more without giving great concern in many parts of the world. Indeed, lest further rate increases might reverse the flow of the short-term credits, causing a withdrawal rather than an influx, if suspicions of severe financial trouble were spread by raising the rates too much, this procedure was not followed.

There is another reason why such a corrective could not be applied. The chief difficulty was that short-term credits were too large, and their withdrawal could precipitate a crisis at any time. Since it was their withdrawal which could precipitate the crisis, to increase their amount by simply tightening the rates was to aggravate the difficulty in case a withdrawal should occur. Certainly it was not a remedy.

Moreover, it was recognized, as we all know, that in post-war years the volume of international securities held all over the world and salable in any one of several big investment markets, such as London, New York, Amsterdam, Paris, and, to a certain extent, Berlin, had become very large indeed. Such

securities might be dumped on any one of the markets on which they were salable and lead likewise to a pulling away of gold from that particular market.

Since the ordinary device of tightening rates was uncertain and treacherous in a situation of this sort, those in authority began to look around for more permanent correctives, and they hit upon the perfectly obvious solution. If they could sell more abroad and import less, they would get an inflow of gold to pay for the excess of exports over imports; or they could turn the balance of payments in their favor by simply reducing an unfavorable balance of trade, as in the case of England, if they could encourage exports at the expense of imports.

Gradually in various parts of the world governments began to adopt bounties and various other types of encouragement of exports. On the other hand, import tariffs were increased. Certainly a protective tariff is the readiest way to cut off imports. This particular device was especially popular because of the fact that each country that put up its tariffs cherished the illusion that probably such action would raise domestic prices. All gold standard nations—bear in mind—have been suffering, as we have, from continual liquidation and decline in commodity prices.

All over the world protective tariffs have become more general than ever and much higher than ever. Indeed, I should say that mercantilism had reached its climax in the period of the world's history in which transportation and communication have made their most phenomenal advances.

There is one other device which is just as hard on foreign trade. One by one the countries have been turning over the control of the foreign exchanges to the central banks. Any one in these countries who wishes funds to pay for anything abroad will send his application through channels to the central bank of the country, and if this central bank approves, all is well. In many cases, however, the bank refuses quite arbitrarily to grant exchange for certain purposes, for the simple reason that the gold situation will not stand it.

The point I am trying to make is this: *Because of the great growth of international credits all over the world, countries are finding themselves very uncomfortable with the com-*

paratively small gold supplies on which they might otherwise operate quite comfortably.

At the same time, we have a most extraordinary maldistribution of the world's monetary gold supply. These two factors operate together.

In order to get permanent relief from these factors, governments are restricting foreign trade to an extent that has never been known before in modern times. As a result, international trade in many instances has been almost completely blocked, and world trade has been greatly reduced.

Instead of raising prices internally, the establishment of these barriers is causing a fall in prices all over the world. In other words, nations are throwing as many goods as possible on the international markets while taking as few as possible therefrom, and the net result has been a continual decline of prices, and especially of international prices, for raw materials. That, as I see it, accounts for a considerable portion of the rapid and very drastic decline in prices from which the world is suffering.

I do not have to emphasize the relation between falling prices and business depression. Whatever you may say about the question as to whether falling prices are a symptom or a cause, certainly you can say this, that a continued rapid price decline, however caused, will itself cause depressed conditions. I think I can establish that in a very few words.

There are two explanations, as I see it. The first is this: As business is at present organized, costs usually precede selling prices. If, during the period of production, prices so fall that selling prices are no longer sufficient to meet previously incurred costs, profits will certainly turn into losses.

There is another reason which I consider just as important. It is this: Although we are accustomed to talk about declines in prices as though prices were all going down at one time, and all going up at another time, in fact there is every degree of flexibility and inflexibility in the price system. Some prices do not decline at all, and have not declined yet in this depression; other prices have fallen by a very large proportion of their original amount. In between are all gradations of flexibility. Most costs are relatively inflexible, while many selling prices are relatively flexible. Anyone who is produc-

ing a commodity with a highly flexible price is sure under these conditions to find his profits turned into losses.

The way out, as I see it—if we are going to find a way out—is to relieve the maldistribution of the gold supply, if we can. If we cannot do that, we certainly must utilize the gold supply more effectively. The world is trying to adjust itself to a situation where gold is maldistributed, and where many countries need more gold than they used to need, while at the same time there is very little new gold forthcoming rapidly. Prices, in other words, are adjusting themselves to that sort of situation; and as prices adjust themselves, our debts are forced to adjust themselves. If we fail to take care of the falling prices we shall have to take care of the debts in the bankruptcy courts. We are at present taking care of them very rapidly in that way; but if we have to take care of them much more rapidly we are going to have a terrific collapse on our hands.

If, therefore, this situation is to be relieved, we must find some way of expanding credit. I have thought for a long time, and I still think, that if it is applied vigorously enough this remedy will prove effective. The Federal Reserve banks, by using their open market powers to purchase government securities, can thus put funds into the hands of the banks, and presumably into the hands of the public. In this way, credit expansion can be forced.

I realize that the banks are practically on strike and must be given quantities of funds in order to make them move under present conditions. Moreover, the policy must not be interrupted. Once started, the funds must be pushed out rapidly enough to keep the bond market at least stable. As I see it, that is the only way to stay on the gold standard. Under the Glass-Steagall bill, we have much room for that type of operation. If we do not utilize it, my personal guess is that we shall face some sort of a wild scheme of inflation intended to correct a situation of almost universal bankruptcy.

[12]

THE EFFECT OF CURRENCY DEPRECIATION ON INTERNATIONAL TRADE

JOHN H. WILLIAMS

Professor of Economics, Harvard University

SOME understanding of antecedent conditions is prerequisite to any analysis of the effects of currency depreciation. In the present instance, as almost always in the past, currency depreciation has been the consequence of a collapse of the gold standard. According to the theory of the gold standard international monetary stability is achieved by the flow of gold between the banking systems. The theory assumes sensitivity of credit, prices and costs to gold flow, and on these assumptions links the maintenance of monetary equilibrium to the balance of international payments. To take the simple case of goods trade, if one country expands credit relative to others, its prices will rise, its imports will increase relative to exports, and gold will flow out on balance; gold outflow will contract credit, reduce prices, increase exports and bring gold outflow to an end.

The gold standard works best when four conditions are fulfilled: (1) when banking systems are fully loaned up to the limit set by their reserves, so that the flow of gold must cause a proportional variation in the amount of credit; (2) when capital movements and goods movements are sensitive to each other, requiring little flow of gold to induce equilibrium in the balance of payments; (3) when the demand for international products is elastic, so that a fall of prices will produce an increase in value of exports relative to imports, and contrariwise; (4) when unit costs of production are responsive to money price variations, so that when prices change in response to increases or decreases of gold, production and trade will respond to the movements of prices.

These conditions are never found fully and simultaneously developed. How the gold standard will work in practice must depend upon the magnitude of economic disturbances and upon the degree of friction encountered in the several stages of the

[13]

adjustment process. Fundamentally, the gold standard has broken down by reason of the uneconomic character and the enormous magnitude of international capital and trade movements brought on by the war. We have to recognize that we are dealing with a highly abnormal situation which had a highly unusual cause.

The post-war frictional difficulties have been of various sorts. The collapse of the gold standard in the agricultural countries was a case of inelastic demand-supply. When prices fall such countries find it peculiarly difficult to curtail production; moreover, total value of exports is likely to decrease relative to imports, which consist of industrial products for which demand is more elastic. Meantime, new capital borrowings are cut off, whereas interest on previous debt must still be paid. With prices falling, the debt payments and the imports entail a progressive increase in quantity of exports relative to value of exports, but increasing quantity depresses prices further. It becomes a case of indeterminate equilibrium, and gold flows out persistently until collapse ensues. The possibilities of trade adjustment have then to be considered under conditions of depreciated currency.

England's difficulties have displayed another type of vicious circle. Her trouble has been in part a bad balance of productive forces—too much labor and capital for her natural resources; in part, war-time dislocation of foreign trade; but in part it has been the increased rigidity of her economic structure. Wages and other costs have not come down with prices, with resultant losses and unemployment. Under these conditions, foreign investment was preferable to home investment, but export trade did not respond because costs were high relative to foreign costs. Imports increased relative to exports. The result was an insistent pull on England's gold, which was fought off for some years by importations of short-term balances in response to comparatively high bank rates. Given, then, a severe shock to confidence and the headlong withdrawal of these balances last summer, collapse of the gold standard ensued. England found herself on a basis of depreciated currency.

Under such circumstances as these, depreciated currency is sometimes described as nature's cure; where man has failed

nature steps in and sets in motion a set of forces opposite to those producing the collapse. If costs will not come down, currency depreciation will put prices up, restoring profit margins and reducing the burden of fixed charges upon both industry and government.

In its broad outlines the theory of international trade adjustment under depreciated currency is fairly simple. When a nation's currency depreciates relative to other currencies, world prices translate themselves into higher prices in terms of the depreciated currency. If domestic prices and costs have not changed correspondingly, the exporter will experience a windfall profit. He will buy at home at the same prices as before and sell abroad at the same prices as before, but owing to the fall in the value of his currency relative to the currencies of the countries to which he sells, he will be getting in payment more in terms of his own money than before. The importer is in the opposite case. He pays the same foreign prices as before, but his goods cost him more in terms of his own money. With domestic prices unchanged, he is not able to get back the extra cost. The consequence is a readjustment of international trade. Exports increase and imports decline. What gold flow had previously failed to achieve by depressing prices is accomplished by means of currency depreciation and rising prices.

But this simple theory gives only the very broadest statement of the case. One would be naïve to accept it without reservations and apply it all round the world without due examination of the particular circumstances which may arise. For example, it is not necessarily or invariably true that exports will increase relative to imports when a nation's currency depreciates. Precisely the opposite may happen. The result will depend upon the impact of the depreciation. If the depreciation begins internally—as it might, for example, as a result of an unbalanced budget requiring the issue of fiat money to meet domestic fiscal expenditures—domestic prices would be the first to feel the new spending and would rise relative to export and import prices. The home market would then be a better market to sell in and a poorer market to buy from than before. Exporters would experience losses and importers windfall profits. Imports would increase and exports decrease. The

actual result would be precisely the opposite of the theoretical result which was previously indicated.

In a case, if there could be any such, where the degree of depreciation is the same, externally and internally, where domestic prices and international prices are affected equally and at the same time, there would be no effect at all upon international trade; there would be no redistribution of trade as between the domestic market and the foreign market, no change in the relative parts played by the various nations in world trade. The theory of purchasing-power parity, which Professor Cassel made famous after the war, is based upon this assumption of equal depreciation in all markets. As a statement of final results the doctrine expressed a half-truth (it might better be called a truism); but such a theory throws little light upon the processes of change. Like the quantity theory of money it is concerned with normal relationships after conditions have settled down, rather than with the phenomena of transitional disturbance. We are interested in changes in the value of money, in inflation and deflation, just because those changes have their impact unequally as to amount and as to time on different sets of prices.

The condition, then, that is necessary in order that depreciated currency may correct an international trade position and give relief from the forces that have driven a nation off the gold standard, is that the export and import prices shall rise relative to domestic prices, including costs. In general, this is the most likely result. It is especially apt to be the case in countries where foreign trade predominates; in some of the agricultural countries the domestic market is so little organized and so dominated by the more sensitive and better organized foreign trade that changes in the value of money, whatever their origin, are almost certain to show themselves first and chiefly in the foreign exchange market. For other countries the same results would ensue in so far as the forces driving the nation off the gold standard were primarily international. If the case, for example, were that of reparations driving Germany off gold, one would look to the foreign exchange market as the spearhead of the processes of change. But there is a further reason, under present conditions, for expecting such a result. The world has become more closely knit and the

[16]

factor of international confidence has assumed a new importance. The gold standard will not work when the world becomes afraid of it. Under present conditions, it seems probable that depreciation of currency, whatever its initial impact, would be registered immediately and with greatest force in the foreign exchange market. If, for example, a condition of unbalanced budget in the United States, or an attempt to balance the budget or to pay a soldiers' bonus by issues of fiat currency, should shake confidence in the government credit, the first effect might well be seen in the foreign exchange market, in an international run on our gold reserves.

In general, there is ground for concluding that the effects of currency depreciation upon international trade are usually in accordance with theoretical expectation. But statistical verification sometimes yields surprising results. For example, in Germany just after the war, as the mark depreciated from about seven cents in 1919 to a fraction of a cent by 1922, imports increased and exports decreased. Never was theoretical expectation more strikingly confounded. Yet that the forces which the theory describes were at work is indicated by the fact that in 1919 Germans were selling abroad their capital equipment to take advantage of the exchange profit. The explanation of the paradox seems to have been that Germany had little to export, and needed as a prerequisite to export trade the prior importation of raw materials, food products, working capital. Moreover, her exports were highly competitive finished products. Expanding exports of such products is likely to require drastic price-cutting, which will have two important results: the exporter finds himself forced to give up a large portion of his windfall profit in favor of the foreign consumer; and foreign producers will seek protection from the influx of cheap goods by demanding tariff barriers. After the war such a wave of protection against German exports swept round the world. We have witnessed it again in the past year, though this time it is evidently directed by all nations against all nations. A further result, if export capacity is limited, may be to denude the home market and to give rise to domestic buying booms which will cause domestic prices to rise more rapidly than would otherwise be the case, thus depriving the export trade of its differential advantages. Such

[17]

phenomena also were witnessed in Germany, and gave rise to the foreign trade control boards.

There is always danger that currency depreciation may be a temporary palliative rather than a permanent corrective. If the depreciation should become cumulative, and in the past that has usually been the case, the cure may be worse than the disease. A vicious circle may develop quite as readily as in the opposite case of a deflation feeding upon itself. The foreign exchange value of the currency falls, export and import prices rise, exports expand relative to imports, increased exportation increases domestic prices and costs, government expenditures rise with prices while revenue remains comparatively fixed, the increased demand for money from both business and the government raises prices further. Though the relation of exports to imports may be improved by such a process, the advantage gained is more than offset by the other effects of the inflationary process, which as it tears forward toward collapse will diminish outputs and incomes generally.

A similar point can be made with regard to depreciating currencies which are the products, as at present, of severe depression. Their stimulating effects may be real enough for the countries concerned, but unless they can overbalance the forces of depression in the world at large the most that can be gained is a somewhat more favorable redistribution of world trade, which in its aggregate continues to dwindle. A similar question is raised by the area of the disturbance. If one or two nations are pushed off the gold standard, they can perhaps improve their international trade positions by the processes of currency depreciation, but if all or most nations are pushed off the standard their relative advantages from depreciation are largely nullified.

By judicious currency management, which aimed to secure a definite devaluation of currency and to prevent progressive inflation, such countries might achieve relief from the burden of debts which is the worst consequence of falling prices, and by improving their domestic business conditions they might contribute to world betterment. England is engaged upon such an experiment at present, and so far the results have apparently been favorable; but they are more visible in her domestic production than in her foreign trade. Exports have expanded very little, and the decline of imports seems to have

been more in response to her successive tariff increases than to depreciation of sterling in the foreign exchange markets; indeed had the latter worked effectively the former would have been less necessary. The effect of sterling depreciation upon prices appears also to have been very moderate. Prices have at no time risen more than ten per cent, which is much less than in proportion to the fall in sterling, and in the most recent months prices have been declining, though more moderately than in gold standard countries. The chief advantage of the drop in sterling thus far, apparently, has been in the return of confidence and the relief from international strain in the British money market.

The chief weakness in England's new position probably lies in the instability of the exchange market. It is difficult to keep exchanges stable when they are not tied together through being tied to gold. The foreign exchange control fund provided for in this year's British budget may make some interesting history. Lack of stability is always the great difficulty of depreciated currencies; there is the ever-present danger that the cumulative processes of an uncontrolled and uncontrollable inflation may get under way. Under conditions like the present, people are tempted, sometimes, to welcome even that. But there are more orderly and more controllable processes of credit expansion. I favor as heartily as does Professor Rogers the present program of open-market operations by the Federal Reserve Banks.

From the world point of view, it is not probable if we make proper adjustments now, that we shall soon again have to face international disturbances of such magnitude and of such uneconomic origin and character as have been witnessed since the war. The world's monetary problem is how to make the best reconciliation possible between external and internal monetary stability without sacrificing either unduly to the other. Granting that the chief emphasis already is, and must be, upon central bank management, it seems probable that the gold standard still provides the best general framework within which management can function effectively. The logical end of the evolution of credit management, and the only real hope of solving the problem of monetary instability, would seem to be closer coöperation of central banks looking toward some form or degree of super-national management.

THE ECONOMIC POSITION OF THE RAW MATERIAL INDUSTRIES

FRANZ SCHNEIDER, JR.
Vice-President, Newmont Mining Corporation

SPEAKING generally, raw material industries are suffering from excessive stocks, subnormal consumption and low prices. As the recent prosperity drew to a close, over-optimistic ideas of consumption stimulated production and created excessive productive capacity. As depression deepened and consumption fell, curtailment of production lagged and stocks accumulated. Burdensome stocks, restricted demand and general pessimism finally have brought prices that in some cases fail to cover out-of-pocket costs of production.

Whether raw material industries are suffering more than industries in closer touch with consumers is debatable. But it does seem true that production of raw materials is not as quickly adjusted to current demand as that of more highly manufactured goods. Agricultural commodities that are produced in yearly crops, and metals that require months to pass from ore to refined products, have an inertia in respect to production that increases difficulty of adjusting supply and demand. When, in addition to this inertia, raw materials are made subject to uneconomic schemes for maintaining prices, the results, as in many present instances, are likely to be lamentable.

Current depression in raw material industries has, of course, a most seriously depressing effect on countries producing these raw materials. The Latin-American countries, for example, over-borrowed during prosperity and are now beset with fiscal difficulties, depreciated exchanges, and adverse trade balances. Study of Professor Williams' excellent book on *Argentine International Trade under Inconvertible Paper Money* suggests that in redressing these trade balances, the major effect will come from reduction of imports rather than expansion of exports. It also suggests that the process is likely to be a slow and difficult one, which will be reflected in the business

[20]

No. 1]

RAW MATERIAL INDUSTRIES

21

that manufacturing countries can do with the more extractive countries.

However, one should guard against being too pessimistic over the outlook. Progress, even if delayed, is being made in readjustment of supply and demand. Production is being brought in line with current low levels of consumption and prices have now fallen to levels which tend to destroy producers' illusions and promote decisive action. No general betterment in position of these industries can be expected until business begins to revive and consumption to improve; but it may be just as well to remember, when we are feeling particularly gloomy, that past business recessions, like the rain, always have ended.

While the worldwide depression is the broadest influence affecting these industries, it is far from being the only important factor that has operated to produce present distressing conditions. Many of these industries were ailing long before the onset of depression. Rubber producers did not share recent boom prosperity. They were suffering from too much stabilization and too high prices at an earlier date. Chilean nitrate producers have struggled ever since the war from competition created by war-time stimulus to synthetic nitrate. The iron ore and coal industries, Professor Finley has pointed out, rather suddenly became adult at about the time of the war, when their rate of growth settled down to only that of the population and profit margins narrowed. In the case of coffee, it was apparent by 1928 that Brazil's stabilization scheme of 1925 was stimulating production and piling up stocks that were bound to bring disaster. In the case of wheat, enlargement of productive capacity in the Americas and Australia during the war, followed by Russia's return under Soviet planning to a major exporting position, caused redundancy long before climax of recent prosperity. Sugar producers, too, have found hard going ever since about 1925.¹ The depression developed previously existing weaknesses to the full; but these weaknesses no doubt reflected economic and political influences that contributed to the onset of depression.

¹ An excellent summary of efforts to stabilize many of these important commodities may be found in the chapter on "Attempts at Economic Stabilization," in *The United States in World Affairs* by Walter Lippmann and Wm. O. Scroggs, published by The Council on Foreign Relations, 1932.

[21]

In most instances, producers of raw materials have attempted to combat the depression and prevent decline in prices of their commodities. They have attempted this in a variety of ways, as by coöperative or enforced restriction of production, by organization of marketing schemes, and by securing tariffs or restrictions on imports or exports. In few instances have industrial leaders appreciated the function of price in adjusting supply and demand and promptly sought to lower prices to economic levels. In these few instances, producers have not been able to avoid shrinkage of consumption; but they have minimized accumulation of stocks and so will be rewarded by quicker improvement in prices when consumption turns.

Of producers combating price declines, only two successful instances come to mind. The price of nickel has been maintained at twenty-seven cents in Canada and thirty cents in the United States, duty paid. Virtual monopoly in production of nickel by the International Nickel Company has made possible this price maintenance, notwithstanding reduction in consumption approximating seventy-five per cent. In passing, it is perhaps fair to state that the Nickel Company followed an intelligent price policy during the period of prosperity, not attempting to realize the highest price possible, but one at which rapid expansion in uses could be obtained.

Sulphur is another commodity that has withstood the price decline. Production of brimstone is in the hands of relatively few producers, two companies and the Sicilians accounting for over ninety-five per cent; and new sources of supply were not made available during the prosperity. It is also worth noting that there has been no advance in the price of sulphur since 1926.

The case of copper is interesting as revealing the futility of attempts to abrogate the law of supply and demand and the shortcomings of attempts at coöperative control. By formation of Copper Exporters, Incorporated, under the Webb-Pomerene Act, in 1926, a coöperative selling agency was created, in which the Union Minière du Haut Katanga joined with American producers. For a time, price policies were conservative; but during final prosperity, the price was advanced to eighteen cents. It even touched twenty-four cents; but as demand for copper weakened during the summer of

[22]

1929, the eighteen-cent level was established. It was maintained until April, 1930.

This high bid for additional production did not go unanswered. Belgian and Canadian mines continued to increase their operations; financing and equipment of newly found mines in northern Rhodesia were hastened. Attempting to maintain the price, United States producers not only curtailed operations, but accumulated stocks, meanwhile turning over a larger share of the market to Belgian and Canadian producers. After the collapse of the eighteen-cent price, United States producers attempted to secure coöperation in curtailment from foreign producers; but found that their previous tactics had put them at a disadvantage in negotiations and continued to bear a disproportionate share of the burden.

The curtailment put into effect after conferences at New York in November, 1930, proved inadequate. An abortive attempt for further curtailment was made in May, 1931; and renewed conferences toward the end of that year resulted in a fresh reduction, which once again quickly proved inadequate. A further cut in output is being made this spring, which is designed to reduce the output of coöperating producers to twenty per cent of efficient equipped capacity. Meanwhile, attempts to arrive at stricter coöperative marketing schemes have failed, due to diversity of interest with regard to stocks and to differences in financial condition and capabilities.

During the whole period of business recession and of efforts at coöperative curtailment, stocks of copper rose almost without interruption. In 1931, up to and including September (after which time publication of statistics was discontinued) stocks of refined copper, as compiled by the American Bureau of Metal Statistics, increased by 113,000 tons. For 1930, the corresponding increase was 196,000 tons. This slackness in readjusting supply and demand cannot be blamed on a collapse of consumption. When compared with such metals as iron and nickel, copper consumption has held up well and is still at a rate over half that of the peak year 1929. Unfortunately this rate corresponds to only twenty-five per cent, or less, of present efficient equipped capacity.

The slowness in readjusting supply and demand pretty clearly has been due to obstruction of the natural decline in

[23]

price. Six-cent copper a year earlier would have avoided a year's accumulation of stocks. Even when producers realize that a price is purely nominal and that little can be sold without forcing a sharp recession, they still cling to hopes of improvement and delay taking needed steps to revise operations. The whole system of coöperative curtailment tends to divert attention of the individual producer from the best management of his own business. He is likely to delay taking steps to reduce production or to shut down properties because of possible trading values in the next negotiation. He also is misled by hope that the next negotiation will result in a better price. In the end, the producer who is most anxious to preserve price lands up with large stocks of product and a depleted cash position, if, indeed, he has not acquired debts. He finds himself weak at the critical time and realizes that he has strengthened his competitors. Contemplation of the last few years' experience in the copper business does not strengthen one's belief in coöperative planning and management for an industry as against free action of the law of supply and demand.

An interesting contrast to the copper experience is furnished by the lead industry. Here the price was allowed to sink rather promptly, and while earnings are as bad as in the case of copper, accumulated stocks are smaller. Recuperation, after business revival starts, should be quicker.

In tin, the problem of control was simpler than in the case of copper, partly because tin is not produced in the United States. Progressive reductions in production were prescribed by the International Tin Committee, which has worked in coöperation with the governments of tin-producing districts, the governments enforcing export quotas. Accumulation of additional stocks during the past year has been avoided, but the decline in price has proceeded.

In the case of petroleum, practically none of the recent difficulties can be attributed to disappointing consumption. The latter continued to increase until the present year; and the current decline is very small. Economic trouble in the oil business was started by the post-war illusion that only ten years' supply of oil existed. High prices stimulated exploration and invited large amounts of capital into the business.

[24]

Natural decline in price was resisted, finally by introduction of proration, under which system a great supply of drilled-up oil underground was added to stocks above ground.

Finally, early last year, discovery of a great new East Texas field and its rapid development glutted the market. Oil dropped to five or ten cents a barrel in East Texas, and demoralization became so intense as to cause a most unusual development. State authorities in the Southwest exercised military power to close oil wells and restrict production in order to force higher prices. Quite possibly certain steps taken were illegal, but they were supported by public opinion.

The existing oil situation is thoroughly artificial and offers the interesting spectacle of somewhat radical state authorities coöperating with large oil companies to restrict production and maintain prices. If control remains firm enough and prices are kept moderate enough, the system may prove workable—at least temporarily, or until the prorated supply of oil has been reduced. However, it is worth noting that only disastrously low prices brought the present arrangement into existence.

One is tempted to conclude that the position of most raw material industries has been worsened during the current depression by attempts at coöperative control. The difficulties inherent in these attempts are many: they include the difficulty or impossibility of securing adhesion of all or substantially all producers to the control scheme; diversity of interest between different adherents to the scheme; the general illusion created in the minds of many producers by hopefulness; lack of resoluteness and decision in meeting a changing situation; and the pretty general desire to maintain an uneconomic price which operates to defeat the curtailment. Offhand, one would assume that leaders of an industry would be best able to judge its position and needs; but experience suggests that the integrated interests of all consumers and producers—not to mention speculators—as registered in a free market, furnish the best means of control. One is reminded of the economic dictum that no man or group of men is wise enough, let alone disinterested enough, to fix prices for an industry.

Certainly the industries and companies that grasped quickly the significance of the change in the business outlook, and

[25]

acted promptly to readjust their operations, have saved themselves losses and embarrassment and are in position to enjoy an earlier recovery of earning power. Those that resisted the economic tendency now can realize that one should either sell what one produces at the price the market provides or produce only what one can sell. The law of supply and demand continues to operate in expression of the interests and actions of all the people and without regard to the conceits of individuals; and the longer it is defied the worse is the eventual wreckage. In a very real sense, the severity of the present depression is an expression of the collapse, at long last, of the multitude of schemes devised during the post-war period to secure profits greater than were justified by the existing economic situation. One may venture to hope that the coming decade will see less illusion as to ability to fix prices according to desires and better appreciation of the function of price as the adjuster of supply and demand.

[26]

TARIFFS AND THE MOVEMENT OF GOODS

WILLIAM ORTON

Professor of Economics, Smith College

THE time has come when we must ask ourselves quite seriously whether international trade as we have known it in the past can be expected much longer to continue. During the past decade the movement of goods in world commerce has been subject not merely to more serious, but to more frequent and more vexatious interruptions than ever before; while at the same time the export market has become not less but more important to almost every country: owing, among other things, to the inflation of every major branch of productive activity. The plain and emphatic warnings of the bankers' manifesto in 1926 and the World Economic Conference of 1927 have proved powerless to stay the development of this dangerously paradoxical situation. Since those warnings were issued we have witnessed the failure of no less than seven major international efforts to clear the channels: the two League conferences of 1927-28 for abolishing arbitrary obstacles to trade; the three conferences of 1930-31 on the tariff truce; the Austro-German customs-union scheme of March 1931, embodying the open-door principle; and the Danubian States four-power conference in London of April, 1932. Not without reason did Mr. Runciman remark, in introducing the British tariff proposals to the House of Commons, that "The Government had for some time past found that appeals against the raising of foreign tariffs were absolutely useless. Since the resolutions of the World Economic Conference not one of the signatory countries has made the slightest attempt to carry them out."

It is not alone the increasing level of general tariffs, especially since 1928, that forces itself upon our attention; there is the increasing resort to other methods of obstructing import trade. In the forefront of such methods is the quota system, of which France has recently been giving a startling demonstration to American exporters. Then there is the license

[27]

system, applied also by France to such basic commodities as coal, coke, lumber, sugar, dairy produce and fish. None of the western nations is innocent of the charge of indirect interference with foreign commerce. Sanitary restrictions, embargoes, consular regulations, stipulations as to marks of origin and branding, differential transport rates, the interpretation of dumping laws, classification of cargoes or consignments—all these devices add to the difficulty of doing business, and in so far as they are matters of administrative rather than legislative action, add perhaps even more to the uncertainties of the situation than do the tariff schedules themselves. They also leave the foreigner in an even weaker position for protest than he is in regard to legislative tariff-making. But it must be added that if American business men now find the Europeans a little hard of hearing, the United States in 1930 turned no very sensitive ear to the rumblings coming from the outer world. Unfortunately such deafness proves contagious.

The level of international trade, according to the statistics of the National City Bank, stood in January of this year at from 35 to 40 per cent of the 1929 level by value. There is no point in asking how much of this is due to the world depression as distinct from the effects of the universal tariff war; the two factors are not separable. It is true that there have been certain financial influences making for a world credit inflation since 1923 which can—and indeed must—be corrected apart from the trade situation altogether. But there have also been abnormal influences at work directly upon the trade situation, rendering a stable position impossible. Foremost among these we must place the pressure in the export field arising from political rather than economic causes. There is the case of Russia, debarred—whether rightly or wrongly—from access to the principal financial markets of the world, and therefore forcing her exports in order to acquire current purchasing power for imports at present essential to her industrial reconstruction. Then, and more important, there is the pressure of the debtor nations to acquire and maintain foreign balances for transfer in the face of a closed world market. So long as this necessity exists—and Mr. Stimson has denied all likelihood of the Hoover moratorium being prolonged—export

prices cannot possibly be other than demoralized. No tariff on American imports can in the least degree arrest this demoralization of export markets; on the contrary, the tariff vastly accentuates it. England, Germany, France, Belgium, Italy do not enjoy the sacrifices involved in this forced underselling of the American exporter. Germany in particular did not relish the ten per cent cut in all expenses of production, including interest rates, that she forced through last December. European powers do not adopt low standards of living because they prefer them. They accept them because they must at all costs endeavor to undersell one another and the United States so long as the pressure of political obligations injects its extraneous influence in the economic area.

The political factor is, however, not the only one standing in the way of normal economic intercourse. There has been since the war no reasonably adequate correlation between the investment of capital and the prospect of profitable commerce in the goods produced. The fact is patent when we consider the dilemma now facing the investors who sent eighteen billions of American dollars to earn abroad during the foreign investment boom. The willingness of the public to buy securities—perhaps we may say, the willingness of the bankers to sell securities—took no sufficient account of the obstacles and uncertainties that would be involved when it came to disposing at a profit of the results of the investment. The fact was repeatedly noted, so far as Germany was concerned, by Mr. Parker Gilbert. It was therefore unfortunate, from the American point of view, that America by reason of her own policy was not in a position to give a lead in the only direction that could render her vast foreign investment really secure. And until America is in such a position it is probably useless to expect any widespread improvement in this respect.

This lack of correlation between capital investment and trading prospects is enhanced by every new phase in the international tariff war. The export of capital to Europe was after all based fundamentally on a natural development of production and trade. We have now to reckon with a much more doubtful export of capital. The new investment of well over two billion dollars in the last two years made by American manufacturers in the establishment of foreign plants and

subsidiaries in Europe and in Canada raises a fresh problem. Such a development—perfectly natural as a short-run policy—can perhaps snatch a temporary advantage in the abnormal circumstances which have called it into being. But how much advantage must it secure, and how long will it take, to recoup the original outlay and pay a reasonable rate of return thereon? Consider too that a very large part of this investment (in so far as it arises from the tariff situation and not from transportation costs) represents an economically unnecessary duplication of the world's fixed capital. Does it not seem as though the final crisis might come from the growing insecurity of capital even sooner than from the arbitrary depression of the standards of mass consumption which tariffism imposes?

We may pursue this argument into the field of domestic industry itself: for the lack of adequate correlation between industrial development and the international trading prospects obtains there also. The American export percentage of production is in most fields relatively small. In normal times—so far as we can talk about normal times—it stands at about one-sixth of agricultural production and around one-tenth of total manufactures by value. Certain important classes of goods, of course, run much higher. In 1925 about 30 per cent by volume of American wheat production was sent abroad, 58 per cent of the cotton, 35 per cent of the tobacco, 48 per cent of the copper, 20 per cent of the agricultural machinery, and so on. But these percentages do not tell the whole story. Their importance varies, firstly, according to the elasticity of supply, and secondly, according to the relative size of the fixed charges upon production. In the agricultural industries, where supply is distinctly inelastic, and in heavily capitalized manufacture where the financial overhead is very considerable, even a small export percentage, or small variations in the export percentage, may make all the difference between profit and loss. The public is beginning to realize this in regard to agricultural production. It becomes increasingly important in regard to manufacturing production also, on account of the continual growth in size of the financial structure.

A very significant consequence ensues, which we can see at work in several of the industries which operate under international cartels. The primary aim in practically all these

cases is the preservation of the domestic market from the competition of the other members. Then with some measure of stability, and frequently price-pegging, in the domestic field, the export quotas are allocated and export sales are made primarily in order to take up the slack of productive capacity. The result so far has been, broadly speaking, to lower rather than to raise export prices, since export prices are set on the by-products principle rather than on an inclusive cost basis. Thus, for example, the German members of the international steel cartel have found it more important to maintain capacity by manipulating export prices than to keep those prices at an independent level of profit. The same thing has been true of Canadian newsprint reaching London, of copper at certain periods, and of several other commodities for which it is possible to maintain differential home and export prices.

How far such action should come under the scope of anti-dumping laws is a very debatable question. But it has an interesting consequence in regard to foreign trade. It may be no disadvantage to country B to receive the cut-price exports of country A. But in so far as A is concerned, the cut-price exports obviously do not create as large a volume of foreign exchange to buy B's goods as would otherwise be the case; and if B's goods are essential to A's industries, A may find the course of exchange running against it despite an increase in the volume of its exports. This will particularly be the case if B's exporters are trying to make a separate profit on their export trade, and pricing their goods accordingly, while A's are not. Country A may in fact be led into imposing restrictions on its imports in the interests of its gold reserves. Whether it does so or not—all the more if it does—what actually happens is that B's exporters are forced into the downward movement of export prices, even to non-remunerative levels; and it thus may come about that a considerable part of the foreign trade of both countries, taken in itself at the international prices, is insolvent.

A situation of this kind—which deserves fuller study than it has yet received—obviously introduces an extreme instability into the world situation which must affect not merely foreign but domestic trade also. And there is every reason to suppose that situations of this kind are on the increase, arising in re-

spect of both agricultural and manufactured production. In such cases no amount of foreign credit injected into the domestic money markets can permanently arrest the international demoralization.

Only one thing can be said with any certainty in regard to this and other factors obstructing the course of trade: the way out—if there is a way out—must involve some form of international consultation or agreement. The tariff is not in fact a domestic issue, and politicians who insist on treating it as such are merely fooling themselves and their constituents. On the other hand, the experience of the last five years has given little hope of major results following upon general conferences; and the upshot—openly admitted by both the League and Great Britain—is that the less ambitious road of bilateral or trilateral negotiations must be followed for an indefinite time to come. This method, however, raises in an acute form the question of most-favored-nation agreements. Especially it calls in question the claim of the United States to unconditional most-favored-nation treatment, backed as that is by the vindictive retaliatory clauses of the Hawley-Smoot tariff. If every time any two powers move a step on the road back to international sanity they are to be regarded as “discriminating” against this country, and confronted with the demand of the United States for the lowest terms they give each other, without any *quid pro quo*, the eventual result can only be a concerted defiance of this country’s position. Experience since 1927 shows conclusively that an unconditional most-favored-nation policy cannot be pursued with either fairness or success in total disregard of the respective levels of duties of the nations concerned. The State Department has in the past been rather fond of quoting the latter part of the third of Woodrow Wilson’s Fourteen Points in defense of its position—namely “The establishment of an equality of trade conditions among all the nations.” It is high time to remember the first half of that same sentence as Mr. Wilson announced it: “The removal so far as possible of all economic barriers.” Is it too much to hope that a nation traditionally concerned with liberty as well as with equality will see, before it is too late, the wisdom of giving the world a lead toward the recapture of its lost freedom?

[32]

DISCUSSION: THE BREAKDOWN IN WORLD TRADE¹

CHAIRMAN MOON: Our speakers² have set before you four of the major factors in the present economic situation. It is now our opportunity to criticize, to question, to examine what has been said and to attempt to put these various factors into a composite picture, into a reasonable synthesis.

Precisely because the topics which have been presented are so many of them controversial, we have allowed rather more time than usual for discussion. I will call first on Dr. B. Haggott Beckhart, Professor of Banking, Columbia University.

PROFESSOR B. HAGGOTT BECKHART: I find myself in very complete agreement with the last speaker. Foreign trade totals over the past three years have declined by something approximating forty per cent, somewhat more in the case of the United States and somewhat less in the case of France and of Great Britain, somewhat more in the case of the raw material countries, and somewhat less in the case of those countries producing manufactured goods.

Despite this very large decline in foreign trade totals, the nations of the world have been busily engaged in adopting policies of further trade strangulation. Inconsistent and self-defeating though the policies are, every effort has been made to reduce imports on the one hand and to increase or to maintain the volume of export trade on the other.

The result has been a further acceleration of the downward movement. The last speaker pointed out that tariff barriers have been established or raised in many countries. He also indicated that for fear the tariff barriers might not be fully effective, various countries have established quotas for different classes of imports, and this has been particularly true of France and Belgium.

One of the motivating factors in the case of France has been an increasing differential between import and export trade. The adverse balance of commodity payments was becoming larger. France had to import a considerable quantity of cereals last summer by reason of the failure of the French wheat crop. This increasing differential between the export and the import trade of France led France to adopt a quota system, with the result that there has been

¹ An abstract of the discussion at the close of the First Session.

² James Harvey Rogers, John H. Williams, Franz Schneider, Jr. and William Orton.

[33]

a substantial decline in imports received from the United States and in imports received from Great Britain.

Other nations have imposed rigid foreign exchange controls so that importations and exportations are impossible without the consent of the government concerned. This is particularly true in the case of Germany and Austria. It is not believed, however, that these foreign exchange controls have been fully effective. It is said, for example, that the Austrian schilling is subject to a twenty per cent discount in the illegal trading which prevails.

Other countries have abandoned the gold standard in order that the differential existing between the internal and external values of their currency might have a further effect in stimulating exports and retarding imports. This has been true in the Scandinavian countries.

The British Treasury has attempted to maintain the external value of the pound at a low level in order that the differential between the external and internal value might persist for as long a period as possible to give added stimulus to British trade. Of course, that differential cannot continue for long in the absence of inflation at home.

In short, during the past few years state control over foreign trade has been substituted for the price controls of competitive capitalism, with the objective always in mind of reducing imports and of expanding exports, which for the world as a whole becomes a *reductio ad absurdum*. At a time when debtor nations are struggling with the problem of debt payments, further barriers are thrown in their way. Nations are being swayed by illusory short-run policies, which are expensive now, and likely to prove more expensive with the passage of time.

Beginning with the Treaty of Versailles and continuing thereafter, the world has persisted in the adoption of policies which would inevitably result in the present débâcle. The Treaty of Versailles, itself, balkanized Central Europe and engendered an intense spirit of nationalism which has found expression in trade restrictions and trade barriers. To revert now to conditions approximating those of twenty years ago along the Danube, as has been suggested by the proponents of a Danubian customs union, seems to be impossible. In the interim Austria has developed her beet sugar and wheat industries, and the Austrian producer now asserts that he cannot compete with the beet producer of Hungary. Also in the meantime Hungary has developed her textile industry, and Czechoslovakia her electrical industry, and the manufacturers assert that in the event of free trade within what once constituted the Austrian Empire the Hungarian textile producer could not compete with the textile producers of Austria. Nor could the electrical manufacturers of

Czechoslovakia compete with the electrical manufactures of Austria. Therefore to establish a Danubian customs union seems a political impossibility.

In addition the Treaty of Versailles levied a heavy annual tribute to be paid by Germany. Not since the Romans levied tribute on the Egyptians, had there been exactions of such magnitude, but the Romans always permitted the free entry of wheat from Egypt; whereas when the nations levied tribute upon Germany they immediately erected tariff barriers to make it as difficult as possible for Germany to pay reparations.

The tribute was somewhat lightened by the Dawes and Young plans, though the burden of the Young Plan has increased greatly by reason of the decline in commodity prices.

If little progress has been made by way of solving or settling the reparations question, it is largely by reason of the attitude of this country on the matter of the inter-Allied debts.

It was hoped by the Micawber-like politicians of the world that the burden of reparations and debt payments would be considerably lightened by reason of an expected secular growth in foreign trade; but how the expectation of a secular growth in trade was to be reconciled with the adoption of trade barriers has never been explained.

That the breakdown did not come sooner was due to the huge volume of capital exports from the United States. The capital exports of the United States from 1924 to 1929 were in part a reflection of the easy money or inflationary policies followed by the Federal Reserve banks. They enabled Germany to meet her reparation payments by borrowing from America; they enabled America to maintain its export trade despite its creditor position and its tariff policies. The capital exports camouflaged the underlying factors in the situation and did so by engendering widespread inflationary conditions, which have made the world crisis all the more severe when it occurred.

Capital was exported in many instances, as we all well know, without thought as to the capacity of the debtor nations to repay or the productive or non-productive use of the capital employed. Investment banking houses laid emphasis on the commissions to be secured through the flotation of securities. In some cases they resorted to unethical practices to secure the business of underwriting foreign issues in order to obtain the commissions to be derived therefrom.

A consequence of all these policies is now reflected in the present price quotations prevailing on foreign bonds, which presage a heavy loss on the part of the American investor. In view of the practices

employed by our investment banking houses, not only as regards foreign issues but also as regards domestic issues, I think one might very well raise the question as to the desirability of some form of social control over investment issues. The world has attempted to control the volume of commercial credit through the discount rate policy and through the open market policy of central banks. Just as the world has attempted to control commercial credit, so the world might attempt to control investment credit. At least, we may conclude that the losses suffered by American investors on foreign issues will make them very reluctant to buy further issues in the future.

When the interest rates prevailing in the stock market became such through 1929 that foreign debtors could no longer borrow on long-term account, use was made of the short-term money markets. Through 1929 Germany in particular made use of the acceptance market. When borrowings on short-term account were no longer possible, debtor nations were forced to ship gold until the dwindling nature of their gold reserves forced an abandonment of the gold standard, and defaults on the interest and principal on foreign obligations resulted.

In other words, while the inflationary character of the huge capital exports from the United States did suspend for a time the fundamental factors at work in the international trade situation, they did have the ultimate effect of making the crisis all the more severe. The breakdown would have come sooner and probably would have been less acute. For a creditor nation to export huge amounts of capital, to be followed by a complete cessation, is to invite the very situation from which the world suffers at the present time. In the erratic nature of its capital exports, America must share a large measure of responsibility for the international breakdown of the gold standard.

International trade, I think, might be restored if the principles of competitive capitalism were allowed free play. This remedy would involve recognition of the fact that tariff and trade barriers must be removed, that price-fixing schemes, subsidies and subventions must be abandoned, and that economic spheres of influence must be eliminated. Foreign debts must be written down substantially. On the basis of the freer trade obtained, a gradual return to the international gold standard could be made, and the torn fabric of international finance rewoven.

It is, however, probably too much to expect that mankind will follow enlightened policies of this character even though in the long run they would redound to its advantage. More likely is it that the present crisis will tend to accelerate the movement towards state

capitalism. In the economic treatises of the future the period from the close of the Napoleonic wars to the outbreak of the World War will receive emphasis as that in which the principles of private capitalism attained fruition. In the past decade or more, in different nations, and with varying degrees of intensity, the principles of private capitalism have been discarded for those of state capitalism. One of the difficulties in the present situation is that we appear to be in the transitional period between the eras of private and state capitalism. This circumstance may account in some measure for the present dilemma in national policies. Nations are not willing to abandon trade restrictions, i. e., to revert to the principles of private capitalism, nor are they ready to adopt well-knit cohesive programs of state control.

Assuming then that a return to a régime of freer trade is an impossibility, it is probable that the nations of the world might group themselves in the future into various economic units. Trade between these units would be on a barter basis. Foreign trade and the exportation of capital would be under the strict control of the state. Nations would divert their energies inward, and be forced to develop programs of economic development. The international gold standard as it was known in the nineteenth century would cease to exist.

I believe that this type of state control, of state capitalism, is likely to emerge from the present situation unless the nations of the world are willing to approach international economic problems in a conciliatory and coöperative spirit, which seems quite unlikely at the moment.

CHAIRMAN: Our discussion is to be continued now by Mr. Peter Molyneaux, editor and publisher of *The Texas Weekly*.

MR. PETER MOLYNEAUX: Quite naturally my approach to a matter of this sort will be a little different from that of most of the speakers whom you have heard today. With us in Texas these problems are very practical every-day problems. For example, I dare say it will startle you if I tell you that in Texas one family in every three, approximately, lives on a cotton farm, and that ninety per cent of their product must be sold outside of the United States. Do not misunderstand me. Of course, we do not export ninety per cent of all American cotton, but normally about sixty per cent of that must be exported. To use a very popular phrase, it "burns us up" when we hear gentlemen declaring that we only export ten per cent of our production, and that the recession in foreign trade has not disturbed our business to anything like the extent that people believe, or that, as the President has said more than once, we can achieve a

great measure of recovery independent of the rest of the world. We know better than that in Texas; that is, some of us do.

It is an interesting fact that the history of the entire South has run almost counter to the history of the North and East. If there were time, an interesting interpretation could be put on all of our history in view of that fact. The South did not abandon its colonial relation to Europe with the Declaration of Independence and the adoption of the Constitution, but continued it up to the Civil War, in the sense that more than eighty per cent of the cotton produced by the slave-holding and slave population of the South prior to the Civil War was sold outside of the United States. Up until this very moment cotton is produced partly for export, and in Texas we produce it primarily for export.

Now, as I say, we have been hit very hard by this situation, and we can see no recovery independent of the rest of the world.

Before the collapse of world trade occurred, cotton was going along as well as any such commodity could. Of course, prior to the war the balance of trade was being affected by the income from the American securities owned abroad. Now understand, I know it is not so simple as that, but for our purposes that is a perfectly true statement. Then during the war we shipped to Europe enormous amounts so that over a period of five years we had a favorable commodity balance of something like \$18,000,000,000, and our problem was—aside from that unpaid trade balance—how could we resume selling to Europe, when the war closed, twice as much as we bought from it under these new conditions? For a little while it seemed impossible. In 1921 cotton dropped from forty cents a pound to something around fifteen cents, or very low in any event. But what happened, of course, was that we started on a period of buying foreign securities, of exporting capital. Then when the Wall Street boom attracted the capital away from foreign investments, we had the inevitable collapse.

That is not a comprehensive explanation of what happened, but for all practical purposes it is what happened to us.

Now we are facing some very definite problems in the matter of cotton, and it is not merely an industry that is involved; it is practically a people. There are six million people, at least, in the South who depend entirely on cotton for a livelihood. I mean they produce cotton. There are at least six million more whose purchasing power is practically determined by it. That, my friends, although it is very difficult to make Eastern industrialists understand it, is a very big factor in the economic set-up of the United States, and you cannot disturb it without disturbing at the same time the economic situation of the United States.

How are you going to explain the action of fourteen Texas members of Congress—representing a population who depend on foreign trade more than any other population represented at Washington when that vote was taken—who voted against ratification of the current moratorium? Why? Simply because the public mind of Texas is not yet aroused to the realization of the absolute dependence of Texas on foreign trade.

I was very much struck Monday upon reading the declaration of Dr. Butler about this situation. If there is anything needed in this country now, when we see the spectacle of a presidential year with no outstanding candidate in either party, Democratic or Republican, speaking out clearly on these questions, when these are the questions on which our very future depends, on which our very livelihood depends, the thing that is needed is a very definite and very active plain-speaking on such matters as this.

We are facing the proposition as to whether it is possible to continue our foreign trade in the light of the difficulties that are in our way today. That is a very big question to us. There are some advocates in this country of a policy of self-sufficiency. Until very recently it was the expressed policy of the Administration; it may still be. But self-sufficiency to the cotton-growing industry means to cut its production in half. When you have a commodity being produced by six million people in little units, that means creating an enormous unemployment problem because you cannot over night, you cannot in a short period of time, even take half of the people employed in one industry and find other work for them. We are asking whether we can go on.

We want to raise the standard of life in the South. We want to bring the standard of life up to the great American standard which we heard so much about before 1929, but it may be questioned whether we can even maintain such standards as we had in the past, in view of the present world exchange situation that has resulted primarily from such great exports of capital from one country to another.

Fundamentally that situation remains. After you reform the tariffs and after you cancel the debts, you still have the investments abroad; you still have the income from those investments abroad flowing in the opposite direction from what used to be their course when we were selling our cotton outside of the United States regularly with readiness.

If I can contribute anything to this discussion, it is this: It is a very striking fact that during January and February cotton constituted, in dollars and cents of course, more than 23 per cent of all American exports as compared with something like 14 or 15

per cent during 1928. It had been declining steadily before then. Prior to the war it was something above 25 per cent.

Now that may indicate the direction in which we are going, that and the investment of American capital in the establishment of factories and branch factories abroad by manufacturing industries of the United States which formerly exported goods. I think that we are inevitably headed toward what is known as an unfavorable trade balance, which is a very misleading term. But it is possible to do an enormous foreign trade even with an unfavorable trade balance.

When we achieve the maximum of the possible international coöperation in removing barriers and restore whatever basis is possible for the reconstruction of international credit, we may, in plain language, make it possible for other nations to buy cotton and certain other things that they need a little more than most things.

I dare say many of you are familiar with Dean Donham's thesis that America must withdraw from the exporting market. I believe that a great many manufacturing industries that do not depend primarily on foreign trade will help the situation very materially if they will get out of the foreign market so that foreign nations can buy some things they need more than most things.

CHAIRMAN: The meeting is now open for discussion from the floor.

MR. RALEIGH RIFE (31 Nassau Street, New York): One of our speakers here today in discussing our heavy overseas investment of capital has indicated that this is something new in world economic history, and that the American public would never indulge in it again.

I would like to go back to 1825, when the Erie Canal started the great internal development in the United States spreading to the Ohio River and the lower Mississippi Valley. That was financed by Great Britain. Great Britain after the Napoleonic Wars began her great first overseas investment of capital. The panic of 1837 wiped out, it seemed almost over night, a good part of the British investments in the United States. Default after default took place almost immediately. We had a balanced budget in the United States. We had a surplus. We were getting ready to distribute that surplus among the various states, and yet the collapse came. It was not felt immediately in Great Britain, the creditor nation, the exporting nation, but two years later the Bank of England began to feel the pressure of gold, and from 1839 on for about three years there was a succession of bank failures. I think some sixty banks in England failed in that period of time. That sounds a good deal like our recent history in this country.

There is the parallel of the new creditor feeling the repercussion of the temporary failure of its overseas investments. But did England stop? She went on pouring money into the development of the United States in the seventies and on through the nineties, and I presume even after 1900.

Just remember the history of the British export of capital and see how many times they did it over and over again, and yet the wealth of Great Britain that was built up with some of that capital opened the way for great expansion of world trade and commerce.

While I am usually as pessimistic as any person here today, I wish to express this one thought, that the world economic opportunity for growth and expansion is relatively as large today as it was in 1815. We are just opening up the great continent of Africa with railroads north, south, east and west, and that continent is rich in natural resources and larger than the continent of North America. The development of Africa is going to be just as important a factor in the next fifty or one hundred years as the development of North America was in the last.

MR. GARDINER H. MILLER (ex-President of the New York Cotton Exchange): Mr. Molyneux mentioned a subject very close to my heart—cotton—a business in which I have been engaged my entire business life, which extends for thirty-nine years. I have listened to some of the addresses here and have not heard a single remedy proposed for our troubles except inflation. I believe, gentlemen, that democracy is on trial. I believe that the most of the evil consequences of the war resulted from "too many cooks" at Versailles. They did not know their own minds, and the result was a compromise. . . . I think it is high time that the people who have brains should get together and make our government do what we are all doing, that is economize. It is high time to stop these lobbies down in Washington. This business of \$2,400,000,000 going to veterans is ridiculous. The labor lobby, the farm lobby, what are all those people doing? We are not going to get out of our difficulties if we do not eliminate these lobbies, so that we may maintain the credit of the United States on a sound basis, and on an honest basis, so we can pay our debts.

CHAIRMAN: Mr. Finlay would like to know how Texas can sell her large and increasing production in the face of the fact that the other parts of the world are increasing their production and supplying their own wants.

MR. MOLYNEAUX: It is not strictly true that they are increasing their production. They have increased their production in recent years and in the last fiscal year more foreign cotton was consumed by the world than American cotton. But quite the opposite is the situation this season. There are shortages in most of the other cotton-growing countries. India itself is importing American cotton. Japan is getting more than twice as much American cotton this year as it did last, with a large increase last year over the previous year. As a matter of fact, if it had not been for the Oriental countries' consumption of American cotton this year, we would be in much worse shape than we are.

If it were true that other countries are increasing their production, in the long run I would rather have them capture our foreign trade if we can divert our economic activities to maintaining a decent standard of living rather than competing with them in the foreign market.

MR. CHARLES F. DE GARRAHL (White Plains, New York): I am just going to express one word of sympathy with the gentleman who spoke about racketeering and grafting, and I have a suggestion to make. That is, that we start attacking the bears in Washington, that we follow that group which is undermining the whole American nation from beginning to end, the grafters and racketeers.

CHAIRMAN: Mr. Mazzini Lapolla would like to inquire of Professor Rogers: Would not the adoption of international bi-metallism solve the problem of a falling-off of the world's gold supply?

PROFESSOR ROGERS: There is no doubt that the introduction of bi-metallism even in this country alone, if the ratio of silver to gold were made low enough, would enable us to get rid of our depression difficulties very, very rapidly. However, I am not sure that we could maintain bi-metallism as such if we made the ratio very low, or low enough to pull us out extremely rapidly. We would probably find that we were on a silver standard instead of a gold standard. I think, too, there are many difficulties which come out of this particular type of inflation scheme, as out of most of the others.

My opinion is, however, that unless our Federal Reserve authorities expand credit sufficiently greatly—and that means very greatly at the present time—there is much evidence that some sort of drastic inflation measure may be before us very soon. This is one of them.

PROFESSOR ROYAL MEEKER (New Haven, Connecticut): Ladies and Gentlemen: I was impressed by a remark made by Professor Seligman at the beginning of this very illuminating conference. He

spoke of the two schools of economic thought, one of them advocating as a cure-all for depression tackling the money end of the game, and another school of thought advocating tackling the problem from the side of commodity production control.

I want to emphasize the fact that no matter what each individual may call himself, he is necessarily a member of both schools, and he cannot help himself. I want to emphasize as far as possible the need for reversing the present policies of regulation of trade, international and domestic, and regulation of production. Inevitably, such regulation affects the whole schedule of prices. We do thereby affect the standard of living, consumption, trade and production. If, on the other hand, we start with inflationary or reflationary or anti-deflationary measures, tackling the currency-credit angle directly, we reach the same result. We do affect the price schedule. We do affect consumption, trade and production.

Now, obviously, the more practical method of attack is the one that Professor Rogers has outlined. I am wholly in accord with his mode of attack, but I would like to emphasize the difficulties in the way. Frankly, Professor Rogers, I don't believe that if we had free and unlimited coinage of silver it would pull us out of the pit we have dugged for ourselves very, very rapidly. I don't believe it for a minute. I don't believe that if the Federal Reserve system at this late stage of the game should increase credit, expand the reserve funds in the possession of the member banks and of other banks to an incredible degree, it would pull us out of the pit very, very rapidly. We have gone too far.

The orthodox economic vicious circle has developed into a malevolently diabolical circle. Bankers are scared to lend, and they could not lend if they would, because the business man is too scared to borrow, and he could not borrow if he would, because the banker in turn is so scared that he won't let a dollar escape from his till, not at the point of a pistol. The circle is a malevolent, diabolical one. It will be a long, slow process, this process of breaking the circle and transforming it into an upward spiral. Oh, it will come, of course! Great Britain and many other countries have passed through deep depressions and they have recovered. We shall recover, all right enough. The question is how many of us will be alive when the recovery comes. That is the whole question; it is a question of hanging on.

As I see it, we must induce the Federal Reserve system to expand credit. We must work on the regulatory end at the same time. We can't divorce the two. We must, if necessary, almost compel producers to borrow and to start the machinery of production going again. We must almost compel people, if necessary, at the point

of a pistol—I am exaggerating now, but you won't mind that—to consume in order to start the machine going.

This liquidation process does not liquidate. That is the trouble with it. The more we pay, the more we owe. I have just finished a computation of our debts. It is a rough one, to be sure—mostly guesswork, but that is what economists and statisticians are for. Leaving out of account the total book credits, the total personal loans from individual to individual, the pawnbroker loans, etc. as beyond even the pale of the economic-statistical guesser, I have estimated that in 1929 all other indebtedness in the United States amounted to about \$214,000,000,000, or something like that. The total indebtedness, now, in dollars, I have estimated at approximately \$180,000,000,000. That is a decline in dollars, please note, but not in identical dollars. The decline in dollars is about 16 per cent. What is the decline in the real debt? There is no decline. The dollar since 1929 has become a dollar and fifty-three cents approximately, that is the business dollar, and that is what we are talking about. Thus an apparent decline of 16 per cent is transmogrified into an actual increase of 30 per cent. All our pinching and scraping and economizing has brought about only an apparent decline of 16 per cent and an actual increase of the debt burden by nearly one-third. And the liquidation process is still going on. The more we liquidate the heavier becomes the burden of debt. If we keep on liquidating, what is the ultimate outcome? We are going straight towards the standards of living so eloquently advocated by Mr. Gandhi of India, the goat milk diet and the loin-cloth wardrobe standard!

I have an idea that the process of liquidation will be stopped, partly by Mr. Rogers' method, partly by the method of really inducing captains of industry to forget the racketeers in Washington for a moment and concentrate upon their own business, namely, captaining industry. That is the business of the business man. If they will get busy and give us a workable program of production, of trade, of consumption, we can start the slow process of getting out of the depression; otherwise we are going right on to lower and lower standards of living. It is very important that we should stop right now. Many of us have economized to the bone, and if we have to economize much longer, we shall be wiped off the map.

PROFESSOR ROGERS: Since the remarks of the last speaker seem to be addressed particularly to me, may I simply tell a story, which will confirm to a very considerable extent what Professor Meeker has just said. At one of the big investment houses, a few days ago, I was talking with the gentleman in charge of obtaining information

[44]

on concerns who come in for refinancing. One such concern was a very well managed public utility corporation that had been financed since its birth by this particular investment house. The president asked for refinancing of a bond issue which was coming due. He was refused, as is practically everyone who applies today. Then the bank official raised the question: "What are you going to do about it?"

"I will tell you what I am going to do about it because I am already doing it," he replied. "All improvements have been automatically eliminated. We have been making improvements every year, but this year they are eliminated completely. Many improvements that we have usually charged to maintenance are likewise automatically eliminated. We have fired everybody that we could fire. We expect in that way to save enough cash to meet a considerable portion of this refinancing. The rest of it we *hope* we can borrow from a bank."

That situation is becoming very general in American industry because of the fact that the big accumulation of refinancing—not new financing but refinancing—cannot be met. Someone has superficially estimated that the absolutely necessary refinancing may amount in the next two years to more than \$600,000,000 a month.

Notice that refinancing is different from new financing, and that a comparatively small amount of funds will take care of it; but until we can get a bond market that will at least take care of refinancing, we cannot even stand still; the liquidation must continue.

The scheme that I have been proposing for almost two years now is that the Federal Reserve Banks use their powers of expanding credit. This credit would come automatically to the banks very quickly. In a period of liquidation like the present one the banks are meeting continual drains of currency and losses of reserve. The indicated solution, it seems to me, is to give them cash. They are given cash by Federal Reserve purchasing of bills and government securities. The explanation is very simple: The central institutions purchase a government security from me. I take the check which the Federal Reserve bank gives me and deposit it in my bank. The funds come to the bank, and it has that much increase in reserve at the Federal Reserve bank. If the Federal Reserve banks buy from the other banks, the latter get the funds directly. In other words, funds are put out to the banks; and if any conservative credit policy can stop this disastrous liquidation, that will do it. I do not say that it is the only credit measure that will do it; there are other measures, wild inflation measures, which will likewise do it.

I agree with Professor Meeker that the banks will not lend freely. They are virtually on strike at the present time. They will not lend

[45]

to many borrowers because the borrowers under present conditions are not credit-worthy. If, however, funds are pushed out continually and in sufficient quantity to the bankers, the normal lenders, I hope that they will still be willing to invest in some sort of high-class bonds. In this way may be started first a high-grade bond market, which will take care at least of much refinancing, and as things go on perhaps provide for more and more new financing.

I am not convinced that the Reserve banks can apply this remedy rapidly enough to cure the malady now, although since the passage of the Glass-Steagall bill they have very great power of expansion; that is, they could expand the basic credit, the reserve of the member banks, to a literally huge amount without endangering their own liquidity. Assuming no further loss of gold and no unprecedented volume of hoarding, they could expand these reserves at least two and one-half billion dollars and thus provide for a loan and investment expansion of more than twenty billion dollars. Moreover, they will not have to expand them nearly so far before banks, one after another, will begin to buy securities and make a bond market which will take care at least of refinancing.

In the absence of this Federal Reserve action, I think that we should expand irrespective of the gold standard. The penalty of inaction might be worse than departure from the standard. I think we can expand sufficiently on the gold standard, but I am in favor of expanding even if it takes a discarding of the gold standard to make it sufficient.

MR. JAMES A. FULTON (McKeesport, Pa.): Our favorable trade balance, amounting in a peak year to four billion dollars, has been dwindling away until it is practically *nil*. Our imports and exports are just about equal, with the prospects apparently favoring the imports to outstrip the exports for the year 1932, unless there is prompt action to forestall such result. In 1931 both exports and imports of goods decreased in value, as compared with the preceding year; the exports by \$1,418,990,000, and the imports by \$970,801,000. We unanimously regret the export drop of last year. Any further recession of exports this year would be considered as continuing and aggravating the breakdown of last year. But how about the *import* factor of our world trade? In 1931 we imported less than in the preceding year, but the drop was a favorable, not an unfavorable happening, from our viewpoint. In some degree it furnished an antidote for the injury arising from our lessened exports. If it were certain that the volume of imports would be further reduced this year, a vast majority of our people would be profoundly grateful.

We want the favorable and not the unfavorable balance of trade.

[46]

We would keep our exports up and our imports down. We should frankly proclaim such desire and purpose.

It is folly to expect any amicable world-wide agreement of action upon trade matters, for the present self-interest of nearly all nations prompts them to seek and strive for the favorable balance *which quite obviously cannot be secured by all*.

The *natural* basis for international trade is for the nations to sell to each other in an amount equal to supply the natural and unavoidable deficits in the production or capacity of each other. This natural and beneficial basis is almost wholly ignored in the prevailing methods of world trade. Nations use almost every known trick, subterfuge and opportunity to force vast volumes of superfluous and unwanted goods upon each other, to the detriment and possible disruption of the home production, capacity and well-being.

It is a travesty for our nation, or any nation, to be importing anything that its people are ready, anxious and well-equipped to produce for itself and of which it already may have a surfeit.

It would clarify the situation and quickly produce a much more cordial world-feeling if each and all of the nations (with the United States leading the way by its own independent action) would flatly bar out unwanted goods, competing with home production, and give easy entry to the goods it needs or desires but which it is unable to produce, by reason of climatic or other obstacles.

Our most vulnerable point is in the fact that we are now the great creditor nation, to the amount of twenty or twenty-five billions of dollars. The return or liquidation of the creditor balance, in goods, as it was mainly created, is one of the storm-clouds hovering over the nation, threatening our best interests. Our government, when it insists upon or collects its foreign claims, is potently working for the reduction of our exports and the increase of our imports.

From the standpoint of our general welfare, it would be a hundred-fold better to strike the entire creditor balance off as a total loss to its public, corporate and individual holders, by cancellation or any other method, than to permit its return through imports.

The most available method of surely preventing such destructive return of the creditor balance is by fixing our tariff rates high enough to be practically prohibitive, except upon such non-competing articles as we desire but cannot produce.

[47]

PART II
REPARATIONS AND WAR DEBTS

REPARATIONS AND WAR DEBTS¹

ALANSON B. HOUGHTON

President of the Academy of Political Science
Former United States Ambassador to Germany and to Great Britain

THE subject put down for consideration this afternoon is "Reparations and War Debts." No subject, it seems to me, could possibly be more timely or, if I may say so, is in greater need of clear elucidation. The distinguished gentlemen who have consented to address us this afternoon are, of course, in themselves an assurance that the discussion will be authoritative and useful.

Before introducing them, however, may I say just one word? It has been my fortune during the past eighteen months or so to travel more or less about the country and to meet a number of audiences and to talk about this particular question with a great many individuals. The net result of that experience has led me, contrary I suspect to what seems to be the prevailing view, to believe that public opinion in regard to the disposition of the war debts has not yet focused or reached a final decision. I am strongly of the opinion that the question is still wide open, is still capable of decision. I am strongly of the opinion also that our people taken as a whole are not demanding impossibilities or seeking to make any settlement which disregards underlying realities. Naturally, differences of opinion among them exist. Some of them seem content to assume that inasmuch as certain nations owe this nation money, they should pay it. Some of them, plenty of them, on the other hand, recognizing the difficulties and the complications of payment, are urging that the debt should forthwith be cancelled. But so far as my own observation goes—and I recognize of course that it is limited—I do not believe that our people yet have come to accept either of these extreme positions. They may yet accept either, or they may prefer

¹ Presiding officer's introductory remarks at the opening of the Second Session.—Ed.

some middle course, but at the moment at any rate—and this is what I wanted particularly to stress—I believe their minds are still open. Therefore, I really welcome the opportunity given us to hear speakers who are so competent to advise us, and I hope sincerely that the discussion this afternoon may be of genuine service to our people in what I am certain is their wish—to reach a settlement of the war debts which will be fair and just to all the great nations concerned.

[52]

THE NEED FOR A NEW APPROACH TO AN OLD PROBLEM

FRANK ALTSCHUL

Of the firm of Lazard Frères, New York

I DEEPLY appreciate the opportunity that has been afforded me of addressing this distinguished gathering today. We meet to discuss this subject in the midst of a profound world depression. That reparations and war debts have contributed to the disturbed economic condition in which the world finds itself today, I am sure no one will question. The payments which they involve are themselves unrelated to any purely economic movements, either of goods or of capital. Some believe that the abnormal influences which these payments have set up in world trade are in large measure the cause of the catastrophic fall in commodity prices, with all the dislocation this has entailed. Others argue that the fall in commodity prices, which has so greatly increased the burden weighing upon debtors, furnishes in itself the reason why reparations and war debts have assumed the importance that they admittedly have today.

Regardless of where the truth lies between these two views, it seems to me that there is one thing on which we can all agree. I believe one can fairly state that the question of reparations and war debts has constituted, and still constitutes one of the major continuing causes of disturbance in the post-war world. It has poisoned the political and undermined the commercial relationships between nations. In the political field, the desire to collect has given rise to constant discord, where harmony was essential; similarly, in the commercial field, the attempt to pay has led to a forced and unnatural competition to which world markets have until now been unable to accommodate themselves.

To just what extent these factors have been responsible for the present troubled state of the economic world must remain largely a matter of opinion. If we are to understand the problem in its true proportions, however, I think we must turn our

[53]

attention for a moment to some of the aspects of the economic landscape which forms its general background. Much evidence of a statistical nature can be adduced to support the statement that we are experiencing a disturbance more violent in character than any other similar one in modern economic history. And behind this statistical material there lurks an appalling picture of human misery and suffering. Unemployment in our country has reached an incredible total, variously estimated between six and eight million. This condition finds its counterpart in all leading industrial countries. Countless other millions live in constant fear of finding themselves forced into the ranks of the unemployed; in many quarters despair is growing; dread and apprehension, to say the very least, are on every side. That sense of personal security which until recently was so widespread and so agreeable a feature of our American life is rapidly vanishing.

The breakdown in the machinery of commerce and industry has gone so far that it threatens a breakdown in morale. Confidence has given place to distrust. Nations, no less than individuals, eye one another with suspicion. We have lost faith in our neighbors. We are in danger of losing faith in ourselves. On every side, one hears the question asked: "Is this just another crisis like so many of the past, or is it perhaps the prelude to a disruption of the social order, possibly a symptom of the decay of a civilization?"

It was inevitable that such intense confusion in the economic world should have violent repercussions in the world of politics. One of the most significant of these has been the ever-widening spread of a spirit of intense economic nationalism. The new burdens which depression has fastened upon nations have led them to turn more and more to experiments in the direction of nationally protected economies. As problems became more difficult of solution in an international sense, it was only natural that attempts should be made to deal with them, in so far as might be, along national lines. If one failed in the search for a formula to permit one to join with one's neighbors in averting a common disaster, possibly one could devise a method of avoiding, for oneself at least, its severest consequences.

Some such general consideration lies at the roots of the post-

war history of protective tariffs. That these perfectly logical measures of defense have not been attended with the success that was expected of them is evidenced today in every industrial country by the spectacle of millions of men, safely entrenched behind tariff barriers, searching in vain for the work that these barriers were supposed to provide.

There was a time—not so very long ago—when many of us would have contended that a complete and final readjustment of reparations and inter-Allied debts would, in itself, have proved sufficient to arrest the downward sweep of economic events. Today the depression has deepened to such an extent, and so many complicated forces have been set in motion, that I believe it would be rash to ascribe any longer to the solution of this one problem the qualities of panacea. On the other hand, it seems to me quite clear that, without fear of being fairly charged with exaggeration, one may still confidently voice the opinion that no recovery is likely to take place, or in any event to make any great degree of progress, while this issue remains unresolved. It is on this account that it has lost none of its fundamental and far-reaching importance.

Now, why is this problem one of such extraordinary difficulty? Why does it constitute an issue with which great democracies have until now struggled in vain? Why has it led merely to a series of compromises, no one of which has proved to be a solution?

The answer would seem to me to run somewhat along these lines. The amounts at stake appear very large, and they easily assume for the man in the street an importance out of all relation to the part which, in most instances, they actually play in national budgets. The mere fact that the payments in question affect budgets at all, quite regardless of degree, has led from the start to their becoming in each country matters of violent internal political controversy in which questions of national pride, prestige, and purpose soon became involved. Thus, an economic problem exceedingly complex in its nature, requiring the most dispassionate judgment of enlightened statesmanship, with ramifications leading far beyond national boundaries, was, in every country concerned, early thrown into the arena of party politics.

As a result, the broader aspects of the issue gradually be-

came more and more obscured. In each country there developed a tendency to over-emphasize increasingly considerations of a purely domestic nature at the expense of a more international view. And so, policies gradually crystallized which, while in themselves diametrically opposed, represented in each instance no more than the honest interpretation of a sincere and deep-rooted national conviction concerning the equities at stake.

Leaving England out of the discussion for the moment because of the special position which she assumed at the time of the formulation of the Balfour principle, the powers most concerned are Germany, France and the United States. Germany and France, in the matter of reparations, and France and the United States, in the matter of war debts, have taken up positions that appear to be, and maybe are, fundamentally irreconcilable; and curiously enough each of these nations, purely from its own point of view, is clearly and essentially right.

Let us examine the German thesis. The reparations clauses are not only based upon a more or less generally admitted violation of the spirit of the pre-Armistice agreement, but they flow from the sole-war-guilt theory of the Treaty of Versailles, which the world outside of France has by and large long since abandoned. Notwithstanding this—they say—under pressure of impelling necessity, Germany has already made huge payments on reparations account. These payments were made during a period in which a new generation has been growing up—a generation that played no part in the events which led up to the war—a generation which played no part in the negotiations (if such they can be called) which resulted in the Treaty of Peace. This new Germany is rankling under a sense of crying injustice, and it finds in the reparations clauses of the treaty, materially modified though these have been, first by the Dawes and then by the Young Plan, the direct or indirect cause of all the ills from which the German economic body today is suffering.

Beyond this—they argue—apart from any question of theoretical right or wrong, the practical impossibility of continuing payments on reparations account has been amply demonstrated to the satisfaction of most of the civilized world.

Payments, in the last analysis, must largely be made in goods; and recent developments in tariff policy indicate that the unwillingness to receive is almost as great as the reluctance to deliver. In their view, reparations, as we have known them since Versailles, are at an end. The only question which remains is through what machinery is this situation in fact to become recognized in law. To seek such recognition at an early date has thus become the cardinal objective of German policy; and from a purely German point of view, at any rate, this objective seems fair, just and right.

The French position is obviously far different. Twice in a generation—they tell you—their territory has been subjected to invasion by the Germans. They require security for the future and reparations for the past. As a result of their inability to obtain the approval of the Three-Power Guarantee Pact of Paris, they have been obliged to seek security through a series of continental alliances, and through a strong military establishment. Reparations they seek through an attempt to maintain more or less in its integrity the Young Plan, in accordance with which France is to receive from Germany an amount materially in excess of her out-payments on account of inter-Allied debts.

It would be unthinkable—they say—that the French people should have to assume the continuing burden of the interest charges traceable to their expenditures for the rebuilding of the devastated regions. It would be immoral to suggest that they should be called upon to make any payments on account of inter-Allied debts which did not find their equivalent in receipts from Germany. This question, in their opinion, is in no way related to any consideration of a real or fancied French capacity to pay; seriously to contemplate such net out-payments even for an instant would be to be faithless to the memory of those who died at Verdun.

So, in a word, runs the French argument, and from a purely French point of view, it too is clear, logical and right.

Our own position is equally unassailable. The war debts represent obligations willingly and unconditionally assumed. They had not, at their inception, and have never since been accorded by us, any official connection with reparations. Reparations is strictly a European question, resulting from a

European war, over European issues, in which in spite of ourselves we became involved. We have made with France a generous settlement, taking into account her capacity to pay, which, parenthetically, since the date of the settlement has apparently materially increased. To cancel or, to any considerable extent, to reduce her obligation to us would merely result in fastening to an even larger degree on the shoulders of the American taxpayer the burden of a purely European adventure. From the point of view of the preponderating body of American citizens, this position too, is eminently fair, reasonable and right.

Under these circumstances, in what direction does hope of progress lie? I can see only one. Secure in the knowledge of the essential justice of its own position, each nation must come to understand that the justice of widely conflicting and divergent views may be none the less passionately and sincerely believed in by others.

Dangerous as intense nationalism is, when it interferes with the natural flow of goods, it becomes possibly even more vicious when it impedes the normal flow of ideas. It seems to me that, if progress is to be made at all, we shall each of us have to abandon our intellectual self-sufficiency, and develop in its stead a willingness to import and assimilate foreign concepts. We must be prepared to deal with others with some attempt at understanding their mentality, and their problems. Then only can we reasonably expect others to deal with us in a similarly sympathetic and enlightened spirit.

If once this new understanding should prevail, progress would, in my judgment, be rapid. We would no longer find ourselves committed merely to the task of winning an argument, or even of establishing a sacred principle which happened to be in conflict with principles equally sacred to others. We would be fired with an intense desire to resolve with finality this vexatious question, which has so long troubled the world; and we all would soon see with striking clearness that each of us had infinitely more to gain by arriving at a definitive solution, even though it involved a compromise with some of our own most cherished ideas, than by continuing to insist on the sanctity of purely domestic formulæ to such an extent as to render any solution impossible.

[58]

When and if we adopt this new approach to an old problem, the problem itself will lose at once much of its apparent complexity. Detailed statistical analyses of what Germany has paid to date will cease to have any considerable interest, excepting for historians. It will not matter, for instance, whether, or at what valuation, the Germans included in their statement of payments effected the fleet which they sank at Scapa Flow; or whether their calculations are in accord, or at variance, with the arithmetic of the books of account kept by the Reparations Commission. And the question of the competitive industrial advantages of a Germany freed from the reparations burden, which has loomed so large in recent discussions and which until now has defied any clear-cut statistical analysis, will be seen to have little more than theoretical interest.

Considered in this new atmosphere, matters of pure detail, which until now have formed the basis of endless controversy, would lose the importance they have hitherto had. The question in its essence would become in fact as simple as this: What concessions can each nation bring itself to make in order that there may be promptly reached a final settlement, so essential to the welfare of all?

The situation is one which calls imperatively for concessions on all sides if success is to be achieved. The views of no party to the discussion can conceivably be maintained in their entirety. German insistence upon an end of reparations will, of necessity, have to undergo modification. A continuing payment on their part, no longer designated as "reparations", if you will, but rather as their contribution towards making a general settlement possible, is clearly indicated. It is equally certain that the French will be obliged to recede from their maximum demands. It is obvious that they will be unable to secure the equivalent of their out-payments, together with an amount substantially as great as the net receipts to which they are entitled under the Young Plan. It is evident, too, that in some form and to some extent, we, as our contribution, will have to re-examine and review debt settlements.

While I have never been an out-and-out cancellationist, I am an ardent advocate of early and of drastic revision. In this I know I plead what has come to be considered in our country a lost cause; and yet I cannot, on that account, refrain

[59]

from suggesting how desperately important it seems to me that this cause should none the less prevail. Better late than never, it is true, but how infinitely better early than late!

I am convinced that among the European nations there is already a far greater recognition of the absolute necessity of compromise than as yet is generally supposed to be the case. With the return of British initiative, counsels of moderation appear at long last to be making real progress. It is just possible that, before the summer, accords will have been reached in Europe which require nothing but eventual American coöperation to make them completely effective.

It seems more likely, however, that if this new spirit is to flourish, some early expression by us of sympathy with its objectives, no matter how tentative this may be, is all but essential. If we could bring ourselves to the point of indicating a willingness not to cancel, but to consider with an open mind, and if need be, to review; if we could do this in no matter what uncertain and non-committal terms in time to give heart to the Allied statesmen when they meet in conference in Lausanne, I would be full of hope that much good might still eventuate.

What general lines would such a settlement take, you may ask? For a moment I shall enter the realm of the imaginary and the speculative to sketch merely one of the numberless possibilities which this new attitude would open up. The amount of the continuing German contribution would first become a matter of negotiation and determination. Once determined, it might be expressed through the creation and delivery to the European powers concerned of an issue of bonds secured on the German railroads, unconditionally guaranteed as to principal and interest by the Reich. In order that during the period of convalescence the world economy should not again needlessly be disturbed, the interest on these bonds, in the early years, should be payable, in my opinion, at Germany's option, in Reichsmarks, available to the recipients for purchases within Germany only. As I see it, the interest on this issue would be substantial in amount, but it would still fall materially below the amount of the theoretical net receipts of France under the provisions of the Young Plan.

In addition, if it seemed desirable or necessary, there might

be created and delivered an issue of German railroad income bonds, which would give creditors of Germany an opportunity to share in the future to some reasonable extent in any great revival of German trade.

In view of some such undertaking by Germany, France, in the interest of a general settlement, should find it possible to abandon any claim to net in-payments, with the exception of such interest as might accrue to her in future on her share of the German railroad income bonds. Nothing less than such an important scaling down of her net receipts would justify the sacrifices demanded of others. This would represent a material concession from recent French demands, but it seems to me an essential one.

It would then become our task to review the debt agreements, in order to bring these settlements, in so far as we reasonably and fairly could, into harmony with the general terms of the European compromise. This would involve a recognition on our part that as a practical matter reparations and war debts had of necessity to be dealt with together, even though in theory they might remain in our opinion totally unrelated. We would thus be obliged not only to modify a point of view, but to give this modification concrete expression in the form of American financial concessions. In connection with these, we might in all fairness, if we wished, exert our influence in the direction of progressive disarmament and of the budgetary control of armaments.

The foregoing is of course intended to be no more than vaguely suggestive; and in the present temper of American political and public opinion, it is frankly visionary and Utopian. It ignores many difficulties, and hurdles others; and purposely so, for it presupposes an atmosphere of conciliation, and in such an atmosphere problems which, in the last analysis, have become matters of pure arithmetic, will readily yield their answers.

The tangible results of such a program would, I am convinced, amply justify whatever sacrifices it involved. Reparations, more than any other single factor, has been in recent years responsible for the tension in European affairs. Although essentially an economic question, it has probably contributed more largely to the development of friction between France

and Germany than any purely political issue. To dispose of it once and for all would be to facilitate enormously a return to the spirit of Locarno.

Furthermore, if I am right in the opinion that no improvement is likely to take place or, in any event, to make any great degree of progress until the problem of reparations and war debts has been finally dealt with, then the most obvious tangible result—and this I consider of prime importance—would lie in the removal of an insuperable barrier to any prolonged and far-reaching world recovery.

Beyond this, one would only be justified in going to the extent of expressing a hope and a belief. Once this new spirit of coöperation and concession had led to a successful issue in a matter of prime concern, it should be relatively simple to develop the technique for extending its usefulness. It is possible that the related problem of tariffs might next be explored, and if in this manner we were successful in correcting bit by bit some of the mistakes of the recent past, the best possible foundations would have been laid for a real attitude of hopefulness towards the future.

What is the alternative to such a promising line of approach? It may be that we will continue to look at the problem, not as it is, but as we would like it to be. It may be that we will continue to adopt solutions today which might have proved adequate had they been adopted last month. It may be that we will continue to insist on our own views, with scant consideration for the views of others. Possibly some such attitude is inherent in the manner in which democracies function. If so, the outlook, I am afraid, must remain troubled and uncertain.

Failing a negotiated agreement, the definitive nature of which in the absence of American coöperation it is difficult to foresee, there is little likelihood of any early payments on account of the German commercial debt, and none whatsoever of any payments on account of reparations. The official confirmation of this fact must then, sooner rather than later, take the form of an avowed default. What new disturbances, politically, economically, and possibly even socially, may attend such a development, it is exceedingly difficult to anticipate. Faced with the fact of such a default, is it probable

that the inter-Allied debt structure will remain unshaken? I doubt it. Will France be able or willing, in such circumstances, to plead successfully her incapacity to pay? I am far from certain. And if she is not, will her public opinion sanction to any material extent net out-payments? The answer is clearly in the negative. One may sympathize or not with this mentality; the important thing is to recognize it. And what of Great Britain? She will no doubt make, as she has heretofore made, gigantic efforts to meet her engagements to the last farthing. Will the world be the better off for watching her succeed or fail in the attempt? I am inclined to think not.

This is the sequence of grave uncertainties to which a failure promptly to take a helpful attitude would expose us. I admit there is little to justify any feeling of hopefulness that we can be led to act in time; but at least we should recognize and appraise the dangers implicit in delay. And we should understand that by inaction we in no sense prevent the inevitable and material downward readjustment of reparations and, in all likelihood, of war debts as well. We merely elect that this should take place in a catastrophic and destructive manner.

The world at large knows today that on anything even remotely approaching the scale of the unconditional annuities of the Young Plan, reparations are at an end. The world may learn tomorrow that debt settlements in their present form and amounts are hardly more secure. In my opinion the choice which confronts us is merely whether they are to be readjusted by agreement or through default. Default is a dangerous medium in personal and in corporate affairs. It becomes infinitely more dangerous when it enters the financial intercourse between nations. It undermines that confidence in contract and in treaty on which the security of our social and political structure rests. Should it be allowed to occur in connection with reparations and war debts it would cause the most intense disturbance in international relations, and would everywhere accentuate that growing sectionalism which already is so seriously restricting human opportunity.

On this account it is my earnest plea that we at last approach the problem of reparations and war debts in terms of realism; and that without further delay we cast the full weight of our

influence on the side of readjustment by agreement. If we fail to do this, we help to subject an already weakened economic and political system to a most severe and, as it appears to me, a quite unnecessary strain. In this modern world of ours it seems the part of folly to contribute in this manner to the accumulating forces of disorder.

[64]

SHOULD WAR DEBTS BE CANCELLED?

BAINBRIDGE COLBY
Former Secretary of State

THE war debts can be cancelled only by the government of the United States. They can be repudiated by the debtor nations; or paid in part and defaulted for the balance; but cancellation can be effected only by the voluntary act of the creditor.

To the question, shall the war debts be cancelled, the United States has given its answer. It is an unmistakable negative, and while the question "*should* they be cancelled", is perhaps not finally disposed of by a refusal to cancel, further studies of the ethical, economic and political aspects of the question lead to a similar and an inescapable negative. The joint resolution by which the House and Senate ratified the President's action of June, 1931, declaring a year's moratorium with respect to debts owed the United States, contained this significant provision:

It is hereby expressly declared to be against the policy of Congress that any of the indebtedness of foreign countries to the United States should be in any manner cancelled or reduced; and nothing in this joint resolution shall be construed as indicating a contrary policy, or as implying that favorable consideration will be given at any time to a change in the policy hereby declared.

In a quasi-official memorandum released in Paris on January 20th of this year, the American position was again stated. This memorandum, evidently intended as a notification to all concerned, consisted of five declarations:

1. There is no connection between war debts and reparations.
2. The European powers must take the initiative on reparations.
3. A demand for a new debts moratorium could not obtain approval in Congress, and the Senate opposes a cancellation or reduction of the debts.

[65]

4. The United States would look with displeasure on the formation of a united front of the debtor nations.

5. The existing debt arrangements, having been concluded separately, can be eventually revised only by separate accords.

Furthermore, it is announced that the Lausanne conference on reparations, originally called for January 18th and now scheduled to be held in June, will *not* concern itself with the question of the allied debts to the United States. Great Britain has insisted, and France has agreed, that settlement of the reparations problem for them is a matter which is without relation to their respective debts to the United States.

The subject of debt cancellation — i.e. the annulment or reduction of Europe's war-time debts to the United States — is therefore no longer a live question.

The persistence, however, of the belief, which in many quarters is doubtless sincere, that there is some defect of equity in the American position; that the grievous economic situation of the world is due in substantial degree to the existence of these debts, and that their cancellation would contribute to a restoration of normal world trade, merits attention, although the limits of this discussion admit of no more than brief and general treatment of these viewpoints.

Let us recall what these debts are and how they were incurred. Congress passed the first Liberty Loan act in April, 1917. It provided that the United States government should sell \$5,000,000,000 of Liberty Bonds to the public, and use \$3,000,000,000 of the money thus raised to buy bonds of the allied governments. The principle on which the act was drawn was that our loans to Europe were to be self-supporting and never a burden to the American taxpayers. It was therefore provided that any foreign bonds taken by our government in payment should bear the same rate of interest as our Liberty Bonds and mature and become subject to retirement at the same time. The first Liberty Loan was followed by a second, third and fourth.

In none of these transactions did the United States deal with the allied nations collectively. Each loan was an individual matter between this government and the particular foreign nation involved, and each foreign nation signed demand notes for the amounts loaned to it by the United States.

The Armistice was hardly concluded, the peace treaty of Versailles had not been drafted, when the effort began to revise downward the amount of Europe's indebtedness to us. During the peace negotiations in Paris, the British and French governments called a conference between the allied nations and the United States to discuss the inter-allied debts, with a view to pooling them and bringing about either their cancellation or the substitution of Germany as the debtor nation, in place of the allied powers, to whom the loans had been made. President Wilson refused to participate in any general conference on the subject of these debts. He pointed out that they had been contracted separately and individually by the allied nations and insisted that any arrangement governing their payment should be reached in the same manner. The idea of substituting Germany as the debtor nation, he rejected, calling attention to the fact that America neither had sought nor would receive reparations from Germany; that it had neither asked nor derived any benefit from the war; that it had not acquired nor did it desire additional territory; and he insisted and always maintained that the debts of the allies had no relation to reparations, but rested squarely upon the allies themselves and no one else. He also stated that the United States would entertain no suggestion of the cancellation of these obligations. To this position he adhered throughout his term as President. In these discussions Mr. Wilson pointed out that America was the only nation which had contracted no war debts except to her own people; that cancellation would mean that the allies would be relieved of a great part of their debt burden, while America would experience no relief at all, as our taxpayers would be obliged to pay into the Treasury the full amount of which our European debtors were relieved.

There has been no departure from Mr. Wilson's position on the debts by his successors. The right and duty of this country to collect the sums owed to it has been publicly affirmed by ex-President Coolidge; and President Hoover, in proposing a year's moratorium, assured the country that "he did not approve in any remote sense of the cancellation of the debts to us".

Despite all effort to keep our position on this question distinct and free of confusion, the declaration of a moratorium was

hailed throughout Europe as an abandonment by America of the position it had so consistently adhered to. European economists and statesmen, with one accord, announced the American debt to be a thing of the past. But such declarations merely mark the unbroken continuance of the European effort to undermine our position as a creditor by every device calculated to attain that purpose. Every plea that could be invented, every consideration that could be twisted into service, has been employed to sustain the continual pressure for cancellation, or at least drastic reduction.

It is undeniably true that, as a people, we still have something of the simplicity of children. We fall ready victims, it has been said, to the illusions of ethical and humanitarian dogma.

The Balfour note, issued in 1922, which maintained that the allied and associated powers were really partners in the cause of freedom, and that the debts incurred were really loans made not for the separate advantage of particular states, but for a great purpose common to all, awakened a noticeable response in this country. Even the Columbia Faculty of Political Science was moved to declare that in its judgment "the war debts settlements were unsound in principle and that our advances should be regarded as joint contributions to a common cause", thus echoing the Balfour position.

The flaw in the Balfour note was that while it aimed to abolish the economic and financial problems of reparations, and thus to exorcise all the political evils which afflicted the world, *it placed the entire cost of so doing upon the American people.* Debts were to be abandoned. The allies were to scrap reparations, but the American taxpayer was to liquidate the transaction.

The British thesis was much too naïve. Its formula—abolish reparations, cancel debts and let America pay—was a trifle more than this country could stand. While we all wish America to be just, and even generous, we are not willing that it should be treated as an easy mark.

The equity of our position has its foundation in the prodigal generosity with which we responded to Europe's cry of distress during the welter of war. Our loans were our answer to Europe's appeals for aid, lest she perish. They enabled the

debtor nations to purchase food and munitions, to sustain their armies in the field and to feed their civilian populations. They were made in the face of threatened military defeat and at a time when internal civil disorders threatened to engulf and destroy the borrowers.

While we have maintained that the repayment of our loans has nothing to do with the collection of reparations, we have nevertheless advanced, in private loans to Germany, the money with which she has paid all that has thus far been paid on account of reparations. What our allied debtors have received on account of German reparations, has been derived from American loans, and these loans are the source of a large proportion of what our allied debtors have paid on account of their borrowings from us. When the American investor ceased in 1929 to buy German bonds, and the vast stream of American loans to Germany stopped, Germany's payment of reparations stopped also.

The truth of the matter is that Germany has never had any intention of paying reparations. Her persistent policy since the Versailles treaty has been one of indiscriminate sabotage with reference to it. She has resisted all requirements of the treaty, so far as she could, and has sought particularly to evade its military and financial clauses. With the stoppage of American loans, Germany is confronted for the first time with the problem of actually paying reparations. She finds herself, however, in the favorable position of having involved Great Britain and the United States so heavily in her financial difficulties, that all she thinks it necessary to do is to threaten financial suicide, which she counts upon to bring to her aid additional credits, postponements in maturities, and the inter-ested endeavors of her private creditors in both Great Britain and the United States, to save themselves by lightening her public obligations. It is estimated that the loans to Germany and purchases of German securities by the United States and Great Britain aggregate \$4,000,000,000. If bankruptcy should now overtake Germany, she feels that she will have sympathetic and not unpowerful fellow-sufferers.

It should be borne in mind, first, that it has never been proved that Germany could not pay large sums abroad on account of reparations, and second, that it has never been

established that the essentially generous debt settlements made by the United States with her war-time allies exceeded the capacity of those nations to pay. Dismissing the question of Germany's paying power, because it does not pertain to my subject, I think it can hardly be contended that our immediate European debtors have even drawn substantially upon their capacity to pay us, to say nothing of exceeding it.

It is only necessary to refer to the loans made by France to foreign countries since the war ended. They total 13,277,000,000 francs, not including a loan to Czechoslovakia of 600,000,000 francs made on January 20th of this year, nor a loan of 300,000,000 francs to Finland, nor a loan of 400,000,000 francs to the Polish railroads. France is reported to have loaned Rumania 2,090,000,000 francs, and to Poland, in addition to the railway loan just mentioned, the sum of 2,000,000,000 francs has been advanced. France has loaned 770,000,000 francs to Turkey, and 23,000,000 francs to far-off China. Can the plea of France, that she is unable to repay the money borrowed from us since the close of the war, be expected to move us profoundly, in the light of these facts?

As to the economic consequences of our insistence upon the payment of the war loans, much has been said which is erroneous, insincere and misleading. As a matter of fact, the troubles through which the world is passing are traceable, in hardly an appreciable degree, to the existence of Europe's war debts to us.

And it should be borne in mind that Europe has paid us nothing on account of these debts since January, 1931. The rapid accentuation of the world's financial distress may be said to have occurred since that date, a period in which nothing has been paid, nothing collected and nothing demanded on account of the war debts to the United States.

In the last year in which any payment on account of principal and interest was received, only the relatively modest (albeit considerable) sum of \$215,000,000 was paid to the United States Treasury on the war debts. This amounted to but one-half of one per cent of the estimated national incomes of the countries which made the payments, and to but 2.7 per cent of their annual budgets. They spend more than that for almost any other purpose that seems agreeable. For arma-

ments alone, they spent eight times as much as they are called upon to pay us on war debts account, in other words, \$1,800,000,000. From the standpoint of economics the payments amount to but 1.1 per cent of the total volume of the foreign trade of the debtor countries,—an almost negligible percentage, altogether incapable of exercising a disturbing effect or appreciable influence upon world trade.

Of the arguments urged for a reduction of America's claims, there is one which is capable of differentiation from those with which we have grown familiar, and which may be described as the plea in avoidance. I refer to the contention that owing to the fall in the price level of commodities, the obligations of the debtor nations are heavier than those which they assumed. There is a degree of validity to this contention at the moment. The answer to it, however, is that there are other variables which equally deserve consideration, such as the "capacity to pay" on the part of the debtor nations.

Take France as an illustration. The France of today has a very different capacity to pay than the France of five years ago. Then, the franc was worth less than two cents in our currency. Its government was hard pressed to meet current bills. Today the financial position of France is buttressed by a gold reserve second only to that of the United States, and still growing as ours diminishes; while her industrial activity both at home and in her colonial possessions, which were greatly augmented as the result of the war, has made a steady progress, which will be continuing.

Against such inevitable variations are to be reckoned the great concessions made by this country in the funding of the debts, which today represent far less than the amount of the obligations as contracted, and which the borrowing nations bound themselves to repay.

The last gasp of repudiation is the plea that under modern democratic conditions, no government which depends upon the people for its existence and must rely for its continuance in power on re-election by popular vote, can undertake to impose upon its people the burden of paying the war debts. It is maintained that the debts are identified in the popular mind with a limitation upon national independence and carry the suggestion of tribute, national inferiority and persecution.

As one writer puts it: "No democratic government can live, which assumes in the eyes of its own people, the guise of a mere collecting agency for foreign creditors". I can only comment that if the good faith of governments is to be swallowed up in the bad faith of peoples, then the world is due for a sad disillusionment. If the pledges of nations, threatened with overthrow, have no value; if the confidence shown by the United States in the engagements of her European allies has no foundation, then what becomes of the hope of trustful coöperation between nations?

The dangers that lurk in conflicting national policies, in oppression of the weak by the strong, in the threat of invasion—take on new gravity if a nation which is unjustly assailed can no more look for help in any quarter of the world, for the reason that repudiation has displaced honor in international relationships.

[72]

POLITICAL DEBTS OF ALL NATIONS AND THEIR RELATION TO DEPRESSED AGRICULTURE

CHARLES C. ISELY

Lumber and Grain Merchant, Dodge City, Kansas

WHAT I have to say will be at considerable variance from the thesis that you have just listened to so intently, and which has been so splendidly presented. Permit me, before I present my own views, to raise one question. Senator Shipstead put forward the theory in the Senate, the other day, that because European countries spent so much for armaments, they could pay their debts. I notice a similar thought in Mr. Colby's argument that France has made loans and therefore should pay. I have a friend in Kansas who said that if England would not drink any beer at all for a year, she, too, could pay. What I fail to understand is how abstention from beer, or from making loans, or from armaments would help France, or Britain, or Germany to find foreign exchange for debt payments.

I am very glad to stand here beside the splendid gentleman from Texas, who this morning was pleading for a market for cotton. I stand here as a pig and wheat raiser, if you please, pleading for a market for wheat and pigs.

The price of wheat at Liverpool last summer was the lowest that it had been for 300 years. The price in the United States is less than it has been since the white man's agriculture supplanted the crooked stick of the Indians. The unadjusted post-war problems, particularly the failure to settle properly the political debts of the nations, are the underlying cause of farm distress.

It is said we Westerners are to blame. Stanley Baldwin, British statesman, nine years ago, greeting angry newsmen before he debarked at Southampton after negotiating at Washington the preliminary war-debt agreement with our Debt Funding Commission, said that there were financiers in New York and statesmen in Washington who understood the fiscal

[73]

difficulties that confronted the United Kingdom, but that the representatives of Western pig and wheat raisers, in Congress, would not permit a more generous settlement.

Being, primarily, a pig and wheat raiser, I called his attention to a resolution by the Kansas State Board of Agriculture urging a debt and reparation conference, showing that we "Westerners" were not so ignorant, but that the problem had never been presented to the West. I expressed apprehension of future difficulties if the settlement were finally ratified as set up at Washington. I still say that farmers are not now either dense or dumb, but that these problems have never been cogently presented to agricultural America.

Restore farm prices, give the farmer a satisfactory basis of operation and all other business will recover speedily, for over thirty per cent of the consumptive demand of this nation is to be found on the farms. That fact is still not fully apprehended.

One of our sanest economists, reviewing the year 1923, noted that the year was quite satisfactory in spite of the severe agricultural depression then prevailing and further observed that America had grown so great that it apparently could prosper even if farm conditions were adverse. Before April and May, 1924, however, this brightness had turned to gloom. The yellow light from the wheat fields of Kansas, in July, dispelled the gloom, for the promise of the Dawes Plan opened the markets of Germany and the rest of Europe. The temporary adjustments of the Allied war debts due to our treasury, also aided in relieving the congestion of agricultural products and we had five fairly prosperous years on the farm and five years of unparalleled prosperity in the cities.

The farmer is solemnly told that prices for his commodities are governed by the law of supply and demand; that the law is inexorable; and that he has produced a surplus. He then reads of millions in the cities without bread and tens of millions in Europe on various restricted rations, and he feels that something has abrogated the law of supply and demand. There is wheat today in the bins on Kansas farms, harvested in July, 1931, grown in fields for which the soil was prepared in July, 1930. If this wheat had not been grown, and if there were no accumulated supplies, famine would threaten the world before mid-July. Production of the roast beef served on our tables

today must be anticipated by the farmer in his breeding operations by three years. A manufacturer of farm machinery, on the other hand, sometimes makes actual sales of finished products before going to the iron mine to get his raw ores. Indeed, agriculture is less able to anticipate unusual fluctuations and has less control over the price of its finished product than any other industry. Agriculture, therefore, above every other industry, requires stability for its successful operation. When farmers receive a profit on their operations they pay their obligations and buy the output of our factories. Your problem then is to give the farmer a fair price and reasonable stability and he will be happy and city soup lines will fade into joyous lines of shoppers.

War always provokes dislocation of industry and derangement of the monetary stability of the nations. It has become trite to say that we must expect economic disorder and hard times after all wars. We are informed that there is nothing to do about it. Farmers, a year ago at farm outlook meetings sponsored by the Department of Agriculture, were shown a graph showing that there was a thirty-year price decline after Napoleon's wars and a thirty-year price decline following the Civil War. Indeed, wars usually have been settled by boundary adjustments and political re-alignments without regard to the economic maladjustments growing out of displacement of the commercial life of the nations. For these disorders public men are prolific with plausible proposals that bring no relief and that only prolong the agony. Ferrero points out that the destruction of the world's merchant and banker, Carthage, in the third Punic War, provoked the hard times in Rome in the second century B.C. That depression gave expression to the first farm relief and the first dole system in recorded history. Unfortunately, politicians from Cato and the Gracchi down to date have learned little about the real causes of economic disorders. But they remember too well plausible fallacies.

Wars, of necessity, produce price rises and inflation. They also produce monetary disorders. Politicians can do nothing directly about price levels, but from the time Caesar's head appeared on the coins of Rome until now, politicians have had everything to do with the monetary stability of a nation. Our constitution particularly charged our Congress with that duty,

and congressional monetary tinkering has aggravated nearly every period of inflation and depression.

The trouble with America is that we have forgotten elementary economics. We are entranced with the sales talk of those purveyors of so-called economic services who measure the crest, the dip and the length of the curves of past cycles and attempt to forecast the propitious curve of the cycle which is to usher in good times tomorrow. Watching the curve of a cycle will not cure our economic ills. I note that that clever Englishman, Keynes, has recently approved an observation of mine made some eight years ago that the world's major depression, called the Dark Ages in our histories, lasted many centuries.

A glimpse at past periods of distress, however, will be helpful and does not confirm the thesis that they are periodic or move in cycles; on the contrary, they are man-made and can be cured by appropriate action. If my old seventh-grade history serves me well, the crisis of 1873 followed "greenback" inflation accentuated by the Franco-Prussian War and was liquidated by the unpopular gold specie resumption decision. Probably the price declines in 1872 and 1873 were influenced by payment of the French indemnity. The 1893 trouble grew out of silver inflation, was precipitated by a doubt as to gold resumption, was prolonged by free-silver agitation, was ended by the unpopular reaffirmation of the gold standard. The panic of 1837 followed unsecured state bank currency inflation after Jackson had destroyed the National Bank, and wore itself out painfully; recovery in the end was probably aided by the gold discoveries in the West. The minor disturbance of 1907 was geared to a currency stringency which induced us to establish the Federal Reserve System. Even Shays' Rebellion was a reflex from continental currency inflation and from the disordered state of public affairs with no adequate public money of any kind. Hamilton saw it, made it an argument for closer federation, and in the 15th *Federalist* pointed to farm distress as he urged votes for the Constitution. That sane political economist never stopped his program for farm relief until he had consolidated the public debt and had established his National Bank with adequate stable currency. Then the farmers forgot surpluses and prospered. These old stories

are recited to refresh our failing memories. There were many other factors in the equations but we need to keep in mind the fact that there is an intimate relationship between periods of depression and monetary disturbances. Two of the worst of these depressions, in 1837 and 1893, had no war background.

But false gods are always attractive. Always there are those ready to breach the walls if necessary in order to introduce a wooden horse full of destructive forces. Today one can hear the crash of the pick and crowbar loosening the capstones on the walls of our economic citadel while others are busy with spade and shovel undermining the foundations of our free government.

Almost all the futile proposals can be classed under two heads:

First, inflation plans, schemes to devalue the dollar, including re-emergence of the free-silver idea.

Second, a plan to create a domestic economy with America isolated as Japan was when Commodore Perry stormed her gates. This latter plan includes price-fixing for farm produce and frantic proposals for crop curtailment, in short, a scheme that would sovietize our agriculture and our commerce.

The World War upset everything. During the two and one-half years we remained neutral, our gold stock increased over a billion dollars. We also accumulated four billion dollars worth of American securities owned abroad. The need to check this flow of credit instruments and gold to America, indeed, the imperative necessity to prevent monetary panic in the Allied camp, while we prepared to fight, gave birth at once to the War Loan Act. In the words of this law, "For our national defense and for the better prosecution of the war", our Treasury prepared to furnish ten billions of credit to the United Kingdom, France, Italy and the rest.

That statement of purpose is not an economic argument, but it is in the law. I don't know why the politicians put it in. I suppose they thought it would sound more reasonable than to lend the ten billion without giving any reason. They did not lend the ten billion for 5 per cent, nor 3 per cent, nor 2 per cent, but they did it for our own national defense and for the better prosecution of the war.

The war over, this ten billions of Allied indebtedness to our

Treasury and the reparations assessed to Germany at once became the problem of the respective parliaments of the nations concerned. Being a mere pig and wheat raiser, I have not had one peep behind the scenes, but I assume that if the dozen or twenty leading and responsible statesmen had had a free hand these problems might long ago have been resolved. Not so with the politicians in the representative halls of the countries involved. They feared responsibility for giving away to some foreigners one dime of the taxpayer's money.

Always ready to experiment with the monetary standards of the United States, our own Congress probably did not perceive that here was a worldwide monetary disorder disrupting the economic security of every citizen of the republic. Here was a disaster encircling the planet and reaching into every home and into every farmstead in our own land, but they apparently did not realize that in their hands lay the greatest responsibility to find a solution. Money, a medium of exchange and a measure of value, is also a lubricant of commerce. Sound money throughout the world would permit business to pick up. But the parliaments of the nations have disregarded the relationship of these intergovernmental debts to world-wide monetary stability. In the words of the prayer book, they have done everything that they ought not to have done and have left undone everything that they ought to have done. Naturally there is no economic health anywhere in this upset world.

Permit me to discuss here, briefly, the case of wheat. Wheat, more than steel, is the barometer of trade. Especially does it reflect farm health more readily than anything else. More than any other production on the planet, it is sensitive to world currents everywhere. Find a sane remedy for the wheat problem and that remedy will be a cure for all farm problems.

Seven years ago I had a wheat graph prepared. It registered supply and demand conditions, reports of drouth in Argentine or Australia, excessive yields in Canada and Kansas, but it also reflected the murder of Rathenau, the disagreement of Lloyd George and Poincaré, the failure of Briand at Cannes and an expression by President Harding to newsmen that we should do something for Europe, which last sent the price scurrying upward. But none of these events

were coincident with the major wheat-price movements. Later, while furnishing some material on war debts to a high school debating league, we prepared a gold export and import graph and geared it to the wheat graph. We found a rather startling relationship between the gold movements to and from America and the price of wheat. Indeed, the largest wheat-price movements invariably occurred without regard to crop news or grain shipments. The tragic drop in November, 1920, with one of the smallest world grain crops for twenty years, followed the heavy gold movement to America to meet the accruing Anglo-French commercial loan that was then maturing. Germany's efforts to pay reparations in the fall of 1921 and the coincident broadcasting of marks with a heavy gold movement again precipitated a major wheat decline. By May, 1922, Great Britain made a first considerable payment on the war debts with substantial gold shipments and again the wheat price tumbled down. The next payment by the United Kingdom, in May, 1923, with another abnormal gold movement, sent wheat down again. The promise of the Dawes Plan as to reparations and the progress of debt-funding agreements calling for low payments for a period of years, sent gold abroad for the first time late in 1924, and early in 1925; and the wheat price shot rapidly upward.

War debts and reparations disappeared from the press and from congressional discussion for several years. Our international bankers, by loans, assisted in making the payments for several years. Occasionally some economist warned that there would be trouble when these payments rose to higher levels. Farm commodities brought fair prices, not for one or two items in the list, but for practically everything. Especially was this true in 1928, when the low discount rates at the Federal Reserve sent gold outward. There was still complaint from certain farm organizations, but the vast majority of farmers were well satisfied with the prices and conditions obtaining.

Moderately good times on the farm, moreover, were reflected in abnormally good times in the cities. The redundant gold in America expressed itself in the California and Florida booms and finally in the stock-market orgy. In 1929 we again drew gold from all the world to supply our high call-

money market. Neither Germany nor any other country could extract any more gold from our coffers. Our tariff bill, unconsciously designed to prevent them from selling us goods to meet international engagements, was the signal for the similar efforts abroad. The latter were especially set up to prevent us from shipping wheat to them. This was only half the trouble. The necessity, in the fall of 1929, to make payments on reparations forced Germany to sell goods abroad at any price. The result was reflected in the sharp down-turn in the commodity price curve, first in Germany. A similar price downturn soon occurred in the United Kingdom as she paid a war-debt installment.

Agriculture had been observing the stock boom with something like amusement. Farm prices were not high. Why should we worry? Let the city boys have their fun. But the necessity of Germany and Britain to meet war debts and reparations set in motion an evil chain of forces that sent prices on the toboggan. As to farm prices, the frantic political efforts only added to the trouble. Over-advertisement of the difficulty and over-emphasis on Russian possibilities drove out the speculators and added another weight to the market. The unprecedented world wheat crop in 1930, nearly five billion bushels, was most inopportune for the wheat farmer. But Russia's enormous crop, after all, resulted in less than 100 million bushels of exports. For her 1931 crop the exports will be much less. It is now evident to those familiar with the problems of mechanized agriculture that the Russian experiment on communal farms is doomed to failure. These mechanicians and farm experts received their training in a book written from field notes made in Dodge City by a Russian Commission. The intricate farm machines successfully operated by mechanically minded, well educated young farmers in our West will not lend themselves to the use of communistic experts whose mechanical experience has been with nothing more complicated than a wheel barrow. I also understand that cotton culture abroad has not succeeded in any substantial measure.

Thus our two prime items of export, cotton and wheat, if not interfered with by artificial barriers like payments on war debts and reparations, can resume approximately their

normal position. In a world so badly disordered as ours now is, man's basic, elemental need will be met first. Wheat, the staff of life, will joyously lead the procession to better times if the economy of the world can be reorganized on a rational basis.

I have not here time to develop the fact that the public agitation of this problem in Congress and in certain sections of the press, with frenzied hysteria against making any adjustments, has increased the difficulty tenfold. For this public advertisement of a very difficult situation has engendered fear and distrust, has undermined confidence in the stability of Germany and Great Britain and has added to the panic psychology. Nor will I linger longer on the academic problems presented.

When everything is wrong nothing is so damnable as to do nothing about it. The time is past for appointing commissions of experts. The time is past for reorganizing the Debt-Funding Commission. The time is ripe for carrying this problem out to the field, the sidewalk and the kitchen. The West knows it is suffering from worldwide difficulties. It needs an opportunity to look this problem squarely in the face.

Dr. Seligman wrote me a number of years ago that it would take a more protracted distress out West to bring statesmen to their senses. The distress that we are enjoying out West is severe enough and has been protracted for all the days that we think necessary; but statesmen who in private conversation admit that the European monetary disorder must needs be remedied, still are hopeful that they will not have to go on record as having given away one dime of the taxpayers' money to help someone in Europe. They even seem to hope that by repudiation on the part of some of the transatlantic countries the difficulty may solve itself. They seem to lose sight of the fact that such action would lose those markets to us forever.

With crop disaster impending over millions of acres, with supplies dwindling, Ivar Kreuger's suicide sent wheat scurrying to lower levels a few weeks ago, showing again our intimate relationship to affairs in Europe. Wild fluctuations in sterling for three days following the Easter holidays should call our attention to the fact that money defined as a measure of

value was lacking in some of its functions. Normal commerce cannot function while such fluctuations prevail. If those frantic and hysterical members of our public and our Congress would grant a responsible unhampered commission authority to adjust these debts to a rational, performable basis, based on an honest measure of capacity to pay, sterling could probably be stabilized in three hours, though probably not and preferably not at the old par. Once that was achieved the rest of the world's business machine would begin to function more normally. The rest of the problem would not be settled so easily. French politicians would have to be conciliated as well as our own at Washington, but the French are already expressing themselves in much more conciliatory manner than our own statesmen.

Our own Congress is asked to consider again the equalization fee or the debenture for agricultural relief. Since the debts solution would open the gate to Europe's market, might it not be worth while to give our Congressmen something more tangible to present to their constituents? Why not suggest that by adjusting debts, markets could be found for the surplus production of our farms? A hard and fast rule might provoke trouble but (since markets are what we would get anyway, without a rule) Congress might be permitted at least to make a rule if it would break the impasse that now has stopped political consideration of the problem in America.

For example Robert Sterling, in the *Northwestern Miller*, has made the definite suggestion that for every one hundred dollars worth of annual exports of farm produce to Europe and debtor countries we remit a certain sum on the debts—10, 20 or 30 per cent. If we would now remember that the rule of capacity to pay was never really invoked in the adjustments that have been made in the last ten years, it would help many to understand this difficulty. The rule invoked was what statesmen thought would sound plausible to their respective publics. Capacity to pay is not what sum one's grandchildren can be cajoled into paying; capacity to pay is such a sum as an investor or a banker will pay for one's note.

A formula set up with such a rule to measure capacity and having regard for the monetary stability of the nations involved, and with a softening of the rule out of regard for our

moral obligations in the premises, will resolve the political debts into two categories: those that can and should be paid on the one hand, designated as the A portion, and the remaining part of the obligation, which we will denominate the B portion.

With such a formula before them, two Westerners, Dawes and Traylor, could resolve these problems in a few hours. If they were reluctant to serve, I could find five Kansas pig and wheat raisers, competent men, who will serve without pay. Once the A and B portions were discovered we could determine whether it would be better to seize an island belonging to Great Britain to save the B portion, as suggested by the most rabid proponent of collecting the last dollar, or whether it might not be worth while to suggest that we annually remit 20 or 30, or even 40 cents of the B portion of these obligations for each dollar of farm produce, wheat, cotton and meat—elemental necessities needed by European nations—that they purchased from us during that year.

No prudent creditor and merchant wants to force his customer to default. The airing of the difficulties by the debtors at Lausanne will not solve the difficulty, will not help much. It may do infinite harm if by evincing hopelessness it should provoke collapse in Germany. Let the biggest banker and merchant concerned take the lead. Thus will prices for farm products be restored. Thus can agriculture lead the procession to better business and a happier world.

Money, a medium of exchange and measure of value as I have already noted, is a lubricant of commerce. The world's business machine has plenty of gas in the tank, the ignition and the starter are in good order, the headlights are shining; the tires are properly inflated; the body does not even need repainting. But the gears are jammed. Lubricate all its parts! It's ready to go.

THE BASIS OF GERMAN CREDIT

O. C. KIEP

German Consul General, New York

IN the hectic days of 1923, when "billions" and "trillions" of demoralized paper marks were being printed and the people of Germany were clamoring for a new stable currency, the German government of the time felt great hesitation in taking the necessary legislative steps. Action was delayed for a long period. There was a threefold inhibition: First, they doubted whether any new monetary unit would be accepted by the people unless backed by gold, of which, however, none was available. Secondly they feared that the people might have lost confidence in the banks and savings institutions which, in the popular view, had just stolen all their lifelong savings. The people, it was feared, might proceed to hoard the new currency, thus preventing it from fulfilling its purpose. Finally, in view of the total bankruptcy through which the economic system of the country had passed, and the losses thereby incurred by foreign holders of marks and mark credits, the new currency might lack support outside of Germany and the country might thus be cut off from foreign credits for an indefinite time, until new confidence should have been established. As a matter of fact, however, these fears proved to have been groundless. For, when the new currency was introduced, the "miracle of the Rentenmark" happened. The German banks and savings institutions were entrusted by the people with new savings which grew at a surprising rate, and a stream of foreign credit started flowing into the country within some twelve months. This influx was regarded as a further miracle, in view of the complete devaluation of the old mark. What was the explanation of this surprising restoration of confidence at home and credit abroad, after the fearful experience of the German economic system in the process of total inflation?

Credit or, expressed in the abstract, confidence in financial and economic relations, is founded upon a threefold basis:

[84]

technical, psychological and political. The technical basis of credit under our capitalistic system is a stable and sound *currency* which assures the future fulfilment of pledges expressed in its terms at the same value as at the time of commitment. Conversely, the general belief in the existence of such assurance is the condition precedent to acceptance and maintenance of a currency not backed by tangible gold values. This assurance appeared at the time to be given by the guarantees against inflation embodied in the laws creating the Rentenmark and, later on, the new Reichsmark secured by gold. The acceptance of the Rentenmark, secured by no actual gold, but through gold mortgages attached by government decree to the privately owned real estate of the country, was at first more or less an act of despair: exasperated by the experience of the past five years during which the currency had incessantly been dwindling away in their hands, the people grasped at anything which promised to maintain a stable value. And they brought their newly acquired Rentenmarks to the same banks which, in their eyes, had just robbed them completely of their lifelong savings. Through a careful system of control, preventing the Rentenmark from going outside of the country and protecting it and the remaining paper marks, now stabilized, when they did appear on foreign markets, it proved possible to give and maintain to the new currency also outside of Germany a parity value. This was so at least until, with the assistance of the gold acquired by Germany under the Dawes Loan, a regular gold-secured currency with unchallengeable domestic and foreign acceptance and valuation could be established in the Reichsmark. Thus the primary or technical condition for a return of German credit after the debacle of 1923 was fulfilled through the creation and maintenance of a stable currency.

The second factor which made possible the economic comeback of Germany in 1924 and which I have termed the *psychological* basis of credit, comprises all those material and ethical elements on which the business structure of a country is built up under our modern capitalistic system, such as: natural resources, industrial and business organization, physical, intellectual and moral man-power, the traditions and ethics of trade relations at home and abroad. During infla-

[85]

tion with its strong urge to capital investment—the so-called “*Flucht in die Sachwerte*” (flight into physical values) as we termed it in these days—Germany had been able to rebuild her industrial and agricultural machinery and, through the premium of low costs of production, extensively to reestablish her foreign trade in a world calling for replacement of war losses. Thus Germany presented an attractive proposition to the foreign investor. This incentive to industrial and foreign trade development was, incidentally, the one redeeming point of inflation, as we experienced it. The terrible ordeal of the people affected by its expropriative action is often overlooked by those who have not gone through the actual experience at their own expense. The effect of German inflation outside of the country had, as a matter of fact, not been so much felt as might have been expected apart from the competitive factor in world trade just referred to. Foreign trade, at its resumption after the war and just when the value of the mark had so declined, was pretty generally transacted on a gold or foreign currency basis. Losses, therefore, were more or less restricted to the holders of German currency and securities—largely on a speculative basis—, against which a substantial offset was formed by the easy acquisition of values within Germany, mainly real estate, bought up on a large scale by foreigners paying with guilders, francs, kroners, etc. This is probably why the devaluation of the old mark did not act as a deterrent to foreign investors to the extent feared by the German government in 1923. The reestablishment of the technical basis in a stable currency paved the way, while the promising and apparently prosperous condition of the German industrial and business structure offered the inducement to the superfluous capital in the world, for the great movement into Germany that followed. This confidence of the outside world was at the same time the main reason for the reestablishment of confidence at home, which inflation and its effects had in the preceding period so deeply undermined. The people returned to their old habits of saving and the creation of new internal capital available for investment proceeded at a surprising pace. So strong is that human urge to save and provide for the future which is the basis of our capitalistic system! The introduction of the Reichsmark on an actual gold basis con-

stituted the second and decisive factor toward establishing confidence of the German people in themselves and in their government. It was at the same time the strongest expression of confidence on the part of the foreign countries from which the gold was loaned. Thus the technical and psychological basis was furnished for the new era of German credit following immediately on the bankruptcy of inflation.

A third factor was, however, requisite in the sphere of *politics*. In entrusting this great volume of their superfluous capital accumulation to investment in Germany, at that time mostly on long term, the individual investors and governments were guided by the conviction that the new era of war liquidation inaugurated by the Dawes Plan was to be of some duration and that the process of liquidation had been definitely freed from the political conflicts which had been responsible for the destruction of the past. And in like manner, by accepting this great volume of credit with its responsibilities, as felt by the conscientious borrower, by returning to work, to business enterprise and to new saving, and by confiding in their government and its policies, the German people were also expressing the belief that stability was now permanently established and that the fruits of their labor were not again to be destroyed by political conflict, reprisals and sanctions.

Thus with the year 1924 a new era was ushered into Germany and German credit rose high in the world of finance and business. It was contemporaneous with a new era throughout the rest of the world; with what appeared to leaders in all countries to be not the first replacement boom traditionally following wars, but a completely new epoch in the economic development of the world, reaching out to dimensions heretofore unknown and representing the realization of newly discovered devices in the organization of national and international production and trade. I shall not undertake within the framework of my present theme to offer any suggestions as to the soundness of this belief or its possible correction. But I may be permitted to express a thought in connection therewith which has a bearing on my subject, Germany's credit basis, and is perhaps of interest to those of Germany's creditors who have voiced doubt respecting the conscientiousness of their debtors in the use of the monies loaned. It is, that the

lenders were largely the propagators of the new era theories and that their well meant and friendly advice, based on experience in their own countries and given with the authority of the successful business man, had doubtlessly considerable effect on the minds of the business leaders of Germany. In counselling against the seemingly too expansive policies of the latter, responsible Germans were frequently met with arguments taken from the arsenal of the new era theory; whilst in the movement for high wages which the German trade unions were able to carry through during the period of expansion, the theory of financing consumption in order to promote production was successfully argued in a country burdened with the paramount duty of expanding production at all costs in order to earn the wherewithal to pay a prodigious political debt. It was very hard indeed in these days to advocate in Germany and for Germany the very reverse of the policies which the whole world was proclaiming and apparently prospering on; and it was difficult to convince the German business leader and workingman of the old truism that an expansion of production and consumption can only be safely embarked upon by him who can finance the increase from his own accumulated savings.

The history of what has happened in Germany since the peak of this era of expansion and prosperity in 1927-1928 and of the development of the world economic situation since 1929 is too well known to require repetition. As far as Germany is concerned, it has been stated in classic form by the reports of the two committees convened under the auspices of the Bank for International Settlements in August and December, 1931, and presided over by Mr. Wiggin and Professor Beneduce. The figures cited in these reports give the picture of the present economic and financial situation of Germany, aggravated in the meantime through three further months of industrial and business contraction, of increased unemployment resulting therefrom with consequential reactions in public and private finance, and of continued withdrawal of funds by all permissible and forbidden methods available, as a result of progressive weakening of confidence at home and abroad. These figures and further developments form at the same time the background for an appraisal of present-day German credit and its basis. Of the factors determining the credit basis today the following may be said.

[88]

The technical or currency factor the German Reichsbank has been able to maintain with the aid of ever more stringent measures of control and with the generous coöperation of the foreign private creditors united in the so-called "Standstill Agreements". This has, in spite of all hardships and hindrances involved in the control system, been gratefully appreciated by the German people and business world; and I hope I may add, also appreciated by the foreign creditors, as whose trustee the Federal Bank is largely acting. The guarantees against internal inflation continue to act as before, at least as far as the most important factor in the technology of our modern monetary system is concerned, namely the restriction of the volume of currency and credit issued to a legitimate correlation with the volume of trade and movement of goods. For this reason it has been possible fairly to maintain the parity exchange value of the Reichsmark, although it has been menaced on its external front through the recurrent extensive withdrawals of gold while on the internal front it is still jeopardized by hoarding. The former of these two factors is a danger to which every country with a passive balance of payments is exposed, but which can be coped with in practice, to a large extent, through governmental control of all payments to and receipts from abroad, as exercised under the German emergency decrees, and the application of corrective action when required, even though at the expense of foreign creditors. After the credit crisis of last July Germany was obliged to take resort to much the same system of controlled currency which has been in force for extensive periods in other countries lacking gold. The menace of hoarding which arose in Germany as a consequence of the temporary closing of banks and savings institutions at that time, but which since then has to a certain degree subsided, is, of course, a danger that, be it applied to gold or to notes, can befall any country as the consequence of a psychosis of fear and distrust. If not checked by the available remedies, it can lead to the complete destruction of any monetary system, even though it be backed by the greatest supply of gold. For the monetary system is a technical machinery provided for the transaction of the ordinary business of a country and cannot be used to mobilize the whole national wealth. Thus we may assume—and German domestic

[89]

and foreign credit is today based on this assumption—that a continued rigid and correctly handled control supported by further coöperation of the foreign creditors, as provided by the Standstill Agreements, will continue to uphold the currency basis of Germany's credit structure.

The same, I venture to say, refers to the second basis of credit, the psychological or general economic factor. For no one is more interested in upholding the country's credit than the people themselves and their agencies in industry and trade. Being deprived, through its industrial development of the past and by the further increased industrialization under the pressure of post-war obligations, of the possibility of sustaining itself, Germany is dependent on foreign trade for the nourishment and occupation of her people; and her foreign trade, which today is financed by foreign credits, requires these in present and future as in the past. Thus the tradition of German business in respect of conscientious fulfilment of financial and other engagements will remain unaltered in the same manner as the people will continue to coöperate in a stable management of their country's currency and economic life with the utmost insistence. For they fear and abhor nothing more than the thought of new disorder and inflation. If we add to these psychological factors the capacity and urgent desire of the people to work and the availability of an excellent industrial and trade machinery, rationalized for greater and better production in the period of prosperity, there is no reason to doubt that service on the present foreign investments in Germany and their repayment in due time is assured to the creditors. They require today the sum of about 1600 million marks annually whilst Germany was able to export a surplus of about 3 billion marks in the year 1931; and though this was achieved under special conditions of pressure to realize and liquidate for the purpose of repaying withdrawn short-term credits, and called forth a worldwide reaction on the part of the recipients of that export surplus by way of tariff safeguards and import restrictions, it is to be assumed that an export surplus of half that volume produced primarily through limitation of imports should prove feasible under normal conditions.

For such normal conditions, as far as Germany is concerned,
[90]

a satisfactory adjustment of the third component part of the credit basis, the political factor, is essential. The German people and their creditors must be reinspired, as in 1924, with the belief and confidence that economic stability is not to be menaced by political conflicts; and herewith we arrive at a problem the discussion of which has been assigned to another speaker, namely the reparation question awaiting solution some weeks hence at a new international conference. Assuming such solution to be found, I have no hesitation in closing my analysis with the finding that the basis of German credit was safe and sound in its various aspects, technical, psychological and political, when the present volume of foreign capital was confided to the German people by private investors from all parts of the world; that it is fundamentally sound today and will continue to be so, if peace and stability can be assured to the economic system of the world.

If I may be permitted, I would add a thought that has frequently occurred to me during the many discussions we have all participated in or been subjected to during the past year and in which so many accusations have been raised against our capitalistic system on account of its alleged responsibility for the ordeal of depression and its asserted incapacity to manage the economic affairs of the world in an orderly way. My thought is, that there has perhaps never been witnessed in history an economic process more expressive of the inherent material and ethical value of the capitalistic system, than the great migration of private capital from wealthy to impoverished countries during the post-war period of reconstruction of which Germany was so extensive a beneficiary. It is just this characteristic of capital in private ownership that it knows no national prejudices or inhibitions, which lends to it its most appealing quality: that it cannot stay idle in the hands of its owner, but must go forth to work for him who is in need of it and can employ it. All economic and social progress in our modern civilization has been brought about by this feature of the capitalistic system, all spreading of this civilization throughout the world, all development of new countries, elevation of backward peoples. The same effect is inconceivable if we imagine the wealth of peoples and states controlled by their governments. What dictatorship or what democracy would
[91]

undertake the responsibility and risk of devoting the superfluous national wealth of the land governed by it to the assistance or advancement of another land without the desire of conquest or other political aim? But our much maligned capitalistic system does so: the private owner of accumulated capital who lends it out for investment has at all times been the pioneer of economic progress and has in the time of post-war reconstruction been the chief agent of healing the wounds of war. Germany has, as I stated, been one of the main beneficiaries of this feature of the capitalistic system and, in striving today to uphold the service on the private monies loaned to her nationals in replacement of their own former savings, which were consumed by war, inflation and war tributes, and assuring their repayment at maturity, she is not only seeking to maintain her good name in the world and to maintain that without which she cannot live, her credit, but she is also carrying on a fight for the capitalistic system in which all who are interested in its upholding should lend their support.

It has been subject to many trials and demoralizing influences during the last eighteen years, this capitalistic system, and its fundamental and foremost principle has almost been obliterated from the minds of men: namely that capital is built up by accumulation of savings and that only that which has been earned can be spent. In the war all nations proceeded to financing by borrowing on a scale which alone almost spelled destruction to the whole system. As borrowing alone did not suffice, additional funds were supplied by the bank-note printing press and all the laws governing currency organization were disregarded with the most destructive effect to most of the existing monetary systems. The demoralizing effect of inflation on the economic and social system, as on the human character, cannot be exaggerated: forcing, as it does, men to spend in order to avoid the confiscatory effect of devaluation; enabling exploitation by some at the expense of all and finally robbing the economically most valuable part of the population, those who have saved and thereby furnished the foundation on which their country has been built up, of all they possessed. The German people went through all this and then started to build up a new financial system in which

the people of almost all countries in a position to do so, helped and participated. Now again this new structure is threatened and already a new demoralizing influence is at work on it in the governmental control and interference enacted by the emergency decrees since the crisis of last July. Again the individual is being subjected to confiscatory measures on the part of the state, again the private owner is being deprived of his property rights and responsibilities. The disease is spreading beyond Germany, in that already almost twenty countries in the world have resorted, for one reason or another, self-defense or retaliation, to measures of exchange control and replacement of the gold standard by "managed" currencies. Truly, an appalling sight and one calling for the most serious apprehension for the future maintenance of the capitalistic system among responsible thinking men throughout the world. If this process continues, if political powers and considerations continue to override the rights of private property, as in the war, and if the delicate structure of international credit relations, which has been built up by the honesty and reliability of private business through generations, is further to be made the machinery of political conflict, then *caveant consules!* The question of Germany's credit, which, in its fundamentals, still rests on the soundest basis and can be maintained thereon if the tenets of the capitalistic system are upheld by those in a position to do so, thus appears to involve a question of principle vital to all other countries that participate in the economic organization of the present world.

THE POLITICAL ASPECTS OF WAR DEBTS AND REPARATIONS

SHEPARD MORGAN

Vice-President, Chase National Bank
Former Finance Director, Office for Reparation Payments, Berlin

THE political aspects of war debts and reparations are not separate from their economic aspects; they include them. Or, to put it another way, the relationship between the two is reciprocal. The interplay of political and economic forces is indeed not confined to war debts and reparations but must be admitted as a general truth with which we must always reckon. Not once but many times, both here and abroad, we have seen economic causes producing profound political results; and, on the other hand, political causes have produced economic results, some of a beneficial but more frequently, of late, of a catastrophic character. Political and economic forces weave and interweave, and in the complicated web they make there is no clear picture, either exclusively political or exclusively economic.

This is a truth which Americans on the whole are slow to accept. When we do admit it, we apply it only in rudimentary fashion and often in a local and usually personal sense. Business is as free to blame Congress with playing politics with finance, as Congress is to blame business with playing finance through politics. Such exceptions do not alter the central fact that Americans want to keep politics and economics in separate compartments. For when politics and economics mix we think something is wrong and the evil must be stamped out whether its elimination is against nature or not.

So it is not to be wondered at that we have insisted as a matter of national policy upon regarding war debts as an exclusively financial matter. Indeed, we have gone further. In our discussions of reparations, and in the efforts to solve that problem which Americans from time to time have undertaken, we have endeavored to exclude all political factors both from our minds and from the solutions. We have gone at both

[94]

reparations and the debts in a thoroughly business-like way, have applied the usual financial tests, have supported the capacity-to-pay principle to the limit of reason and, where we have had the determining voice, have carried it out to the limit of business liberality. We have regarded the debts as money borrowed and reparations as debts incurred. Therefore, we have assumed that both would yield to ordinary business treatment, and that because political considerations were nominally excluded they did not exist.

In addition to this assumption we made another, which interlocks with the conception that the debts are exclusively economic. This assumption, earnestly upheld from the beginning, is that the debts and reparations are separate and distinct. According to the usual financial test, this position is unassailable. It is no affair of a creditor where the debtor gets the money to pay with, unless specific assets or revenues are pledged for the purpose. In our debt settlements we exacted no security from our debtors, least of all reparations as security. Consequently, the business transaction of reparations has nothing whatever to do with the business transaction of the debts. We look no further than the faith and credit of our debtors; where they get the money to pay us, whether they receive reparations or not, is their own affair and not ours.

Our debtors have always questioned this assumption. While to us it was most natural to treat the debts according to the ordinary rules of business, it was equally natural for them to treat them according to the rules of politics. When it was disclosed that we were really in earnest in regarding the debts as a commercial obligation and were unwilling to throw them into the general political settlement at Versailles, the debtor countries added them to the German bill. The policy then established has never been departed from. The Balfour Note of August, 1922, fixed the amount which Great Britain would expect to receive from her debtor Allies and from Germany as identical with the amount of her payments to the United States. The Concurrent Memorandum of June, 1929, which was attached to the Young Plan but not made a part of it (for it was not signed by the American members of the Experts' Committee) was even more explicit in the same sense. For after listing the net amounts the creditors of Germany

[95]

were due in turn to pay out in satisfaction of war debts, the memorandum provided that three-quarters of any relief they might eventually receive should be passed along sooner or later to Germany. The Concurrent Memorandum later became part of The Hague Agreement of January 20, 1930, and is therefore a part of the present reparation settlement. It establishes the principle, effective upon all interested parties except ourselves, that German reparation payments and the inter-Allied debts are in fact connected. But more than that, it constructively denies our assumption, again without our admitting it, that the question of the debts is purely economic, and interjects them headlong into the field of political controversy.

I have taken this much of my time in order to suggest to you that our effort to keep reparations and the debts in the cool atmosphere of economics has been in vain. I speak both of the debt settlements which have been officially carried through, and the reparation settlements—the Dawes Plan and the Young Plan—in which we have had leading but unofficial participation. The fact is that we deliberately set our minds against the political aspects of these things, partly because we took debts and reparations at their face value as affairs of finance, and partly because we considered strictly economic solutions to have the best chances of success. We tried to exorcise the political factors by denying them. But they did not stay exorcised.

The cost to us has been immense. Detached as we were from the political antagonisms which the war vastly intensified, we went ahead to carry on business as usual, and before long we found ourselves carrying it on rather more than usual. In Germany alone, confident that the political factors of disturbance were dormant, we invested about two and a quarter billions of dollars. Except for the unpredictable operation of political factors, I believe these loans taken as a whole to have been safely placed. With the same reservation, even after the dislocations of this period of unparalleled depression, I believe them still to be safe. The trouble was that we forgot the war, whereas Europe remembered it and still remembers it. Suppose our neglect of the political factors to have been justified, suppose they had remained dormant,

[96]

no doubt we would have suffered an economic set-back in any case; but it would never have passed, as we have seen it pass, from slow business into depression and then into panic.

Consider for a moment the politico-economic sequences of the past four years. I start from the decision, reached at Geneva in September, 1928, to set up a committee of independent financial experts who were to draw up "proposals for a complete and final settlement of the reparation problem". The Dawes Plan had already been in operation for four years and had gone far to justify the American theory that if reparations were taken out of politics, the problem was solved. But the time had come to change it, and from the moment the political representatives of the governments at Geneva resolved to summon the Young Committee, the political sky darkened; for it was on the proposals of this committee, as it was then supposed, that the whole future course of reparations was to depend. Overnight the problem of reparations resumed its political aspect, which it has not lost from that day to this. The Young Committee, notwithstanding the fervent efforts of several of its leading members to exclude political considerations, and notwithstanding its success in arriving at an ingenious financial solution, was obliged to take account of political factors. It said in its Report:

Throughout our deliberations and in our present proposals we have endeavored to reach our conclusions on economic and financial grounds. But we have realized, like our predecessors [the Dawes Committee] that political factors necessarily set certain limits within which a solution had to be found if our proposals were to secure acceptance. We had therefore to base our decisions not only on economic, but also to some extent on political considerations.

In the course of the Young Committee's work an incident occurred, which in retrospect takes on a singularly sinister aspect. This was the decisive fall in the reserves of the Reichsbank, threatening if carried much further to undermine the whole German credit and currency system. The German banks, then as later, were heavily in debt to foreigners, who of course were at liberty to withdraw their funds at short notice. As the negotiations of the Young Committee approached a deadlock, these funds began to be withdrawn with a corresponding decline in the Reichsbank's stock of gold and

[97]

foreign exchange. When the deadlock appeared inescapable, the withdrawals intensified into a run on the Reichsbank's reserves. Here was a new instrument ready at hand for exerting international pressure, and we have seen it in use many times since. The question at once arises whether it has been deliberately used as an instrument of national policy. Whether the answer is yes or no makes little difference in practice, for the result is the same. Capital is extraordinarily sensitive, and it takes fright whether told to be alarmed or not. In this case, the Germans broke the deadlock by yielding, and the run ceased.

The remainder of the record is too fresh in your minds to require detailed exposition. The political factors in it include of course the recurrent problem of reparations but they are by no means confined to it. Reduced to their simplest terms the political factors are these: On the one side, the French desire for security, which all of us must admit is an inalienable and unquestionable right. But in practical application it raises numerous issues which have become matters of international negotiation and sometimes of controversy. These include questions of armament, of offensive and defensive alliances, and what is more important still for the purposes of the present discussion, the use of financial authority as an instrument of national policy. This last point concerns us particularly in the United States, for whenever it has been used it has exerted a direct and powerful influence on the course and intensity of the depression.

On the other side is the German desire to escape at last from the restrictions, burdens and discriminations imposed by the Treaty of Versailles. Like the French desire for security, this desire on the part of Germany has, I believe, the support, on the whole, of American public opinion. But in practical application it also raises questions of the utmost complexity and difficulty, such as the Polish Corridor, armaments, commercial arrangements with Central European countries, the charge of exclusive responsibility for the war, and of course reparations.

From our detached American point of view these two desires do not appear to be necessarily in conflict. To us, in our own security and at a distance of three thousand miles, the

[98]

methods adopted by France to buttress her security have seemed adapted at times to impair it, because they have tended to put her neighbors in a state of psychological armament against her. Similarly, and from the same vantage point of distance, we consider the behavior of Adolph Hitler and his supporters to offer no promise whatever of obtaining the concessions which they in common with the rest of the German people want. But the fact is that the conflict exists, and the sequence of events arising from it has converted the depression into a panic.

The chain of cause and effect is complete. As in 1929, when deadlock in the reparation conference resulted in a run on the German Reichsbank, the success of Hitler in the Reichstag elections of 1930 was promptly followed by withdrawals and losses of gold. Again, in the spring of 1931, when the German and Austrian governments announced their plan of a customs union, the political disturbances thereby created immediately revealed the weakness of Austrian finances and precipitated the collapse of the principal Vienna bank, putting the whole Austrian credit and currency structure in danger. The French offered a loan, but on terms which were tantamount to renunciation of the customs union. The offer was declined, and the Bank of England made the loan instead, thereby temporarily relieving the situation as far as Austria was concerned. The storm then spread to Germany, where the incidents of 1929 and 1930 were repeated, but on a far greater scale. The Hoover moratorium failed to give relief, largely because it did not meet political requirements, and it became urgently necessary to stop by arbitrary means the loss of funds. Under the terms of the so-called standstill agreements which were the only alternative to a complete moratorium of payments, the foreign banking creditors pledged themselves not to withdraw except within narrow limits the funds they had owing to them from German banks. The freezing of these immense sums, preponderantly American and British, prevented their being used to repay funds which they and we owed abroad. When the latter were called for, the difficulty of paying them was thereby increased. The British crisis of September, 1931, was intensified by that fact, just as it derived its initial force and momen-

[99]

tum from political disturbances; and culminated in Great Britain and the Scandinavian countries going off the gold standard. Our own crisis of October and the crisis which we are now in are to be read in the same light.

The deduction to be drawn from the foregoing sequences is that while the economic stage was doubtless set for a business reversal, it is to the political factors that we owe its peculiar virulence. Economic mistakes account for the depression, but political forces have turned it into a panic.

I desire at this point, before proceeding to my conclusion, to lift out of the political perspective one particular element. This is the part played in the political scene by the inter-Allied debts. Nominally, as we have seen, these are strictly financial obligations. Practically they have proved far otherwise, and the political advantage has not been to us but mainly to France. From the moment that the size of the reparation debt was made contingent upon the size of the debts owed to us, the latter became a means of political control over Germany. The French have made no secret of their use of financial authority as an instrument of national policy, of which the numerous loans made to the countries to the east and south-east of Germany are sufficient evidence. Reparations, augmented by the inter-Allied debts, have worked precisely to the same purpose but from the opposite direction. Perhaps by reason of this readily acknowledged principle of French foreign policy, France has been blamed in these recent months for numerous private adventures in international finance which have added to the distress of embarrassed countries. It should be said that the Bank of France and the French government did not encourage such adventures but on the contrary often moved to counteract their effects. The troubled state of the world's economic and political waters is enough to account for them without charging deliberate intent.

If it be so, as I believe, that political causes, among them war debts and reparations, have given the depression its unparalleled intensity, the question now arises as to what we are going to do about them. Is it beyond human ingenuity, does it put too great a strain on human character, to rid us of this burden?

Let us canvass two solutions. The first is briefly stated. It

[100]

proceeds from the assumption, perhaps correct, that the inter-Allied debts are uncollectible. It is argued that we should therefore make a virtue of necessity and cancel them, on the understanding, however, that the entire benefit is passed along to Germany for the reduction of the reparation annuities. This solution, it should be observed, was already foreseen at Paris in 1929 and found expression in the Concurrent Memorandum attached to the Young Plan but not made a part of it. The fact that the Concurrent Memorandum provided that only three-fourths of the contemplated relief should go to Germany does not alter the similarity of the two in principle.

To this solution I think there are two controlling objections, among others. In the first place, it involves a complete retraction in singularly literal form of our national policy. The rule that reparations and war debts ~~must~~ be considered separate and distinct was established by President Wilson in 1920 and has remained the official declaration on this issue ever since. After all that has taken place it is too late to change it.

In the second place, this proposed solution does not go far enough. Of all the political factors disturbing European stability at this time it affects only ~~one~~, namely reparations. And it does not eliminate that. The amounts due to us on inter-Allied debt account are only a part of the German reparation obligation. Accordingly, if we were to cancel the debts we would not get rid of reparations; we would only reduce them. The amount that would remain would be roughly equivalent to the unconditional annuity provided for under the Young Plan, a sum quite sufficient to keep political antagonisms alive. Perhaps in time now past the practical relief to German credit which such a reduction would give, would have eased German economic stress and have put political unrest under an anaesthetic. But that time has gone by; at this stage a resumption even of the unconditional annuity would impair German credit still further. Granted the point at which we have arrived, I see very little advantage in this solution over a simple process of default all around. In both cases we lose the debts without getting anything in return.

Let us now consider a second solution. Here also I must make an assumption, for to argue the matter would take

[101]

W-72, N15
N134.15

me far beyond the limits of my subject and my time. This is the assumption—and it comes in the economic class—that as long as the debts exist they will delay recovery from the depression, and so prove more costly to collect than they are worth. Nevertheless, we have an unquestionable right to them, and if we are to give them up in whole or in part we should obtain counter-value while we still have the chance.

This solution, in simple outline merely as a statement of principles, and leaving out all the innumerable checks and balances which would be injected into it in the course of negotiation, is the following:

1. Total cancellation of the debts.
2. Total cancellation of reparations, with the exception, of course, of payments on the Dawes and Young loans.
3. Suppression for a period of ten years from the adjournment of the present conference on arms limitation of all political issues arising under the Treaty of Versailles.

The demerit—and perhaps the merit—of this solution is that no nation attains its full list of desires. Consider first the case of Germany. Germany obtains relief on reparations account. But she has to continue under the political disabilities of the Treaty for ten years and in addition runs the risk that ten years of psychological peace in Europe will lead her own people as well as her former enemies to settle down to the existing condition. But she has the assurance that at the end of that time the problems that still remain will at least be opened for discussion.

Next consider the case of France. France loses her share in the unconditional annuity, which at present is nominally about 125 million dollars a year. But she gains relief from her liability to pay the United States whether Germany pays or not. Far more than this, however, she obtains the surest buttress to her security, which is peace in the minds of her neighbors. She shares also in the incalculable economic benefits which would come to the world if the spectres of political disturbance are driven off the European scene. No one who knows the concrete French mind, however, will suppose that France would accept in lieu of the tangible control which the reparation claim now gives her, a set of intangible assurances

such as are here contemplated. For that reason it will be necessary to provide her with guarantees that the assurances are kept.

And now as to the United States. In a financial sense—assuming that the debts are good—the United States would be called upon to give up a claim worth now about 250 million dollars a year, and later worth more than that. With the cancellation of the claims, substantially the same amount would become immediately a charge upon the budget, which Congress is already having difficulty enough to bring into balance. This is a fact to be freely and fully admitted, but it is a fact which we may have to face whether we make our contribution to a general settlement or not. Furthermore, as matters stand we are paying higher and higher taxes out of incomes and values which are falling lower and lower. Indeed, it is because of this collapse of incomes and values that budgets are out of balance and that taxes have to be raised. I know of no one who would not willingly pay larger taxes if he stood to get more money to pay them with—if instead of depression and panic he could once more face a rising tide of business.

In my conception the release of our debtors as part and parcel of a European settlement would produce this very result. For political causes, among them reparations and the debts, if not the sole source of our distress, have intensified it and continued it. As I see it, these causes can be removed by sacrifices both financial and political—political on the part of Germany, financial and political on the part of France, and nominally financial on the part of the United States. The bargaining power which the debts give us lessens month by month. The question for us is not whether we will lose or keep 250 million dollars a year, but whether we will use before it is too late what leverage they give us to break the European deadlock.

Unless we have lost faith in the power of man to govern his own affairs we must believe him capable of making the sacrifices necessary to relieve at least his own distress.

DISCUSSION: REPARATIONS AND WAR DEBTS¹

CHAIRMAN: The meeting now passes under the ten-minute rule, and the first speaker will be the Honorable Eliot Wadsworth, former Assistant Secretary of the Treasury, and former secretary of the United States World War Foreign Debt Funding Commission.

MR. ELIOT WADSWORTH: I am glad so many hardy political economists are staying through this long and serious discussion. It is one of the most interesting discussions of the war debts I have ever attended. However, I must say that after listening to the many thoughtful papers read this afternoon, my feeling is just about as uncertain as to what ought to be done, as it has been ever since 1929.

I am quite familiar with the original debt settlements, and believe we made as practical arrangements as we could with each debtor. The need was to get the debts settled and out of the way, as they constituted an uncertain liability of a huge amount, and were a serious handicap to world recovery. When Mr. Baldwin, then Chancellor of the Exchequer, and Mr. Montagu Norman, Governor of the Bank of England, came to America and said: "We want to settle the English debt", the Debt Funding Commission sat down with them at once, and with the wise broad vision of Mr. Mellon, Mr. Hughes, Mr. Hoover and the other members of the Commission, reached what seemed to be a fair conclusion. The settlements with the other debtor countries soon followed.

I would say for the benefit of the gentleman from Kansas, Mr. Isely, who now aspires to be a Senator from Kansas, that the Westerners in the House and Senate at that time were very obdurate about getting the money. One Senator remarked that the farmers needed that money, they had to pay ten per cent on their own borrowings, and why should England be let off with three and one-half per cent. The spirit was very strong in Congress at that time, which was expressed in a brief remark attributed to President Coolidge when a delegation of cancellationists went to see him—"Well, they hired the money, didn't they?" Perhaps we have gone a long way from that attitude in some quarters, but by no means everywhere.

The Debt Commission tried to base settlements on the capacity to pay of each debtor, not the maximum capacity, but what they could pay in their stride without undue hardship in normal times.

¹ An abstract of the discussion at the close of the Second Session.

The settlements were made on that basis, and payments went along very smoothly for several years, but who could expect, or anticipate, the tremendous changes in prices which were to take place and which have profoundly affected international payments?

The price of rubber was then about 60 cents per pound, and the United States was buying largely from England and her colonies a billion pounds a year. Rubber is now 4 cents per pound, so that the cost of our imports has dropped from \$600,000,000 a year to \$40,000,000. This is a relief to the United States, but a serious handicap to those countries which sold us the rubber.

Cotton, on the other hand, was at that time selling from 10 to 15 cents per pound more than its present quotation. A drop of 15 cents per pound in the price of cotton means a saving to both England and Germany of about \$150,000,000 a year in their purchases of cotton from this country.

In other commodities and unfinished articles there has been a tremendous change in price as well as in the volume of exports and imports. It was not possible to look forward and estimate how these changes would affect the relative burden of the debt payment. But remember this, that from 1924, when the debts were settled, to 1929, the debt payments were made without serious difficulty. They might have continued except for the economic crisis which has developed since 1929, and has made all debts two or three times more burdensome.

Now people ask what we are to do next, and whether the war debts are to blame for our present difficulties. The demand is often made, "why doesn't the United States do something about the war debts and then times will be better." I do not personally believe that the war debts were predominant in bringing about the present distressful situation. Of course they are one factor, but not a sufficiently large item in the total of world transactions.

It is probable that reparations have much more to do with our present difficulty. Reparations have been a great cause of political turmoil and financial uncertainty. They have, at different times, brought on serious international problems in which the United States is not a principal factor, although on two occasions, Americans have gone to Europe and helped to devise temporary solutions in the Dawes and Young Plans. But it hardly seems as if reparations had yet been arranged on a practical payable basis. Until they have, it is hard to see how the war debts can be permanently settled.

It seems most probable that what caused the present trouble is not the war debts, or entirely reparation payments, but the fact that we maltreated the most perfect credit machine which the world has ever known. We drove that machine too fast and too hard. With its

assistance, we built up a structure of debts, national, state and municipal. We got into debt individually and issued corporation bonds, debentures and stocks, which, together constituted a paper structure like a huge card house. That structure was founded upon physical property, farms, factories, railroads, which could not possibly support it, and it has now begun to blow away in the tempest of a world financial crisis.

Already billions of dollars of the lighter stuff, beautifully engraved common stock certificates, have disappeared, together with some of the preferred stocks, and many of the more stable securities are in a fair way to go out of existence. The physical property remains just where it was three years ago. Factories, cities, railroads, farms are still there, but the paper structure on top of them and the credit system which made all this possible is badly damaged. It was not the war debts, and only in part reparations, but the excessive and ridiculous use of instruments of credit which made us think we had reached a new era that brought about the present crisis.

It is interesting to hear the statement of the German Consul General that the idea of a new era had permeated Germany and encouraged the Germans to borrow great sums which they are now having such trouble in repaying. Is there any part of the world which was not influenced by the new era theory?

America is blamed for a great deal, and often unjustly blamed. Perhaps America is not so much to blame because of the war debt settlement as because of our overenthusiasm. Will Rogers said in one of his articles the other day that when he was in England he found that everything in Europe was blamed on the Americans. He said that he had read in the paper that day that the birth rate in England was going down, and he was going to leave England right away, because he was afraid they would begin to blame it on him.

Public opinion has changed somewhat, but conditions have changed tremendously since we settled those debts in 1924 and 1925. Perhaps they will need settling again, but that is not necessarily a reason for cancelling them because of conditions at the moment. If America should be forced into some kind of inflation, it might well be that the war debts would become as easy to pay as they are apparently difficult to pay at the moment.

Take France as an example. We made a very favorable settlement with France at a time when she was in great financial distress, but within a few years the world came to look upon France as the strongest financial nation in the world in proportion to her size, far better able to meet the small payments on her war debts than other debtors who did not receive such good terms.

There is no reason for entirely abandoning the war debts without

[106]

regard to the future, and yet we may well use them as a lever if we can to bring about some more permanent settlement of reparations and other problems. Whether we should ask for a conference or not is open to question. Ordinarily the debtor asks for a conference, not the creditor, but we ought to go into a conference if one is called and use our position to the best possible advantage for the betterment of the general situation, but by no means with a complete abandonment of our own national interest.

It would not seem at all impossible that the war debts would some day be settled at what might look like a fantastic basis at the present moment. There might be payment in full, as now arranged for, or a further discount may be necessary. Perhaps we must get some kind of elastic settlement based upon the value of the dollar, or the pound, or some other yardstick, which will apply from year to year. It might be something like the old income bonds that were put out after the panic of 1893 by several railroads, on which the holders received their interest in proportion to the income of the company. In good times they received their income in full; in bad times, no income at all. So far no yardstick has been found on which to create such elasticity.

May I say in closing that, for the sake of the world's peace of mind in the future, I would hope that if any nations get into such a difficulty as in 1914-1918, and decide to help each other out financially from one national treasury to the other, they will give the money, and not lend it. If that had been done in the last war it would have eliminated a great post-war problem. But do not forget, that in lending money to the Allies America followed the plan which the Allies had been using among themselves during the entire war.

We have proven one thing in dealing with the post-war problems, namely that governments are not very successful in dealing with other governments on financial questions. Governments are not too successful in dealing with each other in the field of diplomacy, but when a Prime Minister or a Secretary of the Treasury has a financial problem to settle with another country, he must always be looking over his shoulder at the taxpayers, whom he represents, and whose opinions are not always governed by the broadest judgment of the international financial situation.

Governments will go on borrowing from individuals of their own and other countries. There is a certain safety valve in that form of borrowing because it depends upon the willingness of individuals to lend, and so prevents, to a large extent, excessive overborrowing. When one government borrows money from its own people and lends to another government, a very different situation exists.

The war debts, which we are considering today, and on which no

[107]

interest is being paid at the moment, are only one detail in the present economic chaos. Perhaps they must be laid aside as they were between 1919 and 1924 until more stable days and a better business situation throughout the world makes it possible to even guess as to what might be considered a fair settlement.

The basis, the terms, the politics, the international forces which will dictate that settlement are almost as unknown today as they were on Armistice Day in 1918. Public opinion as it develops in the future in the debtor and creditor countries can alone dictate a settlement, the terms of which debtors will meet and creditors accept. There is little sign today of how such accord can be reached.

CHAIRMAN: Finally, I am going to ask Mr. Constantine E. McGuire, economist, of Washington, to speak to us under the ten minute rule.

MR. CONSTANTINE E. MCGUIRE: There are, I think, very clear evidences from the papers presented this afternoon, and from Mr. Wadsworth's discussion, that the seriousness of this problem is now fairly widely realized; and although one slightly optimistic note was contained in one part of Mr. Wadsworth's address, to the effect that this problem would, of course, "some day be settled," the general result of the discussion, I think, must be put down as unfavorable and discouraging.

If you take into consideration merely the calendar for the balance of the year 1932 and for the year 1933, you will find that Congress, adjourning in all probability in two months from now, will assemble again only in December for a short session, the closing session of the Seventy-second Congress lasting approximately sixty working days. The Seventy-third Congress will meet in December, 1933, and there appears to be no likelihood either of a special session of the Seventy-second Congress in the summer of 1932 or of the Seventy-third Congress after it comes into constitutional existence, but before its first regular session.

The national conventions of the Republican and Democratic parties will meet June 12 and 27, respectively, and their platforms must inevitably deal with this question. It seems fairly clear from the tenor of much of the discussion in political circles and in the press that the two platforms will reaffirm the principle that obligations must be upheld and that cancellation is contrary to national policy.

In June, an international conference will meet in Lausanne, for the consideration of the policies to be followed after the first of July. Whatever may be the outcome of that meeting, the Congress of the

[108]

United States will not be in session to take action upon the findings or recommendations of the Lausanne Conference. In the resolution of December 23, 1931, Congress has shown it is not in a mood to consider appeals for the further reduction or for the cancellation of these obligations. It is fairly clear that, even if Congress is called in special session by the President before election, it would simply reaffirm that principle unless a very different sort of argument is presented and a different type of leadership developed.

There are certain due dates involved in all these obligations, and it must be borne in mind that as far as the record is concerned the entire indebtedness stood in default for eight days last December. Certain very large sums were due on December 15, and although the Treasury was inclined to accept the substance for the form, as a matter of strict fact it was only on December 23, when the President approved the resolution of Congress, that the deferment of payment from, and as of, December 15 became properly authorized.

These are very close shaves that we have had, and we seem destined to go through many more, and through more serious ones, before the question can be, as Mr. Wadsworth put it, definitely and finally cleaned up.

Looking back over these papers, certain things seem to stand out as rather decisive. In the first place, it has been pointed out that a new approach is essential. It has been made fairly clear that strong opposition is to be counted upon from those who insist upon the legal rights and equities set up under certain instruments signed, and in effect political treaties between governments.

It has also been pointed out that the great intermountain region of this country is not essentially opposed now to the liquidation of these obligations, or at least to their writing down on a very great scale; although ten and eight years ago a considerable degree of feeling existed in that region that no reduction should be effected, and certainly no long-term postponements, so long as the bulk of the agrarian population itself had to face the recurrent private obligations piled upon it.

It has been pointed out, too, that the residuary debtor has strained every nerve and has gone as far as it could safely go, perhaps has gone considerably beyond the point it could safely have gone, in an effort to carry out the obligations imposed upon it by the Treaty of Versailles.

The point was made, and I think it of very great importance, that this problem has a common thread of interest—national and individual interest, running through it, whether we call it economic or political. The share of economic policy in the whole field of public policy is far greater than we are in the habit of admitting.

[109]

The problem of settlement with the debtor nations, whether under the Treaty of Versailles, or under the treaties that have been perfected by the Debt Funding Commission and ratified by the Senate, is essentially a question of national interest. All of those agreements have arisen out of concepts of national interest, reconciled or not, as the case may be, with certain other types of interest which are not essentially economic; but in the main economic interests have guided and directed these agreements.

We acquired these great masses of obligations largely through subsidies which we gave our own producers between 1917 and 1919. We have alternative policies which, given conditions at that time and given the general attitude of political leaders in a country so constituted as ours, could not very easily have been put into effect. We did essentially and in the last analysis effect a great subsidy, and we chose to put it upon the basis of a great series of international loans.

We must face the settlement in the same way, seeking first of all to analyze our interests and then to measure the conditions in which those interests will be served, with due regard for practical possibilities.

[110]

PART III

WORLD ORGANIZATION IN FINANCE AND TRADE

WORLD ORGANIZATION IN FINANCE AND TRADE¹

PAUL D. CRAVATH

THE subject of discussion tonight will soon be recognized, I am sure, as the most important economic subject before the world. We are all conscious of a growing feeling that the *laissez-faire* system of dealing with trade and finance that is part of our liberal Anglo-Saxon inheritance has broken down, and that we must find some new system of organization to save us from a repetition of the era of over-production and unrestrained competition that has brought us into our present sad economic plight.

We have been offered all sorts of plans, ranging from the plan of self-imposed organization thrown out for discussion by Mr. Young and his associate, Mr. Swope, to the system of state planning and state capitalism, which has thus far prevented Soviet Russia from entering the ranks of nations with unemployment problems.

We are very fortunate in our speakers tonight. For many years I knew in Wall Street a relatively young and very successful and highly esteemed banker known to his friends as Fred Walcott. I had followed with interest his excursions in Belgian Relief and Polish Relief as an associate of Herbert Hoover, and finally into the Food Administration during and just after the war. But a few years ago he disappeared from my vision, and I have just realized that when he disappeared from my vision he disappeared into the United States Senate. It must have been during one of my long absences that that happened. I presume I brand myself as a hopeless ignoramus and a back number when I confess that I did not until a few days ago realize that Senator Walcott of Connecticut, of whom I had read and heard so much, and whose performances in the Senate I have so admired, was no other than the Fred Walcott whom I had known in Wall Street a few years ago.

¹ Remarks of presiding officer at Dinner Meeting.—Ed.
[113]

While he was still only a banker, few men would have been better qualified than he to discuss the subject of tonight, because he was more than a money-maker. He must have been that when he retired a few years ago from business. He was always a profound student of finance and trade from its public aspects, and today he comes to us with the added qualification of his three years' experience as a prominent and important member of the United States Government.

[114]

HOW MUCH CAN THE GOVERNMENT HELP?

FREDERIC C. WALCOTT

United States Senator from Connecticut

IT is a genuine pleasure to gather at this forum to exchange ideas and to welcome again one of the world's most distinguished economists, Sir Josiah Stamp, whose voice was heard crying out in the wilderness, several years ago, to proclaim to a war-stricken world the troubles which were then accumulating. Great Britain, with her long dominion over the seas, has sent us one of her master mariners to help us correct our compass, and we shall profit by his presence.

During the last thirty years, more than half of the population of the world has emerged from the monarch's yoke. Crowns are no longer at a premium, crowned heads are few and far between. This government of the United States is probably the oldest representative government in existence.

We find ourselves suddenly the greatest creditor nation on earth. We have temporarily lost our bearings. Storm-tossed, we ride the waves of inflation, mount high at one time, and then sink into the trough of an angry sea. The peaks of a false prosperity are unavailing to fill up the deep valleys of depression. We must steer a new course. We must play a new rôle, of which we have not learned the technique.

The world is groggy with advice. Panaceas for all our ills are the order of the day.

One of the great problems which confront the world today is the *price level*, the problem of the purchasing power of the monetary unit. We all know that inflation brings discontent and a cry of "high cost of living," while deflation causes depression and unemployment. This is a matter of international concern and is closely related to the problem of the gold standard and the distribution of gold. It is a grim joke that among the victims of deflation today are those countries that have the most abundant supply of gold. In America this paradox is largely traceable to certain technical kinks in our Federal Reserve laws, which have so tied up our gold as to leave little of it free. We have recently passed legislation

[115]

to remedy this situation. The Glass-Steagall Act released and added to our free gold supply \$750,000,000. While this has quieted the fears of other countries as to our ability to maintain the gold standard, it has not cured the disease of deflation. We sorely need a rise in our price levels and then, of paramount importance, some degree of stability at the new level.

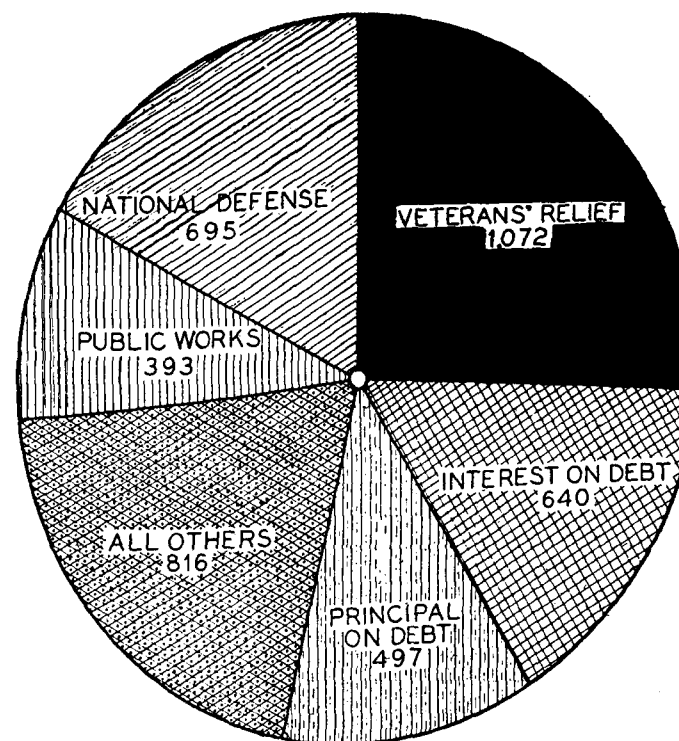
With this in mind, let us see where we stand before the world as a producer of raw materials. We have on hand, available in storage and for sale, among other important commodities, 64 per cent of the world's visible copper supply, 452,000 tons; 67 per cent of the world's supply of cotton, 6,863,000 bales; 41 per cent of the world's wheat supply, 261,900,000 bushels, and a very large portion of the world's supply of petroleum, 632,030,000 barrels; metals, foodstuffs and fuel. We have approximately 40 per cent of the world's gold. In 1928 we had 40 per cent of the trade of the seventeen leading nations of the world, which, in turn, did 90 per cent of the world's business. We therefore had at that time 36 per cent of the world's trade.

Let us look at our gold dollar. Accepting the purchasing price of the dollar for 1913 as our standard of measure, we find that this same dollar, in 1920, as the result of inflation, was worth only forty-five cents, or less than one-half the purchasing price of the dollar in 1913. Today, that same dollar, always a gold dollar, will buy ten per cent more of commodities at wholesale prices than it would have bought in 1913, and three times as much as in 1920.

These violent fluctuations clearly throw our entire industrial and commercial fabric out of joint. The wage-earner was hard-pressed in 1920 and is apt to be out of employment in 1932.

Our banking structure has proved wholly inadequate. From 1900 to 1910 the number of banks in the United States grew from approximately 10,000 to nearly 20,000, and we have lost through failure nearly 10,000 in the last twelve years, an appalling calamity. Today nearly \$2,000,000,000 belonging to innocent depositors is locked up in closed banks, and more than \$1,000,000,000 is being hoarded in this country as the result of fear occasioned by bank failures. What can we do about it?

[116]



ESTIMATED EXPENDITURES OF U.S. GOVERNMENT
1932-1933
(IN MILLIONS OF DOLLARS)

The world is still suffering from the aftermath of the World War. It will take generations to recover from the ghastly destruction of life and property, for war is always the destruction of the fit. War is largely responsible for the growth in bureaucracy and the further centralization of our federal government, and is almost entirely responsible for the tremendous increase in the cost of running the government. Approximately seventy-two cents of every dollar that we raise for federal expenses through excessive taxation is spent as the direct or indirect result of war. The largest part of this, of course, is the annual payment to veterans in the forms of bonuses and pensions. Think of it! Over \$3,000,000,000 out of a total of \$4,000,000,000, the annual expense of the federal government! And this same story can be told in

[117]

almost the same terms by all the other contestants of the great war. It cost England and Germany and France even more than it did the United States. And now, engulfed by war, Japan and China are committing financial suicide, with the rest of the so-called civilized world. No country wins a war today. The winners are merely less defeated and it takes years to determine that. Modern warfare is a diabolical form of national and economic suicide!

It is perfectly clear that we must put our own house in order first. We have done our full share in helping others, and we have become seriously embarrassed. Now we must face our own problems frankly and solve them with courage and intelligence.

To quote Sir Josiah's own words:

The world has advanced so rapidly in its scientific aspects, in its complexity, that it has left us all behind in the subtle and overwhelming question of money. We are just in the stone age in economic thinking, compared with the immense advance which we have made in other directions. . . . And it is our task to make every man, when he is looking for the cause of things, ask first and not last the question, "What is the price level? What is it doing to me? What is it doing to the wage earner? What is it doing to the profit margin, to the whole balance sheet and the profit and loss account?" In that way will some day dawn on the world what we mean by stable money.

A year ago many of our bankers and leading business men felt that this country was emerging slightly from the worst phase of the depression. Tremors and minor quakes occurred during the summer months, following the acute situation that had developed in Germany in June, which was temporarily relieved by the moratorium.

Then came the larger shock, toward the end of September, when England abandoned the gold standard, which forced a flood of selling of American securities from abroad. England's declaration was followed promptly by the now famous White House conference, which brought us face to face with realities and the adoption of a series of emergency measures.

The National Credit Corporation was formed over-night, led by a group of New York City bankers. \$500,000,000 was pledged by a number of banks, which agreed to advance two per cent of their deposits whenever called. Thirty per cent of this \$500,000,000 was called by the following January in three

[118]

calls of ten per cent each, totaling \$150,000,000, and practically all of this was loaned for the relief of contributing banks in distress. This had an immediate and beneficial effect during the months of November and December, but this patriotic, volunteer effort was not enough to stem the tide of bank failures.

The Reconstruction Finance Corporation, proposed at the White House conference and modeled after the War Finance Corporation of 1920 and 1921, was planned and agreed to by Congress. The bill was signed by the President on January 22, and during the week previous to the signing, twenty-seven banks closed their doors. This corporation was set up with a capitalization of \$500,000,000, and a provision for three times this amount in cash assets through the sale of Reconstruction debentures or United States Treasury notes, making a total of cash resources available for lending of \$2,000,000,000. By February 2, the Board of Directors approved 000,000. The bill was organized and applications began to pour in. The effect was instantaneous. Courage displaced fear, and in two months more than 1,300 applications for loans, aggregating more than \$230,000,000, were approved by the Board in Washington; of this sum, nearly \$200,000,000 in cash has been actually advanced to financial institutions and railroads throughout the country. Bank failures have been reduced from ten or fifteen a day to one or two a day, and lately, reopenings have exceeded closings.

The same bill also set up a fund of \$200,000,000 for the relief of the depositors of closed banks, both state and national, and \$200,000,000 for crop and seed loans, to be made, subject to the approval of the Secretary of Agriculture, directly to farmers in distress throughout the country.

Immediately upon the heels of this gigantic relief measure followed the passage of the Glass-Steagall Bill, which broadened the base of eligible paper to enable the banks to borrow from the Federal Reserve upon secondary collateral, relieving the banks from the fear of exhausting their prime eligible paper. Although at the time of the passage of the bill the eligible paper in the possession of member banks throughout the country amounted to more than \$8,000,000,000, the fear of withdrawals of deposits was so great that a still larger

[119]

accessible reserve fund was needed. This the Glass-Steagall Bill provided. This bill also authorized the use of United States Treasury bonds owned by the Federal Reserve as backing for currency, thereby freeing over \$750,000,000 of gold.

These two measures had a marked stabilizing effect, and the successful launching of them materially helped to unite the conservative members of both parties, Republican and Democratic, in Congress, for the relief and support of our entire financial structure, as well as the railroads. This harmony was then and is now vital to the solution of our problems.

It is important to distinguish between permanent legislation and emergency legislation. Every civilized country in the world has adopted emergency measures of relief to offset economic chaos resulting from the World War. These emergency relief measures will help allay fear and reestablish courage. But the end is not yet, for these measures will not, in themselves, start the wheels of business. There has been a serious drop in security values during the last thirty days, occasioned largely, no doubt, by the failure of Congress thus far to balance the budget. We must face the facts, however disagreeable they may be.

Certain elements are absolutely essential to our upward trend: the recovery of our commodity prices, the relief of unemployment, an increase in the purchasing power of the people, and the basic adjustments necessary to restore confidence, including a balanced budget.

The Senate is now wrestling with the tax bill in the hope that a way may be found to nearly balance the budget with an equitable tax that will not rest too heavily upon any one group, and I believe that the solution of this difficult problem will be found.

But there is another highly important element in the balancing of the budget, which should be of permanent relief, and that is a drastic cut in federal expenditures. Careful calculations have been made upon the possibilities in this direction, and it is believed that a saving of between \$160,000,000 and \$200,000,000 can be made by combining certain bureaus, eliminating some of the least important of the government's functions. This will prove a difficult and a very distasteful undertaking, but it must be done, and the Admin-

[120]

istration is prepared to undertake it with courage and determination, if authorized by Congress.

Lower costs and higher purchasing power are what we need today as never before.

The problem of unemployment is increasingly serious, for private and municipal funds have been partially exhausted and unemployment cannot be decreased until business can start with reasonable certainty of finding profitable outlets for its products. Many of our states and municipalities are unable to meet their full payrolls today or borrow additional funds.

The agricultural sections of the country are suffering as the result of a prolonged deflation in prices, which are now far below the cost of production.

These are the problems which lie immediately ahead of us. We must face them squarely, for they must be solved. Complete coöperation is the essential factor in the solution of our distress. Our wisest heads and most courageous leaders must work shoulder to shoulder to find the way out. Each individual business must study its own problems unceasingly.

Our state and city governments must economize rigidly. We must keep our Federal Treasury impregnable. The wealthy may be forced to learn many valuable lessons which are taught by privation. Our orgy of extravagance is long since over, and may be for some time. We must adjust our minds to the abandonment of the fleshpots of Egypt and the adoption of the simple life. We must pull up our belts another hole and press forward with a liberalism which will save us from plutocracy as well as from the rule of the mob. The time is ripe, in this winter of our discontent, to strike out from our federal code all sumptuary legislation, to revise our banking laws along sound lines (for we need a unified banking law and should begin before long to lay the foundation); to practice tolerance in all things, to cultivate vision, courage, and faith. We have the genius for organization, the scientists, the raw materials going begging, and the money. Surely we can put these together for the common good. Herein lies our hope and our triumph.

The primary necessity at the present time is a general restoration of confidence. That cannot be produced by any panacea, but can only result from each citizen's under-

[121]

taking vigorously, both in his business and in his personal affairs, to set his house in order. Governments must balance budgets. Industries must adjust their costs. A thousand and one adjustments must be made to a new economic condition. It is only on the basis of such changes that our extraordinary supply of gold and credit can again be put to work, that business activity may be renewed, prices restored to more normal levels, and recovery assured.

One of the most remarkable exhibitions of the capacity of a nation for carrying on under trying conditions is provided in Germany. I wonder if most of us realize the stringent regulations which the German people have imposed upon themselves through the emergency decree of last December. These restrictions include the following:

- (1) Domestic commodity prices fixed by agreement are reduced by 10 per cent,
- (2) Railway freight rates are reduced by from 5 to 20 per cent,
- (3) Interest rates are generally reduced,
- (4) Building rentals are reduced by a minimum of 10 per cent,
- (5) Wages and salaries in government and private undertakings are reduced 9 or 10 per cent,
- (6) A federal sales tax of 2 per cent is put into effect.

We do not require in this country this kind of rigid restriction, but we do need to introduce in our whole economic life an element of elasticity which will enable us to adjust ourselves to changed conditions, and the German example is inspiring as indicating a state of public opinion, and a will to achieve.

May I give you a quotation from a personal letter recently received from England? "My wife and the boys will *not* go to Switzerland this year, as it is not considered patriotic to leave England. The poorer people are taxed one-fourth of their income, and the rich, one-half; but the English people have put their backs to the wall. We are not complaining. We have balanced our budget, and we are jubilant, for we are the only country in the world which has balanced its budget." Fellow Americans, we have the courage and the faith. We shall not be found wanting. Our country will be the next country to balance its budget.

[122]

CONTROL OR FATE IN ECONOMIC AFFAIRS

SIR JOSIAH STAMP, G.B.E., LL.D., D.Sc.

I AM quite sure that owing to the activities of an omniscient press most of you are aware that the main object of my visit to America was not economic. It was not even to make this speech. In fact, when I knew I was coming over for other reasons I referred to the well-known maxim that silence is golden, the maxim which has ruled my conduct up to now; but inasmuch as England has gone off the gold standard, it seemed that I might be absolved from any self-imposed restrictions.

But even if I had come on an economic mission, I must beg Senator Walcott and our respected Chairman to absolve me from the necessity for approaching my problem tonight from exactly the point of view they gave me, namely, that of coming here to help you or show you the way out of your difficulties. Far be it from me, coming from the difficulties of Great Britain, some of them half solved, some of them once again dodged, others concealed, and others postponed, to attempt any such thing, as it would be presumptuous to come here to advise you how to get out of your troubles. I have really come over to see what you think about England, much more than to tell you what England thinks about you. So I approach this matter, particularly in a conference like this, as a fellow inquirer.

After all, any truth is many-sided, even simple truth, but the complex truth of today is so many-sided that even the same set of facts needs approach by many methods of analysis and many different types of mind before we can get even an approximation to the truth. Anyone who tells you that he has a ready-made solution to the difficulties in which all the world now finds itself, it seems to me, is either wilfully dishonest or not fit for the present age. The world is sick, there is no doubt about that, but I do not come to you with any particular panacea of my own. I come as an inquirer point-

[123]

ing out what I imagine to be vital points in the present situation that must be set right before we can get further.

A recent biographer in England, referring to the great Croker, the great *littérateur* and politician, speaks of him in a certain Cabinet crisis as being in an "ecstasy of exclusive information." Well, I am in no such ecstasy, although people have a habit, a disarming habit, of coming to one and expecting in a sentence or two to hear the way out.

Several people here have said to me that this is a most "interesting" age to live in. Of course, it is interesting, but I notice that the people who make the statement that it is interesting are those who are close enough to what is being done and to the decisions that are being made to criticize them freely without being actually responsible for them. When you are both near and also responsible for the decisions in some measure, it is perhaps rather more alarming and tiring and anxious than interesting.

We are faced with a great flood of speeches, articles, addresses and books, all dealing with this problem and telling us the way out. I do not complain of them. I do not say that we may not be able to get some help from them. What we want is not less talk but better talk, and I would weed them out not for quantity but only for quality. Even so, any simple statement which represents an individual point of view faithfully is welcome in the sum total of knowledge. But if one glances through these different characterizations one finds they classify themselves under a number of fairly distinct heads, I do not say to the exclusion of others, but each person emphasizes a particular point of view. You have, for example, those who point out quite rightly that economic frontiers do not coincide with political borders, or with racial ideas; that it is the attempt to dragoon the one into conformity to the other, by tariffs, by financial policies, by all kinds of methods, that is bound to lead us into trouble and into difficulty; that the best we can do is to get some closer approximation to the economic realities and to subordinate political ideas and barriers in some measure, if we would get the greatest good for the greatest number, and the greatest prosperity for the world.

Others point out that we are endeavoring by a framework

[124]

of government based on eighteenth-century principles and philosophies, those canons of nearly two hundred years ago, to deal with the complex world of the twentieth century, when we have in many respects annihilated distance, universalized instantaneous knowledge and made every conceivable change in the things which govern political representation, political pressure and the whole science and art of government.

Then there are those, the third class, who point out quite rightly that science and production are outrunning all the other factors of society, and that mental powers, and particularly our moral endurance, have not advanced equally to deal with them; that we have, therefore, in a complex society a breakdown until such time as we can make up the leeway in these other factors compared with those particular advances in science and production.

This is simplified by a fourth class who would put it in this form: the problem is one of the coexistence of plenty and scarcity. You have on the one hand enormous potentialities or actualities of production, greater than the world has ever known, and on the other hand you have the greatest difficulty in matching this with purchasing power. Somewhere between the two the bridge is broken or overcrowded.

There are two kinds of bridges that are emphasized. One I may call lubrication and the other balance. Those who refer to lubrication, by which I mean the medium of exchange in currency and finance, tell us that we must have a stabler measure of value and a simpler and more resilient method of exchange so that the translation from the one side of the equation to the other, viz. production and purchasing power—for they should be equal—may be successfully achieved. And they say we must have much greater control, whether by governments, international bankers, central banks or new banking systems, over the total amount of purchasing power in relation to the requirements of production. They agree that such control lies in a new world of ideas, extremely subtle and difficult to envisage as being successful in all circumstances. Those who say that the question is one of balance point out that certain production advances much more rapidly than the ultimate real demand for it in relation to other things, and so by a lack of balance between different elasticities of demand

[125]

we bring about ultimately a complete breakdown of the machine. They put forward projects for productive control which, if carried to their logical conclusion, really raise the whole issue of the present order of society because that kind of control of production, as I hope to point out, requires something autocratic, either within an industry, or within the nation, or between nations, such as the world has not yet seen.

Another group regards it merely as a question of the industrial rhythm, the financial rhythm and cycle that has been with us ever since modern civilization has been internationally active. They point out that, however caused, whatever may be the immediate impact or incidents that start it going, there is a rhythm, there is a period or cycle, uneven in length, but absolutely unavoidable; that what we have to learn to do is to find out the critical points in that cycle so that we can damp it down whenever it needs it so that neither our optimism nor our depression may be too great; they acknowledge that it would be very destructive of the whole world's progress if we had no rhythm at all and only a stagnant level. But the danger lies in excessive amplitude.

The next class, however, say that with all our efforts modern civilization is so complex that no matter what we do we are bound to fail really to control the situation; they say that fate, beneficent perhaps, perhaps not, will ultimately settle it however much we may try to control the situation; that the most we can do is to set matters in such order that when the difficulties do come they will not completely destroy us; but that beyond that we have no power; that there are so many unforeseen accidents in such a complex set of circumstances, over which we have no power of final determination, that we have no means of settling what our economic destiny shall be.

I think that many people take that view of our economic destiny, and they become or are becoming at the present moment economic agnostics. They say that they do not see how we are going to do anything, and throw up their hands in despair. As Senator Walcott has said, perhaps the underlying note of all this is that there is a breakdown of individualism and *laissez faire*, and we have to face the problem of control, not only the kind of control and the measure of it, but by whom it is to be administered, whether democracy is strong

[126]

enough for it, whether autocracy is wise enough, or can be trusted for it.

Some of us long for an autocrat, and we say that the finest government would be by a benevolent and wise autocrat; and yet we know that even an autocrat may be under complete domination by some sentiment, or some prejudice for that matter.

A friend of mine says that his greatest ambition in life is to break into the house of Mussolini and to overhear a conversation between Mr. Mussolini and Mrs. Mussolini, which would end in this way: "All right, my dear, all right; have it your own way."

Our present discontents, in the absence of an autocrat and not under such beneficent guidance, have driven us to a popular attitude, or two popular attitudes. The first is disillusionment with economics and disgust for economists, an entire lack of faith in them as having failed to rise to the occasion when they were needed. Events, it is said, have taken place which were contradictory of the economists' teachings. These critics themselves are making economic judgments of all kinds. They are like Molière's character who had been talking prose all his life without knowing it. They, themselves, are really practically posing as economists all the time they are abusing economists.

But there is a second class who are suddenly showing an injudicious trust, a pathetic trust, in economics. They are rushing to textbooks and hoping by an hour's or two hours' reading of economics without tears to discover the secret of the whole problem.

Concerning the first class, who are disillusioned and say that they will have nothing more to do with economics or economists, I wish to say that there is a common idea that the proper task of economics and the test of its being a valid science is that it should forecast. It should foretell not merely tendencies. It is not enough to say that if such and such a set of circumstances continues, a definite consequence will ensue. It must be able to say that the turn of the tide, the price level, or the bank rate, or whatever it may be, will come in June, or if you like, on June 15, at four a. m.

Such forecasts would entitle economics to rank as a science,

[127]

with accurate statements of cause and effect. I do not know whether you have ever examined that idea, but if you do so for two or three minutes, you will see that it is a contradiction in terms and the supposed parallel to physical science is quite invalid. Do you not recognize that a forecast fully believed in would be cancelled out as soon as people acted on their belief? Suppose, for example, you are told that a certain index of stock or bond prices is going to change in the month of September. You are all presented in advance with that information and if you believe in that forecast, and act upon it in your selling or buying, it will disappear as a prophecy. Such prophecies can be right only if they are in sealed envelopes or if people do not believe in them. It is quite possible for an omniscient economist to forecast what will be the mass action of a vast body of people who do not believe in his forecast, but the moment they believe in his forecast it disappears. The reason is that so long as you have, either individually or in the mass, the control of an issue in your own hands, and you understand it fully, you are in a position to try to avoid the consequences of that issue. The more you examine the problem of forecasting the more you will see that the mere projection of a past curve of incidents depends upon mankind's acting independently of the belief or knowledge of that forecast. You get a different forecast if you assume that one half the market will believe you, and your forecast must be one of the effect of mixed psychologies.

Then you have the danger, among those people who are disillusioned, of the men with the older economic ideas, some of them professional economists. There is no more dangerous man than the man who knew the correct, and absolutely correct, answer to every economic problem thirty years ago, if he has not gone any further than that, because every problem is so altered in its character that it requires new analysis.

For example John Stuart Mill was certainly not altogether wrong for the time in which he was living. Probably if he were living today he would write altogether differently, about today's facts, because economics is a mode of thought and not a body of permanent doctrine. It requires activity of the mind up to date, and there is no good trying to live up to the teaching of the past, without some consideration of the differ-

[128]

ent present-day problems. I would rather have the man in the street with no pretension to knowledge at all than the man with a correct answer to every problem a generation ago and a static mind since.

The second class have a pathetic trust in economics and are rushing to it as though all our problems could be solved in two or three minutes. They want a quick way out. I always say to them, "Either leave it alone or do it as far as you can thoroughly." Realize that it is a discipline just as serious as becoming a doctor, or a physicist or a chemist, to understand such a complex world as the economic world, or at any rate to dogmatize upon it. The average man has not given very much thought to it, and if he examines himself to see where he got his principles and his facts, he will be surprised to find how many hazy ideas he has on the subject derived from the most miscellaneous sources. His mind is, generally speaking, a ragbag. I always say to him, "If you must have a mind like a ragbag, at any rate you can sort the rags and see what you have got."

We shall never get the kind of collective wisdom or response to true economic principles, for which I am pleading, until we recognize our limitations in that direction.

We have first of all to learn that even the plainest and most positive of economic rules and principles has a point of reversal under stress and in particular conditions. It may be true, for example, that a rise in the bank rate retains reserves, draws in money, commands confidence that the situation is in hand; but there are situations in which raising the bank rate has the very reverse result, and such situations have been clear in several countries, particularly in England in late years. There was a time when to raise the bank rate at a particular crisis would not have been taken as showing that the position was in hand, but it would have been suspected as indicating that the situation was much worse than people had thought, and so far from attracting favorable balances it would have caused such an alarm that a panic would have ensued.

There is a point of reversal, too, not only in the rate but also in the whole principle of the quantity of money. Sometimes the quantity of money may be so great as to be inactive and not to stimulate business as people had hoped. It

[129]

may be very well to say, "Let us put in the shop window double the money we have had in the past, let us halve the price"; but double the money and half the price does not affect the man being carried by in an ambulance. He has to be sitting up and taking notice. We can be so sick in mind that we can take advantage neither of cheap rates nor of large quantities.

There are points in practically every economic principle, even the elasticity of demand in reference to price, where the whole curve turns upside down, so that the matter is much more complex than the mere mastery of a few simple rules.

Perhaps I may be permitted, not in any critical sense, but rather as a casual observer who has been here this past fortnight, to give you my observations as to the different characteristics that I have observed during this present time as compared with, say, a year or two years ago. First of all, I notice a great loss of faith in institutions; institutions of government, institutions of control, institutions of finance, institutions of education no longer command the general confidence. People, to take a word we use in England, "blow upon" them. They feel doubtful about them. They have discovered, rightly or wrongly, that they are not the source of all wisdom. Also I see a considerable lack of confidence in men whose names you would have considered as infallible, something to conjure with, a year or two ago. But worst of all, from the American point of view, there has been a loss of faith in slogans—and heaven help America when she loses faith in slogans! I suppose so many Couéisms have been tried and found not altogether satisfactory, that that is to be pardoned.

But we must see that there is a limit to this loss of faith. There must be no loss of faith, I hope, in the superiority of thinking over drifting. Somehow or other we must realize that the cardinal sin is to lose faith in intellectual solutions. It must be better to think hard and work hard to discover a way out than merely to blunder around in the dark, fumbling vainly for the switch.

But if we are to have intellectual solutions, they must be intellectual in the best sense of the word, not merely academic exercises in books and within four closed walls. They must be intensely human and in touch with every-day facts. Where

would the clever analyst have been if he stuck simply to first principles, mulling them over in his mind, and did not take cognizance of what had happened in the world for the past two or three months in relation, we will say, to that extraordinary problem in India? No economist, no statesman, not even a missionary living for years in their midst, could have told you the precise point or the exact amount of pressure that would have changed the psychology of a people from their age-long, century-old habit of hoarding into a habit of "dis-hoarding", as the economists would say. Yet it happened, with the profoundest influence upon the ability of England, at any rate, to get on her feet again financially and to repay her creditors. Even the habit of hoarding in France and in the United States is a factor that might have been left out of account by the most profound economist engaged in his own studies but not looking closely at the world of actualities.

The second thing about our intellectual solutions is that we must not expect perfect solutions. We must not despair if we don't get perfect solutions. The only possibility is that we may get a little nearer than we have been. As we should say in golf, we may get a little nearer by making a good approach shot. We cannot expect that at one bound we are going to get any perfect solution, and we must not discredit solutions simply because they are not complete. If we can get them with any large percentage of completeness or accuracy, we must be grateful.

As the poet says, we want to mold the world "nearer to the heart's desire." But what is the heart's desire? There is not much good in molding the world unless we have a clear idea of our goal, what we are really after, what is our heart's desire. Is it quantity? Is it a suffocating mass of commodities for the world to use? Or is it quality? Is it a nice balance of human affairs and enjoyments and satisfactions? Is it getting all we can today and not bothering about the happiness and stability of society tomorrow? Or is it a blissful tomorrow bought at great price today? Or is it a nice balance between them? Does it admit of moral and artistic and spiritual judgments, or is it just one mad rush for the comforts of today? We must know what the heart's desire is before we can even make a good approach shot to it.

Many people are very intolerant of getting down to first principles. Their whole instinct is empirical, to act upon the impulse of the moment. They have no use for abstract principles. It is a British characteristic to distrust abstract principles, and I dare say that it is a characteristic here as well. You remember the picture in *Punch* of the two golfers who were partners. The one had left the ball where it gave a very easy nine-inch putt. His partner was about to attempt it. After a very careful selection of the right putter as to size, shape, smell and weight, and very careful deliberation on the lie, his partner began to get impatient, and finally exclaimed, "Not so much of your science—bung it in!"

This is the attitude, I think, of the average business man, but there is a time in the affairs of man which does not admit of quite such an easy solution, and in which this reliance upon instinct or upon the experience of the past is altogether misplaced. We have to remember that we have evolved an extremely complex machine which is capable of productivity such as the world has never known before, while it is functioning smoothly, but that the effect of psychology on that machine is all the greater because of its complexity; that an error of human judgment can do more damage in aggravating conditions in this complex civilization than it would in a simpler state of society. Why? If in the old days your wheelbarrow went bad on you, any handyman could fix it, but today if the complicated product of the automotive industry goes wrong, you must have the right man, with the right understanding, at the right place (he may be a long way away), with the right parts, to make the adjustments; and it may take a long time. It is an extremely complex affair. This is a very poor analogy, but it does illustrate that the more complex you make society the greater is the possibility of complete derangement. That is the situation today. Psychology plays an infinitely greater part than it ever could have done in a more primitive state.

It is no small wonder then that in finding our way out we are seeking a way of planning and controlling the situation. Everybody is evolving some solution, which means control, interference, or a plan of some kind. We have societies and companies in England that are doing nothing but theoretical planning of production, government and every activity of life

[132]

in order to coördinate them and make them run smoothly, and to prevent any further possibility of such disruption as we have had.

Contrast the other extreme of fifty or sixty years ago, the extreme of uncontrolled individualism and *laissez faire*, representative of the thought of Herbert Spencer, with the opposite extreme, the complete manipulation of the life of the individual, as it is being attempted in Soviet Russia today.

There is a long line, in between, of increasing interference and control, and we are all of us occupied in finding some position for ourselves between the two extreme points. Our desire is to get the best of both worlds, and according to our intellectual makeup we are trying to secure the maximum advantage. We weigh the profit incentive in individuals, which we believe to be indispensable for progress, and must not be interfered with, against those superior advantages which may come from having an aggregate and collective knowledge of what is happening, and a common aim, instead of disjointed ignorance.

We know that if men only knew collectively what was happening—over-production, under-production, or over-investment and the like—we might avoid many extremes. Some of us are very jealous of our individualism and are near the one end, while others are planning this, that or the other thing, and are near the other end. Some of us would have a central control of stocks of commodities. Others would have a central or international control of the value of gold. But whatever our interest may be, it is almost a platitude to say that we are all planning today at some point or other along that long line.

Let us look at one or two of these points. Senator, you have referred to the American banking system.¹ Far be it from me to say anything more definite on that than you have done; but from an outsider's point of view, it seems clear that just as you made a tremendous step forward in the Federal Reserve System, the time is now ripe for a very distinct advance as a next stage to making the rest of your banking system resilient. I will not say foolproof; that is a wrong word to use in this country, but mass-proof or ignorance-proof.

¹ Cf. Senator Walcott's address, *supra*.

It is becoming increasingly recognized that the receipt of deposits and the granting of credits is a much more subtle and extensive business than opening a grocery store, for any defect of knowledge is so much more far-reaching in its effects. It is the handling of contagion itself, either toward hope or toward fear. It ought not to be possible for an advanced community to have thousands of banks closing their doors under local pressures. The survival of the fittest cannot take place without tremendous danger to the community.

Now I do not care to say exactly how it ought to be done, but in some form or other interdependence and interregulation seem to be desirable in order that local shocks may be minimized; that there may be greater diversification of risks; that final decision upon large groups of risks should not be too close to the facts that are being judged.

Moreover, the fact that two whole systems compete side by side in the granting of credit multiplies the possibilities of unsoundness.

Then if you are to have improvements in these directions, they seem to me, looking as an outsider, to require a greater boldness on the part of politicians than history would justify us in expecting. In every country we are paying a terrible price for political prejudice. In this particular instance,—I do not know but I suspect—the influence of the small bankers in the various localities may be as important a factor as any other in securing any genuine reform.

But looking at the United States as a whole, from this point of view of control, it seems to me that its potential wealth, even without any consideration of foreign trade, is as great as ever it was, and the ingenuity and skill of its people also as great as ever. It has a circulating system sufficiently resilient for all ordinary variations of hope and fear. It is clear that at the present time all that marks it off from a period of prosperity is the psychological element or a certain spiritual quality. That mass psychology should be capable of destroying material wealth must now be evident even to the most material of men; and in all countries—not the United States alone—the manifestation of stability of character in individual institutions is the prime necessity.

This stability of character, as I see it, includes certain moral

[134]

qualities. It includes a general resistance to the instinct of getting rich quickly by the exchange of titles to production as distinct from increased powers of production. I think that the American habit of looking so exclusively or so continually on capital values for its source of satisfaction or despair, as distinct from incomes, perhaps makes the American people more peculiarly susceptible to waves of psychological optimism and pessimism.

As I see it, the stock exchange ought to be the residuum of what is happening in industry and in the banking and financial world. It ought to register those kinds of values which result from them. Instead of that, it seems to be in the seat of movement and of control. What happens on the stock exchange influences the feelings of the banks, and very often their actual stability and solvency, and certainly influences their feelings toward industry. They in turn carry on that psychology, and industry is depressed or improved in its prospects, from the wrong end. It seems to me that until all the countries where the stock exchanges are powerful see that the latter are made once more the resultant and residual rather than the actual focus or stimulus of power, we shall not be able to lift ourselves from our present difficulties.

When I come to the question of control in other spheres, I will take for example the British wage level. You all know that one of the difficulties of the British situation and the balance of trade is the question of export costs, and that the British wage level is a very important factor in those costs. It is so resistant to change that we are beginning to regard it as a fixed level, and we say that everything else must be adjusted around that level. So long as you have marked changes in the value of money and the price of commodities you are bound to be in difficulties with a fixed set of costs or a fixed financial structure; and in our financial structure we have certain very fixed things, the two principal of which are: firstly, the unionized wage level; secondly, a very large amount of debentures and other fixed debts. There is a third, a very large internal debt.

Look at our internal debt for a moment, 7,800 million sterling in 1924 when it was at its lowest weight on the community, either in the service or in the total proportion to the

[135]

national wealth. We have repaid since then something in the nature of \$2,000,000,000 painfully out of our budgets and taxation, reducing it to 7,400 million sterling; but its actual weight in terms of 1924 has gone up by \$20,000,000,000 owing to the change in the price level. It is now nearly 11,000 million sterling in the terms of the production in reality of 1924. Now there you have a relatively fixed situation, and the elements of control are invoked in two ways: There are those who say that when you have an exceedingly violent change in the price level you ought to have modifications of all things measured in prices, and wages should be correspondingly adjusted. On the other hand, you have people who say that the fluctuations in gold and the price level ought not to take place, and if they did not occur you would not want to adjust wages and prices.

Take the unionized wage level. I was speaking to one of the labor leaders, and he said, "It is idle for you to say when you make a mistake nationally or internationally in the handling of gold, that money wages should adjust themselves to that mistake, and that I should go to all the workers and try to alter the habits of thought of hundreds of thousands of them and make them adjust their wage scale and their age-long notions about the sanctity of a particular money wage to accord with that mistake. I know the fallacy of trying to keep up living wages under those conditions, but it is not my job to go to the men to alter their minds because of your mistakes. It is your job to keep gold prices steady. As long as I go about correcting the effects of your mistakes and those of your fraternity, you will never learn your job. It is the job of you bankers to keep gold steady, and you are up against it now. So long as we give way to you, you will never do it."

That is a very difficult complaint to answer and a very cogent argument, but you can readily see that on both sides control is asked for. On one side the desire is to control men's minds and make them accept what to them would be an autocratic and unjust change, even though you know that it really involves no change in real wages at all; on the other side, control of the price level is asked for, which only a much greater coördination of national and international thought can bring about; but control is wanted, baffling as it may seem, in both ways.

You have those, as I have said, whose ideas of control are focused on commodities. They would not leave it to choice to determine what the stocks of commodities should be. They would have the stocks of commodities made known and controlled as to their disposition and the level of prices at which they should be sold, either by pools, national or industrial, or by other international action.

This idea, however, raises the extraordinary problem that we have seen in rubber and other attempts at control, when there exists a free supply subject to no particular inhibitions, side by side with a controlled supply. Whether control is attempted in wheat, or in rubber, or even in money, in gold, if half the world is controlled and the other half free, you may stumble into even greater difficulties than if there were no control at all.

At the bottom of all extensive planning there is this particular difficulty, that the planning of production, if it is to proceed far, must enslave consumption. Ask an enthusiast on planning what proportion of mankind's consumption of goods and satisfactions is absolutely unalterable, or changes with price, or changes with fashion. If a very large proportion is unalterable, then you can ascertain it by large statistical aggregations and say such and such will be the demand of the world and aim your production to fit that; but I am afraid there is so large a part of the demands of men which will change by fashion or with price as to render every forecast of aggregate production liable to much more than a five-per-cent error. The moment you have that variability of consumption coming into the picture you are lost, and the economics of consumption, to say the least, are extremely precarious.

I have referred to the necessity for control in the area of gold. We are not at the present moment making very much advance in this respect. The possibilities of international misunderstandings are as great as ever, and until we can bring the ideas of all the different countries much closer together, I do not see how we can make more than a very remote approach to this problem—vital as it is to all the others.

We ought to recognize today, too, that the lending and borrowing of money between nations is ultimately an inter-

ference with trade and is fraught with much greater consequences than we have hitherto realized. It must affect future trade, because the volume and the direction of lending and borrowing may or may not correspond to the ultimate convenience of the natural direction of imports and exports.

No country can become a foreign lender merely by having large resources and a complete willingness to lend; that is, not a successful lender. It has to be able to stay out and to control its feelings in bad times as well as in good. It must not change its position in the international boat when the storm comes on, otherwise it will rock and frighten everybody. International finance, such as is involved in supporting bills of exchange, or even lending on bonds to smaller foreign governments and smaller countries, demands a close study and a long experience, and a willingness to ask the question, "What shall I do about this money I am lending when bad times come?" In answering this question, it requires great powers of endurance to withstand the temptation to clear out, even though clearing out may destroy the credit of the borrowing country in times of difficulty and danger. No country can, under modern conditions, really help forward the problem of stability and control unless it is confidently in possession of these qualities.

I doubt whether all those in the United States and elsewhere, with their frequent clamor to be independent of other countries, realize how the policy of obtaining a surplus of exports and being lenders of capital involves them in sharing in the responsibility for the economic prosperity of the rest of the world. It is possible by tariffs to establish a closed system, but it is not possible to combine with this successfully the profits or interests and risk-taking involved in large export trade and foreign loans. We need to think of these problems as a whole.

If I had time I would like to refer to the problem of sterling at length, and here I should deal with the problem not as a director of the Bank or even as an adviser of the Government, but I should try to give you the consensus of the opinions of the leading economists of Great Britain. May I express the opinion for them that what they are aiming at first of all is not to find first the level of exchange, but to find that price

[138]

level in our country which will enable the country with its various rigid factors to function to its maximum possibilities,—a price level which will not involve increases in money wages, but which will enable business to function profitably.

When we have achieved that level, it will correspond to a certain rate of exchange in foreign currency. Of course during the last three or four months gold has altered more rapidly in its value than sterling. People have been rather surprised to find that sterling has not risen with the depreciation in the exchange of gold. As a matter of fact the explanation is quite simple. You would expect that with the 30 per cent depreciation in the exchange a 30 per cent appreciation in the price level, or thereabouts, would occur. If you take the sterling price of commodities in international exchange and the gold price level you will find that a rise in one taken with the fall in the other accounts for this. Sterling since we went off the gold standard has risen 8 points and gold has fallen 11. The result is 19 points, which comes near the two-thirds we should expect. So all the time that gold prices are falling abroad, the problem of finding a stability of exchange between our price level and the outside price level is a really great one in Britain. Let us assume that we find a stable price level of our own and the price level abroad is stable, then there is a stable equilibrium between them, and that is the level at which we may come back to gold successfully. But I think nobody in England wants to come back to gold with the same risks of being thrown off it as heretofore. The pound at \$4, or at \$4.50, or whatever it may be, may fall just as easily as it did from \$4.86 if there is not some general international understanding about the regulation of money markets and the control of prices.

May I conclude by saying that in all these questions of control we presuppose a certain probity and a certain steadiness of character on the part of our populations and of their leaders. It is being borne in on me the longer I live in the economic field that the greater the bargain that you achieve in business as against the other man or against the other country, the more it seems that you have succeeded in driving a good bargain for yourself and a poor one for him, the less likely the bargain is to last and be to the satisfaction of everyone. These bargains

[139]

with one-sided advantages are really never worth while. The real balance of the world is only secured by letting every man having a fair deal.

It has been said that we all of us get our deserts, but it is only the successful who really acknowledge it.

My final word is this, that we are engaged, at the most serious point in the world's history, in reconstructing society, not only our own but the world's; and I would quote the words of a great poet of your own:

"Weak was the old world,
Wearily war fenced,
Out of its ashes
Strong as the morning,
Springeth the new."

[140]

PROCEEDINGS
OF THE
ACADEMY OF POLITICAL SCIENCE

Volume XV

JANUARY, 1933

[No. 2]

STEPS TOWARD RECOVERY

A SERIES OF ADDRESSES AND PAPERS PRESENTED AT THE ANNUAL
MEETING OF THE ACADEMY OF POLITICAL SCIENCE
NOVEMBER 18, 1932

EDITED BY
PARKER THOMAS MOON

THE ACADEMY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY
1933

COPYRIGHT BY
THE ACADEMY OF POLITICAL SCIENCE

CONTENTS

	PAGE
Preface	iv
<i>W. Randolph Burgess</i>	Introductory Address 1
<i>Henry A. E. Chandler</i>	Federal Reserve Policy and the Problem of Fugitive Gold 3
<i>Pierre Jay</i>	The Structure of the Banking System 11
<i>Robert H. Brand</i>	International Monetary Prob- lems 22
<i>Lewis W. Douglas</i>	Economy in Federal Govern- ment 32
<i>George McAneny</i>	Economy in State and City Government. 38
<i>Alexander Dana Noyes</i>	} Discussion: Monetary and Fis- cal Policies 49
<i>Robert B. Warren</i>	
<i>Thomas S. Adams</i>	
<i>Jackson E. Reynolds</i>	Introductory Remarks 56
<i>Edward Grant Buckland</i>	The Railroad Problem 57
<i>Leo Wolman</i>	The Problem of Unemployment 67
<i>Frederick E. Murphy</i>	The Agricultural Problem 74
<i>George B. Roorbach</i>	Tariffs and Trade Barriers in Re- lation to International Trade. 84
<i>Chris L. Christensen</i>	Discussion: Major Problems of Readjustment 95
<i>Alanson B. Houghton</i>	Introductory Remarks 99
<i>Thomas W. Lamont</i>	Primary Steps for Banking Re- form 100
<i>Viscount Astor</i>	World Agriculture and Dis- armament 111
<i>Silas H. Strawn</i>	Steps Toward Recovery 113
<i>Sir Arthur Salter</i>	Steps Toward Recovery 126

PREFACE

BLIND stumbling in the dark may be one way of seeking escape from the somber valley of economic depression. There is more hope, however, of finding the path to recovery by deliberate, intelligent search. The route is not wholly obscure. Can economic science and practical experience together point the way, if only for the first few steps toward recovery? To answer that question, a group of most eminent economists, financiers, and leaders in business and public life took part in one of the most important and best attended meetings ever held by the Academy of Political Science, the Fifty-second Annual Meeting, on November 18, 1932, at the Hotel Astor in New York City. The present volume contains in full the addresses delivered and papers presented at the Annual Meeting, but not the informal discussion from the floor. In these pages readers will find authoritative statements on money, banking and credit problems, economy in government, the railroad problem, unemployment, agriculture, trade barriers and the world economic situation.

For the marked success of the Academy's Annual Meeting, as well as for the content of this volume, credit and gratitude are due to the distinguished speakers who addressed the meeting and to the Committee on Program and Arrangements. The members of the committee were: Mr. S. Parker Gilbert (Chairman), Miss Ethel Warner (Director), and Messrs. Winthrop W. Aldrich, Frank Altschul, W. Randolph Burgess, Nicholas Murray Butler, James Byrne, Joseph P. Chamberlain, Frederic R. Coudert, John W. Davis, Norman H. Davis, George L. Harrison, Alanson B. Houghton, Pierre Jay, Thomas W. Lamont, Sir Walter T. Layton, Samuel McCune Lindsay, R. C. McCrea, Ogden L. Mills, Wesley C. Mitchell, Parker T. Moon, Shepard Morgan, William L. Ransom, Jackson E. Reynolds, E. R. A. Seligman, Jesse I. Straus, Thomas J. Watson, Louis Wiley, Garrard Winston, Leo Wolman, and Owen D. Young.

INTRODUCTORY ADDRESS¹

W. RANDOLPH BURGESS

Deputy Governor, Federal Reserve Bank of New York;
Trustee of the Academy of Political Science

THERE is only one general topic to which this Fifty-Second Annual Meeting of the Academy could possibly be devoted and that, of course, is the problem of recovery from depression.

There are today two approaches to this problem: the first is the fatalistic approach of those who feel that the business cycle is an immutable force which moves on, influenced but little by the considered conclusions or actions of men. If we adhere to this belief all we can do is draw ourselves into our shells and wait for the tempest to subside. Just now the fatalistic point of view takes the form of believing that now the recovery has begun, it will move forward on its own way, no matter what we do. One has to admit that there is considerable evidence to support this point of view. Certainly all human efforts to stay the course of business have failed to avert either overexpansion and speculative excesses or severe depression and distress. Certainly we cannot boast that our knowledge and skill have given us complete control over economic forces. A fatalistic philosophy has all too much supporting evidence.

But an inspection of today's program shows that our Program Committee, at least, has a quite different viewpoint, a belief that something can be done about the depression, that steps can be taken which will be helpful. It is not too much to hope that this meeting may prove an important instrument in organizing opinion toward taking those steps which may hasten recovery.

Each one of the topics listed in this program could well consume an entire day's program. We realize that we have asked distinguished people to come and present their views on large subjects within very brief time limits. The justifica-

¹ At the opening of the First Session.

tion we trust will be found in the resulting summary view of the whole situation, showing the picture in perspective. That is, I believe, the essential need of the moment. As far as may be, we should see the picture in its entirety and against its background.

Our morning program deals with monetary and fiscal policies. The first three speakers deal with monetary policy; the next two with fiscal policy.

[142]

FEDERAL RESERVE POLICY AND THE PROBLEM OF FUGITIVE GOLD

HENRY A. E. CHANDLER

Economist, Guaranty Trust Company of New York

I

FEDERAL RESERVE policy falls into three principal divisions: discount rate policy, open market policy, and gold policy. Discount policy at present is not of outstanding importance, and no important principle seems to be involved in the more distant picture. Open market policy is concerned with the immediate situation, and will be considered at the end of this paper. I will first discuss gold policy.

Gold is the foundation of our credit structure, and in our credit situation nothing can be more important. During the past winter this country has occupied the most extraordinary position in the history of the gold standard. According to opinion widely held abroad and in certain domestic circles, we have as a result of unwise economic policy in the past, obtained possession of a disproportionate share of the gold reserves of the world—and yet, last year there developed widespread apprehension lest the foreign drain on our reserves drive us off the gold standard. The amount of fresh liquidation, and losses due directly or indirectly to this fear, will never be known, but it was very large.

These developments necessarily raise several very pertinent questions: (1) If, as is widely held, we had on our own initiative garnered in, and for a number of years withheld from the outside world, this excess gold, why could the outside world take it from us? (2) Was there a sound basis for fear concerning our gold standard? (3) Can the conditions responsible for this fear be corrected?

Now excess gold has been the initial cause of much of our trouble in the past; it was not the only factor, but without it overexpansion at all approaching that culminating in 1929 would have been impossible, and the resulting reaction could

[143]

not have been so severe. And the amount and use of excess reserves in this market may have an important bearing upon our course in the future.

The presence of the excess gold in the United States has frequently been attributed to one or all of three factors: our protective tariff, Allied Debts, or our failure to meet our responsibilities as a creditor nation, that is, failure to lend enough abroad.

Now before I consider this question, lest the necessary brevity leave a wrong impression, I wish to make it clear that I have no intention of defending our system of protective tariffs; nor do I wish to suggest that I am opposed to revision of Allied Debts. It is not within my province this morning to discuss either of these questions, and I am touching them only so far as they appear to be related to our gold policy.

The simple truth is that all three assumptions as to the presence of excess gold in this country are without foundation, as any competent student can ascertain who will examine with care the records of our international balance of payments for the last four or five years, or for the last ten years.

Contrary to oft-repeated statements, here and abroad, during the past decade we did not deprive the world of the means to pay for our goods, or to meet the debt services due us,¹ and therefore we did not force it to pay us in gold.

Our favorable merchandise balance considered by itself gives a highly distorted impression. To get a true picture we must take into account: five billion dollars² spent abroad by our tourists for foreign commodities and services during the last ten years; two billion dollars for donations to foreign countries; and a number of smaller amounts representing our purchases of miscellaneous foreign services. Over a period of ten years, instead of a favorable balance on our combined commercial and donation account, we had a substantial unfavorable balance; or to put it in another way, our purchases from, and donations to, the rest of the world exceeded its aggregate

¹ Of course this does not mean that every country whether it be debtor or creditor is enabled to balance its accounts with us exclusively by direct interchange of commodities and services and by direct credits. No nation does that. International balances are effected by triangular operations.

² Net.

purchases from, and donations to us by not less than one and one-half billion dollars. Also during this period, notwithstanding the deficit on our combined commercial and donation account, we lent the outside world on long term more than our total permanent net income on foreign investment account. In short, during all this period, instead of depriving the world of the means to get back its gold, we, through our purchases, donations and loans, transferred a sufficient balance to enable the world to take back every dollar of excess gold in this country.

Why, then, did the excess gold which was accumulated during the war remain with us; and why did more come periodically throughout the postwar period? In the answer is to be found the key to our gold problem.

Quite aside from the working balances which foreign institutions normally require here in connection with commercial and financial transactions was another large aggregate of funds which had no necessary relation to normal trade development. These funds were sent here partly as a matter of convenience, largely because many foreign citizens or institutions hesitated to invest in their own or other countries, and much was sent here for investment or speculation in our markets.

Had it not been for these facts, the world never would or could have built up the large balance against us on short term account, or the enlarged potential claims attached to foreign-held dollar securities, which together caused many during the period of hysteria to question our ability to remain on the gold standard.

Now, let us turn to our second question, namely: was there at any time a real basis for fear concerning our gold standard? We had in our possession more than enough gold to meet the foreign drain even if every foreign liquidable claim against our gold was cashed in. With respect to the outside world, our position could be made impregnable by utilizing the means already provided by the Federal Reserve Act. Of course, there never has been a nation that could not be driven from its standard at any time if enough of its citizens lost their heads. The question therefore was solely one of how many of our own people would lose their balance.

In our Reserve Act is a provision placed there by its founders to take care of abnormal situations, namely, section 11-c, providing for temporary suspension of the reserve requirements. In other leading reserve banking systems there is some emergency plan for meeting temporary situations, and these plans have been used effectively in the past. Had we been able to avail ourselves of this provision sufficiently early, we could have demonstrated to the world the strength inhering in our gold position, and the gold outflow in all probability would have ceased well before we had approached the limit of our technically free gold (and our so-called free gold was only part of our excess gold, and of course back of that is a still larger amount).

But there were unusual conditions which raised some question as to the possible effect upon our own people of the resort to this measure. Apprehension, initiated in some quarters by knowledge of the claim against our gold, but not of our means to meet the claim, plus a widespread fear of inflation, and an irrational, although apparently irresistible conclusion that all emergency measures necessarily tended to inflation, raised a doubt in the minds of some as to whether the hysteria might not attain such magnitude as to cause our own people in their ignorance to precipitate a temporary departure from the gold standard. It was an unparalleled and in a sense ridiculous situation: The wealthiest nation in the world, with the greatest stock of gold of all time, apprehensive lest the standard be jeopardized by use of the gold reserves for the very purposes for which they were accumulated.

Many other aspects of this question would have to be considered before a complete picture could be presented. I will simply say that our experience of the last twelve months raises a real question as to whether, exclusively by means utilized in the past, we can in the future always keep our monetary gold movements within limits which the maintenance of public confidence requires; and also as to whether, when large exports are impending, we can feel confident that the emergency provision will be availed of in time to prevent serious losses. It is not enough that we remain securely on the gold standard. We ought in the future to avoid the losses incident to apprehension concerning our standard.

[146]

The pre-war system whereby protection of gold reserves was effected independently by each nation by changes in the bank rate, is no longer adequate. The vast fund of short-time money created since the war by virtually swapping long-term loans for demand deposits or short credits, and the tremendous flows of short funds from one international money center to another that can occur in a short time, irrespective of discount rates, render impossible complete assurance of successful administration of gold reserves by relying exclusively upon the principles which were sound and adequate under the older conditions.

This is not the place to discuss the specific means required to meet the problem. Any satisfactory solution obviously requires international action.

Whether it may be necessary for us by our independent action to prevent excess funds from accumulating here by re-investing in other centers (some central banks invest in our market); or whether it may be necessary by a new method of computing Federal Reserve ratios or by other means practically to segregate or earmark these funds when their accumulation promises to disturb our credit situation; or whether, as is to be hoped, we can through international coöperation (either directly with the leading central banks, or through the Bank for International Settlements) effect the return of these funds, or reinvestment in centers where most needed—one thing seems clear: our own interest and the best interest of the rest of the world require that we do not again let too much of the foreign fugitive funds become a part of the base upon which we expand domestic credit.

In short, I believe that the newer conditions in the international monetary and credit situation require a new gold policy, the principal objective of which shall be adequate control of the flow of fugitive international funds, to the end that: (1) we shall no longer be an unwilling agent in the maldistribution of gold; (2) we shall not again overexpand credit at home upon the basis of excess but fugitive gold; (3) the outside world shall never again build up such a claim as to raise question in the popular mind as to the soundness of our monetary position.

This control ought to be accomplished through interna-

[147]

tional coöperation. The problem is by no means exclusively American. In view of the experience of the last few years it is not to be expected that other countries will be willing to return to the gold standard under the same conditions as following the war. Among the necessary conditions of the return of other countries to the gold standard are: some assurance of a reasonable distribution of gold; and such a control of international funds as shall not again jeopardize their standards.

In view of the great problem of the relationship between price levels and debts which in part is a monetary problem and a world-wide problem, and in view of the uncertain status of the gold standard in other countries, I am convinced that much closer international coöperation in monetary matters is required, and that because of our preponderating influence in world monetary affairs we should accept leadership. The necessity of Reserve Bank coöperation with other central banks would seem to be obvious. And further, if the Federal Reserve System is to accomplish the most possible (by monetary influence upon the price level) to reduce the weight added to debts here and abroad, it must be permitted freedom of action to coöperate with foreign central banks. But as we advance to do our full share in international coöperation (and I feel sure that we can well afford to go more than half-way in meeting other countries) the principle to be kept in mind is that one of the best ways to help the rest of the world as well as ourselves is to keep our own position sound.

Now as to immediate policy.

II

This depression may be divided into two parts: (1) the earlier part, which was a necessary correction of an overexpanded financial and business situation; (2) the later part, which was the demoralization that carried liquidation far beyond anything required to correct the previous over-expansion.

The key to the later, and more serious, part of the crisis was the widespread mania for converting assets into cash or other liquid form. This was not limited to any one group of

individuals or institutions. It was nationwide. The amount of liquidation attempted was so large relative to the cash and other liquid assets available, as to render inevitable a continued series of declines until the liquidation could be stopped. It was necessary therefore to find some means of stopping liquidation, and of inducing idle and liquid funds to return to investment channels. The several emergency measures adopted by the government had made considerable headway in accomplishing the first, but it became evident early last spring that if the second was to be accomplished, something must be done to inject new life into the investment markets.

In turning to the records of past depressions, there could be found no case sufficiently analogous to give us a basis for a confident judgment as to what should be done. The records of the past, however, seem to establish a fair presumption that the pressure of excess reserves on the money market at the proper time injected new life into the situation. Now almost continuously during the past year the question had been considered as to whether an injection of credit in quantities sufficient to exert a strong pressure of excess reserves would not accomplish the desired end. No one could possibly know when was the proper time, or how much pressure was required, but we had reached a point where vigorous measures were called for, and the purchase of government securities in large amounts by the Reserve System seemed to be the only sound method that had some promise of being effective. Outflowing gold gave added reason for such action.

At that time the Federal Reserve began placing each week something like 100 million dollars of reserve funds in the market by the purchase of government securities. Part of these funds served to offset the outflow of gold, and part eventually resulted in the accumulation of excess reserves by the member banks, which was accompanied by a rapid decline in money rates.

With the improvement that soon set in you are all familiar. It is impossible to say how much of the improvement is to be attributed to this action. The apprehension later injected by the political campaign renders it impossible to know whether the favorable trend would otherwise have been entirely uninterrupted. In so far as we can appraise the situation, it would

seem that the Reserve System was fully justified in the action taken.

Now what of the immediate future? To a large extent credit conditions have reversed themselves. Gold has been flowing in, currency returning, new national bank notes going into circulation, and New York money rates have declined to the lowest level in history.

Should the Reserve System reverse its policy, or should it maintain its present volume of government security holdings, and thus passively contribute to the continued pressure of excess reserves? I have not time to discuss the many aspects of this question. Two things however may be said. Sufficient time has not elapsed to permit the full effect of the Reserve action to be felt, even if there had been no interruption by the political campaign. The ultimate good to be gained from the successful completion of this program so far outweighs any temporary inconveniences, that I believe the Federal Reserve System should carry through, and not relax its pressure until the job is completed.

[150]

THE STRUCTURE OF THE BANKING SYSTEM

PIERRE JAY

Chairman of the Board, Fiduciary Trust Company of New York;
former Chairman of the Board, Federal Reserve Bank of New York

THE present banking structure of the United States is the development of about a century of "free banking", as it was called in the 1830's, under which almost any reputable group has been able to obtain a banking charter. The structure, in its barest outlines, is as follows: There are about 18,750 banks which do business with the public. These consist of (1) national banks, (2) state banks and trust companies, and (3) mutual savings banks and private banks. With the last two, we are not greatly concerned. For mutual savings banks, with perhaps a dozen exceptions, exist only in the territory from Pittsburgh east and from Baltimore north; while private banks, except for a few in the great cities, are a fast-disappearing element in our banking structure. All these banks start as local unit banks. But some now maintain branches: city-wide, county-wide or state-wide. A few even have branches in foreign countries. Moreover, in states where branches are not permitted, many unit banks have associated themselves together as "groups" or "chains", under central managements. Viewed externally, then, the banking structure consists principally of independent local units; but with a strong tendency towards branch banking, greatly accelerated during the past decade, and held in check only by legal or administrative restrictions.

Viewed internally, all the banks, whether unit or branch, exercise some or all of these four principal functions—commercial banking, savings banking, fiduciary work and security distribution. The time limitations on this paper permit of no discussion of functions.

Over every individual bank stands a supervisor, national or state, to endeavor to enforce the law and correct abuses.

Back of the entire structure stands the Federal Reserve System, a coöperative organization of the member banks, to

[151]

of portfolio is lacking; there are too many eggs in one basket. Second, that the smaller the place, the less bank officers are likely to apply the perspective of general credit conditions to their local credit problems or to realize the necessity of a substantial element of liquidity in the portfolios. That some city bank officers have also been equally short-sighted does not alter the case.

Remedies. The various remedies which have been suggested for this situation center about two proposals: (1) greater unification; (2) widespread branch banking.

(1) *Greater Unification.* The most authoritative proposal for greater unification in the banking structure is that which the Federal Reserve Board unanimously made to the banking committees of Congress on March 29, 1932, as follows: "It should be recognized that effective supervision of banking in this country has been seriously hampered by the competition between member and non-member banks and that the establishment of a unified system of banking under national supervision is essential to fundamental banking reform."

There can be no doubt that the proposal of the Federal Reserve Board, if it could be brought about, would be an important step in advance. There are today about 6,085 national banks and 11,520 state banks (other than mutual savings banks). All state banks with sufficient capital have had the option for many years of either converting into national banks or of joining the Federal Reserve System. It is obvious, therefore, that unification of a banking structure whose roots go far back into our history could be brought about only by force. We have already twice exerted such force—first, when the National Bank Act was passed; and second, when the Federal Reserve System was created. Each accomplished its immediate objective, but neither has prevented bank failures.

It should also be observed that unification within the framework of the National Bank Act would not reach the great mass of small state banks which now have insufficient capital to qualify as national banks. Their number would be further increased if the minimum capital of national banks were increased from \$25,000 to \$50,000 as the banking bill now before Congress proposes. Yet these very small state banks,

as already indicated, are the source of most of our bank failures.

Clearly, there would be advantages in unification under national supervision. It would remove present competition between national and state authorities resulting in lowered legal restrictions, less strict supervision and lower standards in granting new charters. Nevertheless it appears to me not to go really to the root of the trouble. For, as already indicated, supervision is largely negative and exerted after the fact. Even the proposal of the banking bill to permit the Federal Reserve Board to remove officers and directors of banks which engage in unsafe or unsound practices does not provide safe and sound officers or directors to take their place. What is really needed is something positive, namely better bank management. The small banks, I am convinced, can neither find nor afford better management except through a change in the banking structure which will permit them to be operated as branches of a larger bank.

(2) *Widespread Branch Banking.* This leads directly to the second proposed remedy for the recent flood of bank failures, namely widespread branch banking. This in itself would doubtless bring about, not by force but by evolution, an important measure of unification. A large bank with branches could hardly afford not to be a member of the Federal Reserve System. Moreover, the unification would probably occur largely within the framework of the national banking system, since only the National Bank Act is capable of permitting branches freely to cross state lines unless, indeed, such Federal branch legislation should stimulate some of the states to offer reciprocal branch bank courtesies among themselves.

Advantages of Widespread Branch Banking: (1) It would offer to small communities, as well as large ones, the banking services of institutions sufficiently large to be able to hire competent and experienced management.

(2) The portfolios in which the deposits of small communities would be invested would be diversified instead of mainly local; and under any reasonably conservative management they should also have a substantial element of liquidity.

(3) In addition to present outside supervision, the branches

of portfolio is lacking; there are too many eggs in one basket. Second, that the smaller the place, the less bank officers are likely to apply the perspective of general credit conditions to their local credit problems or to realize the necessity of a substantial element of liquidity in the portfolios. That some city bank officers have also been equally short-sighted does not alter the case.

Remedies. The various remedies which have been suggested for this situation center about two proposals: (1) greater unification; (2) widespread branch banking.

(1) *Greater Unification.* The most authoritative proposal for greater unification in the banking structure is that which the Federal Reserve Board unanimously made to the banking committees of Congress on March 29, 1932, as follows: "It should be recognized that effective supervision of banking in this country has been seriously hampered by the competition between member and non-member banks and that the establishment of a unified system of banking under national supervision is essential to fundamental banking reform."

There can be no doubt that the proposal of the Federal Reserve Board, if it could be brought about, would be an important step in advance. There are today about 6,085 national banks and 11,520 state banks (other than mutual savings banks). All state banks with sufficient capital have had the option for many years of either converting into national banks or of joining the Federal Reserve System. It is obvious, therefore, that unification of a banking structure whose roots go far back into our history could be brought about only by force. We have already twice exerted such force—first, when the National Bank Act was passed; and second, when the Federal Reserve System was created. Each accomplished its immediate objective, but neither has prevented bank failures.

It should also be observed that unification within the framework of the National Bank Act would not reach the great mass of small state banks which now have insufficient capital to qualify as national banks. Their number would be further increased if the minimum capital of national banks were increased from \$25,000 to \$50,000 as the banking bill now before Congress proposes. Yet these very small state banks,

as already indicated, are the source of most of our bank failures.

Clearly, there would be advantages in unification under national supervision. It would remove present competition between national and state authorities resulting in lowered legal restrictions, less strict supervision and lower standards in granting new charters. Nevertheless it appears to me not to go really to the root of the trouble. For, as already indicated, supervision is largely negative and exerted after the fact. Even the proposal of the banking bill to permit the Federal Reserve Board to remove officers and directors of banks which engage in unsafe or unsound practices does not provide safe and sound officers or directors to take their place. What is really needed is something positive, namely better bank management. The small banks, I am convinced, can neither find nor afford better management except through a change in the banking structure which will permit them to be operated as branches of a larger bank.

(2) *Widespread Branch Banking.* This leads directly to the second proposed remedy for the recent flood of bank failures, namely widespread branch banking. This in itself would doubtless bring about, not by force but by evolution, an important measure of unification. A large bank with branches could hardly afford not to be a member of the Federal Reserve System. Moreover, the unification would probably occur largely within the framework of the national banking system, since only the National Bank Act is capable of permitting branches freely to cross state lines unless, indeed, such Federal branch legislation should stimulate some of the states to offer reciprocal branch bank courtesies among themselves.

Advantages of Widespread Branch Banking: (1) It would offer to small communities, as well as large ones, the banking services of institutions sufficiently large to be able to hire competent and experienced management.

(2) The portfolios in which the deposits of small communities would be invested would be diversified instead of mainly local; and under any reasonably conservative management they should also have a substantial element of liquidity.

(3) In addition to present outside supervision, the branches

would be subject to continuous internal supervision. This would be really authoritative supervision because it would have power instantly to change local management wherever it was proving unsatisfactory. Head-office control over the larger loans should tend to check over-extensions of local credit, which have proved to be as ruinous for local borrowers as for local banks. And head-office purchase of securities should be more expert and conservative.

(4) Branches could be opened tentatively in small places and later withdrawn if they proved unprofitable. Under unit banking, such small local banks, once established, seldom withdraw except by failure.

Objections to Widespread Branch Banking: (1) The traditional American prejudice—one may almost say fetish—in favor of the administration by local bankers of local deposits and credits, and against allowing a distant banker to say when and how much a local man may borrow.

(2) The fear that local deposits may be drained away and loaned in larger cities.

These I believe are the objections usually advanced, and they are closely allied. In theory there is much to be said for both of them. In actual experience, however, they largely disappear. Cases can doubtless be found under existing branch banking, here and in other countries, where local borrowers do not get all the credit to which they consider themselves entitled and where local funds that local people would like to borrow are sent away or otherwise invested or loaned. Such complaints have arisen under unit banking also. As late as 1928 and 1929, when local banks were extending large local credits which later proved disastrous to both lender and borrower, one frequently heard both these complaints. In the main, however, banks with branches, like unit banks, are in business to make money; rates for local credits are nearly always higher than money market rates; and the fastest way a branch can grow and become profitable is by making all the *good* local loans it can. Moreover, backed by a larger capital, the branch can extend larger individual credits than the local bank, and it can draw on the head office for additional funds when local credit requirements exceed local deposits.

(3) There is this further objection—that if a bank with say one hundred branches were to fail, every one of its offices would close, whereas if each of its offices were a local bank, probably a fewer number of them would fail. This, to my mind, is the one fundamental objection to branch banking over a wide area. There is, of course, no way of assuring sound management for all banks having widespread branches. But to shrink from branch banking because of this risk is to yield to a counsel of despair. Both Great Britain and Canada, where, as with us, deposit banking prevails, have had failures of banks with branches. But the percentage of their resources involved has been so much less than in our unit bank failures that the answer to this objection is reasonably satisfactory. In Canada, for example, where recent economic conditions have closely paralleled ours, there has been but one failure, involving 78 branches, in the past eleven years, while we have had over 10,000 failures. In Canada this failure affected about $\frac{1}{2}$ of 1 per cent of the average banking assets during the period, while about 10 per cent of the assets were affected by our failures.

Experience shows that the lending and supervisory organizations which banks doing extensive branch banking have to maintain and can afford to maintain contribute powerfully in themselves towards careful management, while the wide area covered brings diversification of risk.

Progress of Branch Banking in the United States. Whatever the arguments in favor of and against branch banking may be, the fact is that during the past eleven years the number of branches has greatly increased and would have gone much further but for legal and administrative restrictions; many groups and chains have been formed awaiting the necessary authority to convert into branches; the course of events has greatly weakened the opposition of the smaller unit banks; and the banking committees of Congress have introduced a bill providing that a national bank may establish branches within its own state and fifty miles beyond its borders. Thus, as a remedy for the obvious weaknesses of unit banking, we appear likely soon to embark upon branch banking side by side with unit banking. If and when we take this fundamental step towards a far-reaching change in

our banking structure, it seems important that we should take the step not tentatively or half-heartedly but fully convinced of its desirability as a national policy designed to afford better protection to deposits.

Conditions of Success. Like many other supporters of unit banking, I have been forced by recent events to change my views, and I now regard branch banking as the only fundamental remedy for the demonstrated weaknesses of unit banking, particularly in the smaller places. But to become an effective instrument of national policy branch banking should be permitted to develop under conditions most favorable to its success. These conditions involve questions of: (1) area; (2) supervision; (3) competition with unit banks.

(1) *Area.* Under the banking bill, a national bank may establish branches anywhere within the limits of its own state and within contiguous territory fifty miles outside. This provision, while a tremendous step in advance, still savors of half-heartedness. If we are willing to go this far, we might better recognize at the outset that state lines are usually political rather than economic; and that we shall soon have to amend the law to permit branches over more natural trade areas, as ex-Comptroller Pole recently recommended. To shut our branch banking up in forty-eight separate compartments as if it were something we feared, is to ignore the experience of all the other countries of the world where, as far as I know, there is no territorial restriction. This does not mean that I would contemplate for the United States, even for the distant future, branch banking which covered the entire country. Distance and sectional feelings are against it; proper diversification does not require it; and obviously there must be *some* limits. But surely all will agree that a state—plus fifty miles—will in many cases prove a limitation that has elements of unsafeness. In states overwhelmingly agricultural, for example, state lines will render it difficult to attain that fundamental requisite of branch banking—a diversified portfolio. The limits, it seems to me, should be sufficiently wide, and more than this, sufficiently elastic, to permit of sound diversification. The twelve Federal Reserve Districts approximate natural trade areas, in spite of some

[158]

arbitrariness, and they appear to me to be the most practicable limits within which to work. But the Federal Reserve Board, which under the proposed bill is to authorize all branches, should, it seems to me, be empowered to allow branches to overstep district lines when necessary to cover trade areas or to assure diversification. This would reduce maximum branch banking areas from forty-eight to twelve, without, however, placing any limits on the number of cities from which branch banking might proceed. No one can foretell, from experience elsewhere, what the evolution will be in this country or in its various sections. The important thing is, from the outset, to give it natural scope rather than to restrict it to artificial boundaries so that we do not foster unnatural and inadequately diversified branch systems which it may be difficult later to alter.

(2) *Supervision.* Widespread branch banking introduces into the structure the possibility not of more bank failures, but of larger and more serious failures. The banking bill wisely provides that the establishment of every branch shall be subject to the approval of the Federal Reserve Board. This places both properly and squarely upon the Board and the Federal Reserve Banks the primary responsibility for the sound development of branch banking. It seems important that they should also have authority to prevent weak state institutions with branches from becoming members of the Reserve System by conversion into or consolidation with national banks. Whether the branch banking institutions which are permitted to develop shall be strong and sound or shall merely represent a cross section of existing unit bank management depends, in the main, upon the standards which the Federal Reserve Board sets up as a guide for its action, and the rigidity and ruthlessness with which it declines to authorize branches for any bank whose past record and policies have not been sound and safe. There should be no place in branch banking for officers or directors who seek to operate banks in their own selfish interest. And there is no question that the public is in a mood to give full support to ruthlessness exerted in the public interest.

The supervision of these larger institutions will bring heavier responsibilities to their supervisors. But on the other

[159]

hand, with fewer units to supervise, more concentrated attention can be given; and the ability of these larger institutions, both to find and to pay for good managers, should remove one of the present difficulties in the supervision of small local banks.

A second element in the development of branch banking is the speed with which it proceeds; and it is possible that here again the Federal Reserve Board may be able to exercise a restraining influence. Proper organizations to manage branch banking systems cannot be developed overnight. Some unsatisfactory situations would be likely to occur if a competitive scramble for branches, such as has recently taken place in certain areas, should be repeated over the country as a whole. Fortunately the present difficult period favors moderation in the speed of establishing branches.

A third factor, with which no national or state supervisor has yet been able to cope, but with which it is to be hoped the Federal Reserve Board may find a way to deal, is the competitive paying of high rates of interest on deposits, particularly savings deposits. Where not controlled by clearing house or other arrangements, these rates have quite generally led directly to the purchase of inferior bonds with high coupons, among which, on the law of averages, the mortality is high.

(3) *Competition with Local Unit Banks.* The initial establishment of branches will doubtless proceed along the lines of least resistance by absorbing local unit banks. Many strong local banks, however, may decline to become branches and the question will then arise whether a larger institution should be permitted to put a branch in such places. While the size of the place will have a bearing on the decision, I should like to express a purely personal view that as sentiment in small places will naturally favor the local bank, the willingness of a strong well-managed bank to maintain a branch alongside the local bank should at least be an important presumption in favor of granting the application. Certainly in the medium-sized places, there will be many such cases, while in the larger places, there may well be several branches and several purely local banks as well. Perhaps this is going beyond my province and attempting to look too far ahead.

[160]

But if we finally and deliberately decide to permit widespread branch banking as the best means of strengthening our banking structure then it seems to me that it should not be regarded as a monster to be caged and hampered. Provided a bank has good management, it should, in general, be allowed to bring its services and advantages to those places where its managers think they can profitably operate.

This closing thought serves to emphasize my belief that changes in the banking structure should be approached primarily from the standpoint of safety of deposits rather than from the standpoint of amount of credit to be extended locally. Too often in the past the latter has appeared to be the primary objective of banking legislation. With full recognition of the fact that loans create deposits, we shall be on safe ground, nevertheless, if we paraphrase the familiar English adage, and say, "Let us take care of the deposits and the loans will take care of themselves."

[161]

INTERNATIONAL MONETARY PROBLEMS

THE HON. ROBERT H. BRAND, C.M.G.

Of Lazard Brothers and Company, London; British Member of
the Standstill Committee

IT would obviously be impossible for me to discuss intelligibly in twenty minutes all aspects of the huge and complicated international monetary problem. I do not intend, indeed, to discuss currency questions at all, but rather one or two problems which lie at the base of most of our monetary troubles.

You are, I expect, all weary of explanations of the crisis. The subject matter is so extraordinarily complex that a complete explanation is difficult and still more difficult the remedies. I sympathize indeed with the recent speech of the Governor of the Bank of England when he said he did not see his way through the maze. At the same time, speaking not as an economist, but as a practical banker engaged day by day in international finance, I have come to certain broad conclusions which may or may not be of value but which I should like to put before you.

You have often heard that the crisis is due to the scarcity of gold. I have never believed that and I think this explanation can be dismissed. Many of the evil developments have arisen, it is true, from the maldistribution of monetary gold of which two countries, the United States and France, hold between them about \$7,000,000,000 or \$8,000,000,000 out of a total of between \$11,000,000,000 or \$12,000,000,000. But the fact of this striking maldistribution tells nothing, unless one seeks for the underlying causes of it.

You have often heard, and this indeed is a very popular and widespread opinion, that the crisis is a crisis of overproduction, that we are suffering from our rapidly growing capacity to produce, that we are starving because we have too much wealth. I do not hold this view. I certainly would not deny that the greatly improved methods of wealth production and their extended use in many new countries bring with them, as they

[162]

have always done for the last 150 years, very difficult problems and require on the part of the business world great powers of change and adjustment. I would not deny that this cause has intensified, perhaps greatly intensified, the crisis in which we find ourselves. But I certainly do not think it is the root cause. Had we never had the Great War, I am convinced that day by day, week by week, month by month the necessary adjustments would have been made without too much suffering, certainly without a collapse of the whole international monetary mechanism, and that we should have seen not a reduction by more than half of the world's international trade, but rather its constant growth. No. I attribute the crisis to the dislocation caused by the war and by post-war policy. I do not think we appreciate the extraordinary complexity of the world, now that it has yearly been drawn closer and closer together, or the delicacy of the international credit fabric. In normal times and after many years of peace, the world's monetary and price structure and the current debit and credit relationship between the different nations acquires a certain stability, which enables the vast mass of individuals and institutions engaged in business to work very satisfactorily more or less as bees work, quite unconscious, so to speak, of the honeycomb which has been provided for them by this stable structure. It is this comb which has been smashed since 1914. Governments are now engaged in the task of trying to recreate it, and there is a large mass of opinion which wants them to go further and make the honey itself. Indeed one of the most profound cleavages of opinion today is between those who believe it is best that human beings should work—subject no doubt to many qualifications—more or less as bees or ants, provided with as stable a monetary structure as possible and guided in the main to right decisions by the economic forces of price and interest, and those who believe that the activities of whole nations should be consciously determined by the reason and foresight of the supermen, whom their natural intelligence will lead them to choose as their governors. Personally my belief is that whether these supermen are Russians or others we shall require a few more thousands of years of evolution before human beings are completely equal to the task. This however is by the way.

[163]

Now my view is that the Great War had the same effect on the world's economic and financial structures as a man has on an ant-heap when he takes a stick and pokes it into complete confusion. Who would expect it to be restored except after all the infinite number of connections and strands had again been painfully restored? I believe indeed that our present complicated economic structure cannot stand war or enduring hostility between great nations, and that we have to choose between a generous friendship between them, or a simpler form of civilization and less international intercourse, which would involve a lower standard of life, in some countries might call for a large reduction in population, and in the transition period at any rate would be fraught with great social dangers.

Out of all the dislocations and disequilibria produced by the war I am today however only going to deal with one, namely, the dislocation caused in the relations between debtor and creditor nations and in the consequent process of the international lending of capital. The war ended up with some nations richer and a good many nations much poorer than before; some nations that had been debtor nations were creditor, and others which had been creditor nations were debtor. The world was entirely changed. If human beings had been all-wise, what would they then have done? They would have recognized that we all grow rich or poor together, that riches acquired out of other people's poverty are not lasting, and they would have attempted so to act as to bring up the poorer nations more nearly to the level of the richer, so that we all might march along step by step. They would have placed as few burdens of debt as possible on the poorer nations; the creditor nations would have used their surplus not in importing gold in huge quantities, not even in lending back the surplus at high rates of interest to the debtor countries, but more largely at any rate in buying goods from them. In other words, we should have tried to restore equilibrium as far as possible by buying and selling, and not by lending and borrowing. France would have gladly seen Germany recover and the United States Congress would have cancelled War Debts by acclamation.

No doubt such a procedure would have demanded from human beings far greater foresight and magnanimity than they

[164]

are accustomed to display. But, unfortunately, these are the sort of qualities which in the future they will have to display if our civilization is to progress smoothly.

This process of international lending has never to my mind been sufficiently studied by the economists and I would like to see one or two first-class economists devote all their attention to it.

Before the war, as you no doubt all know, England was the greatest creditor nation; France came second; and Germany third. I have been a banker only for twenty years or so, and it is an indication how far we have traveled in that time that I can remember American dollar loans, I think for American railroads, being issued in Berlin. These creditor countries had developed over years a more or less steady lending program; the loans were made in the main to developing countries, which were growing fast themselves in wealth and which found then that they could sell an increasing amount of commodities abroad to cover the service of the loans, while the creditor countries were enabled by these loans to increase the export of their own more finished products. In other words, the trade in commodities moved in harmony with the international lending and moreover the chief lending country was a free trade country constantly increasing its imports. Even so, however, I do not feel certain whether these great international loans represented a really permanent process. I am not sure how long the borrowing countries could have gone on borrowing, or rather whether the only method of their meeting the service of their loans was not to go on borrowing, and at a constantly greater rate. However that may be, the plan worked harmoniously up to the war and, what is all-important to note, these loans and the import and export trade which accompanied them enabled the creditor and debtor nations to balance their positions with relatively small movements of gold, and therefore without encouraging or compelling great inflationary or deflationary movements or endangering the international gold standard.

The war destroyed this whole process. The relative creditor and debtor position of the different great nations was violently altered. The United States became almost in a night a creditor rather than a debtor nation, and the seeds of important

[165]

future developments were laid in the consequent big gold imports into the United States during the war. The war ended with the defeated nations heavily debtor; with France even for a short time on the debtor side; and with England's creditor strength diminished. The United States continued her great export trade, which had been built up since the war, and other nations being also heavily indebted to her in other ways, she continued to take part of her surplus in the form of gold imports.

These gold imports due to the unbalanced creditor position of the United States during these years formed the basis, I think the indispensable basis, of the subsequent over-inflation of credit and resulting boom, which in its collapse has been so preponderant a cause of the world's present troubles. This however is anticipating. The post-war creditor and debtor position would have been unbalanced anyway, but this evil was of course greatly intensified by the Reparations and War Debts payments and, in particular, by the fantastic Reparations demands. The extreme pressure on Germany over years brought about the huge depreciation of the currency; this led to Germany's "auction sale", which depleted her of working capital, and into this vacuum flowed inevitably later the loans long and short made to her by European creditor countries and particularly by the United States. The effort was made to balance the disequilibrium between the creditor position, particularly of the United States, and the debtor position of other countries by lending and borrowing on a large scale. The United States, indeed, encouraged by the internal growth of credit, lent more than her surplus, balancing her position by taking short-term deposits from the whole world.

Before 1925 the creditor countries—namely England and the United States—made loans mainly to non-European countries, e.g., South America, Australia, Canada and so forth, encouraging the production in the main of food and raw materials. After 1925, when European countries showed more currency stability, the loans flowed largely to Central Europe and Europe in general developed her production up to the pre-war level, without too much regard for the production which had been stimulated in non-European countries.

About this time another unbalanced creditor position began

[166]

to cause trouble. France had no doubt been a creditor nation for some years, while her currency was depreciating. But she made no loans abroad, her nationals preferring to build up balances abroad and particularly in the United States. On the stabilization of the franc these were repatriated, and since by this time the borrowing countries were getting a bit shaky and also French taxation almost prohibited foreign issues in Paris, no loans were made and the repatriation took the form of huge gold imports.

This development more or less coincided with the period when the boom in the United States had persuaded the American investor that there was more money to be made at home than in buying foreign issues and indeed persuaded multitudes of investors in debtor countries that they had better take a hand in the game and remit their money for investment or speculation, whichever you like to call it, in New York. Consider, therefore, what was happening to the debtor countries in the world in these years and months before the end of 1929. Many of them had become used to and had based their whole economy on a constant flow of loans; these loans began to dry up, particularly those from the United States, owing to the progress of the boom. Their whole economic and financial life began to be thrown into confusion and the prices of their products began to fall. On the top of this France had been extracting huge amounts of gold from the world. On the top of this the American boom sucked capital back even from the debtor countries. And on the top of all that, after prices had begun to fall in Europe and elsewhere, the security boom collapsed. It was this collapse which to my mind more than anything else caused the unparalleled fall in prices.

My object in giving you this short historical résumé is to try and convince you of what I believe, namely, that the crisis is due in the main to the lack of balance between creditor and debtor nations. The boom in the United States was due to her being too largely and too suddenly a creditor nation; it was the inflation of credit based on her gold imports that led her at first to over-lend abroad; the over-borrowing by other nations with all its consequences was due, in the case of Europe at any rate, to their being in too unbalanced a debtor position,

[167]

and both these results flowed inevitably from the war and after-war policy. It is because this is my view that I never agree with those economists and bankers who do not attribute much importance to Reparations and War Debts. Both, and particularly Reparations, profoundly accentuated an already very difficult problem. The characteristics of this period therefore, compared with the pre-war era, were the much more violent fluctuations in the movements of long-term capital from creditor to debtor nations, and short-term capital back to the creditor nations, the far greater amount, in consequence, of short-term deposits ready to be transferred at a moment's notice, and the far greater movements of gold. Since the proper working of an international monetary standard depends to my mind on the accounts between nations being balanced with only comparatively small movements of gold, it was to be expected that these developments would end in the collapse of the gold standard.

In the last two years or so the underlying development has been, I believe, that debtor and creditor countries are being forced, in the most drastic manner, to find a new equilibrium and it appears that it can only be found, not perhaps at zero, but at a much lower level of international trade. Creditor countries are being deprived of their surplus, because the debtors cannot either buy their goods or pay their debts, and debtor countries by not paying their debts or not buying imports are painfully diminishing their deficit. The task before a debtor country reminds me very much of that which has faced so many banks in all countries. Their one task in the storm was to meet their obligations. New business, existing assets, all had to be thrown overboard. The same ruthless measures had perforce to be taken by the debtor countries. Imports had to be sacrificed wholesale and, since one country's imports are the other's exports, all trade went down together and with every step in the process the pressure became ever greater.

We are moving no doubt in the direction of reaching a new equilibrium, but we seem still a long way from it and there are some big rocks ahead. The debtor countries are still unable to meet their obligations, gold is still flowing toward the United States, and international trade continues to decline.

[168]

Above all the Reparations and War Debts problems remain unsettled.

These are the circumstances in which, unfortunately, the War Debts problem has again to be discussed. It is not my purpose to deal with it here beyond pointing out that insistence on the transfer at the present of large sums must postpone equilibrium and intensify all the evils which have arisen from what I call the unbalanced debtor and creditor position. One despairs sometimes of it ever being possible to get an understanding in the minds of the public at large of the real problem. I am reminded of what Mr. J. A. Spender, a well-known English editor, told me years ago: He was traveling by train in the Middle West and discussing with a business man the War Debt problem. After a heated argument, he finally said, "Well, which is it you want? Do you want our goods or our gold? You must take one or the other." The business man replied, "We don't want either; we want your money."

Let me take for a minute the position of England. So great has been the fall in our "invisible exports", shipping freights, interest and dividends on our foreign assets, banking commissions, and so forth, that without our making any foreign loans and at our present level of imports and exports, and leaving all short-term capital movements out of account, we are, I think there is no doubt at the moment, daily running into a considerable debit on our current balance of payments. If, therefore, War Debts, which in sterling now amount to, say, £50,000,000, are to continue to be paid out of our current annual earnings, and if we exclude the method of paying you merely by shipping all our gold, we must, unless there is an immediate world improvement, find the means either by an increase of exports or a reduction in imports.

For this purpose there are, I think, only two courses open to us. One is drastic deflation, reduction of wages and all other costs, so as to depress our internal price trend, which would enable our exporters to sell more in competition with other countries, and at the same time make our market a less favorable one for imports; the other is a definite regulation and diminution of imports along the lines Germany and other countries have been forced to follow in order to maintain their currency. Or in the alternative, of course, we can sit by and

[169]

watch the depreciation of sterling. All these courses would be in my opinion very damaging to ourselves and to the world at large, not excluding the United States. Gold prices would again be forced down as they were when we went off gold; all the problems of internal indebtedness, which face you and other countries, would be accentuated. Unemployment would probably be increased everywhere and production diminished. Just at a moment when things are beginning to look up and confidence is returning, the world would receive another smashing blow. I believe it is difficult to exaggerate the dangers.

If, however, we exclude for the moment War Debts, are there any other methods by which the process toward an equilibrium can be helped?

It cannot be done to my mind by any public lending at the present time on the part of the creditor countries to the debtor countries. For one thing the investor cannot be induced to lend and for another the debtor countries are already sunk in debt. That process, it seems to me, can only begin again when we are nearer to an equilibrium and the debtors can see their way more clearly. Nor can progress toward equilibrium be made by the debtor countries trying to improve their position by further deflation so that their goods may be so cheap that they jump the tariffs of the creditor countries.

Progress can however to my mind be made if the creditor countries will lower their tariffs, or if by a rise of prices internally their market becomes more profitable to foreign importers.

In some way or other creditor countries, if they are to continue to have any export trade, must let the debtor countries live and import into their markets so that these in turn can buy the creditor's exports.

It is very difficult for a real movement toward improvement to come from the debtor countries. Their first aim must at present be to pay their way. They can continue to improve their own internal position but the improvement must be short-lived unless they are helped from outside. I think myself that your great country is the best situated to help. You are sufficiently independent of the world to be able to get going on your own account. World prices might then begin to rise,

[170]

international trade would then slowly recover, and indebtedness all over the world would be lightened. But nothing of this kind can take place if the world is again to be thrown into confusion.

I have tried in too short a space of time to deal with too big a subject and you may perhaps say that I have not dealt at all with the subject of my title, "International Monetary Problems". But that is not so. The matters I have dealt with are the real underlying influences in monetary problems. I consider a restoration of an international monetary standard—and I think it must be the gold standard—of the first importance. But that cannot be while the relations between debtor and creditor countries remain so obscure, and while the future level of gold prices is so uncertain. I believe we are still a long way from the time when England can safely tie sterling to gold again. A relationship between countries must be restored whereby the price level is more stable and whereby balances can be settled by only small movements of gold, and so that a settlement with creditor countries does not enforce constant deflation on the debtor countries. Until then we in England must do our best to maintain the internal stability of sterling and, so far as our interests permit, the stability of sterling in relation to gold currencies. The problems I have dealt with are in my view therefore the real underlying problems. We are, I hope and if politics do not prevent it, on our way to a more stable equilibrium. But a big swell at sea does not subside at once, and we have still a long way to go before we reach the stability of pre-war days.

Finally, I would state my conviction that unless the great democracies through their rulers can appreciate each other's problems and recognize that we all, even the strongest of us, sink or swim together, we may still be moving away from rather than approaching the return of prosperity.

[171]

ECONOMY IN FEDERAL GOVERNMENT

THE HON. LEWIS W. DOUGLAS
Congressman from Arizona

THE World War and its termination let loose a host of economic factors which are now becoming sharply silhouetted as contributing to if not actually causing the intensity of the present world-wide decline in commercial activity. Debts, an inevitable aftermath, have imposed heavy interest and amortization charges upon national treasuries. Pensions and other payments to World War veterans make up an almost equally heavy burden upon national incomes. But this is not all. Though, had there been no war, additional national expenditures might have been undertaken as a natural incident to technological developments and to tendencies inherent in democracies, nevertheless it is probably true that the war accelerated the expansion of budgets. It may be unfair to impose upon the war this responsibility. But whatever the cause, the naked fact remains that since the war national budgets have increased many times in size while the cost of local governments has increased, in this country at least, by an even greater amount.

This situation would have contained no great element of danger had national incomes risen with governmental costs. When, however, the commodity price level began to decline, and finally took a sudden plunge, and when as a result, and as an effect of many other factors exercising their influence coincidentally and in the same direction, national incomes declined correspondingly, then the cost of governments became and still is a matter of grave importance.

In almost every nation budgets fell out of balance—some with resounding and continuous crashes. Where no efforts or merely feeble attempts were made to bring them into equilibrium not only the governmental credit suffered but the credit of industrial agencies too became impaired. And the effects were felt not only intra but also internationally. In some instances uncontrolled inflation of currencies resulted.

[172]

The effects were cumulative, intensified and almost ruinous. They forged links in the chain binding the world to the depression.

Where substantial efforts were made to bring expenditures within revenues the emphasis more frequently than otherwise was placed upon increased taxes, new methods of deriving revenues, rather than upon curtailment of costs.

Where the methods adopted were in the form of property taxes the margin of profit, already low, was reduced or eliminated, production was curtailed, unemployment increased, consumption diminished. Another force tending to retard rather than to encourage recovery was set in motion.

Where the method adopted was in the form of sharply increased income taxes, though the effect was not so apparent, nevertheless it was evidenced in a decline in consumption, a reduction of capital available for investment in productive enterprises. There followed curtailment in production, increased unemployment, further decline in national income and further retardation of recovery. In this connection it is relevant to refer to an argument sometimes made to the effect that since we now suffer from overproduction there is no necessity for capital investments in productive enterprises and therefore there is no injurious effect to be feared from elevating income taxes to the very maximum. Without here questioning the soundness of the theory that overproduction is the cause of our ills, it is pertinent to remark that the argument is predicated on the assumption that industrial technique, manufacturing processes and human desires are static, that they do not change, that there is no necessity for either developing new and cheaper methods of production or manufacturing both new commodities and modifications of old ones. That this assumption is refuted by experience is obvious. I call attention to our experience with the automobile, the radio and the airplane.

The mere imposition of new taxes or substantially higher old ones as principal methods of bringing budgets into equilibrium, though the better course to pursue when compared with that of continuously spending beyond income, nevertheless has unfortunate effects strangely mixed with the good—the good represented by a balanced budget, the bad evidenced by a tax

[173]

burden ranging, according to the government, from 20 per cent to almost half of the total national income.

If expenditures increase as they have during the past decade and if national incomes continue to decline, it will not be long before the entire world income will be absorbed in taxes. The same result will be attained, though within a longer period, if costs follow their present trend and if national incomes remain constant. This is not an encouraging picture. History has demonstrated too frequently the serious consequences of heavy tax burdens for us to lightly pass over, to ignore those now imposed.

It is therefore at this point that economy in government assumes a position of importance, not only in and of itself but also as the method upon which emphasis should be placed in restoring the balance between governmental expenditures and revenues.

But there is another reason for the importance of retrenchment. If the diversion of too large a portion of national incomes to meet the expenditures of government is an influence retarding recovery, it not necessarily but in all reasonable probability follows that a reduction in the amount so diverted will at least lay a firmer foundation for economic revival.

How is this foundation to be laid? An examination of national budgets discloses two general categories of expenditures. In the first is to be found those which have to do—(1) with unemployment insurance funds or in their absence with unemployment relief; (2) with expenditures for the general social welfare such as for example, education; (3) with payments to veterans of past wars; (4) with aids to industry, commerce and agriculture; (5) with the police force; (6) with the construction of public works.

Though the extent to which these items absorb national incomes and throw budgets out of balance has an important bearing upon the credit of a given government and therefore is not purely domestic in effect, nevertheless a reduction in them is a matter of purely municipal action.

That substantial reductions in our federal budget can be effected is made clear by an examination of these expenditures. Within the items listed as aids to industry, commerce and agriculture there are to be found large sums devoted to

futile attempts to lift off the market surplus agricultural crops and almost equally large items designed to increase the production per acre; important items for the purpose of encouraging a foreign trade made impossible elsewhere in the statutes by a tariff law that is almost an embargo. Within the field of public works there are items for the construction of great arterial public highways to be used by competitors of the railroads to whose assistance the government has already come and in the future may be compelled to come, to a greater extent, in order to preserve a part of our financial structure. And within the same field there are items for the construction of at least one great project designed to increase the arable acreages and surplus agricultural crops for the attempted disposal of which in another field large sums are expended. These few examples are indicative of the amazing inconsistencies to be found in our budget. In some measure they contradict, nullify one another.

But there is another reason for holding firmly to the belief that economy can be accomplished. Only 25 per cent of our budget goes to service the public debt. The remainder or 75 per cent is clearly susceptible to reductions. Within that 75 per cent there are such items as payments to veterans and the administration of a Veterans' Bureau. But there is no reason why either the administration of that bureau or compensation and pensions must be considered to be so sacred that to them there may not be applied a horizontal reduction or the elimination of obvious and patent inequities. And within that same 75 per cent of the budget there are items for the national defense. Here too, in the absence of an international agreement limiting armaments, smaller economies can be effected through increased efficiencies. And after disposing of these two substantial items amounting to approximately 42 per cent of the budget there remains another 33 per cent devoted to various activities all susceptible of substantial reductions or even elimination. One of the most important is that having to do directly and indirectly with prohibition. Surely then it cannot be successfully maintained that with only one quarter of the budget absorbed in literally fixed charges the expenditures included in the remaining three quarters cannot be reduced. On the contrary this statement

coupled with the examples here given of extraordinary inconsistencies demonstrates that large curtailments can be attained.

Yet whenever an attempt is made to reduce the inconsistencies, to eliminate obviously useless expenditures, there is encountered a stubborn resistance on the part of the bureaus and bureaucrats, a political defense so well entrenched and so well fortified that it is justifiable to speculate on the question, have the "servants become the masters". And when there is added to the power of the bureaucrats that of the groups and organizations opposed to retrenchment in items in which they have a particular interest, the attainment of the objective becomes a matter of great difficulty requiring an equally great firmness and resoluteness of purpose.

The accomplishment of the task requires then as the first pre-requisite a fixed unalterable determination to succeed, "a will to do". And this determination must inspire not only the legislative but also the chief executive, for the legislative legislates on the recommendations, among which is the budget, submitted by the president.

But in addition there must be made by a competent non-political group a comprehensive impartial analysis of the items included in the budget, an evaluation of their purposes, a determination of the extent to which they are contradicted by other items. In short the whole field of governmental expenditures, the hit-or-miss result of hit-or-miss political acts, neither synchronous in point of time nor coherent in design, must be completely studied, valued and reconstructed in one complete and consistent plan harmonizing present needs with present abilities to pay.¹

¹ My meaning can best be demonstrated by an example. During the last half of the last century there was passed by Congress an act making mandatory the appropriation of certain sums of money for the encouragement of agriculture, for the purpose of increasing the per acre production. The act was passed at a time when there may have been a need for such an appropriation. The appropriation is still carried every year in our budget. As I say, the appropriation was made mandatory by the act. Now how does that appropriation fit in with our present requirements? In view of the surplus in wheat, in cotton, in apples, in oranges, in almost every agricultural product, how can it be maintained that there is today a necessity for devoting a part of our national income to increasing those surpluses? And yet, unless

This investigation must include not only the items carried in annual appropriation bills but also the acts authorizing them. It must likewise examine into what are known as permanent appropriations.

To accomplish the task it may be necessary for Congress to discard its traditional policy of appropriating for each item and to grant reduced lump-sum appropriations for each department, relying upon the departmental head to distribute the funds in accordance with needs.

And finally—and upon this probably the success of the program rests—Congress must be supported by a swell of public opinion not only for reduction in annual appropriations but also for the revision and in some cases repeal of authorization acts and permanent grants.

Into the second category of national expenditures there are to be found items which have to do (1) with debts, interest and sinking fund requirements and (2) with armaments. It would be beyond the scope of this paper to engage in a discussion of intergovernmental obligations. It is, however, relevant here to discuss briefly the item of national armaments. In almost every budget they absorb a substantial percentage of the national income. Few if any of the great powers will make material reductions in their national defense programs in the absence of a commitment on the part of the other powers to do likewise. If budgets and peoples are to be relieved of a substantial portion of the crushing burden of the cost of armies and navies it must be through international agreement. The spirit of nationalism makes this the only course to pursue.

It seems clear, then, that both international agreement and intra-national retrenchment are necessary if we are to have a sound governmental economy. More and more as this depression runs its bitter course there is dawning on the minds of men the conception that the decline in economic activity is due to a group of worldwide causes and that if there is to be permanent recovery the remedies must be equal in scope to the causes.

that act and its amendatory acts, now made obsolete by present conditions, are repealed, that appropriation must still be made by Congress.

ECONOMY IN STATE AND CITY GOVERNMENT

THE HON. GEORGE MCANENY

Former President of the Borough of Manhattan; former Acting Mayor of New York City; former Executive Manager of *The New York Times*

THE growth in the cost of state and local government during the sixteen years since the beginning of the war, and in the consequent burden of taxation, has been unquestionably one of the most disturbing developments in the post-war economic situation. The figures, in millions, based upon ten-year intervals, so adjusted as to take in the year 1913, the year immediately preceding the war, are as follows:

GOVERNMENT EXPENDITURES (in millions of dollars)				
Expenditure	1903	1913	1923	1929-1930
National	475	692	3885	3932
State	182	383	1242	1990
Local	913	1844	4793	7126
Total	1570	2919	9920	13048

The proportion of this sum raised through taxation has in each case been not far from the total, running in 1913 for all three classes to \$2,187,000,000; in 1923 to \$7,234,000,000; and in 1929 to \$10,251,000,000.

The margins between these figures and those for total expenditures represent, of course, money raised upon credit through the issue of the securities of the various taxing units involved. But it is the item of taxation that pinches closely and nowhere so closely as in the municipalities. It is here that taxation gets down closely to a man's home, to his costs of living, within his town. The total tax burden amounted to \$22 per capita in 1913 for all purposes, to \$64 ten years later, in 1923, and to \$83 in 1929. Taxes for municipal purposes, coming back again to my immediate theme, were \$12 per capita in 1913, \$29 in 1923, and \$41 in 1929. This means that the total cost of taxation borne by the average

[178]

American family for the year 1929, as figured by the National Industrial Conference Board (accepted, I think, as the clearest and most reliable authority), was \$416.

In New York City, which I cite as a convenient example for various points, the figure is considerably higher. The per capita cost of local government alone, in New York City, both in 1931 and 1932, was approximately \$100, the peak of all the cities of the land. After allowing the average of \$41 cited for *all* municipalities in the United States, there would be, therefore, an excess of \$59 per capita still to be taken into account in the case of New York. This, averaging four to a family (the basis of Federal computation), would mean an additional charge of \$236, or a total annual family cost for taxation of all classes (direct and indirect), in New York City, of \$652.

The bonded indebtedness of the Federal government in 1913 was 1,000 million dollars; that of the states, 300; and that of the municipalities, 2,900; a total of 4,200 millions. By 1929 the aggregate debt had grown to 30,000 millions, a large part of which, of course, is the residue of the national war debt. The municipal indebtedness had, however, in the sixteen years intervening since 1913, more than doubled, rising to 6,300 million dollars.

These astonishing increases are frequently credited—or at least chiefly credited—to the mere following of the “pace” set by the war. In the national government, however, the volume of annual expenditure had at least reached a maximum level three or four years ago, and has now set in toward reduction. In the states and cities the upward growth has continued, without any substantial interruption; although in a number of cities during the past year compulsory retrenchment has commenced to produce signs of difference.

Beyond the acceleration of war expenditure, the increases in the states and cities may be attributed to the assumption of new and more varied public functions; broader provisions for both higher and common school education; the increasing necessity of public provision for unemployment relief; the wide growth of investment in highways for the accommodation of increasing motor traffic; and to the inauguration of vast schemes for public works of every other description, encour-

[179]

aged, during the years prior to 1929, by the general feeling of prosperity; with corresponding additions in annual cost budgets to meet interest and amortization charges upon bonds issued to provide for them. Other contributing causes have been the natural increases in costs of both labor and material during the war and earlier post-war years; wide increases in rates of salaries paid, rates that it has been exceedingly difficult to restore to old levels since the years of depression set in; the alarming increase of political pressure for the creation of new positions and jobs of every description, and — with comparatively few exceptions — culpably loose methods in city budget making.

Whatever the causes, the results of the tidal wave of increased spending and increased taxation have been disastrous. Coincidentally with advances in the amount of taxes collected, private property values have gone sweepingly down; in a multitude of instances the pressure of taxation alone is hastening foreclosures or other liquidations. With the disappearance of equities, current taxation has often amounted to a total confiscation of investment values, taking on, in this respect, the nature of a capital tax. Notwithstanding the force of the pressure for prompt tax payments, exerted by the cities themselves, or by the holders of mortgages, the ratio of taxes collected in many cities has seriously decreased. Municipal credits have been impaired, and a vicious circle thus established, resulting in lessened business vitality and arrested growth, among the cities, upon a scale previously unknown to the passing generation.

Chicago perhaps holds the first place in the experience of practical disaster. The failure of that city to meet interest and sinking-fund charges upon its securities, or to collect its taxes, has resulted in an amazing state of economic anarchy and of individual distress. Fall River, Mass., defaulting in its interest payments, has been taken over by a Finance Commission appointed by the governor of the state. There are many similar instances.

Unquestionably the difficulty with local taxation in America is further complicated by the multiplicity of taxing units. The forty-eight states are divided into many counties — in some states over one hundred. In addition to taxes paid

[180]

directly and indirectly to the Federal government, there are state taxes and county taxes, taxes for city purposes, for school districts, sanitary districts, and so on. It is the sum total of these various payments that is represented in the figures and the ratios I have cited.

With all that has been said and done in the effort to swing the country around to a better comprehension of its economic condition, it cannot be said that much headway has as yet been made in changing the spending practices of the states and cities. There are many of the services paid for through the new taxation that cannot be reduced materially, or at least rapidly; some cannot be cut at all. It is clear that in whatever programs of retrenchment may be developed, there can be no denial of adequate appropriations for established needs, whether economic or social. All of this must be taken into account in campaigns for cutting downward.

There remains, however, an abundance of opportunity for drastic retrenchment in annual operating costs; and for greater economy, as well, in the matter of capital outlays. Among other things requisite, there should be:

(a) The setting up in each city, where it does not already exist, of up-to-date and approved budget-making machinery, and the limiting of future appropriations to the necessities of the city's life, always keeping in mind the fact that proper social and educational enterprises should be viewed as necessities. Particularly, under this heading, the reduction of salary schedules to the figures prevailing before the abnormal upward tendencies of the so-called "peak" years, and the cutting out of all luxuries of service and of non-essential departmental costs of every description.

(b) The limiting of capital investment also to actual need; the completion, as a matter of course, of all public works already under construction, or essential to healthy city growth; but the deferment, as a rule, of all others.

(c) The development of new sources of city revenues, particularly the adoption of policies under which all charges for transit service, for water supply, or for other public utilities conducted by the municipality, shall be self-supporting and self-liquidating.

[181]

(d) The development of new forms of local taxation. The present practice under which the major burden of taxation is laid, in the first instance, upon real property, results undoubtedly in a great deal of inequality in the assessment of municipal costs, and in consequent injustice. This subject is a broad one; but there is little disagreement as to the need for the substitution of occupational, residential and even poll taxes—in appropriate degree—for the taxes on real property.

The strongest support for the argument that there should be more direct taxation, and less indirect taxation, in the cities, lies in the fact that under the present system, the majority of voters who do not pay a direct tax of any sort, cherish the notion that they pay no taxes at all; that there is nothing, consequently, in the question as to whether city taxes shall be high or low that directly affects their individual interest; and that they may therefore continue to vote, in city elections, without reference to questions of economy; but rather upon questions of so-called city "politics".

In New York, for instance, while there were 2,400,000 registered as qualified to vote at the late election, the number of tax bills annually sent out is 800,000, and probably one-half of these are repetitious; that is, served either upon corporations, or upon non-residents, or upon individuals holding a number of separate taxable parcels. In the case of the Federal government, where the burden of taxation is also either indirect, or based upon a graduated income tax that affects directly only a minor group of the voters, the same misconceptions prevail.

In addition to the reformation of taxing and of budget-making methods, the broader reforms, essential to the attainment of better and less costly municipal government, in my judgment, include:

(a) The complete separation of national from local politics in the nomination and choice of mayors, Council members and other elective city offices;

(b) The extension of the civil service laws to include, through some process or other, the highest administrative officers and their deputies, thus minimizing the opportunities for the misuse of the higher offices for partisan political services;

[182]

(c) The adoption of better and more up-to-date forms of charter legislation; the elimination of useless departments or other administrative agencies, the consolidation of others, and the simplification of governmental methods wherever practicable;

(d) Consideration, at least, of the wisdom of establishing the rule of proportional representation in filling elective offices—a plan that has worked admirably in Cincinnati and gone far to put that city in the foreground of the better governed cities of the country.

The government of the State of New York is at the present moment facing huge deficits, and every attention is being given to methods either for cutting expenses there or for establishing new sources of revenue. The State Income Tax rate has already been doubled—under legislation of last spring—in order to provide more ample allowances for public relief. An Advisory Budgetary Commission appointed by the governor will shortly report upon further measures to be taken.

New York City in the meantime, with its power, within certain constitutional limits, to tax property within its borders to whatever figure may be necessary to offset its budget, continues as the outstanding example of what the habits of municipal waste and extravagance engendered during the past several years mean to taxpayers of every class.

The consolidation of the various cities and other municipalities constituting what is now the Greater New York, was effected in 1898. Two years later, in 1900, the city budget, covering not only all departmental needs and outlays but both interest and sinking fund payments upon the consolidated city debt, amounted to \$92,500,000, or \$26.88 per capita. The figures since have been as follows:

1910	\$163,130,000
1920	273,690,000
1929	565,000,000
1932	631,000,000

All of these figures are augmented by certain payments made to the city annually, on account of the educational service, by

[183]

the state. For 1932, these payments and certain other revenues spent outside the budget, bring the actual total to a few thousands short of \$700,000,000, and the per capita charge, therefore—based on the census figures of 1930—to a trifle over \$100.

The budget figures since 1926 have included annually increasing allowances applied toward meeting the huge capital costs of building the city's new so-called "Independent" subway system, the ultimate total cost of which will be in the neighborhood of \$850,000,000. In the budget for 1932, the quota so charged to taxation—not for operation, but for construction and equipment—amounts to \$75,000,000.

Attending the making of the budget for 1933, there has been more public investigation and more public discussion than has occurred for many years past—led by the Citizens' Budget Commission, a privately-organized body of citizens representing various sections of the city's industrial life, and employing a body of expert investigators and advisers.

Notwithstanding this broad campaign for economy, the city's budget for 1933 has been cut only through the elimination of \$55,000,000 for subway charges, accomplished through a change in the terms and consequent amortization needs of some of the bonds issued for construction, and through other "bookkeeping" savings, and through the elimination of only \$19,000,000 from the departmental costs. The campaign for further cutting continues, however, and the issue will no doubt be a tense one throughout the year 1933.

In the six years from 1926 to 1932 the number of employees on New York City's payroll rose from 116,000 to 148,000, an increase of 32,000, and the payroll itself rose from \$248,000,000 annually, to \$368,000,000, an increase of \$120,000,000, or 48 per cent. During the same period the population of the city increased 19.7 per cent.

Offsetting the claim frequently heard that the major part in the increase in municipal expenditure is attributable to the assumption of new functions and to the natural expansion of others, lies the fact that in the New York City Police Department, for instance, during the six years in question, with only 19 per cent more population to take care of, and notwithstanding an actual decline in the number of felonies com-

[184]

mitted, and but slight increases in other statistics of police activity, the cost rose 61 per cent.

In the Department of Education, although the census of pupils enrolled increased but 8.5 per cent, the cost increased 38 per cent. In 1929 a combination of various departments and bureaus brought into existence the Department of Sanitation, justified largely upon the score of better opportunity for economy. The payroll costs here rose, nevertheless, from \$33,000,000 in 1929, to \$39,878,000 in 1932.

It was in the Department of Sanitation, by the way, that the investigators of the Citizens' Budget Commission found, among other costs carried from year to year, an item of something like \$830,000 for the care and upkeep of horses owned by the Department; for hostlers and stablemen, and farriers and veterinarians and whatnot. It was found that there were 260 horses still in the sanitary service, the residue after motorization of equipment had been carried practically to completion. But a recent physical examination conducted by the S.P.C.A. disclosed that only 20 of these were fit for service, and that as these 20 and the 240 invalids cost \$830,000 a year, the annual bill was \$41,500 apiece for the able-bodied ones. The force of employees belonging to the days of the horse had, in short, been carried, after the horses had gone, without substantial reduction, and for the simple reason that the powers that be would not let the Department drop them. This condition seems incomprehensible; but it has been only with the framing of the 1933 budget that it has been changed.

So one might go on. What I say of New York you all know is but too typical of most of the cities of the land, and the time for correction is certainly upon us. We have reached the point where the old order will not do, and the old excuses no longer hold water. We have reached the point where excessive taxation drawn by the cities from their people is bringing about, as I have put it, the practical confiscation of the property values and the conversion of budgetary taxation into capital taxation.

Fortunately, as we have reached the last point of endurance, we have also reached the point at which the demand for drastic retrenchment and the subjection of city government, in particular, to the rules and standards of private business

[185]

administration, is supported throughout the country by an aroused public opinion.

A further note of encouragement may be found in the increasing insistence on the part of the banking interests of the country upon the reduction of budgets and the adoption of business methods as conditions of further municipal loans. Too many people have the idea that the bankers are men who have cellars filled with gold that they have only to shovel up and put at the disposal of those who want it, provided their onerous terms may be met. In New York, where this phase of the crisis is acute, we even hear cries now and then about the "oppression" of the bankers. Actually, the bankers are commission merchants for the sale to their customers of the issues of city securities or of those of the utilities or of any other form of corporate enterprise, at such prices as their customers are willing to bid; and bids are based upon the faith of the bidders in the complete solvency and the correct business methods of those who want to borrow.

The City of New York, in its borrowing, has two kinds of credit to be taken into account. There is the long term credit that underlies bonds put out for capital improvements, amortized over a long period of years, and there is the short term credit upon which temporary and intermediate financing must be based. The City of New York, like many another, spends its tax moneys, for the most part, in advance of their collection. Its collections in any given year are payable on the first of May and on the first of November. But the need for money for running expenses commences on the first of January. When the first of January arrives, the collections of November have been pretty well spent, and to cover the period before the May collection date, the city must borrow on revenue notes issued in anticipation of collection. New York, collecting something over \$500,000,000 of taxes last year, had to borrow during the year, over graduated terms, something over \$400,000,000 to cover these interim periods, carrying interest charges running toward \$10,000,000, also to be paid.

Much has been said about the way in which New York City's credit has recently been driven. It is in the second class of borrowing, however, that most of the difficulty has occurred. What with the swollen scale of spending, indicated by such

[186]

annual budget figures as I have cited, and, on the other hand, severe reductions in the volume of tax collections, due to the present condition of real estate, the ability of the city to redeem promptly its short term notes has naturally affected the short term borrowing market. Such a condition sets in motion at least a tremor of fear and doubt, even among those who know that the City of New York itself is impregnable, and that its credit is impregnable.

In this situation, the insistence of the bankers that the budget of the City of New York be cut much more unsparingly than has as yet been attempted, is easy to understand. In the attitude they have shown, and in the course they have followed, they have, in my humble judgment, proved themselves not only bankers and industrial leaders, but also exemplars of a useful kind of citizenship. In the long run the city will profit greatly through their present intervention in its fiscal affairs.

Might I, as another encouraging sign of the times, mention the progress that has been made throughout the country in the establishment of City Planning Commissions and the adoption of modern and scientific methods of planning city growth. There has been a great advance, as the need of more businesslike administration has developed, in the spread of what might be termed "planning-consciousness". The cities are accepting the truth that not only must their physical construction and their industrial and social growth be planned well ahead and along definite lines, but that their capital investment in public improvements must be shaped with every possible future economy in view. We have in this respect, also, the good example offered by the Federal government through the program of its Federal Employment Stabilization Board. We have the fine example of many cities, as well, particularly of Chicago, the construction of which along the lines of the monumental "Burnham Plan", adopted twenty years ago, has been impressive. Here, in the East, we have the more recent instance of the development of the Regional Plan of New York, upon the preparation of which a million and a half of Foundation and other private funds have already been expended, and which has been put at the disposal of the public authorities as a measure of guidance of the future growth, not only of the city itself, but of the entire metropolitan area.

[187]

There are many other encouraging indications throughout the land. Antiquated or outgrown city charters are making way for better structural forms of government. Upon that subject, New York, if I may again refer to it, is becoming greatly stirred. While better forms of government, whether here or elsewhere, can be expected to reduce the volume of public expenditure in but slight degree, unless the element of political interference is also reduced, it seems likely that important progress at least may be expected along these lines. The demand for closer budgetary control and for the sort of retrenchment that will contribute to the immediate relief of a tax-burdened people, remains the most significant of all. Certainly forces have been set in motion that may be expected to carry us far in the direction of correct municipal policy.

It should never be forgotten, however, that the degree of improvement and relief we shall reach must depend not only upon a modified attitude of those who direct our local governments, but upon a more intelligent and a more insistent participation in passing public affairs on the part of the individual citizen and voter.

[188]

DISCUSSION: MONETARY AND FISCAL POLICIES ¹

MR. ALEXANDER DANA NOYES (Financial Editor of *The New York Times*): This is not the first of great depressions. It is probably not the worst of great depressions. Looking back at periods of this kind, we may point out that a prolonged and severe business depression may have its uses, which very often will not be appreciated or understood until the depression has gone. After previous depressions we always have realized, as in the future we shall realize regarding this period, that the policy of public and private economy has been forced upon the community, that the habit of public and private extravagance has been forcefully corrected, and that evils in our body politic and particularly in our economic system have been corrected.

If it were not true that these problems had been both recognized and corrected, how could we explain the fact embodied in all economic history, that a period of great depression was invariably followed by a period of great prosperity? It did not come immediately. Usually it came slowly. If the possibility of such recovery is denied, as I imagine it always was denied in periods of this sort, then what becomes of the theory of economic cycles underlying economic history?

It is in every way fortunate that the new and urgent problems which beset us in so trying an economic era as this in which we are now living, should be discussed with an open mind and with clear recognition of the worst facts by such gatherings as this. It is fortunate that the gravity of these problems is so plainly recognized. The result of such recognition, accompanied by enlightened action, cannot fail to be of the highest benefit to the economic world and to the future of mankind.

Still, there exists at least the possibility, especially with those of us who are tempted sometimes to call these economic problems insoluble, that we may forget how largely the disturbing facts and the discouraging events are themselves the result of the great economic reaction since 1929, which was itself mainly the result of one of the most destructive wars in history. This fact should at least put us somewhat on our guard against assuming that all of these problems, and the particular shape which each of them has assumed, result from a basic and permanent change in the economic structure.

¹ Discussion under the ten minute rule.

Nearly four years ago a selected body of experienced economists and men of affairs, known as the President's Committee on Economic Changes, published an exhaustive report covering these very problems. Their conclusion, as set forth in the early part of 1929, was in general that the problems were largely new and extremely trying, but that the development of human resources, economic knowledge, and the new attitude in the conduct of our industrial affairs promised to smooth the way for the economic future. Even severe economic reaction and depression, in the view of this committee, was likely to be less and less probable as the years passed.

These findings may have been wrong, they may have reflected the economic illusions of the period, but my only purpose in referring to them is this: to suggest that we be careful now lest our present conclusions take their color from the depression of today as they might have done after 1893 and 1873, and as the conclusions of 1929 probably took their color from the seemingly irresistible prosperity of that day.

This seems to me especially applicable to what, after all, is our immediate subject, the monetary and fiscal policies of the period. The past has taught us that such a period of economic change sometimes proves old policies to be erroneous, but it quite as often indicates the need of adapting old and sound policies to the new requirements of the day. It is in that direction, combined with our attack on the extravagant outgrowths of unsound practices, that I believe the solutions of our present problems are to be found.

MR. ROBERT B. WARREN (formerly with the Federal Reserve Bank of New York, now with Case, Pomeroy and Company): In his paper on banking Mr. Jay emphasized the fact that we have in this country a dual banking system. We very narrowly missed having a unified banking system, this year; at least it is my own conviction that if it had not been for the Reconstruction Finance Corporation, virtually every non-member bank would have been closed by now.

If you examine the statement of total loans to banks by the Reconstruction Finance Corporation and set against it the very small amount of discounts and bills payable of the national banks on the last call date, you infer that the non-member banks have been responsible for the heavy borrowing from the Reconstruction Finance Corporation. In other words, we have not only a dual banking system, but a dual central banking system with the Reconstruction Finance Corporation acting to some extent as a Federal Reserve Bank for the non-member banks.

Mr. Jay has outlined the inevitable conclusion of our present dual banking system. I think that we shall move and probably move

[190]

rapidly, in the direction of branch banking, yet I am not sure that the transition from unit banking to branch banking can be made smoothly merely by passing a law to permit the establishment of branches within some designated limit. A fundamental innovation in banking, of such far-reaching character, can hardly be instituted without creating certain new problems in the process of solving the old. I am not at all sure that the general establishment of branches would not result in a very disturbing shift of deposits from the old banks to the new branches. Generally speaking, people desire to keep their money in a large bank. In some of the small communities of which I have a personal knowledge, the establishment of branches of a larger bank would lead to a shifting of deposits from smaller local banks.

I am not sure how serious the disturbance would be. Probably it would be local and spotty. Nevertheless we must remember (and the history of the past year illustrates this fact) that deflation is caused not merely by a contraction in the total of deposits, but also by the shifting of deposits, because the placements of the new institution do not necessarily replace the loans previously curtailed by the old institution. I don't say this as an opponent of branch banking. My intention is merely to venture a suggestion that the transition from unit to branch banking is something more intricate than the granting of legal permission to establish the branches.

Secondly, I am not persuaded that we should make so fundamental a transition in the direction of establishing very large institutions until by law or practice the relation of banks to the security market has been better defined. I am sure that this feeling is responsible for a certain amount of the disinterested opposition to the extension of branch banking. Fear is felt in some quarters that a further magnifying of great financial institutions, far more interested in some instances in the selling of securities either new or old than in the financing of business enterprise, would create very serious social or financial dangers.

In regard to the paper of our distinguished visitor, Mr. Brand, I have but one question to raise. Mr. Brand mentioned among the extremely disturbing influences in world economy the fact that creditor nations won't stay creditors, and debtor nations don't seem to be able to stay debtors; they keep changing their relative positions. My question is whether today we know who are the creditor nations and who are the debtor nations. In 1929 we computed our foreign assets at \$25,000,000,000, but when one estimates the present value of those assets in terms of current annual remittances, I am not sure at this moment that the United States is not rapidly becoming a debtor nation once again.

[191]

Finally, in regard to the paper of Dr. Chandler: Dr. Chandler has given an excellent discussion of the financial and banking history of the last year, including his reference to what I think was one of the boldest and most successful experiments in central banking ever undertaken, that is, the famous open market operation of the spring of this year. But I question seriously whether the collateral effects of that operation have not introduced certain new problems which might invite some modification of the present policy.

In the process of relieving strain, it was necessary for the Reserve Banks to go very heavily into the market for short term governments. That was a matter over which they had virtually no choice, once the policy had been determined upon. This intensive buying by the Reserve Banks and the creation of excess reserves have tended to force a great concentration of credit in the only area which is now considered credit-worthy, that is, the short term obligations of the United States Treasury. Interest rates on short term credits were driven virtually to zero, in fact we have had the unique experience of seeing one of them selling at an interest rate of minus four per cent. We have now got an anomalous money market, coincident with a very low velocity of bank deposits and a very great amount of hoarding in high denomination currency. I raise the question whether there are not some advantages to be gained at the present time by an operation of the Reserve Banks tending to raise the level of short money rates. I raise the question as to whether the present level of short money rates, rather than being a stimulant to business, is not possibly an actual deterrent to the extension of credit to private and corporate enterprise.

DR. THOMAS S. ADAMS (Professor of Political Economy, Yale University): I will confine what I have to say to the subject of public economy and I shall, I fear, at least in the beginning, lay something of a wet blanket upon our hopes and ideals.

I have been interested in this subject, reasonably faithful to its study and execution, for a period of thirty-five years. I suppose I have belonged to at least fifty committees on the reduction of taxes and public expenditures, and I have attended between five hundred and one thousand meetings of this general kind at which everybody was zealous to reduce public expenditures and taxes and almost everybody, including myself, optimistic. I can see very little net result of all those meetings, hopes and expectations. For that very reason it seems worth while to outline a few of the conditions which must be fulfilled if we are to have a more fortunate experience in the future than we have had in the past in this effort to reduce taxes and public expenditures.

[192]

First of all, lest my position be misconstrued, I agree with everything Congressman Douglas said, particularly with his main conclusion that the reduction of public expenditures is primarily a work for will, an exercise of power, and is not to be solved by college professors or even by meetings of this kind. You will get nowhere if you do not bring to bear on this subject every legitimate power that you can possibly exercise. I am speaking with reference to state and local expenditures and taxes, as well as Federal taxes. The first condition of success here is that you appreciate the gravity and seriousness of the task. It is to emphasize this aspect of the matter that I am speaking as I now speak.

In the second place I have very little expectation of any permanent or worthwhile result from either public meetings or ephemeral organizations. There come periods, to be sure, as after the Crimean War, in England, or after the Civil War, in parts of this country, when bursts of popular irritation or the cessation of some peculiar emergency may permit a reduction of expenditures and taxes in particular branches of government. Public debt was reduced generally in this country, say from 1875 to 1890. State taxes for five or six years in the State of New York, for instance, were reduced throughout that period. City taxes were reduced for a short period. But by and large the savings made in one variety or branch of government are sopped up by other branches of government and, in general, economies accomplished in one department are absorbed and more than absorbed by new expenditures in other fields.

Unless we have some sort of permanent organization, manned and directed by experts, coming to know in the long run at least as much as the public authorities know about the details of public expenditures, and continuously on the job, there is, in my belief, little hope of success.

Some of the reasons may be given. As Congressman Douglas suggested, if you are to make a serious dent on the volume of expenditures and taxes, you have got to attack on lines of policy and change decisions of policy. Mere economy and efficiency, while infinitely worth while in themselves, do not in any material degree affect the tax burden or the total budget. If you want greatly to reduce public expenditures, you have got to convince this country in some way that we are spending too much for veterans, or for the public schools, or for the army and navy, or for the maintenance of roads. If there is to be a material reduction, you have got to cease spending so much money upon pensions, upon the hospitalization of veterans and the dependents of veterans; and you have got to cease spending so much money upon the public schools (and, in my personal opinion, you could reduce the expenditures on the public

[193]

schools without grave injury); you have got to stop spending money on the highways and possibly upon Reconstruction Finance Corporations. In other words, you have got to do without things that you want and that are good in themselves.

In the next place, I am convinced (and in this opinion I am in harmony with the best students of the subject that I know, public or private) reduction of public expenditures eventually will require very extensive reorganization of the machinery of American government. It is almost as bad as the machinery of American banking.

Finally, you have got to have extensive reorganization among yourselves, because the very people who sit here and applaud speakers who say public expenditures can and will be reduced, on the show-down, when it comes to particular expenditures, are more likely than not to exert an influence in favor of keeping and not reducing those expenditures, and Congressmen know it.

Finally, one last point. The American tax system has become, in a degree which was unknown twenty-five years ago, a system of class taxing. It is not wholly true but it is predominantly true that the great mass of the beneficiaries of government expenditures are not taxpayers in any important and conscious sense. The legislator, who in the long run reflects volume and preponderance of votes, no longer reflects volume and preponderance of taxpayers. I should like to pursue that topic because it is not absolutely apparent, but it is broadly true.

All this means that you have got to have a national taxpayers' organization, supported by liberal contributions, carried on in a broadminded spirit, but animated by insistent zeal, manned by experts, who in a few years will know or who do now know more than the legislative bodies before which they will appear, about the details of appropriations and expenditures.

It must be a taxpayers' association because political leaders no longer represent taxpayers' interests adequately; they represent voters' interests, an entirely distinct and different thing.

Sixteen years ago, in this very room, I read this statement:

"The continual increase of public expenditures is one of the most irritating, fascinating, and mysterious of social phenomena. It is irritating because it implies a corresponding increase of taxation. It is fascinating because apparently it cannot be checked. It is mysterious because we do not in any general and fundamental way know why it cannot be checked. Regularly after paying the taxes the indignant taxpayer insists that it must be stopped, and regularly before elections aspiring statesmen tell him that it can be stopped, but it is not stopped.

"It characterizes democracies as well as less popular governments.

[194]

It is particularly marked just after a democratic has succeeded a monarchical form of government. It seems to partake of the resistlessness of an elemental form of nature; indeed, one of the sanest and most erudite economists has formulated the fact as an invariable economic law.

"Public expenditures seem to thrive on opposition—here is the element of mystery. They make their way in the very face of one of the most powerful forces known to history; the unceasing opposition of the taxpayer. His resentment has uprooted dynasties, overthrown administration after administration, and generated innumerable upheavals upon which opposition parties have ridden into power pledged to 'retrenchment and reform'. But the politician who is put into office to reduce taxes is frequently thrown out for increasing them. Occasionally, the tide is temporarily stemmed in one department of government, but the saving is soon sopped up by another branch and, surveying all divisions of government, the majestic march of costs goes on undisturbed."

And I went on to marshal the devices for tax reduction, in my usual optimistic way, and I hoped that the picture would soon be changed. But that description written sixteen years ago is even truer today than when it was written.

We must not give up the fight. Let's fight a little more intelligently, with more comprehension of what we are up against, and with the kind of machinery, organization and attack which alone can prove successful.

[195]

INTRODUCTORY REMARKS¹

JACKSON E. REYNOLDS

President of the First National Bank of the City of New York;
Vice-President of the Academy of Political Science

CHAIRMAN REYNOLDS: Perhaps as erudite an audience as this has never attended the "Chauve Souris," but if they have, they remember Balliat, and that is my rôle in this performance, to introduce the acts.

The subject of the program this afternoon is "Major Problems of Readjustment," and the first to be considered is "The Railroad Problem." I have unusual satisfaction in presenting the first speaker, who has been in the railroad world for thirty years or more and whom I have known since we were young men. We were both then counsel of railroads; he was a law professor at Yale and I at Columbia. I don't know of anyone who can discuss this first problem better than he.

As a Yale professor he attained a philosophical point of view and as Counsel, and Vice President, and President, and finally Chairman of the Board of the New Haven Railroad he has a highly practical view. Before the rest of the country had to address itself to the problems of taxation, and grade-crossing elimination, and legislation, and consolidation, and competition of highways and waterways, Mr. Buckland, on the New Haven, had to face those problems. He was a master of them before the others became novices.

¹ Mr. Reynolds was the presiding officer at the Afternoon Session.—Ed.
[196]

THE RAILROAD PROBLEM

EDWARD GRANT BUCKLAND

President of The Railroad Credit Corporation; Chairman of the Board
of the N. Y., N. H. and Hartford Railroad Company;
former Professor of Law, Yale University

THERE are three kinds of problems now confronting the American railroads. One might be termed an emergency problem, the second is temporary; the third, a continuing problem. For convenience of presentation, we may consider the temporary and continuing problems first, and then discuss the emergency.

The temporary problem arises because of the prevailing depression in business. The present financial condition of the railroads is due in large part to this depression, and will be relieved as and when normal business returns.

The solution of the temporary problem will by no means dispose of the continuing problem, which is:—how to maintain and operate a system of railways prepared at all times to handle promptly all the traffic which may be offered; how to give to the owners an opportunity to earn enough to maintain their properties and equipment in such a state of efficiency that they can carry this burden well; how to secure a fair return upon the value of the property devoted to the service; how to stabilize their credit so that in times of depression as well as in times of normal business their securities will be safe investments for savings banks, life insurance companies and trust funds in general.

This continuing problem will not be solved by a return to normal business and yet it should be solved. Its solution may be accomplished if, among other things, the railroads are relieved of: (a) excessive taxation and subsidized competition; (b) over-regulation of themselves and under-regulation of their competitors.

Excessive Taxation and Subsidized Competition

As regards excessive taxation, the railroad suffers in common with the over-taxed public. The general taxpayers

[197]

today are properly insisting upon stopping unnecessary expenditures and reducing taxation. The railroads join with them and add their special protest against general taxation for the subsidizing of their competitors who, without subsidy, could not compete.

A few specific instances will illustrate. Hearings are currently being held by the Senate Committee on Foreign Affairs to consider ratification of a treaty with Canada for the construction and maintenance of the St. Lawrence waterway. If the railroads with which this projected waterway will compete were freed from taxes which they now pay, as this waterway will be free, these same rail carriers could move all the grain they are now moving, plus all the United States grain estimated to move via this waterway, free of charge and at the same time increase their net income. Again, if the government would pay each year to these railroads the amount it will have to pay for annual interest charges, maintenance and operation of the proposed St. Lawrence waterway, they could afford to haul free all grain that would move through the waterway and have a substantial increase in their net income. According to the estimate of competent engineers and statisticians who have given this subject careful study, three double-track, all-freight railroads between the Middle West and the Atlantic seaboard, usable twelve months in the year, could be constructed and equipped for the cost of the St. Lawrence waterway, the use of which will be limited to not over seven months in the year, that being the maximum ice-free period.¹

Another instance may be given. Among the proposed expenditures on the Mississippi River is one for a nine-foot channel from St. Louis to St. Paul. There are railroads substantially paralleling this route, but if there were not, a single-track, water-grade railroad between St. Louis and St. Paul could be built for about one-fourth the cost of the nine-foot channel and could be operated and maintained at an annual cost of 60 per cent of river maintenance and lock operation, and the railroad could be operated every day in the year, the river only when ice-free.

¹ *St. Lawrence Navigation and Power Project*, page 177.
[198]

Another instance. The Inland Waterways Corporation has for thirteen years been operating government-owned equipment on the Mississippi and Warrior rivers. It pays no taxes on its floating equipment, nor interest on its investment. Even excluding these items of expense, it has shown an operating loss during the period of its existence. This competition by government-owned and operated barges has been an important contributing cause of recent receiverships of two major railroads.

Since 1921 the Federal and state governments have spent more than \$13,000,000,000 for highway improvement. Upon these highways, which largely parallel the railroads, there are being operated approximately 3,500,000 freight trucks and some 96,000 passenger-carrying buses. Their contribution to the cost of construction and maintenance of these highways is negligible when compared to the cost to the railroads of constructing and maintaining their roadbeds.

If the railroads are to have what both the President and President-elect have advocated, "equality of opportunity", these subsidies to competitors should cease.

The American railroads have been subjected to this kind of competition and at the same time have for the ten years ended in 1931 paid out in taxes for every \$100 which they have earned from operation \$5.88. In 1931 when the earnings went down, the taxes still kept up and in the year 1931 they paid out of every \$100 earned from operation \$7.24, and from every \$100 of net operating revenue \$31.63 in taxes. Almost one-third of the railroad plant was operated to support the Federal, state and local governments.

Over-Regulation of Railroads and Under-Regulation of their Competitors

To understand the reasons for over-regulation, some knowledge of a century of railroad construction and operation is necessary. Before 1830 there were no railroads to speak of. The census of that year showed a population of 12,866,000. In 1930 there were 249,000 miles of railroad in the United States (almost one-third of the mileage of the world) and the population had increased to 122,775,000. Even the twenty-four states of 1830 had developed largely through the

impetus given to transportation by the invention of the steam-boat, which was the first application of steam to motive power and the first improvement in methods of transportation since the invention of the wheel in some period before history begins its record. So it may be said that the United States grew by and with these new transportation methods and principally by and with the railroads. This is important to remember, because in Europe improved highways came many years before the railroads; in America railroads came many years before improved highways and are intensively bound into the social and economic life of the American people.

With the coming of the railroad, it was natural that the common law, which had for centuries in England defined the rights and duties of carriers of passengers and property, should be applied to these new carriers in the United States, because the common law was and is a heritage of all English-speaking nations. At common law, that is to say, before legislation decreed otherwise, a common carrier of property was defined as one who undertakes for hire to transport the goods of such as choose to employ him from place to place. The method of transporting and the personnel of those who perform the transportation were immaterial. The obligations of the common carrier were to carry for all who offer, goods suitable to be carried, and to charge no more than a reasonable price for the service. There was no obligation *not* to charge less than a reasonable price or to treat all customers alike. From this arose most of the early complaints.

It so happened that the invention of the steam engine not only produced the locomotive for the railroads, but also the steam-driven machine for the manufacturer. Both came into operation at about the same time. The locomotive hauled trains, the machine produced articles formerly made by hand. Thus there were coincident quantity production of transportation and quantity production of manufactured articles. Each was necessary to the other. The railroad brought raw material to the machine and took away the finished product. The machine furnished the railroad a substantial part of the latter's revenue. The economic rule soon began to work by which the buyer at wholesale demands and receives a lower purchase price than the buyer at retail. The common carrier, being

[200]

under no obligation to charge the same to all shippers, naturally sold its product to the large shipper at a lower price than to the small shipper. The small shipper had no redress. There were no other practical means of cheap and quick transportation. The railroad became a monopoly, unregulated and capable of making or breaking shippers and localities. As the railroads, aided by the inventions of the telegraph and the air brake, make their service surer, safer and faster, their power to benefit or injure became greater.

It was inevitable that the injured would complain and so they did. The issue came to the United States Supreme Court for decision in 1876 in the Granger Cases, wherein the Court held that, "When . . . one devotes his property to a use in which the public has an interest, he, in effect, grants to the public an interest in that use, and must submit to be controlled by the public for the common good to the extent of the interest he has thus created",¹—a common-sense application of the maxim, "the safety of the people is the highest law."

Ten years later Congress passed the Cullom Bill, to be known as the Interstate Commerce Act. It is significant that the committee reporting the bill, reviewing the causes of complaint against the railroads, stated that the most important grievances and nearly all of the complaints, "are based upon the practice of discrimination in one form or another."

The two leading prohibitions in the Act were that railroad charges shall not be unjust or unreasonable, that they shall not unjustly discriminate so as to give undue preference or advantage or subject to undue prejudice or disadvantage persons or traffic similarly circumstanced. In other respects the Act left common carriers as they were at common law, free to make special contracts looking to the increase of their business, to classify their traffic, to adjust and apportion their rates so as to meet the necessities of commerce, and generally to manage their important interests upon the same principles which are regarded as sound and adopted in other trades and pursuits.²

Incidentally the Commission, construing the Act, held that traffic in trainload lots did not justify a rate per carload different from the rate applied to traffic of the same kind in single carloads.³

¹ *Munn v. Illinois*, 94 U. S. 113.

² *I. C. C. v. C. N. O. & T. P. R. R. Co.*, 167 U. S. 479.

³ *A. C. Mining Co. v. C. & E. R. Co.*, 19 I. C. C. 592.

For nearly twenty years, this was the limit of regulation applied to the railroads. In the meantime, the working of the economic law above cited had created trust combinations tending toward monopoly to such an extent that in 1890 the Sherman Anti-Trust Law was enacted forbidding further creation or the continued existence of those already created; and in 1903 Congress went further and passed the Elkins Act, which prohibited common carriers by rail from giving or accepting rebates and declaring that any device whereby property shall be transported at a rate less than that named in the tariffs published and filed by such carrier, shall be a misdemeanor, subjecting corporations to fine and persons representing corporations to fine and imprisonment.

Pursuing this policy of further regulation, Congress in 1906, in the Hepburn Act, authorized the Commission to prescribe maximum rates and to require railroads to publish tariffs not exceeding such maximum rates and to adhere to them. Finally, in 1910, in the Mann-Elkins Amendment, the Commission took away from the carriers the right theretofore exercised of making rates, by reserving the power to suspend such rates when filed. All of this legislation was evidence of a protest on the part of the shipping public, and as usual, was carried too far.

Looking back, we believe that the railroads have no quarrel with the prohibitions against unjust discrimination, nor indeed, against the prescribing of maximum reasonable rates after hearing. But it is obviously unjust that when rates are suspended before a hearing and later found reasonable, the carrier should be subjected to all the interim loss.

The effect of these extreme restrictions slowly became apparent. Chief Justice Taft, in an opinion dealing with this period, used the following language,

The railroads availed themselves of the weakness and cumbrous machinery of the original law to defeat its purpose, and this led to various amendments, culminating in the Amending Act of June 18, 1910 (Mann-Elkins Amendment), in which the authority of the Commission in dealing with the carriers was made summary and effectively complete. Whatever the causes, the fact was that the carrying capacity of railroads did not thereafter develop proportionately with the growth of

[202]

the country, and it became difficult for them to secure additional investment of capital on feasible terms.¹

This lack of capacity became apparent particularly during the period of the World War when the railroads were under Federal control. Upon their return from Federal control, Congress, in recognition of the necessities of the case, passed the Transportation Act of 1920, which, among other things, imposed an affirmative duty on the Interstate Commerce Commission to fix rates and to take other important steps to maintain an adequate railway service for the people of the United States.

In the meantime the railroads were gradually losing their monopoly of transportation. In 1912 Congress, in the Panama Canal Act, had forbidden railroads thereafter to operate water lines excepting in special cases and then only with the regulation applied to water lines so operated, in all respects the same as those applied to the railroads. All but a few of the steamship lines were forcibly separated from their owning or controlling railroads and placed in the hands of independent operators to be operated practically free from regulation. So that as far back as 1912 the railroads were confronted with unregulated competitors carrying a large amount of traffic by water, in which operation the railroads were forbidden to engage.

But that was not all. The improvement in the gas engine gave rise to the passenger automobile and to the auto truck and they in turn brought about improved highways, upon which there has been spent in ten years an amount equal to the par value of all railroad bonds at the end of a century of railroad construction.

Even though the railroads have ceased to be monopolies, all regulations should not be removed. Regulations necessary to protect the small shipper are as necessary today as they were at the time of the Granger Cases. Unregulated transportation will today as surely drive out of business the small concern as it threatened to do when the Interstate Commerce Act was made law. Irrespective of what the railroads in their own interest may advocate, the public interest demands the regulation of highways and water carriers.

¹ *R. R. Commission v. C. B. & Q. R. R.*, 257 U. S. 563.

Federal Legislation

To what extent shall this regulation go? Doubtless all that has been said at this time will by others be brought to the attention of the appropriate committees of Congress and to the committee of the five distinguished men who are now from a sense of public duty giving their services to ascertaining and reporting facts helpful in solving the railroad problem. It would be premature to state in behalf of the railroads what legislation should be asked for. I am not authorized to speak for them, but personally I believe the legislation should include:

1. More effective and speedy methods of railroad consolidation.
2. Repeal of the recapture clause and removal from railroad credit of the cloud now hanging over railroads which are not in the recapture class, and yet are without reserves to meet the government's claim to the contrary.
3. Repeal of laws which forbid railroads to engage in water transportation everywhere on an equal basis with others.
4. Permission for railroads in competition with other carriers to make adjustments of rates to meet competition and, for this purpose, to charge more for a shorter than for a longer haul over the same line and in the same direction; permission in other respects to make rates to meet competition with the same restrictions (or absence thereof) as are applied to their competitors.
5. Limiting the power of the Interstate Commerce Commission to suspend rates so long as the revenues of any carrier are not equal to a fair return upon the value of its property.
6. Placing carriers on the highway and by water under the jurisdiction of the Interstate Commerce Commission or other Federal tribunal, with the same regulations imposed upon them as are imposed upon the railroads.

State Legislation

7. State legislation should in general harmonize with regulation by the Federal government, but, in addition, the states

[204]

should as far as practicable approach uniformity in legislation, covering:

8. Size, weight, speed and operation of commercial motor vehicles and hours of service of drivers.
9. Financial responsibility of highway, commercial carriers, including surety bond for protection of travelling and shipping public.
10. In addition to license fees, adequate charges should be assessed for the commercial use of the highways, the charges being based upon the extent of such use.
11. Expense of separating grades at crossings should be assessed upon the users of the highways and the railroads, respectively, in proportion to benefits received. The railroads should no longer be required to bear the larger part of grade separations to make safer highway operation for their subsidized competitors.

Economy in Railroad Operation

In the meantime the railroads have formally pledged themselves "to avoid all preventable wastes in the competitive relationships between themselves and to devise and apply the most feasible methods for meeting new competitive conditions." The indicia of economy and efficiency with which their properties have been operated in the ten years succeeding Federal control are a proof of their good faith. The tribute paid to them by the Secretary of Commerce, now President of the United States, in 1926, is worthy of quotation:

The railways during the past five years not only have built up adequate service and given complete correction to those ills, but they have, by great ability of their managers, greatly reduced transportation costs and thus made rate reductions possible which would not have been otherwise the case. . . . The result of this great reorganization upon the whole economic fabric of the country has been far-reaching.

Financial Integrity of the Railroads

The financial integrity of the railroads has been no less commendable. During the period of government control and in the succeeding years, the government loaned the railroads \$1,018,000,000. The railroads repaid \$978,000,000 in principal and \$210,000,000 in 6 per cent interest. There is still

[205]

owed to the government a little less than \$40,000,000 but the interest paid at 6 per cent represents a cash profit to the government of \$70,000,000 over the cost of money, so that if the government should not collect any of the \$40,000,000 owed it, it still would have a profit of \$30,000,000 in cash.

The Emergency Problem

Urgent as are the solutions of the temporary and continuing problems confronting the railroads, there is an emergency looming which should have the first attention of the Congress in December. I refer to the limitation of the power of the Interstate Commerce Commission and the Reconstruction Finance Corporation to approve loans to railroads. Such approval may now be given only when the Reconstruction Finance Corporation "will be adequately secured",—a phrase which the Interstate Commerce Commission and Reconstruction Finance Corporation have generally construed to mean adequate security in the form of collateral having a market quotation for an aggregate amount considerably in excess of the face of the loan. With the present depressed market quotations, this requirement will speedily exhaust the collateral of most of the railroads and they may be left without resources to meet interest obligations unless business returns more quickly than now seems possible. In these circumstances there must be some liberalization in the legislation to meet the emergency.

The profitable dealings of the government with the railroads, just cited, justify the hope and request that the Congress will reenact in substance the law under which those dealings were had and so enable the Interstate Commerce Commission to approve and the Reconstruction Finance Corporation to make loans to a railroad to enable it "properly to meet the transportation needs of the public where the prospective earning power of the applicant and the character and value of the security offered are such as to furnish reasonable assurance of the applicant's ability to repay the loan." This is merely following banking practice of relying upon the commercial efficiency and financial integrity of the borrower. The railroads have justified this reliance.

[206]

THE PROBLEM OF UNEMPLOYMENT

LEO WOLMAN

Professor of Economics, Columbia University

THE immediate unemployment problem of this country is that of providing relief for the ten millions of unemployed and their families. So far as the next months are concerned this requirement is pressing and inevitable. Neither the plans for the recovery of business already in effect nor any conceivable new ones can possibly contribute much immediately to the reduction of the volume of unemployment and to the mitigation of the lot of the unemployed. If the jobless of the United States are to receive this winter only the meager standards of relief which they had last year, our total relief funds must be at least twice those of 1931.

Baffling as were the problems of the collection and distribution of relief in the first years of the depression, they are all the more difficult now. Since the spring of 1930 the number of persons without any employment whatsoever has more than tripled. The moderate improvement in employment which has taken place since last July has at the best afforded jobs to but a small fraction of those out of work and, that, by all signs, for a limited period of time. Allowing for all possible errors of measurement and interpretation, the American unemployment rate is at this time the highest among the industrial countries of the Western World.

For a large and increasing proportion of the jobless, this winter will be the fourth winter of unemployment. By this time the personal resources of the vast majority of the unemployed and of their friends and families must surely have been completely exhausted. Appeals to those who are still at work can be of slight avail when the earnings in 1932 of those employed in manufacturing industries had declined to \$18.50 a week; in coal mining to \$17.15; in wholesale and retail trade to \$22.38; and in rail transportation to hardly more than \$26.00 a week.

[207]

Once more there are no accumulated reserves out of which these heavy current requirements can be met. In more than one important community, the relief funds for the coming winter months are yet to be collected; and where the payments of relief have not been suspended or drastically reduced, they are meanwhile being raised in part through borrowing. Private gifts as a source of moneys have steadily declined in both absolute and relative amount until the greatest share of the burden rests upon our local, state and Federal governments. Inadequate as the average dole has been under this hand-to-mouth system, the tragedy of existing conditions is intensified by the gross inequalities in relief which local differences in resources, foresight and organization have produced.

At this time of greatest need, the central and local governments of this country, almost without exception, are sagging under the weights of a huge public debt and excessively high levels of taxes. Barring extensive revisions in outstanding budgets, the prospects for increasing revenues out of either borrowings or taxation are, to say the least, not bright. Among the municipalities, whose outlay for relief represents the bulk of expenditures for this purpose, future revenues depend upon the trend in the assessed valuation of real property. If we may judge by the present condition of the real-estate markets and the movement of rents, the rational outlook is for reduced income from this source of revenue. In the case of the Federal government, the continuance of the depression at anything like prevailing levels and the still unsettled state of the investment markets combine to make both additional borrowing and higher taxation uncertain and hazardous undertakings.

Under the circumstances it is futile to talk of expanded programs of public works, vast loans to the unemployed, soldiers' bonuses and the like. Already the governments of this country have severely limited their expenditures on public improvements. Since the middle of 1930 the amounts spent by local governments on public works have been steadily and substantially reduced. In spite of an increase in the Federal outlay for construction of something like \$300,000,000 a year, the aggregate expenditures of the country for this purpose are in 1932 probably half the amount so spent in 1929 and are still declining. Add to this the even more drastic slashes

in the construction budgets of such quasi-public agencies as the railroads and other public utilities, not to speak of the equally vast shrinkage in residential construction, and the total reduction of construction as a source of employment has assumed gigantic proportions. To plan to make up even a small fraction of this loss through public operations is, as we have already learned from the numerous experiences of foreign governments, an impossible undertaking, doomed from the outset to certain failure. Even the financing of self-liquidating public improvements has turned out to be less attractive than it was regarded at the beginning, partly because the possibility of their becoming self-supporting is in many cases doubtful and partly because public treasuries are unwilling to assume further obligations of whatever nature.

The financing of public works, or relief, through any method of inflation is, in my judgment, unsound and impracticable unless we regard such inflation as an element of a general program for the thoroughgoing control of American business in both its domestic and international operations. However plausible the case for this type of control may be, the adoption of measures leading to it is, assuredly, not an issue in American practical politics at this time. For the rest, inflationary measures can do little more than undermine the financial progress which we have made at such great cost and difficulty during the past year. The injection of new uncertainties and risks into an economic situation that is already too full of them is bound to do more harm than good and to block the process of recovery. Any substantial lifting of the present price level by artificial measures of public finance or banking policy is now more than ever an impossible task. It is one thing to inflate in a world unfamiliar with the methods and consequences of inflation; but quite another to adopt policies of inflation in a world which has inherited from recent eras of violent inflation "a heightened awareness of the possibility of a currency becoming worthless."

The dilemma created by the increasing and unavoidable need for relief and the growing incapacity of private and public agencies to pay is not, by its very nature, susceptible of easy resolution. The time for miracles in public finance is past. Funds for the generous relief of the unemployed must be

supplied; and they can be supplied out of savings in current budgets, out of the diversion of appropriations from less to more essential uses, and by the application of unparalleled social pressure on private contributors. At the most the total relief bill of the country for the year 1932 will not be a large item in total public expenditures. It is doubtful, when all the relief money is raised from all possible sources, that it will exceed for the whole country one and a quarter billions, or \$125 per unemployed person per year. In the budgets of local and central governments there are innumerable and well-known items whose continued support is of much less importance to the community than the adequate care of the unemployed. It is no solution of this problem to hold that the revision of public budgets is difficult. After three years of unexampled liquidation of private enterprise, reductions in wage rates varying from 10 to 50 per cent, increases in the hours of work in many of our most competitive industries to more than 66 hours a week, universal short time for the $\frac{3}{4}$ to $\frac{4}{5}$ of the workers who are still employed, and a drop in the cost of living of more than 20 per cent, it is unthinkable that public spending must continue at its present level and that the budgets of American governments are immune to the force of universal economic readjustment. However slow the acceptance of this idea has hitherto been, it is clear that the time cannot be much longer delayed for the serious and swift consideration of budgetary revision. It is equally clear that no private individuals should be freed from their social responsibilities to contribute to the utmost for the decent support of the unemployed and for the maintenance of our invaluable institutions of private charity and social welfare. At this juncture, finally, it is all the more unfortunate that the effort should be made, through the device of work-spread-and-salaried labor at the cost of still further reductions of low standards of life, instead of putting it, where it properly belongs, on the public treasuries and the incomes of those who can afford to pay.

Our present experience with the grave problems of the relief and the care of the unemployed is not new in the economic history of this country. The breadlines, mayors'

[210]

committees, agitation for public works, and the hearings of the Federal Commission on Industrial Relations during the depression of 1914 are still vivid in the minds of many of us. That episode was repeated in much the same style in 1921. There was the same dread of destitution following the precipitate decline in employment and in wages. The President's Unemployment Conference, not unlike the Industrial Relations Commission seven years earlier, announced its program of stabilization through public works and organization of the labor market through a coördinated scheme of Federal and state employment offices, and held out the promise of an American business system free from the irregularities and uncertainties of the past. Now once more, with an unemployment problem of much greater gravity, we are forced to meet the successive phases of the situation with the same lack of program and policy. From the organization of relief to the conduct of public employment offices, we face the knotty problems of the latest depression not much better prepared than we were twenty years ago.

Meanwhile there has been a radical and universal change in public temper. This, I should judge, may well be the last great business depression in the United States during which the care of the unemployed can, and will, be left to the hastily improvised expedients of the moment. If the right of the jobless to adequate means of relief, granted them under conditions of decency and equity, is not yet recognized in this country, the time is not far distant when it will inevitably be so. The political instabilities of this period, the vast experiments of Europe with relief and insurance, and, perhaps, the example of Russia have all combined to contribute to this end. But of greater influence than all else is the universal realization, particularly in this country, of the capacity of its industry to produce more than the requirements of physical well-being for all of the population. As Walter Lippmann put it, "this is the first great economic depression in which every thinking person has been conscious of the paradox" . . . "of want in the midst of abundance, of poverty in the midst of plenty."

In the mentality of the people there is a profound difference between this crisis and all its predecessors. This is the first time when it is

[211]

altogether evident that man's power to produce wealth has reached a point when it is clearly unnecessary that millions in a country like the United States should be in want. In all previous crises there was some doubt as to whether the wealth of the nation was sufficient. That doubt no longer exists.

Like the solutions of the current problems of economic adjustment and reconstruction, satisfactory future programs of unemployment cannot be the product of economic magic or political legerdemain. If the jobless are to encounter the next upheaval in business better equipped to withstand the losses of jobs and incomes than they are now, it will be as the result of the operation of social and economic institutions of familiar characteristics. I believe now, as I have for many years, that the sole effective and safe measure for anticipating the losses suffered by labor during periods of long business depression is to be found in applying the principles of social insurance to the risks of industrial unemployment. By creating machinery for the accumulation of reserves in good years and making them available in bad years, and by that method alone, is it possible to take the next great step toward managing the problems of involuntary idleness. Two per cent of the total wage and salary bill of American industry would, in the two years 1928 and 1929, have yielded a fund of one billion dollars, and three per cent would have yielded a fund of one billion and a half.

I am well aware of the difficulties which a universal plan of unemployment insurance will encounter; of the abuses to which it is exposed; of the criticism which has been directed against the insurance systems of Europe. But as long as we have boom and depression, overtime and layoff, so long will it be necessary, if we are to act with foresight, to prepare for bad times in good. At its worst, any comprehensive system of unemployment insurance will be incomparably superior to our present methods by insuring at least the insured unemployed the receipt of unemployment benefits as a right; by securing to the bulk of the unemployed something approximating equality of treatment; by providing, through the accumulation of reserves, rates of benefit that cannot help being more adequate than the present dole.

The fact that unemployment insurance, once established, is

[212]

likely to grow in cost, need not be regarded with fear. Increasing expenditures on social services, of infinite variety, have been the feature of all modern economic history. These costs have in the past been absorbed by the rising productivity of industry and the increasing wealth and income of nearly all industrial countries. There is no sound reason for believing that such absorption will not continue for many years to come.

The security which we in America thought we had achieved in the decade of the 1920's acted to retard the slow advance of social insurance legislation in this country. Again face to face with the realities of our economic organization, we are about to resume the progress in this direction which our late prosperity had interrupted. The issues henceforth to be considered are not whether unemployment insurance is essential and practicable, but what form we desire it to take and what safeguards for its efficient and intelligent administration we wish to create.

[213]

THE AGRICULTURAL PROBLEM

FREDERICK E. MURPHY

President, *The Minneapolis Tribune*

IN seeking a formula for our national recovery, we must also look for a special formula for our agricultural recovery. Our agricultural problem is a special problem within our national problem. It is complicated to a bewildering degree. It is made up of almost numberless contradictory factors which seem to defy all our efforts to align them into anything like a practical theory. Yet our agricultural problem with all its manifold difficulties is one that we must face courageously and intelligently. We must come to grips with its many and refractory facts, and somehow we must find an answer.

Those who have watched the economic progress of the nation, are aware that America had an agricultural depression before it experienced this world-wide depression. We know that since 1920, with but few and temporary exceptions, the exchange value of the products of agriculture gradually has been sinking lower and lower. When stocks were at their highest, when factories were operating day and night with constantly increasing wage scales, when professional services were in the greatest demand, and the economic millennium seemed to have arrived, with mass production, mass consumption and higher and higher wages, the general price level of agricultural products was declining. We know that farm mortgages were being foreclosed, that banks were failing in the agricultural districts.

We are forced to the conclusion that for a period of a few years, at least, the majority of this nation may revel in the benefits of prosperity, while 25 per cent of its people on the farms are sinking to distress levels. This actually happened in the period preceding the nation-wide depression.

We may look back on that period of expansion with scorn and contempt. We may assert that it was false prosperity and that it was doomed by its inherent falseness—failure to

[214]

find its way into the lives of the 30,000,000 of our people who are on the farms—to come to a disastrous end. But there is no denying that in the years preceding 1929 the people of the United States, with the exception of the farmers, had more of the good things of life than ever before.

We are justified in doubting that this condition could have long continued. But it is also equally questionable whether the low estate of agriculture had any important part in bringing to an end this era of all but forgotten prosperity. It might have gone on indefinitely, until the American farmer became a peasant.

I am by no means convinced that such a development is economically possible. I am quite certain that it is not politically possible. And I am absolutely certain that it is ethically wrong. I do not believe that the United States, with a population of 120,000,000, can exist as a nation with 30,000,000 of its people economically submerged, so long as they have political power in proportion to their numbers.

No matter what we may think of agriculture, we are compelled to recognize economic facts, and facts are under no obligation to be pleasant. Facts seldom take the trouble to flatter us.

Let us look at the facts.

First of all we must recognize that the exchange value of agricultural products, the world over, is declining. There may be many reasons for this. The world is becoming more and more productive. It produces more and more food, and the mechanization of industry has decreased the per capita requirements for food. The pick and the shovel, the scythe, the hoe, the fork and the sledgehammer have disappeared; and power instruments have come to take their places. Even the home has become mechanized.

The horse has disappeared from the city; and the acres of farm lands that were once devoted to producing the oats and hay that furnished the power for city trucking and hauling as well as for farm work are now—by the use of gasoline—thrown back to produce more food for humans.

Coincident with this decreased demand has come a rapid increase in the world production of food. In the last forty years the world production of wheat has doubled. That of

[215]

the United States has increased from 378,000,000 to 892,000,000 bushels; that of Canada from 42,000,000 to 304,000,000 bushels; that of India from 229,000,000 to 347,000,000 bushels; that of Argentina from 31,000,000 to 219,000,000 bushels; that of Australia from 27,000,000 to 171,000,000 bushels; and so the story of increased food production goes.

Medical and sanitary science have made the tropics habitable for the white race to supervise and develop tropical production of new foods and substitutes for old foods. The tropics with their breech-clout labor have thus been brought into ruinous competition with the farmer in the temperate zone.

One has but to observe the increased use of such a product as coconut oil, to realize the change that has taken place. The average annual importation of coconut oil in the period from 1921 to 1925 was 392,000,000 pounds, but it increased in 1930 to 655,000,000 pounds. The average import of palm and palm kernel oil from 1921 to 1925 was 89,000,000 pounds; for 1930 it was 250,000,000 pounds. And while we are importing these oils, the American farmer is forced to export a billion pounds of animal fats each year. In 1924 the United States was exporting more oils, oil materials, animal and vegetable fats than we are importing. But in 1929 our imports exceeded our exports by approximately one billion pounds. This, of course, is what is driving the dairy, hog and cattle producers into a frenzy. The increase in world production from 1923 to 1929 amounted to five billion pounds.

Coconut oil has fallen in price from 18 cents in 1918, to 4½ cents in 1931. During the same period cottonseed oil has fallen from 24 cents to 7 cents; tallow from 17.9 cents to 4.3 cents. Other vegetable and animal oils and fats have shown similar price declines.

The world production of vegetable oils in 1929 was not far from twenty billion pounds, or ten times the butter production in the United States. The American farmer has to compete not only with the tropics, but with the ocean as well. The world production of marine animal oils in 1931 is estimated at one billion seven hundred and fifty million pounds. Of this, nearly one billion five hundred million pounds was whale oil. Whale oil is now used for the making of butter substi-

[216]

tutes in Europe, and to a small extent in the United States; otherwise, it chiefly goes into soap-making.

The American farmer finds himself in desperate competition with the fecundity of the tropics and the teeming animal life of the ocean, while he struggles with the less bountiful soil along the forty-fifth parallel of latitude.

The American farmer also finds himself at a grave disadvantage in the matter of transportation. A large percentage of our industrial and commercial population lives on or near the seaboard and is more accessible to foreign markets for food and industrial raw materials than it is to the center of our agriculture. A very large proportion of American agricultural products comes from the central states, which average a thousand miles from seaboard, in contrast with Argentina, Australia and other countries, where most agricultural products are produced relatively close to tidewater. Ocean rates are extraordinarily low. In contrast with these low water rates, are the high domestic railroad rates, which must be paid on the mass of agricultural products from the farms of the Mississippi Valley. Flax is grown a few hundred miles from the seaboard in Argentina and laid down at New York at a price which the North Dakota flax-grower can never hope to meet. New Zealand sells butter in San Francisco.

These facts cannot be dismissed with the reflection that the United States is predominantly an industrial nation. The farmers cannot be carried along by the highly paid factory workers, for the simple reason that there are too many farmers. In the *Annalist* of August 12, 1932 was published an analysis of the occupational census of 1930. Out of a total of 48,830,000 gainfully employed persons in the United States, there were 14,111,000 in the mechanical and manufacturing industries. These figures include the proprietors and executive officials, the building and printing trades, and a variety of occupations outside the factory, in which men generally work for themselves.

In agriculture there were 10,472,000 persons employed. The fourteen million industrial workers cannot hope to carry the ten million agricultural workers. This enumeration of the agricultural workers does not take into consideration the millions of others who are dependent directly or indirectly on

[217]

the farm group. Economic equilibrium demands that the farmer must be able to exchange his products for a fair share of the products of industry. This exchange he has not been able to make for over a decade.

The farmer cannot be viewed as a mere dependent upon industry. In the American economic set-up, the farmer must be viewed as a consumer as well as a producer. So any theory of mass production and mass sales and high industrial wages, unless it includes a high exchange value for the farmer's products, must inevitably produce economic disequilibrium.

Industry cannot evade the difficulties that confront the American farmer by the blind theory of "subsistence" farming. Subsistence farming is but a euphemism for peasantry. The peasant farmer is not and cannot be a consumer of industrial products, and farming reduced to a mere mode of life has no place in America. Industry cannot afford to ignore the buying power of thirty millions of our one hundred and twenty million people. Industry cannot exist solely on the buying power of industrial workers; therefore for the purely selfish reason of self-preservation, industry must assume direct responsibility for restoring the farmer to his proper rôle of a consumer.

We must face the fact that in America we have nearly a billion acres of arable land divided into some six million farms on the products of which depends one-fourth of our population. We must face the fact therefore that these billion acres cannot continue to produce food for human consumption at a profit to the American farmer.

Some agricultural economists and business men advocate that the agricultural plant must be reduced by segregating marginal areas. This plan holds an appeal for me, but knowing regional prides and political expediencies as I do, I rather favor charging industry with finding some method by which these marginal acres to the extent of 50,000,000 can be profitably employed for purposes other than the production of food. If 50,000,000 of our food-producing acres could be diverted to the production of raw materials, such as wall board, newsprint, casein and similar products for industrial purposes, our surplus problem would be relatively simple.

[218]

There are only 55,000,000 acres in the United States devoted to the raising of wheat so you can see what 50,000,000 acres taken out of production of foods might do. I believe it can be accomplished if industry seriously attempts it. I realize that it is much easier to state the problem than to solve it, but I feel the necessity of stating it because industry does not appear to realize that the problem exists.

I presume that my own profession—journalism—is as much to blame for this indifference as any other. Our newspapers pay great attention to the other details of our economic life—shipping, financing, manufacturing, mining—sports and politics—while little or no thought is given to agriculture. What thought is given to agriculture is a reflection of the attention paid to farm politicians in Washington. Your Washington correspondent has the political viewpoint rather than the economic. When our metropolitan newspapers realize, as they must some day, the national importance of the economic phases of this nation's farm problem, we shall begin to see the light. The best brains of the country will be loaned to agriculture, not because of altruism, but because industry will understand that it must help develop its sales market as well as exploit it.

The American market is, and apparently for a long time to come must be, the principal market for the American farmer, with the exception of the cotton and tobacco grower. We consume over 99 per cent of our beef, veal, mutton and lamb; over 96 per cent of our pork; 99 per cent of our oats; 99 per cent of our rye; 99 per cent of our corn; 92 per cent of our oranges; 84 per cent of our apples; 99 per cent of our potatoes; 99 per cent of our peanuts; 98 per cent of our beans; and 100 per cent of our flax and hay. As against this domestic consumption we export about 55 per cent of our cotton; 41 per cent of our tobacco; 18.5 per cent of our wheat and 33 per cent of our lard. Our exports of lard are forced on us largely because of our importation of tropical fats and oils, which are used as substitutes for the animal fats produced on our farms.

No consideration of the part that agricultural prosperity must play in the restoration of general prosperity can be complete without a consideration of the world trends that had

[219]

their inception in the World War. Before the war came to an end, Europe was bankrupt. Practically every European nation became a debtor nation. The net result of Europe's post-war condition was a determination to become economically self-sufficient. Europe went farther and farther into debt. Now, being in debt, it has to sell and it cannot buy. Almost without exception European nations have surrounded themselves by high tariff walls.

Tariff battles are being fought on every frontier. These tariff walls constitute a blockade almost as effective as that maintained by the British Navy in the North Sea. International trade is stopped, and with its stoppage comes the curtailment of domestic production, which in turn curtails domestic consumption, and one of the effects of this is that farm products are going begging at any price in the United States today.

Intergovernmental debts are at the bottom of the difficulty, and the fundamental cause for the stoppage of international trade. Intergovernmental debts have forced all the debtor nations on a buyer's strike. The debtor nation obviously must sell more than it buys. The tariff is the device by which debtor nations seek to gain a favorable balance of trade in order to meet their debt requirements. When every nation refuses to buy and strives only to sell, we have an economic stalemate, reminiscent of trench warfare.

And thus it comes about, that the products of the American farm are being sold in diminishing quantities in Europe, and at prices which will not sustain the American farmer.

European nations are today taxing their people heavily to this end. Germany has a duty of \$1.87 on wheat; France, 84 cents; Italy, \$1.23; Austria, 64 cents; Czechoslovakia, 97 cents; Poland, \$1.76; and the limit of absurdity is found in Greece with a tariff duty on wheat of \$7.99 a bushel. Europe is forcing the growth of its own agriculture by keeping out the products of the great food-exporting countries.

The fear of another war undoubtedly plays a part in this determination to attain a food self-sufficiency. So, in this complex world, it has come about that the intergovernmental debts and nationalistic fears of Europe have a pronounced effect on the welfare of Dakota and Nebraska farmers. It

has thus come about that the lack of peace and good will among men, in far distant lands, means dollars and cents to the hog-raiser of Iowa.

It follows that the removal of these causes for suspicion and hatred will redound to the benefit of the American farmer. Unless the United States adopts a policy of isolation, which includes a system of bounties, sufficient to insure the American farmer a fair exchange basis for his products, he must look to the prosperity, peace and confidence of Europe for any immediate benefit to agriculture. So long as the nations of Europe live in fear of another war, so long will they continue to force their own agriculture, by the exclusion of food-stuffs from the Western continent. So long as vast armaments and heavy taxation continue to curtail the buying power of Europe, so long will the food products of the Western hemisphere go begging in search of a buyer. So long as the intergovernmental debts hang over Europe, so long will this tariff war be waged to the detriment of all and not the least to the detriment of the American farmer.

To the extent that disarmament and a revision of governmental debts reduce this need for self-sufficiency, to that extent is there hope for American agriculture. If the nations of Europe confine their productive efforts to those lines which their natural advantages and national talents make economically profitable, markets may be found for our surplus. To that extent the American farmer has a very real interest in the League of Nations, the World Court, the revision of war debts and the peace psychology of Europe.

But after we have settled the question of intergovernmental debts, the fundamental problem of American agriculture will still await solution. We shall still have to consider our domestic allotment plans, our mounting wheat surplus, our floods of tropical oils, our transportation problem, our farm debt problem, and a score of other problems that must be settled in this country, rather than in Europe. The settlement of the intergovernmental debts, disarmament, and the removal of trade barriers are matters of the greatest immediate importance to the American farmer. But even so they do not go to the root of his troubles.

Since industry is concerned fully as much with the con-

sumption as it is with production, it would appear that it is of the gravest import to industry that agriculture should attain the consumptive capacity which its productive capacity justifies. The only method by which this can be achieved is to accord to agriculture a fair exchange for its products. In the changes in our social and economic systems that will inevitably follow the present period, agriculture must receive the consideration that its part in our social and economic life demands.

The problem is squarely up to the leaders of industry and finance. It is they who must solve the problem. Too long have they looked upon it as a political rather than an economic problem. Too long have they viewed it as something of interest only to the West while they have scurried around the world looking for new markets. The time is past when the problems of agriculture can be left exclusively to agricultural economics and agricultural experts. The financial and industrial economists must set to work on this problem. They must discover ways and means for the industrial utilization of our surplus and marginal acreage which is glutting the world's food market. We have these acres and we have people on them and from a purely selfish standpoint it is up to our industrial and financial leaders to see that they have consumptive power.

This is a plain business proposition. We have thirty million American people who do not have to be trained or cajoled to the usage of American-made goods. Their standard of living requires no elevation. They constitute the best market that exists today for American industry, and American industrial leaders will be incomprehensibly blind if they do not see this opportunity.

By now we all realize that the agricultural problem is not a problem that concerns the farmer alone, it concerns banks and all other loan agencies. Bank failures and mortgage foreclosures have made that clear to us. It concerns our transportation agencies. And it concerns our industrial agencies. American industry can no longer delude itself that cheap food means cheaper labor and cheaper production. Cheap food no longer means cheap labor. Cheap food means less buying power among thirty millions of our people. It

is your problem, gentlemen. It is a problem that demands the best brains of the country and it is one that can no longer be shoved into the background as something that will be settled by the passage of time. You have at your command the successful leadership of this nation. Within any one of the boards of directors on which you sit, there is more intelligent leadership than can be credited to all the farmers of this country, sympathetic and well meaning as are most of our farm leaders. I ask you, as a representative of a vast agricultural empire, that has made your industrial, financial and commercial successes possible—an empire upon whose prosperity your prosperity depends—I ask you to accept a responsibility that rests squarely upon you.

I cannot conceive that we will ever have a prosperous America, with one-quarter of its population steadily sinking to the low level of peasantry. We must face this fact, otherwise any plan of recovery which we may contemplate, will have within it a serious flaw that will quickly bring about its failure.

On the other hand, if American industry and American finance will set their minds to the solution of the farm problem, I am sure we can bring about an era of prosperity to the United States which will be continuous and free from the disastrous slumps that have marked our past. We can bring about a social contentment that will make for the security of our government and the principles upon which it was founded.

TARIFFS AND TRADE BARRIERS IN RELATION TO INTERNATIONAL TRADE

GEORGE B. ROORBACH

Professor of Foreign Trade, Harvard University

THE international trade of the world is caught in one of the most vicious of vicious circles. Expanded, like most other business enterprises during the post-war boom, to unprecedented heights, foreign trade was very quick to suffer when the world depression set in. The collapse of prices, the sudden drying-up of international lending, the financial flight of nations over-burdened with debts were the more severe in their effects on international trade because of the intensity of a nationalism that since the end of the Great War had sought to create national economic independence in a world which for 150 years had constructed its industrial life on the basis of an expanding international commerce and a growing mutual economic dependence, nation upon nation.

In the earlier stages of the depression, national governments sought to stem the tide by the familiar method of increasing tariff duties, already high, in order to shut out cheapened imports that appeared to threaten established industries. Later, as the depression deepened, threatening the stability of national finances and currencies, still further duties were added not for the purpose of protection of home industries, but with the aim of replenishing national revenues, balancing budgets, stopping the outflow of gold, and preserving national currencies. Tariffs being inadequate for these purposes, quicker means of restraining imports were employed—import quotas, licensing of imports, actual embargoes on foreign goods.

These measures in turn created resentment and suspicion on the part of other nations and consequently further restrictions to trade were set up, often in retaliation, always with the conviction that home industries must be protected against foreign goods and national finances saved. Still unable to arrest the collapse of national finances by tariffs and quotas, some nations

[224]

finally resorted to the restriction and control of foreign exchange. As a result, international credits were frozen, the settlement of international business obligations blocked, exports further lessened. Thus, each succeeding measure of attempted relief further curtailed the flow of trade; and the curtailment of trade in turn gave rise to additional and more drastic methods of restriction. And so the vicious circle was set in motion, and each succeeding turn has whirlpooled international trade to lower levels and multiplied the barriers to its flow. And the end does not yet appear.

The decline in international trade is indicated by the fact that the value of world commerce in 1931 was 40 per cent less than the average for 1925-29 and the volume 26 per cent less.¹ The declines in 1932, as compared with 1931, have been even greater. The trade of the United States declined more than that of any other important commercial nation. From January 1930 to January 1932, the exports of the United States fell in value 64 per cent, as compared with 53 per cent for Japan, 49 per cent for Germany, 47 per cent for the United Kingdom.² The percentage decline in values of United States trade is given in the following table.

United States Foreign Trade ^a

Percent decrease in values

	1930 from 1929	1931 from 1930	1932 ^b from 1931 ^b
Exports (total)	26.7	37.1	36.1
Finished goods exported	25.0	41.0	47.3
Crude materials exported ...	27.4	31.7	10.3
Exports to Europe	21.5	35.5	38.2
Exports to South America..	37.4	53.0	50.2
Imports (total)	30.4	31.7	32.4

^a Source: United States Chamber of Commerce, *Our World Trade*.

^b First half-year.

The largest declines in American exports during 1931 and 1932 have been in manufactured goods, by far the most important group of American exports. Exports of this group fell 41 per cent in 1931 and 47.3 per cent in the first six months

¹ League of Nations, *World Economic Survey 1931/32*, p. 155.

² The following table shows the percentage decline for a number of countries: (see next page)

[225]

of 1932, while crude material exports in the same periods fell 31 per cent and 10 per cent respectively.

The largest exporting country, the United States was in an especially vulnerable position in respect to its foreign trade, as the world depression grew in intensity. The remarkable expansion of American trade in the post-war decade and up to 1929 was to an important degree made possible by the world demand for equipment material—at first material for restoration of the war-devastated areas, and later, equipment for establishing or expanding productive capacities, since almost all countries set out after the war to make themselves self-sufficient economic units. This type of goods the United States was able to supply to great advantage. The post-war exports of the United States became predominantly manufactured goods, and particularly equipment goods for factory, mine, office and plantation; automobiles and trucks; and those other specialized goods dependent upon large-scale, standardized production in which American industry was especially efficient. Desired by foreign countries to carry out their programs of building up industrially self-sufficient areas, these goods were less affected by protective duties than were most manufactures.

The United States not only produced to greatest advantage these types of goods for export (and in addition many raw materials for industry, such as cotton, copper and petroleum), but financed the export trade by unprecedented foreign loans. Thus it was that by the end of the post-war decade, American exports reached a value of over \$5,000,000,000, of which 50 per cent were finished manufactures.

<i>Imports Exports</i>		<i>Imports Exports</i>	
Spain	62 71	Germany	66 49
Hungary	59 70	Canada	60 48
Yugoslavia	59 65	South Africa	48 47
United States	58 64	United Kingdom	39 47
Czechoslovakia	48 61	Italy	51 46
Poland	63 57	Roumania	61 43
Austria	36 54	Belgium	50 40
Japan	37 53	Sweden	26 33
France	51 51	Argentina	53 31
New Zealand	49 50	Brazil	45 21
Switzerland	21 50		

[226]

It was inevitable that the depression should affect trade of this character with unusual severity. Lending, which was so largely supporting the export structure, was at once cut off. Foreign demand for industrial and other equipment purposes was halted; falling prices lowered the buying power of our customers; our own high protective duties curtailed payments of debtor countries and further weakened the buying power of the foreigner for our goods. These conditions in turn undermined foreign currencies and stimulated the increased number of tariff and other barriers against our trade, partly in retaliation, more largely as a frantic effort to stem the tide of financial and monetary collapse. Thus, at the end of 1932, foreign trade is demoralized, in volume back to pre-war levels, and continuing to decrease.

Modern industrial development which, through the application of power to machinery, has made possible the tremendous increase in man's material welfare, has been possible only because at the same time international trade has also been developed in ever-widening circles. International trade is a necessary corollary of industrialization. The one cannot take place, nor be maintained, without the other. To go back to regional self-sufficiency is equivalent to going back to the spinning wheel and the hand loom. It is to go to lower standards of living, to longer hours of labor, to less of leisure and comfort. Not less, but more, trade flows as all nations swing into the full powers of their productive activities.

And this applies to larger areas and to smaller—less, of course, to countries of continental proportions like the United States than to small regions like Holland or Belgium. To circumscribe the limits of trade to less than the whole world is to circumscribe by that extent the opportunities for industrial expansion and the standards of living of even the largest and richest nations. Foreign trade restoration appears to be an essential step in the road toward recovery. Industry, agriculture, forestry, mining, shipping, banking and finance, domestic trade itself, are inextricably interwoven with international trade. Self-containment cannot be the solution of our problem of depression. To stop up the channels of trade is to make impossible the full functioning of our modern industrial life and progress.

[227]

But any solution of the problem of the restoration of international trade to the point where it will permit the normal and orderly development of world economic affairs must rest, it seems clear, upon international coöperation. No nation, nor group of nations, can of itself create the conditions that will break down the existing barriers.

Lying at the basis of our international trade difficulties, doubtless, was the recrudescence after the war, and largely as a result of the war, of a particularly acute type of nationalism that refused to recognize the interdependence of the world's economic life. The raising of tariff and other barriers to unheard-of heights in the after-war period occurred at a time when high protective tariffs were sure to have a more demoralizing effect upon world economy than normally tariffs would have. These tariff barriers were raised when the belligerent nations on both sides were struggling to get back on their feet. And most of these nations were normally dependent upon foreign trade to an unusual degree. The high tariffs raised by their former customers were serious handicaps even had no other hindrances to trade been present.

At the same time, however, these nations had become burdened with staggering debts—debts contracted to pay for absolute losses caused by the fearful destruction of war and not for the creation of productive enterprises that in time might become self-liquidating. At the same time the citizens and business firms of these nations, and of neutral nations everywhere, contracted other debts for the equipping, often the over-equipping, of their productive enterprises. The payment of these debts, both the war debts and the private debts, required, of course, the flow of goods from debtor to creditor in even larger amounts than normally, if restoration of production and the maintenance of national credit were to be achieved.

Thus developed after the war two absolutely contradictory situations in world economics. On the one hand, the raising of barriers to restrict the flow of commerce; on the other hand, the creation of international debts requiring large payments between nations that could be liquidated only by the flow of goods.

The full force of the tariff restrictions on trade, however,

[228]

was not felt until after the depression broke in 1929. Following that year the shutting off of international investments and lending made it necessary that debt and interest payments be effected in goods or gold; no longer in credits or by the creation of new debts. The attempts by debtors to achieve this result, i.e. payment in goods, at once resulted in further restrictions by the creditors upon imports. Duties were raised, and, to give quicker action, quotas and prohibitions on imports were set up. The debtor nations, on the other hand, finding the value of their exports declining, both because of the falling prices of their export commodities and because of the higher foreign tariff walls the exports must surmount, also began raising their tariffs and setting up restrictions and embargoes of their own. At times, this was done to augment declining revenues; sometimes in retaliation against what were considered unfair restrictions by stronger nations; more often in defense of national finances and currencies. Imports of merchandise, it was argued, must be restricted in order to maintain a favorable balance of trade; to avert national bankruptcy by stopping the outflow of exchange which was desired for foreign debt payments; or to halt the outflow of gold in order to preserve the nation's currency.

Even more drastic means were resorted to when the debtor countries undertook the control of exchange, parceling out such amounts as they deemed wise to meet the absolute necessities of imports and of debt payments. Thus foreign traders and investors have been compelled to see their funds "frozen" in the debtor country, and have been unable to get payment for goods or interest or dividends on their investments. Government control of exchange transactions is in effect today in 31 countries. Thus while creditor nations were increasing barriers to imports to protect their local industries from "debt dumping" and "exchange dumping", the debtor nations were restricting their imports for protection of their finances and currencies.

Even these devices were insufficient in many cases to save the currencies; and today many countries have suspended gold payments and allowed their currencies to depreciate. Between September 1931 and June 30, 1932, the currencies of 22 countries depreciated 5 per cent or more. This, of

[229]

course, resulted in a movement for still further restrictions of imports by the gold standard countries to save themselves from the evils of exchange dumping. Thus both imports and exports continue their downward course.

In the light of these facts, it is clear that national defensive measures are inadequate, if not wholly futile. The experience of the past three years shows that preventive and defensive measures taken by one country are soon nullified by the action of another. Intended to alleviate, they actually aggravate the disease. Trade continues to drop and international nerves become more on edge. Doubtless certain defensive measures are useful temporarily to lessen the harm, the demoralization, that may result in one country from inflows of goods made cheap by sudden currency depreciation in another. These expedients at best can give only temporary relief; they cannot restore the stable conditions that would allow the development of a dependable and prosperous trade.

Regional agreements, like national defensive measures, fail to offer any great promise of solving the problem by freeing trade from its present shackles. The Ottawa pacts are not encouraging in this respect. The net result appears to be not a lowering of trade barriers. Certain new tariffs on imports into Great Britain have been established—notably the duty on wheat—and others have been raised in order to make it possible to grant preferences to the Dominions. And many of the important tariffs of the Dominions have been raised still higher against non-Empire countries, in order that the Dominions may grant Great Britain preferences without diminishing present duties.¹ A serious question may be raised whether such arrangements, reached by sharp bargaining on both sides, do not fasten upon the bargaining parties conditions that limit the wider and more adequate solutions that are necessary to free trade from its hampering restrictions. The history of “bargaining” and “preferential” agreements holds out no promise of remedy in this direction. They are defensive methods, rather than constructive attacks on the problem.

Merely to widen the areas within which trade is allowed

¹ *Economist*, London, Oct. 22, 1932, Ottawa Supplement.

greater freedom, while maintaining trade restrictions between these larger areas, is not to speed, but to delay the process of recovery. Is it likely that a closely knit British Empire, even with complete freedom of trade among its own members, can restore its normal prosperity, not to say reach higher levels of progress, if it restricts its relations with the United States of America or with a United States of Europe? The experiences of the past ten years indicate the interdependence of *continents* as well as of their component national units. The crash of the Credit Anstalt in Vienna at once reverberated in America; and the stock market crash in America in 1929 was soon felt in Europe and around the world.

Likewise, the attempts of private business organizations to control prices and trade are defensive measures that tend to raise barriers rather than to remove them. This appears to be the net result of the movement of cartels and of trade combinations such as those organized under the Webb-Pomerene Act. For the most part, they have failed to bring about stabilization over any prolonged period; often the attempts have ended in greater demoralization. We need only to recall the history of the rubber-control plan or of copper or nitrates to doubt the efficacy of such controls.

Any solution of the problem of releasing international trade from its existing barriers must, I repeat, start with the removal of the chief causes that have been responsible for the creation of such barriers. Among these causes, two are outstanding—first, the *nationalism* that has refused to recognize the economic interdependence of nations, and second, the *war debts* which, through their effects on the trade, the finances, the currencies, and the political relations of nations, have both strengthened the movement for higher tariffs and at the same time set up other defensive measures that have dammed the flow of trade.

We must keep in mind that nations have inaugurated many of their restrictive measures reluctantly and as a last resort in the face of threatened financial and monetary collapse. Retaliation, it is true, has sometimes motivated these national measures, but in large measure individual nations have erected barriers not in spite, not in unfriendliness, but hesitatingly, in the face of actual or of supposed necessity. The man in the street, the politician, and many intelligent men have too often

course, resulted in a movement for still further restrictions of imports by the gold standard countries to save themselves from the evils of exchange dumping. Thus both imports and exports continue their downward course.

In the light of these facts, it is clear that national defensive measures are inadequate, if not wholly futile. The experience of the past three years shows that preventive and defensive measures taken by one country are soon nullified by the action of another. Intended to alleviate, they actually aggravate the disease. Trade continues to drop and international nerves become more on edge. Doubtless certain defensive measures are useful temporarily to lessen the harm, the demoralization, that may result in one country from inflows of goods made cheap by sudden currency depreciation in another. These expedients at best can give only temporary relief; they cannot restore the stable conditions that would allow the development of a dependable and prosperous trade.

Regional agreements, like national defensive measures, fail to offer any great promise of solving the problem by freeing trade from its present shackles. The Ottawa pacts are not encouraging in this respect. The net result appears to be not a lowering of trade barriers. Certain new tariffs on imports into Great Britain have been established—notably the duty on wheat—and others have been raised in order to make it possible to grant preferences to the Dominions. And many of the important tariffs of the Dominions have been raised still higher against non-Empire countries, in order that the Dominions may grant Great Britain preferences without diminishing present duties.¹ A serious question may be raised whether such arrangements, reached by sharp bargaining on both sides, do not fasten upon the bargaining parties conditions that limit the wider and more adequate solutions that are necessary to free trade from its hampering restrictions. The history of “bargaining” and “preferential” agreements holds out no promise of remedy in this direction. They are defensive methods, rather than constructive attacks on the problem.

Merely to widen the areas within which trade is allowed

¹ *Economist*, London, Oct. 22, 1932, Ottawa Supplement.

greater freedom, while maintaining trade restrictions between these larger areas, is not to speed, but to delay the process of recovery. Is it likely that a closely knit British Empire, even with complete freedom of trade among its own members, can restore its normal prosperity, not to say reach higher levels of progress, if it restricts its relations with the United States of America or with a United States of Europe? The experiences of the past ten years indicate the interdependence of *continents* as well as of their component national units. The crash of the Credit Anstalt in Vienna at once reverberated in America; and the stock market crash in America in 1929 was soon felt in Europe and around the world.

Likewise, the attempts of private business organizations to control prices and trade are defensive measures that tend to raise barriers rather than to remove them. This appears to be the net result of the movement of cartels and of trade combinations such as those organized under the Webb-Pomerene Act. For the most part, they have failed to bring about stabilization over any prolonged period; often the attempts have ended in greater demoralization. We need only to recall the history of the rubber-control plan or of copper or nitrates to doubt the efficacy of such controls.

Any solution of the problem of releasing international trade from its existing barriers must, I repeat, start with the removal of the chief causes that have been responsible for the creation of such barriers. Among these causes, two are outstanding—first, the *nationalism* that has refused to recognize the economic interdependence of nations, and second, the *war debts* which, through their effects on the trade, the finances, the currencies, and the political relations of nations, have both strengthened the movement for higher tariffs and at the same time set up other defensive measures that have dammed the flow of trade.

We must keep in mind that nations have inaugurated many of their restrictive measures reluctantly and as a last resort in the face of threatened financial and monetary collapse. Retaliation, it is true, has sometimes motivated these national measures, but in large measure individual nations have erected barriers not in spite, not in unfriendliness, but hesitatingly, in the face of actual or of supposed necessity. The man in the street, the politician, and many intelligent men have too often

looked upon the acts of neighbor nations only as acts of unfriendliness, of diabolical cunning directed against Uncle Sam, whereas actually they were results of unusual conditions for which all are to a greater or less degree responsible. It is for this reason that barriers to trade not only serve as impediments to world economic relations, but are fruitful sources of misunderstanding and enmity and international friction. If trade is to be restored we must look to the removal of causes rather than to palliatives or defensive measures.

With respect to both of the major causes—namely, economic nationalism and war debts—international agreement and international action are requisite. The United States, by virtue of its tremendous economic power, bears great responsibility for leadership both in adoption of domestic policies that will tend to remove the causes of economic conflict and in establishing coöperation with other nations. The recognition of the interdependence of nations is, I believe, surely dawning among the American people; the futility of following policies of isolation is being acknowledged. Education and experience are pointing the way. The irreconcilables in international affairs must be, as they are being, forced from the stage. We are beginning to see that our tariff is not a domestic issue; it concerns all people and all nations. But this development of public opinion is slow and difficult. Will it develop in time?

Our leadership, if asserted now in calling a halt to the rising tide of tariffs at home, would have tremendous influence directly in bringing about tariff reasonableness everywhere and indirectly in establishing a saner and more hopeful outlook. It would give stimulus and hope to international agreements looking toward the lowering of tariff barriers. The world awaits our leadership in moves toward tariff modifications as it has followed our lead in tariff increases. This does not mean the abandonment of protection and a return to free trade; it does mean a more reasonable and selective protection and a move toward greater freedom of trade in the interest of our own welfare, and the welfare of all. It would indicate our willingness to coöperate in international agreements for the reduction of tariff barriers.

Of no less importance for the breaking down of trade barriers is the settlement of the war debts problem. Here,

[232]

again, the United States holds the key position. As the ultimate creditor on war-debt account, as well as one of the largest creditors on private account, our material interests are great and likewise our responsibilities. And yet, if war debts in combination with the desire for national self-sufficiency are the major factors in our international trade troubles—and they appear to be so—then war-debt settlements are imperative if permanent relief is to be obtained from excessive trade restrictions. It is possible that the debt problem can be settled without our aid—by repudiation—but who would wish to reap the harvest of evils that would follow from such a settlement? But settlement must be made. There is no escape from it.

By recognizing this fact now, by showing a willingness to discuss it, by indicating at least a trace of magnanimity in granting some relief, we can reap a harvest of good will abroad as well as material benefits at home. At Lausanne the debtor countries took a tremendous step forward in wiping out reparations. The Lausanne accord was the first ray of real hope in the whole war-debt mess. If we would consolidate the small gains made by that united effort, the United States must now coöperate in the settlement of the inter-allied debts. And we must act at once. World recovery hangs in the balance as we decide.

The economic world cannot continue to function with both trade restrictions and the existing debt agreements. Modifications in both must be secured if we wish to see the resumption of normal trade, the flow of investments, the employment of populations, the fuller utilization of the world's resources and wealth, and the general rise of the well-being of the average citizen in all lands. The task is tremendous, sacrifices of vested interests in all lands must be made, even national aspirations must be modified. But larger sacrifices will be required if settlement is not made.

Unless we choose permanently to limit our material wealth, to keep our living standards at lower rather than at higher levels, to halt the progress of industry and keep it from reaching the productivity of which it is capable; in short, unless we chose to block the progress of civilization itself we must find a way to keep open the channels of commerce between

[233]

nations. And this means the lowering of trade barriers by adopting a sane attitude toward our position and responsibilities in a world economic order, and it means a quick and satisfactory settlement of the war debts.

[234]

DISCUSSION: MAJOR PROBLEMS OF READJUSTMENT¹

CHRIS L. CHRISTENSEN

Dean of the College of Agriculture, University of Wisconsin

IN the ten minutes allotted me for discussion, I shall attempt to present a point of view which I think is basic, fundamental to the future economic and social progress of the United States.

We are not likely to get far in improving economic conditions until and unless we honestly and earnestly tackle the task of restoring the buying power among our 32 million people on our farms—and of another 20 million engaged in furnishing goods and services directly or indirectly related to the agricultural industry. When the buying power of the farms declines, its effect is immediately felt by millions of other people engaged in supplying goods and services to our farming population.

The farming plant—land, buildings, livestock and equipment—of these United States had a pre-war value (average 1910-14) of around 46 billion dollars. This rose to 79 billion in 1919 and dropped to 52 billion in 1930. Were figures available, they would undoubtedly indicate the agricultural worth of the nation at present to be less than that of the “golden era” preceding the outbreak of the world conflict in 1914.

Let us look at this great industry from another angle. The gross income of farmers approached 17 billion in 1919 and is now less than one-third of that amount. The purchasing power of one-fourth of our total population is markedly less than it was in 1914, and only one-third, measured in terms of dollars, of what it was ten years ago. This purchasing power is further reduced by the fact that fixed expenses such as interest and taxes remain at their former high levels and as a result absorb larger and larger portions of the farmers' income. Between 1919 and 1932 the annual gross income of farmers decreased from over 16 billion dollars in 1919 to about 5 billion dollars in 1932. This is a shrinkage of 11 billion dollars of annual income, an amount equal to the inter-allied debt.

It is readily apparent that an annual shrinkage of several billion dollars in gross income to farmers will have a disastrous effect upon the industrial life of the nation. It is this curtailment in the buying

¹ Discussion under the ten minute rule, at the Second Session, following the presentation of papers by Messrs. Buckland, Wolman, Murphy, Roorbach and McAneny.

power of our farm population that has slowed down in part the market demand for manufactured goods and services supplied by our urban people.

Both as individuals and as members of the public it is well for us all to appreciate that the agricultural industry of the United States presents one of our greatest problems—and at the same time our greatest business opportunity.

A basic and fundamental issue, confronting our agricultural industry, is whether the United States will adopt and pursue foreign trade policies which look toward the opening of international outlets or policies that will force agriculture to reduce its farm output to domestic requirements. This, it would seem, is a clear-cut issue. We only befog the situation when we go no deeper than to assume that the agricultural depression is merely a part of the industrial depression and that both go to make up the economic difficulty in which the world now finds itself. We shall hasten the solution if we recognize that the agricultural depression in the United States has certain distinguishing characteristics of its own and if we appreciate that the condition is due, in part at least, to causes quite separable from those affecting industry.

This farm plant of ours has been developed since the beginning of the nation's history on the basis of export outlets for all we cared to produce above domestic requirements. Normally 13 per cent of the produce sold off the farm must find buyers beyond our shores. Now only around 7 per cent leaves our ports. Industry, on the other hand, depends on exports only half as much in comparison to its total volume of production as does agriculture.

Without question the amounts of agricultural products that normally went abroad but now remain in our own storehouses exert a depressing effect upon farm prices far beyond their physical importance. This is indicated by the fact that the volume of agricultural production in the United States is not far from what it was twenty years ago, but agricultural prices are less than 60 per cent as high as they were then.

To the extent that inter-allied war debts and high tariff schedules limit the ability of foreign customers to trade and buy our cotton, tobacco, pork products and wheat they are obstacles to the development of our foreign trade and serve to retard economic recovery. Hence it seems essential that an adjustment of inter-allied debts be made and that tariff schedules be lowered.

Not unrelated to this condition is another important characteristic feature of American agriculture. This is the prevalence of a commercial type of farming. It is commercial in the sense that the average farmer is producing for a market. It stands quite in contrast

with the self-sustaining type of agriculture found in many foreign countries. In the great farming areas of the Middle West, the West and South our farmers are engaged in commercial agriculture.

This commercial farming has given our farmers a cash income that has enabled them to buy a large portion of the output of our industrial plants. The 32 million people on our farms—and another 20 million people engaged in supplying services and goods related to farming activities—have provided a substantial part of the market for our industrial goods. We have developed a type of farm economy which enables these millions to buy lumber, farm machinery, automobiles, gasoline, motor trucks and tractors, telephone service, electricity for light and power, radios and furniture.

In other words, the business of farming and the farm population have afforded a large market for the products of our industry and have drawn heavily for services upon our transportation system, banking institutions and utilities. It is obvious that what happens to agriculture is of tremendous importance to all dependent industries.

It naturally follows that the present situation brings agriculture face to face with the necessity of making a momentous decision. The United States should decide to act in accordance with a planned program upon one of two alternatives: shall the farm plant be dismantled to the reduced capacity required to meet domestic needs or shall we bend our efforts toward opening foreign markets sufficient to permit agriculture to operate at present production levels?

Never in our history have other countries in peace times created so many political barriers designed to restrict the entry into their ports of farm and forest products. Tariffs of unprecedented heights, widespread use of import quotas and licensing systems, compulsory use of domestic products, production and export subsidies, and government-fixed prices have served to shut out in goodly measure our staple commodities which normally go abroad in vast quantities.

As examples of these restrictive measures, let me remind you, for instance, that Germany has a maximum tariff on wheat of \$1.62 per bushel, a rate fully six times the amount received by many of our growers for last year's crops; that Spain will not permit the importation of wheat or flour unless the domestic price of wheat is above 53 pesetas per 100 kilograms or around \$1.20 per bushel at present rates of exchange; that Sweden maintains a monopoly on the importation of cereals, and has fixed the price of wheat at \$1.35 per bushel and rye at \$1.12 calculated on the basis of exchange at par; and that France requires that her millers use from 50 to 97 per cent home-grown wheat in the manufacture of flour. The proportion varies from time to time in accordance with the supply of the domestic product. These practices are widespread.

If we are not in position to reopen the channels of trade, then agriculture has no alternative other than to dismantle, in part, its present plant. This means, for example, that the country would reduce its cotton production on an average by one-half, its tobacco and lard by one-third, and its wheat acreage by one-fifth. All this would mean the continuance of farm foreclosures in wholesale numbers, a diminishing farm population and a lower standard of living in the country, and an attendant lessening of the domestic market for manufactured goods.

The situation affords a tremendous challenge to leaders and members of farm organizations, to educators, to those directing industry, commerce and banking, and to men elected to serve in state legislatures and Congress as well as those occupying high executive positions. The times call for the highest statesmanship.

[238]

INTRODUCTORY REMARKS¹

HON. ALANSON B. HOUGHTON

Former United States Ambassador to Germany and to Great Britain;
President of the Academy of Political Science

ONE of the privileges belonging to the Presidency of the Academy is the right on these dinner occasions to make a speech. That right is not always exercised. It will not be exercised tonight—not that the speech is not a good one; it is; I wrote it myself and I know, but, as man to man, let me say to you that the responsibility of “killing time” until you can present a speaker at the microphone at an exact minute is simply child’s play compared to having half a dozen distinguished gentlemen who must get out shortly after ten in order to sail tonight on the *Europa*. It is a responsibility which I do not feel able longer to carry. I propose without further words to put it where it belongs, on the ample shoulders of Mr. Lamont, who will act as Toastmaster, and who needs, certainly, no introduction to this audience. Mr. Lamont!

¹ At the Annual Dinner Meeting.

[239]

PRIMARY STEPS FOR BANKING REFORM

THOMAS W. LAMONT
Of J. P. Morgan and Company; Trustee of the
Academy of Political Science

NO civilized country of modern times has suffered so cruelly from unscientific and inefficient currency and banking systems as has the United States in the last hundred and forty-five years. Within that period the country has gone through a long series of banking collapses, due largely to like causes and bringing to the American community prodigious losses. The serious banking troubles of a year ago, now happily over, were but another chapter in the melancholy record.

But, contrary to the expressed opinion of many persons, this sad history has been due not to the machinations or deviltry of men or of groups of men; but largely to the inherent conditions surrounding the astonishingly rapid development of a whole continent. In banking the country's experience and mobile resources have never kept pace with its expansion and with its changing conditions. Unwise, reckless and, in occasional individual instances, dishonest management have added to the difficulties. Today in the Federal Reserve System we have a thoroughly scientific and sound foundation. But the System's scope is not yet broad enough, and the ills which the community has suffered in the last three years show clearly enough how much still remains to be remedied.

The Two Banks of the United States

For a century and a quarter attempts to develop a scientific banking system were generally blocked by the country's continuing and deep-seated distrust of centralized banking; despite the success of such banking systems in Great Britain, France and other European countries. The (First) Bank of the United States operated from 1791 up to 1811, and the Second Bank of the United States from 1816 to 1836. The operations of both these banks had on the whole been so help-

[240]

ful that, if they could have been continued, our whole currency and banking history would have been far different.

In the periods following the closing of these two institutions, wild-cat banking ran riot and confusion reigned. Mushroom institutions sprang up throughout the country. Many of them, without even a dollar of paid-in capital, issued their notes and then when times became difficult repudiated them with what, for those early days, were desperately heavy losses for the community to bear.

Further Repudiation of Bank Note Issues

The panic of 1837, which is historic in its extent and fury, came largely as a result of the mad inflation caused by the characterless banks, operating with none of the restraints that would normally be exercised by a centralized banking authority. And the panic and depression of 1857, which followed the collapse of the railway-building boom, were almost as bad. And again the guileless public, which is so slow to profit even by its own experience, suffered grievous losses from the multitude of bank failures.

A Currency System Under Way

The Civil War helped in a way to establish for the first time in our history a national banking system and a national system of uniform currency. As a consequence of the need to facilitate the sale of Government bonds for war purposes was enacted the National Currency Act of 1863-1864, which provided for the organization of banks under a Federal charter, and for a circulating medium secured by the deposit of United States Government bonds by these national banks. This was the system which, working well enough in prosperous times and badly enough in times of stress or fear, carried on until the Federal Reserve System was established in 1914.

The panic and depression of 1873 and the years just following came as an inevitable result of the repercussions and dislocations of the Civil War, and of the greenback inflation that accompanied and followed it. During a good part of the years following the country was so busily engaged in other measures, designed to establish the national finance upon a sound basis, that banking reform came slowly and haltingly.

[241]

The fight for the resumption of specie payments by the Government was won in 1878. Then the struggle for sound money as against free silver had to be fought out. That was won in the McKinley-Bryan election of 1896. Meanwhile, in 1884 and 1893 we had widespread and severe banking troubles with a climax in the disastrous currency panic of 1907.

By this time one might almost have begun to think that the American people had grown hardened to their currency troubles. But the sudden and shocking money panic of 1907, with banks failing all over the land, aroused the country, as no similar trouble had ever done before, to the urgent necessity of revising its wholly inelastic banking and currency system. Public support for the whole subject of reform was aroused and maintained through active discussion and effort to make clear the weaknesses of the situation and the necessity of radical currency reform. Although Senator Aldrich's original bill never became law, it furnished much of the ground work for subsequent legislation. In Congress there was almost a revival of the old arguments of President Andrew Jackson's time over the ill-fated Bank of the United States. The bill creating the Federal Reserve System was finally passed in the first year of President Wilson's first administration, the final organization of the System being undoubtedly accelerated by the outbreak of the Great War.

Federal Reserve System Established

In place of the usual and orthodox idea of one central bank was adopted the plan of twelve central, regional banks of issue, headed by a Federal Reserve Board at Washington, which exercises supervisory control over all the twelve. This plan functions less decisively than is desirable at times, but the recognition thus given to local autonomy has brought to the System greater strength and more complete public support than a central bank with local branches could have had. The workings of the System may seem at times cumbersome, but the marvel is that the genius of our people has evolved systems, political and otherwise, that function on the whole pretty effectively over a vast continent, and to the satisfaction of a great and independent-minded population.

It Took Forty Years for Reform to Come

We have seen how, at best, progress in banking reform is a slow business. It took forty years, following the almost complete breakdown of banking in 1873 (except in New York City and a few of the other large centres) before the country was able to evolve the Federal Reserve Act of 1913. Now we have our strong Federal Reserve System. Yet what our average citizen very naturally fails to understand is why, if the Federal Reserve has such manifest virtues, it is unable to prevent the terrific crop of banking failures which the country has witnessed in the last decade—and especially in the last two years. The answer is, upon proper analysis, not difficult to find. But before we attempt to give it let us look at some of the figures of banking failures in the eleven years, 1921-1931.

Figures of Bank Failures

In that period there have been total bank failures aggregating 9,285, with deposits thus tied up or in part dissipated of \$4,278,000,000. *Of this total only 1,698 banks were members of the Federal Reserve and almost four and a half times as many, namely 7,587 banks, were outside the system.* In the years 1930-1931 alone the bank failures totaled 3,643, and here again the proportion of non-member to member banks was almost as four and a half to one.¹ It should be added that the most of these failures were of small banks, with extremely limited capital. Therefore, one should not be misled by these figures, bad as they are, into thinking that more than a small percentage of the country's banking resources was ever tied up in failure.

No Control over Non-Member Banks

When we study the quoted figures we see at once where the leakage, so to speak, comes in. The supervision which the Federal Reserve Banks are able to exercise over member banks is of course limited. *But over non-member banks the Federal Reserve has no control whatsoever.* These non-member banks are without exception state institutions, subject to greatly vary-

¹ These figures are from the latest annual report of the Federal Reserve Board.

ing degrees and kinds of legislative requirements and of administrative supervision. So that it is no wonder that objective students of our banking system are bewildered and declare it—despite the existence of the Federal Reserve—to be no system at all.

In many instances the paid-in capital of our country banks is so slight as to be subject to impairment under the most ordinary conditions of difficult times, as we have had ample witness in recent years. It is a noteworthy fact that, in number, ninety per cent of the banks which failed in the decade of 1921-1930 were located in rural communities, subject to all the vicissitudes of crop failures, or of the expansion and deflation of business "booms;" without any of the protection afforded by a parent institution fortified with ample capital and managed by experienced men.

The Question of Branch-Banking

There is a strong movement today looking towards some plan permitting branch-banking on an extensive scale. But only eight or nine of our states permit state-wide branch-banking within their confines. A few other states permit it, but within much more limited areas. Hence branch-banking as a system, as developed so successfully in Great Britain, on the Continent of Europe and in Canada (where in each case there is an almost entire absence of banking failures), has had only limited chance of development in this country.

Almost all the failures early this year of small suburban banks around Chicago, and almost all the resultant threats to the general banking situation, could have been avoided if it had not been for the fact that the Illinois statutes permit no branch-banking of any kind within the limits of the state. It was quite impossible under the law for the large Chicago banks to attempt to serve, through branches, the important suburbs around the city. The lessons of such a situation must be glaringly obvious to the whole country. Despite the development of successful chain-banking in a few scattered instances, there is no present effective method under the law by which strong institutions in our leading financial centres can extend the benefit of their ample reserves, their experience and ordinarily careful management to the weaker banks in the outlying districts.

Hoarded Money Returned to the Banks

Although there have occurred, especially in the last two years, striking instances of mismanagement on the part of sizable institutions located in large cities, yet that melancholy phenomenon is nothing like so common as in the country banks. These well-known weaknesses that, as I have just been pointing out, afflict our rural institutions almost inevitably lead, in a time of fear such as came upon our American communities in the autumn of 1931, to hoarding on a grand scale. For a time that movement assumed considerable proportions, but the peak of it was reached about the third week of last July. Since then, the authorities figure, the tide has been steadily back to the banks and \$250,000,000 of hoarded money has been returned. Meanwhile, also, approximately \$375,000,000 of gold has flowed back into this country, thus reversing the gold export movement which had been marked in the first five or six months of the year.

The need in 1931 was not for currency, but for credit aid. The difficulty was, however, that with the extraordinary deflation in the values of commodities and securities, upon which banking credit has normally been largely based, sound credit risks were in large measure unavailable for the banks. Even with the large sums demanded for currency purposes, there has never been a time when the facilities of the Federal Reserve Banks and of the bulk of the institutions within the System have not been more than ample to meet all legitimate credit needs.

Forty-nine Different Sets of Laws

Our chief difficulty, then, as must be seen, has clearly been, not lack of more extended state control, but rather failure of organization and coördination. I have already spoken of the confusion resulting from our varying Federal and state banking laws. In banking, our country has forty-nine different sovereigns. And, as many persons long ago pointed out, a constant state of competition exists between the Comptroller of the Currency at Washington and the forty-eight Banking Superintendents of our forty-eight states. Each one of these forty-nine officials is desirous of having as many institutions

as possible registered under his jurisdiction. The consequence is that, because of this competition, laxity creeps in.

The competition as among the various systems has not been such as to make banking requirements more conservative but to make them more liberal. A promotion not of better banking but of poorer banking has been the inevitable result. This competition has not only found expression in liberalization of the respective legislative requirements governing the various banking systems, but it has also resulted, as I say, in administrative laxity in granting charters and in providing adequate supervision of the conduct of banks.

Thousands of Banks Lack Proper Safeguards

As to methods of curing our troubles, Congress can spend hundreds of thousands of dollars in new hearings and publish volumes of testimony. But it need have no hope of ever coming to the root of the evil until it realizes that *no banking system can function adequately when it comprehends within it only a limited portion of the banking community*. Today sixty per cent in number of the country's banks are outside the strong Federal Reserve System, and this sixty per cent comprises a total in banking resources of over \$12,000,000,000. These lesser banking institutions—whose aggregate resources are nevertheless so considerable—are unable or unwilling to come under the rules of the Federal Reserve System. Thus they lack its restrictions and its safeguards. And the almost unbridled license which these small banks in some states apparently have outside the Federal Reserve System tempts them frequently, as the sad record has proved, to folly and disaster.

The fact is that, despite the melancholy number of eliminations that have taken place, the country has today far too many banks. Our banking units should on the average be far larger than they are today. The small, ill-capitalized institutions should be merged so as to gain the normal stability, diversity, economy and management of the larger concerns.

One reason for the weakness of the small interior bank is that its overhead expenses are proportionately too heavy. The bank is tempted to pay too high rates of interest in order to attract deposits. These little local banks have, because of the

[246]

rapid growth of business units, of communications and of motor transport, been left in a backwater where the better business passes them by. These up-country institutions have no opportunity to diversify and average their risks. If general conditions affect their investments unfavorably, the same conditions are likely to involve them in serious losses from their localized loans, and at the same time disastrous deposit withdrawals. Moreover, far too many of these weak and unsheltered, interior banks have been managed by inexperienced persons desiring the satisfaction of becoming "bankers".

Two Vital Changes Necessary

I repeat what many others have already pointed out, namely, that no thorough-going banking reforms can be brought about until two vital changes have been accomplished. The first is *to bring all the commercial banks of the country, small as well as large, under the single aegis of the Federal Reserve System*. The second is *to establish sensible provisions for regional branch-banking, the geographical limits for each region to be carefully worked out and regulated*. Then we should have something worth talking about. Such reforms, brought about gradually, ought to begin to yield to the country some measure of banking stability.

There are many phases of the banking situation that of course I have not attempted to touch upon. From even this brief review, however, it must be apparent that the development of banking in America has been a gradual process of evolution which has by no means reached its end. Each of the banking crises to which I have alluded has taught the community some one lesson, but each new disaster has revealed a fresh weakness to be remedied. Indeed, banking development in this country has been a slow and painful growth. No pilgrim's progress could have been more arduous or beset with greater pitfalls.

The Trust that Is Reposed in the Present System

The proposition to bring all the commercial banks of the country into the Federal Reserve System has sometimes been opposed on the allegation that the System had already proved itself to be a "Money Trust", and that its authority should

[247]

be curtailed rather than extended. As to such criticism it may be fair to point out that, if the System had actually proved itself to be anything in the nature of a money trust, it was certainly a benevolent and coöperative one; for the record which I have quoted shows that depositors in the banks and trust companies that were members of the System were enormously benefited by such membership; and that within the System—with its care and safeguards—they enjoyed comparative immunity from difficulty as compared with depositors in the banking units which had failed to take advantage of its strength.

The object of banking legislation is not to give advantages to, or to impose penalties upon, banks or bankers. It is to provide the public with safe money and credit, and safe depositories of their funds. In the modern world bank checks drawn against bank deposits circulate as money, and the gold reserves of the Federal Reserve Banks are the base upon which rest not only the Federal Reserve notes issued by the Federal Reserve Banks, but the deposits of the member banks and of non-member banks as well, also the checks that circulate against these deposits. After the Civil War, state bank notes, which had had such a deplorable record of repudiation, were taxed out of existence and national bank notes substituted in our currency system. The reform was incomplete, because it dealt only with one side of the bank's function, the note-issuing power. It did not deal with the other side of the banking picture, the power to receive deposits which circulate in the form of checks and which, as I say, are supported upon the same gold base held by the Federal Reserve Banks. We must come to regard a banking charter not as a privilege conferred upon a chosen few, or upon an unselected many, in order that they may make money with other people's money; but as a *public trust*, and in that sense, and in that sense only, as a money trust. It is the plain duty of the community to see to it that the interest of the American people in the safety of their deposits, and of the whole country in the sufficiency and soundness of our banking system, should be put before the special interest of any bank or banker, great or small.

The Boon of the Federal Reserve System

The hope for progress towards real orderliness and stability lies, as it always does in these matters, in an aroused and intelligent public opinion, and in constant study by the experts of methods to strengthen the Federal Reserve System. No person of intelligence, studying the actual workings of this System, can have failed to be impressed with the immeasurable benefits which it has brought to American industry and commerce. It is hard, too, to see how the Government could ever have carried on its war and post-war financing without the new System. Without it, inflation on an almost disastrous scale (witness the examples of the European countries) might well have been resorted to. In the midst of the distress through which portions of the banking community have been passing in these last few years, the constructive accomplishments of our Federal Reserve Banks may have been somewhat lost sight of. Yet without the resources and the prudent, far-sighted handling of those institutions our plight would have been incalculably worse than it has been. All twelve of them have been like isles of safety, harbors of refuge in the midst of a violent storm.

Let me point out one recent development of the Federal Reserve System that has already proved of immense importance. Up to February of 1932, the System still lacked, under the law, certain powers that it needed to render its scope of operation more elastic and practicable. Such powers the central banks of other countries have always possessed. Through the provisions of the Glass-Steagall law, passed early in 1932, somewhat similar powers were provided for the Federal Reserve System. Under these the System now has the authority to buttress the credit situation where there is the greatest need. Already these extended powers have enabled the System to lighten immeasurably the burdens of the community.

Aided by the provisions of this Act the Federal Reserve Banks have for the last six months been pursuing with wisdom and vigor a so-called open market policy, which has already proved itself to be a great factor in arresting the headlong deflation of credit and prices which was becoming so disastrous.

American Gold Standard not to be Shaken

Finally, it has been the Federal Reserve System, and the wise conduct of it under the leadership of the Federal Reserve Board at Washington, and of the twelve regional banks, that have maintained impregnable for our country the sound, gold standard dollar. Remember this, my friends: among all the alarums and excursions of the last twelve-month we have never been near the point of abandoning the gold standard. No difficulties arising abroad, no external pressure, can or will drive us from that standard. Only the folly of rank inflation at home could endanger it. A Democratic administration, just like the steadfast Republican one before it, will continue to uphold the complete integrity of it. Make no mistake: in a dark troublous world America and the American dollar are, as to material factors, the safest things in all the world to tie to.

[250]

WORLD AGRICULTURE AND DISARMAMENT

VISCOUNT ASTOR

I COUNT it indeed a great privilege and honor to be here this evening as your guest. Mr. Lamont, now that I come to think of it, as I own the hotel, I am not sure that I am not your host. But anyway I do appreciate your invitation to be here this evening, just as I have appreciated the opportunity you have given me during the course of the day of listening to the conference which you have had here where experts and economists have indicated to you the road which leads to recovery.

I am neither an expert nor an economist. I am only a politician, and in England a politician is the man who gets blamed when the experts and the economists make a mess of things. I have been a politician, a member of the legislature, for twenty-two years. I may say I have had a double dose of it as I also have a politician in the home.

You are going to have speeches from experts and economists, but before sitting down, I will just tell you very briefly of a very interesting experience which I have had during the last two years. Two years ago I was asked to be chairman of a study group set up by the Institute of International Affairs in London and this group was asked to make a survey of world agriculture. Our report will be published in a few weeks' time. If you read it, you will find that we have there made a pretty comprehensive survey. We have tried to assess the relative importance of different agricultural commodities in world trade. We have dealt with world prices, with the question of overproduction, with the changing habits of consumers and the effect of this upon the producers. We have tried to examine the protective measures, tariffs, quotas, subsidies, price stabilization plans, and so forth, which different governments have adopted in order to assist their farmers. We have tried to deal with the whole problem in a practical way and not as if we were living in an ideal world.

A very interesting thing happened when we got to the end.

[251]

After making this survey, and putting the facts before the readers of the report, we made one deliberate digression. I haven't got the exact words by me, but I should like to paraphrase the ending of our report. We conclude by stating that after examining all the steps taken by different governments throughout the world, such as tariff duties, quotas, subsidies, and price stabilization, in order to improve the position of the farmers, after making full allowance for the local benefit derived by the farmers in the countries where those devices have been adopted, we desire to bring out the fact that in our opinion the prosperity of the farmers of the world would be more advanced by a successful disarmament conference than by any of these devices.

That is to say, that in agriculture as in industry and everything else, there can be no recovery unless there is confidence; there can be no prosperity unless there is peace; and there can be no peace unless the peoples of the world go forward with a constructive, courageous, far-sighted policy of international coöperation.

[252]

STEPS TOWARD RECOVERY

SILAS H. STRAWN

President of the American Section of the International Chamber of Commerce; former President of the American Bar Association; former President of the United States Chamber of Commerce

IN taking steps toward recovery, I submit that we must consider, first, the steps which we should take in our own country and, second, those which we should take in collaboration with other countries.

I. Steps We Should Take in the United States

I believe the people of this country are now pretty thoroughly aroused to a realization of the fact that our first and most imperative step toward recovery is in the direction of reduction in the costs of government, federal, state and local.

For several years prior to the debacle of October, 1929, we were as prodigal in our governmental affairs as we were extravagant in our private lives. The people demanded of governments everything they could think of in the way of comforts and social service, regardless of the expense, and not realizing that the obligations they incurred in the form of funded debts and deferred installment tax payments must ultimately be met by taxes. They assumed the interest, at least, could be paid and the principal would be passed on to the next generation. So long as the era of prosperity lasted, inflated incomes enabled our people to meet the rising costs of government, but since the depression began defaults have occurred with constantly increasing rapidity and severity. Today the painful fact is that countless millions of state and local governmental obligations are in default, as to both principal and interest. In some of our larger cities, the situation is so serious that policemen, firemen, nurses, school teachers, judges and other officials have received no pay for months, and there is no immediate prospect of relief. The people, as I have said, have become thoroughly awakened to a realization of the fact that the costs of government, federal, state and local, must be reduced.

[253]

The total cost of government, federal, state and local, in 1890 was 855 millions; in 1913, 2,919 millions; in 1923, 9,920 millions; in 1929, 13,048 millions, and now it is more than 14 billions; or, on a per capita basis, in 1890 it was \$13.56; in 1913, \$30.24; in 1923, \$88.94 and in 1929, \$107.37.

In other words, in 1913 the cost of government took about one dollar for every \$15.50 of our national income. Now it takes about one dollar for every \$3.00 of our national income.

During the last two years, the receipts of our national government have been practically cut in two, while expenditures have continued at approximately the level reached at the peak of industrial prosperity. The costs of government have increased more rapidly than the population, while the national income has rapidly declined. The earnings of all the people have suffered drastic reductions and now the costs of government represent a percentage of national income which the people of no nation can long endure.

Notwithstanding the vigorous efforts of the Administration to bring about a reduction in the costs of the federal government during the last session of Congress, no appreciable reduction was made. The directors of the Chamber of Commerce of the United States, at their meeting held in August last, adopted a resolution that, regardless of the efforts of the President and some of the members of the last Congress to bring about a reduction in the costs of the federal government, further savings totaling 800 million dollars might be accomplished.

As an example of the reckless expenditures, I might mention one item, that of War Service Pensions and other Veterans' benefits. The total amount of those benefits in this country in the 141 years from 1790 to 1931 was about 9 billions. For the fiscal year 1931 we paid for veterans 1 billion 13 millions, or one-ninth of the total which had been expended for this purpose during the previous 141 years. The 1931 expenditures represented 24 per cent of all federal expenditures for that year and constituted one of the principal factors, if not the most important factor, in the government cost problem. For Veterans' War Relief, the United States spends 35 times as much as Italy, which had 16 times as many dead and wounded in the World War.

No good American citizen should complain against according to those who have suffered some disability, mental or physical, in the service of their country, a full measure of relief for themselves and their dependents, but it will become increasingly more difficult to persuade the taxpayers, not the vote-seekers, that we should continue to support 375,000 ex-service-men, who are drawing pensions of from 12 dollars to 40 dollars per month for disabilities admittedly not connected with war service. The government today is paying out millions of dollars a year to those who claim that they are suffering from such disabilities as astigmatism, inferiority complex (called social ineptitude in the record), tuberculosis, psychosis and other troubles, that come, not as a result of serving their country but which are usually attendant upon advancing age.

The costs of state and local governments have increased even more rapidly than have the costs of the federal government. This is due, as I have said, to the continuing demand of our citizens for more and better improvements and service of all kinds. For example, borrowing in the State of New York has increased 221 per cent since the war; in Illinois, 8,777 per cent; California, 1,099 per cent; Missouri, 1,842 per cent; New Jersey, 10,476 per cent and Michigan, 808 per cent.

Since the war, the spending in New York City has increased 180 per cent; in Chicago, 339 per cent; Philadelphia, 277 per cent; Detroit, 1,330 per cent; Boston, 163 per cent and San Francisco, 388 per cent.

The funded debt of the City of New York has increased from \$794,930,288 in 1910 to \$2,246,100,944 in 1932, and the funded debt of the City of Detroit from \$23,513,064 in 1918 to \$349,567,000 in 1932. Due to Illinois' constitutional limitation, the funded debt of Chicago has not increased so rapidly as that of some other cities but the tax levy has far outstripped the city's growth. For example, the population has increased 55 per cent in the last twenty years, while the tax levy during that period has increased 560 per cent.

This appalling increase in the cost of government is reflected in the taxes payable not only by those who live in cities and villages but by those living on the farms as well. Con-

temporarily with the increase in the cost of government, the price of farm products has gone down, so that there are hundreds of thousands of farms in this country today which have been sold for taxes, resulting in the poor farmers being evicted from their homes and becoming public charges. In such cases no revenue is being received by the taxing bodies. A like condition obtains in the cities, where property worth hundreds of millions of dollars has been sold for taxes.

The people are thoroughly awakened to the necessity of reducing the cost of government.

Office-holders, the tax-eaters, frequently have no sense of responsibility for the burden they are imposing on the taxpayers. They are actuated solely by the desire to hold their jobs and to increase the number of jobs, so they may be promoted to more lucrative places. Taxpayers, generally, are not organized to meet the raids upon the public treasuries of blocs, groups and others, who are influenced by purely selfish motives. Many of our Congressmen are only half convinced that the country actually wants economy; and in the last session of the Congress they went only so far as to make it possible to retrace their steps without difficulty or appearance of inconsistency. I would not assert that the Congressmen do not faithfully represent their constituents but their ears are much better attuned to the persistent wails of the job-hunters than they are to the less frequent voices of the taxpayers.

To meet the emergencies of the depression, the Congress passed such measures as the amendment to the Federal Land Bank Act, the Reconstruction Finance Corporation Act and the Home Loan Bank Bill. These were all necessary and vital to preserve our national credit and to relieve distress, but they were more palliative than remedial. All of the funds to meet the cost of government thus increased must ultimately be met by increased taxes. We cannot pay the bill by "soaking the rich." There are few rich left to "soak." Too high taxes on income drive capital away from investment in productive enterprises and force it into government securities, which are tax-exempt and must remain so until the Constitution is amended. Government securities were made tax exempt for the obvious purpose of lowering the rate of interest which the taxpayer must ultimately pay. Therefore, unduly

"soaking the rich" hurts the poor more than it does the rich.

For the fiscal year ending June 30, 1932, our federal deficit was \$2,885,000,000. How much it will be this year no one can accurately forecast. Certain it is that it will be very large. This must be so because of our great depreciated revenue, both from income taxes and customs, on account of our greatly reduced foreign trade.

Therefore, I submit that the first step we must take is toward an immediate and drastic reduction in the cost of government, federal, state and local. The integrity and the credit of our governments must be preserved. We must balance our budgets. We cannot repudiate the obligations we have incurred. We must meet them, whatever the sacrifice. But we must lighten the load for the future.

II. *International Relations*

Having considered the most important step we should take in our own country, let us now consider our international relations. I never have been impressed by the argument that, by reason of our great variety of climate and diversity of natural resources, we are the richest and most self-sufficient country on earth, and that the percentage of our foreign to our domestic trade is so small that we can isolate ourselves from the rest of the world and prosper by living on our own. Of course we can live better than any other country on our own, for the reasons I have given, but the people of this country cannot return to the prosperity they enjoyed in 1925 unless we maintain our foreign trade. Foreign trade cannot be all on one side. You have to have imports to counter-balance exports and every country likes to have the balance of trade in its favor. That is what we have done heretofore, and what we want to do. It can be done only through collaboration with the other nations of the earth. Many things that we cannot produce we have to import. Some things that we can produce we import because it can be done cheaper.

I am not here to discuss the tariff. You doubtless have heard about that this afternoon. I heard Mr. Young discuss it the other night in a political speech. I did not agree with him entirely, though there is nobody whom I admire more. The plain truth is that no tariff schedule is perfect. It is

generally the result of a lot of special pleaders importuning the Congress until Congress is worn out. It is more or less a local question. As has been said many years ago, it depends on how much it affects or helps your interests.

We differ a bit from other countries with respect to tariff or trade barriers because we have forty-eight great states among which there are no barriers. Our internal trade moves freely and does not float up and down with the rise and fall of exchanges.

Heretofore we have seemed to be able to pay the tariff, and anything we wanted seemed to climb over the tariff barriers.

Nevertheless we have to look into the situation. We have to have an appreciation of the fact that we cannot consistently exact tariff duties greater than the difference of cost of production here and abroad. I do not think the people of this country can continue to maintain tariff schedules in excess of the differences in production costs. If they do, they will not have any exports.

This problem has a direct bearing on employment. Two and one-half millions of our citizens are dependent on foreign trade. That is only about 10 per cent, but it represents the difference between prosperity and just getting along.

Any one who has given the subject the most casual consideration must know that commercially, financially and industrially, if indeed not socially, the whole civilized world may be regarded as a unit. To establish peace and restore the world to a normal and prosperous condition, the people of all nations should realize that their countries would be more benefited by mutual coöperation than by isolation. The happiness and prosperity of every people at this time depend to a greater extent than ever before upon friendly relations among all nations.

Assuming the truth of that statement to be undeniable, I am not unmindful of the fact that the officials of every government and, to a lesser degree, the citizens of every nation, are motivated by an instinctive nationalistic spirit. In other words, in their contact with other countries the dominant thought seems to be to gain some advantage or concession for their own country, even though it be temporary and national rather than permanent and international in its ultimate effect.

I need not mention existing economic and financial conditions. Everyone knows that world trade is greatly disorganized and that the breakdown in the mechanism of international credit and finance handicaps recovery from the economic and financial maladjustment.

The fallen commodity prices, the decline in foreign trade, the halt in the movement of capital, either for the purpose of investment or for ordinary commercial transactions, and the growth of unemployment, have precipitated great difficulties in private and public finance. This has led to the abandonment of the gold standard in twenty-two countries and governmental control over the purchase and sale of foreign exchange in thirty-one countries. Currency has depreciated in some countries as much as 55 per cent, the net result of which is that the existing tariff rates on more than 52 per cent of the imports into this country for the first nine months of 1932, coming from depreciated currency countries, have paid very much less than the tariff schedule contemplated. The articles thus imported are being sold upon our markets at prices below anything with which our local manufacturers can compete.

A committee of the Chamber of Commerce of the United States has made a recommendation upon which they will insist in the next Congress, namely, that prompt action be taken to balance the difference in production costs due to foreign currency depreciation. We ought to have a tariff sufficient to represent the difference between the cost of labor and of production here and abroad. Personally I have abiding confidence in the ability and capacity of the Tariff Commission. That agency is available to any one who thinks the tariff is too high or too low.

We are all more or less familiar with the conditions which necessitated the Moratorium, declared on the recommendation of President Hoover in 1931. Everyone will agree that the Lausanne Agreement, in settlement of the German reparations, was a distinct step in advance toward world peace, and that when it is ratified one of the disturbing elements in international finance and politics will be disposed of.

Debts Due the United States. It would serve no good purpose on this occasion to discuss different opinions regarding the extent to which European indebtedness to the United

States looms as a factor in world affairs. Some hold that the war debts have largely been responsible for precipitating the economic decline and urge their cancellation in the interests of world recovery and continuing prosperity. Others regard these debts as a disturbing and retarding influence in world affairs and consider them a subject for calm reëxamination by their governments and for further settlement and adjustment on the fairest basis possible. Still others minimize the effect of the debts on the world situation and say that they can be paid on existing terms without undue burden on the debtors or the rest of the world.

Origin of the Debts. It is a matter of common knowledge that these debts are made up of pre-armistice and post-armistice obligations, consisting of cash loans, surplus stocks and relief supplies left by our armies in Europe. The pre-armistice obligations of our fifteen principal debtor countries totaled \$6,879,385,000. The post-armistice debts, being cash loans, totaled \$2,533,262,000, and the surplus stocks and relief supplies amounted to \$722,825,000, making a total of \$10,135,472,000. In general, these obligations were payable on demand, with interest at 5 per cent.

These obligations afterwards were funded, the approximate annual average interest rate of the debts so funded being 2.14 per cent. In the funding settlement the unpaid accrued interest was figured not at the rate of 5 per cent as contemplated in the original obligations, but at $4\frac{1}{4}$ per cent from the date of the loans to December 15, 1922, and at 3 per cent from that date to the date of the funding agreements. In the case of Belgium, there was no charge for interest on loans made before the armistice. The result of such funding was a reduction of the "present value" of the debts by 23.9 per cent if interest is discounted at 3 per cent, or by 43.1 per cent if discounted at $4\frac{1}{4}$ per cent, or by 51.3 per cent if discounted at 5 per cent. This was a very substantial reduction of the amounts to be paid by the several countries. None can deny the legal obligations of the governments whose debts were funded, nor the extreme generosity of the United States in reducing the amounts and in funding them on an average interest basis of 2.14 per cent, when at the time we were paying $4\frac{1}{4}$ per cent for the money.

[260]

The Present Status of the Debts. The settlements with the different countries were not worked out on a standard inflexible plan. They were negotiated with representatives of each of the debtor countries in the light of the situation in each particular country. There were taken into consideration the general economic and financial positions of the countries, their natural resources, their trade, the national economic and fiscal burdens each had to face, and the standards of living of their people. The World War Debt Commission, in reporting its work to the Congress, commented that the foreign debtor

must be permitted to preserve and improve its economic position, to bring its budget into balance, and to place its finances and currency on a sound basis, and to maintain, and, if possible, to improve the standard of living of its citizens. No settlement which is oppressive and retards the recovery and development of the foreign debtor is to the best interests of the United States or of Europe.

In other words, on the one side there was an expression of a desire of the debtor governments to meet their obligations and on the other side an evidence of the willingness of the United States to make such concessions as the world conditions seemed to require and as the interests of our citizens in a prosperous Europe seemed to justify.

Alternative Courses of Action on the Debts. As funded, the total amount of the principal owed to the United States by fifteen debtor countries is \$11,261,178,000. The debt holiday ended on June 30, 1932. Further payments to the United States on principal and interest are due December 15. Our government has received requests from the debtor governments for reconsideration of the terms of the debt agreements. It would seem, therefore, that our government is faced with the responsibility of deciding (1) whether the debts shall be paid, principal and interest, in accordance with the agreements; (2) whether further payments shall be postponed; (3) whether the refunding agreements shall be modified and the debts reduced; or (4) whether the debts shall be completely cancelled. I shall briefly discuss those propositions.

Shall the Debts be Paid in Full, Principal and Interest, in Accordance with their Terms? In considering that proposi-

[261]

States looms as a factor in world affairs. Some hold that the war debts have largely been responsible for precipitating the economic decline and urge their cancellation in the interests of world recovery and continuing prosperity. Others regard these debts as a disturbing and retarding influence in world affairs and consider them a subject for calm reëxamination by their governments and for further settlement and adjustment on the fairest basis possible. Still others minimize the effect of the debts on the world situation and say that they can be paid on existing terms without undue burden on the debtors or the rest of the world.

Origin of the Debts. It is a matter of common knowledge that these debts are made up of pre-armistice and post-armistice obligations, consisting of cash loans, surplus stocks and relief supplies left by our armies in Europe. The pre-armistice obligations of our fifteen principal debtor countries totaled \$6,879,385,000. The post-armistice debts, being cash loans, totaled \$2,533,262,000, and the surplus stocks and relief supplies amounted to \$722,825,000, making a total of \$10,135,472,000. In general, these obligations were payable on demand, with interest at 5 per cent.

These obligations afterwards were funded, the approximate annual average interest rate of the debts so funded being 2.14 per cent. In the funding settlement the unpaid accrued interest was figured not at the rate of 5 per cent as contemplated in the original obligations, but at $4\frac{1}{4}$ per cent from the date of the loans to December 15, 1922, and at 3 per cent from that date to the date of the funding agreements. In the case of Belgium, there was no charge for interest on loans made before the armistice. The result of such funding was a reduction of the "present value" of the debts by 23.9 per cent if interest is discounted at 3 per cent, or by 43.1 per cent if discounted at $4\frac{1}{4}$ per cent, or by 51.3 per cent if discounted at 5 per cent. This was a very substantial reduction of the amounts to be paid by the several countries. None can deny the legal obligations of the governments whose debts were funded, nor the extreme generosity of the United States in reducing the amounts and in funding them on an average interest basis of 2.14 per cent, when at the time we were paying $4\frac{1}{4}$ per cent for the money.

[260]

The Present Status of the Debts. The settlements with the different countries were not worked out on a standard inflexible plan. They were negotiated with representatives of each of the debtor countries in the light of the situation in each particular country. There were taken into consideration the general economic and financial positions of the countries, their natural resources, their trade, the national economic and fiscal burdens each had to face, and the standards of living of their people. The World War Debt Commission, in reporting its work to the Congress, commented that the foreign debtor

must be permitted to preserve and improve its economic position, to bring its budget into balance, and to place its finances and currency on a sound basis, and to maintain, and, if possible, to improve the standard of living of its citizens. No settlement which is oppressive and retards the recovery and development of the foreign debtor is to the best interests of the United States or of Europe.

In other words, on the one side there was an expression of a desire of the debtor governments to meet their obligations and on the other side an evidence of the willingness of the United States to make such concessions as the world conditions seemed to require and as the interests of our citizens in a prosperous Europe seemed to justify.

Alternative Courses of Action on the Debts. As funded, the total amount of the principal owed to the United States by fifteen debtor countries is \$11,261,178,000. The debt holiday ended on June 30, 1932. Further payments to the United States on principal and interest are due December 15. Our government has received requests from the debtor governments for reconsideration of the terms of the debt agreements. It would seem, therefore, that our government is faced with the responsibility of deciding (1) whether the debts shall be paid, principal and interest, in accordance with the agreements; (2) whether further payments shall be postponed; (3) whether the refunding agreements shall be modified and the debts reduced; or (4) whether the debts shall be completely cancelled. I shall briefly discuss those propositions.

Shall the Debts be Paid in Full, Principal and Interest, in Accordance with their Terms? In considering that proposi-

[261]

tion it must be remembered that the debts are admittedly legal. They represent value received at the time they were made, and in principle the integrity of governmental obligations greatly outweighs any arguments that have been advanced in favor of cancellation. The Congress has already spoken quite definitely on the subject of cancellation and I submit it would be futile at this time to bring that subject again before the Congress. Personally, I see no sound basis for entertaining proposals for cancellation of the debts. That brings us to a consideration of the question:

Whether Further Payment Shall be Postponed? This subject cannot be dealt with on a general plan but must be carefully considered with reference to the ability of each country to meet its obligations. It is evident that certain of the debtor countries will be unable to meet payments presently falling due, and, therefore, it would seem that temporary postponement of payment of their obligations to the United States is necessary. On the other hand, some of the countries are able to pay in accordance with their agreements.

The subject involves a careful consideration of all the facts, with due regard not only to the conditions of the debtor countries but also with respect to the fiscal status of our own country. As I have already said, the burden of taxation upon our own citizens is now almost confiscatory, and postponement of the payment of \$250,000,000 a year by way of interest, aside from the payments on account of principal, necessarily increases the burden of our taxpayers to that extent.

Shall the Funding Agreements be Modified and the Debts Reduced? The same elements should be taken into consideration in deciding this question as those which must be considered in deciding the necessity of postponement. Every country is faced with the difficulty of balancing its budget, of meeting its obligations, of raising the needed taxes, of effecting economies in public expenditures, and of establishing and assuring the continuance of sound currency. Every country has been struggling to restore its economic activity and revive its trade. In 1921 the international trade of more than one hundred countries reached a total of about 43 billion dollars annually. This increased consistently until 1929, when it

reached a level of about 68 billions. For the fifteen countries that have funded their debts to this country, the total international trade grew from 15 billions of dollars in 1921 to 22½ billions in 1929. By 1931 the total dollar value of the international commerce of the world had dropped even below pre-war levels, or from the peak of 68 billions in 1929 to less than 40 billions in 1931. In addition, the wholesale prices in the world's chief markets went steadily downward in 1930 and 1931 until now they are below the 1913 levels. As the depression continued the financial position of many countries became more difficult. Resources diminished until finally Great Britain and twenty-one other countries were compelled to go off the gold standard.

Obviously, this had a very serious effect upon the trade of the United States with Europe. Nationalism became intensified, the European countries raised their trade barriers and put in all kinds of trade restrictions, such as quotas, licenses and so on. Then came the British Empire Conference at Ottawa, the result of which, it is estimated, will have a prejudicial effect on American exports to the extent of upwards of 200 millions of dollars a year.

Armaments. In considering the applications for postponement or reduction of debts, it is pertinent to consider the amount of money being spent by the debtor countries for armaments. This amount has substantially increased in all of the debtor countries since 1913. In that year the world expenditure for armaments was \$2,531,000,000. The amount expended in 1930 was \$4,128,000,000. It is now estimated that the amount of the annual expenditures for armaments throughout the world reaches a total of 5 billion dollars. The combined figures for the six great powers—Great Britain, France, Italy, Japan, Russia and the United States—show an increase of 65 per cent. Budgeted expenditure for national defense for the year 1932, per capita, was:

France	\$10.79
United Kingdom	6.77
Italy	6.72
Belgium	3.61
Poland	3.00
United States	5.69

tion it must be remembered that the debts are admittedly legal. They represent value received at the time they were made, and in principle the integrity of governmental obligations greatly outweighs any arguments that have been advanced in favor of cancellation. The Congress has already spoken quite definitely on the subject of cancellation and I submit it would be futile at this time to bring that subject again before the Congress. Personally, I see no sound basis for entertaining proposals for cancellation of the debts. That brings us to a consideration of the question:

Whether Further Payment Shall be Postponed? This subject cannot be dealt with on a general plan but must be carefully considered with reference to the ability of each country to meet its obligations. It is evident that certain of the debtor countries will be unable to meet payments presently falling due, and, therefore, it would seem that temporary postponement of payment of their obligations to the United States is necessary. On the other hand, some of the countries are able to pay in accordance with their agreements.

The subject involves a careful consideration of all the facts, with due regard not only to the conditions of the debtor countries but also with respect to the fiscal status of our own country. As I have already said, the burden of taxation upon our own citizens is now almost confiscatory, and postponement of the payment of \$250,000,000 a year by way of interest, aside from the payments on account of principal, necessarily increases the burden of our taxpayers to that extent.

Shall the Funding Agreements be Modified and the Debts Reduced? The same elements should be taken into consideration in deciding this question as those which must be considered in deciding the necessity of postponement. Every country is faced with the difficulty of balancing its budget, of meeting its obligations, of raising the needed taxes, of effecting economies in public expenditures, and of establishing and assuring the continuance of sound currency. Every country has been struggling to restore its economic activity and revive its trade. In 1921 the international trade of more than one hundred countries reached a total of about 43 billion dollars annually. This increased consistently until 1929, when it

reached a level of about 68 billions. For the fifteen countries that have funded their debts to this country, the total international trade grew from 15 billions of dollars in 1921 to 22½ billions in 1929. By 1931 the total dollar value of the international commerce of the world had dropped even below pre-war levels, or from the peak of 68 billions in 1929 to less than 40 billions in 1931. In addition, the wholesale prices in the world's chief markets went steadily downward in 1930 and 1931 until now they are below the 1913 levels. As the depression continued the financial position of many countries became more difficult. Resources diminished until finally Great Britain and twenty-one other countries were compelled to go off the gold standard.

Obviously, this had a very serious effect upon the trade of the United States with Europe. Nationalism became intensified, the European countries raised their trade barriers and put in all kinds of trade restrictions, such as quotas, licenses and so on. Then came the British Empire Conference at Ottawa, the result of which, it is estimated, will have a prejudicial effect on American exports to the extent of upwards of 200 millions of dollars a year.

Armaments. In considering the applications for postponement or reduction of debts, it is pertinent to consider the amount of money being spent by the debtor countries for armaments. This amount has substantially increased in all of the debtor countries since 1913. In that year the world expenditure for armaments was \$2,531,000,000. The amount expended in 1930 was \$4,128,000,000. It is now estimated that the amount of the annual expenditures for armaments throughout the world reaches a total of 5 billion dollars. The combined figures for the six great powers—Great Britain, France, Italy, Japan, Russia and the United States—show an increase of 65 per cent. Budgeted expenditure for national defense for the year 1932, per capita, was:

France	\$10.79
United Kingdom	6.77
Italy	6.72
Belgium	3.61
Poland	3.00
United States	5.69

The total cost of government, federal, state and local, in 1890 was 855 millions; in 1913, 2,919 millions; in 1923, 9,920 millions; in 1929, 13,048 millions, and now it is more than 14 billions; or, on a per capita basis, in 1890 it was \$13.56; in 1913, \$30.24; in 1923, \$88.94 and in 1929, \$107.37.

In other words, in 1913 the cost of government took about one dollar for every \$15.50 of our national income. Now it takes about one dollar for every \$3.00 of our national income.

During the last two years, the receipts of our national government have been practically cut in two, while expenditures have continued at approximately the level reached at the peak of industrial prosperity. The costs of government have increased more rapidly than the population, while the national income has rapidly declined. The earnings of all the people have suffered drastic reductions and now the costs of government represent a percentage of national income which the people of no nation can long endure.

Notwithstanding the vigorous efforts of the Administration to bring about a reduction in the costs of the federal government during the last session of Congress, no appreciable reduction was made. The directors of the Chamber of Commerce of the United States, at their meeting held in August last, adopted a resolution that, regardless of the efforts of the President and some of the members of the last Congress to bring about a reduction in the costs of the federal government, further savings totaling 800 million dollars might be accomplished.

As an example of the reckless expenditures, I might mention one item, that of War Service Pensions and other Veterans' benefits. The total amount of those benefits in this country in the 141 years from 1790 to 1931 was about 9 billions. For the fiscal year 1931 we paid for veterans 1 billion 13 millions, or one-ninth of the total which had been expended for this purpose during the previous 141 years. The 1931 expenditures represented 24 per cent of all federal expenditures for that year and constituted one of the principal factors, if not the most important factor, in the government cost problem. For Veterans' War Relief, the United States spends 35 times as much as Italy, which had 16 times as many dead and wounded in the World War.

No good American citizen should complain against according to those who have suffered some disability, mental or physical, in the service of their country, a full measure of relief for themselves and their dependents, but it will become increasingly more difficult to persuade the taxpayers, not the vote-seekers, that we should continue to support 375,000 ex-service-men, who are drawing pensions of from 12 dollars to 40 dollars per month for disabilities admittedly not connected with war service. The government today is paying out millions of dollars a year to those who claim that they are suffering from such disabilities as astigmatism, inferiority complex (called social ineptitude in the record), tuberculosis, psychosis and other troubles, that come, not as a result of serving their country but which are usually attendant upon advancing age.

The costs of state and local governments have increased even more rapidly than have the costs of the federal government. This is due, as I have said, to the continuing demand of our citizens for more and better improvements and service of all kinds. For example, borrowing in the State of New York has increased 221 per cent since the war; in Illinois, 8,777 per cent; California, 1,099 per cent; Missouri, 1,842 per cent; New Jersey, 10,476 per cent and Michigan, 808 per cent.

Since the war, the spending in New York City has increased 180 per cent; in Chicago, 339 per cent; Philadelphia, 277 per cent; Detroit, 1,330 per cent; Boston, 163 per cent and San Francisco, 388 per cent.

The funded debt of the City of New York has increased from \$794,930,288 in 1910 to \$2,246,100,944 in 1932, and the funded debt of the City of Detroit from \$23,513,064 in 1918 to \$349,567,000 in 1932. Due to Illinois' constitutional limitation, the funded debt of Chicago has not increased so rapidly as that of some other cities but the tax levy has far outstripped the city's growth. For example, the population has increased 55 per cent in the last twenty years, while the tax levy during that period has increased 560 per cent.

This appalling increase in the cost of government is reflected in the taxes payable not only by those who live in cities and villages but by those living on the farms as well. Con-

temporarily with the increase in the cost of government, the price of farm products has gone down, so that there are hundreds of thousands of farms in this country today which have been sold for taxes, resulting in the poor farmers being evicted from their homes and becoming public charges. In such cases no revenue is being received by the taxing bodies. A like condition obtains in the cities, where property worth hundreds of millions of dollars has been sold for taxes.

The people are thoroughly awakened to the necessity of reducing the cost of government.

Office-holders, the tax-eaters, frequently have no sense of responsibility for the burden they are imposing on the taxpayers. They are actuated solely by the desire to hold their jobs and to increase the number of jobs, so they may be promoted to more lucrative places. Taxpayers, generally, are not organized to meet the raids upon the public treasuries of blocs, groups and others, who are influenced by purely selfish motives. Many of our Congressmen are only half convinced that the country actually wants economy; and in the last session of the Congress they went only so far as to make it possible to retrace their steps without difficulty or appearance of inconsistency. I would not assert that the Congressmen do not faithfully represent their constituents but their ears are much better attuned to the persistent wails of the job-hunters than they are to the less frequent voices of the taxpayers.

To meet the emergencies of the depression, the Congress passed such measures as the amendment to the Federal Land Bank Act, the Reconstruction Finance Corporation Act and the Home Loan Bank Bill. These were all necessary and vital to preserve our national credit and to relieve distress, but they were more palliative than remedial. All of the funds to meet the cost of government thus increased must ultimately be met by increased taxes. We cannot pay the bill by "soaking the rich." There are few rich left to "soak." Too high taxes on income drive capital away from investment in productive enterprises and force it into government securities, which are tax-exempt and must remain so until the Constitution is amended. Government securities were made tax exempt for the obvious purpose of lowering the rate of interest which the taxpayer must ultimately pay. Therefore, unduly

"soaking the rich" hurts the poor more than it does the rich.

For the fiscal year ending June 30, 1932, our federal deficit was \$2,885,000,000. How much it will be this year no one can accurately forecast. Certain it is that it will be very large. This must be so because of our great depreciated revenue, both from income taxes and customs, on account of our greatly reduced foreign trade.

Therefore, I submit that the first step we must take is toward an immediate and drastic reduction in the cost of government, federal, state and local. The integrity and the credit of our governments must be preserved. We must balance our budgets. We cannot repudiate the obligations we have incurred. We must meet them, whatever the sacrifice. But we must lighten the load for the future.

II. *International Relations*

Having considered the most important step we should take in our own country, let us now consider our international relations. I never have been impressed by the argument that, by reason of our great variety of climate and diversity of natural resources, we are the richest and most self-sufficient country on earth, and that the percentage of our foreign to our domestic trade is so small that we can isolate ourselves from the rest of the world and prosper by living on our own. Of course we can live better than any other country on our own, for the reasons I have given, but the people of this country cannot return to the prosperity they enjoyed in 1925 unless we maintain our foreign trade. Foreign trade cannot be all on one side. You have to have imports to counter-balance exports and every country likes to have the balance of trade in its favor. That is what we have done heretofore, and what we want to do. It can be done only through collaboration with the other nations of the earth. Many things that we cannot produce we have to import. Some things that we can produce we import because it can be done cheaper.

I am not here to discuss the tariff. You doubtless have heard about that this afternoon. I heard Mr. Young discuss it the other night in a political speech. I did not agree with him entirely, though there is nobody whom I admire more. The plain truth is that no tariff schedule is perfect. It is

generally the result of a lot of special pleaders importuning the Congress until Congress is worn out. It is more or less a local question. As has been said many years ago, it depends on how much it affects or helps your interests.

We differ a bit from other countries with respect to tariff or trade barriers because we have forty-eight great states among which there are no barriers. Our internal trade moves freely and does not float up and down with the rise and fall of exchanges.

Heretofore we have seemed to be able to pay the tariff, and anything we wanted seemed to climb over the tariff barriers.

Nevertheless we have to look into the situation. We have to have an appreciation of the fact that we cannot consistently exact tariff duties greater than the difference of cost of production here and abroad. I do not think the people of this country can continue to maintain tariff schedules in excess of the differences in production costs. If they do, they will not have any exports.

This problem has a direct bearing on employment. Two and one-half millions of our citizens are dependent on foreign trade. That is only about 10 per cent, but it represents the difference between prosperity and just getting along.

Any one who has given the subject the most casual consideration must know that commercially, financially and industrially, if indeed not socially, the whole civilized world may be regarded as a unit. To establish peace and restore the world to a normal and prosperous condition, the people of all nations should realize that their countries would be more benefited by mutual coöperation than by isolation. The happiness and prosperity of every people at this time depend to a greater extent than ever before upon friendly relations among all nations.

Assuming the truth of that statement to be undeniable, I am not unmindful of the fact that the officials of every government and, to a lesser degree, the citizens of every nation, are motivated by an instinctive nationalistic spirit. In other words, in their contact with other countries the dominant thought seems to be to gain some advantage or concession for their own country, even though it be temporary and national rather than permanent and international in its ultimate effect.

I need not mention existing economic and financial conditions. Everyone knows that world trade is greatly disorganized and that the breakdown in the mechanism of international credit and finance handicaps recovery from the economic and financial maladjustment.

The fallen commodity prices, the decline in foreign trade, the halt in the movement of capital, either for the purpose of investment or for ordinary commercial transactions, and the growth of unemployment, have precipitated great difficulties in private and public finance. This has led to the abandonment of the gold standard in twenty-two countries and governmental control over the purchase and sale of foreign exchange in thirty-one countries. Currency has depreciated in some countries as much as 55 per cent, the net result of which is that the existing tariff rates on more than 52 per cent of the imports into this country for the first nine months of 1932, coming from depreciated currency countries, have paid very much less than the tariff schedule contemplated. The articles thus imported are being sold upon our markets at prices below anything with which our local manufacturers can compete.

A committee of the Chamber of Commerce of the United States has made a recommendation upon which they will insist in the next Congress, namely, that prompt action be taken to balance the difference in production costs due to foreign currency depreciation. We ought to have a tariff sufficient to represent the difference between the cost of labor and of production here and abroad. Personally I have abiding confidence in the ability and capacity of the Tariff Commission. That agency is available to any one who thinks the tariff is too high or too low.

We are all more or less familiar with the conditions which necessitated the Moratorium, declared on the recommendation of President Hoover in 1931. Everyone will agree that the Lausanne Agreement, in settlement of the German reparations, was a distinct step in advance toward world peace, and that when it is ratified one of the disturbing elements in international finance and politics will be disposed of.

Debts Due the United States. It would serve no good purpose on this occasion to discuss different opinions regarding the extent to which European indebtedness to the United

States looms as a factor in world affairs. Some hold that the war debts have largely been responsible for precipitating the economic decline and urge their cancellation in the interests of world recovery and continuing prosperity. Others regard these debts as a disturbing and retarding influence in world affairs and consider them a subject for calm reëxamination by their governments and for further settlement and adjustment on the fairest basis possible. Still others minimize the effect of the debts on the world situation and say that they can be paid on existing terms without undue burden on the debtors or the rest of the world.

Origin of the Debts. It is a matter of common knowledge that these debts are made up of pre-armistice and post-armistice obligations, consisting of cash loans, surplus stocks and relief supplies left by our armies in Europe. The pre-armistice obligations of our fifteen principal debtor countries totaled \$6,879,385,000. The post-armistice debts, being cash loans, totaled \$2,533,262,000, and the surplus stocks and relief supplies amounted to \$722,825,000, making a total of \$10,135,472,000. In general, these obligations were payable on demand, with interest at 5 per cent.

These obligations afterwards were funded, the approximate annual average interest rate of the debts so funded being 2.14 per cent. In the funding settlement the unpaid accrued interest was figured not at the rate of 5 per cent as contemplated in the original obligations, but at $4\frac{1}{4}$ per cent from the date of the loans to December 15, 1922, and at 3 per cent from that date to the date of the funding agreements. In the case of Belgium, there was no charge for interest on loans made before the armistice. The result of such funding was a reduction of the "present value" of the debts by 23.9 per cent if interest is discounted at 3 per cent, or by 43.1 per cent if discounted at $4\frac{1}{4}$ per cent, or by 51.3 per cent if discounted at 5 per cent. This was a very substantial reduction of the amounts to be paid by the several countries. None can deny the legal obligations of the governments whose debts were funded, nor the extreme generosity of the United States in reducing the amounts and in funding them on an average interest basis of 2.14 per cent, when at the time we were paying $4\frac{1}{4}$ per cent for the money.

[260]

The Present Status of the Debts. The settlements with the different countries were not worked out on a standard inflexible plan. They were negotiated with representatives of each of the debtor countries in the light of the situation in each particular country. There were taken into consideration the general economic and financial positions of the countries, their natural resources, their trade, the national economic and fiscal burdens each had to face, and the standards of living of their people. The World War Debt Commission, in reporting its work to the Congress, commented that the foreign debtor

must be permitted to preserve and improve its economic position, to bring its budget into balance, and to place its finances and currency on a sound basis, and to maintain, and, if possible, to improve the standard of living of its citizens. No settlement which is oppressive and retards the recovery and development of the foreign debtor is to the best interests of the United States or of Europe.

In other words, on the one side there was an expression of a desire of the debtor governments to meet their obligations and on the other side an evidence of the willingness of the United States to make such concessions as the world conditions seemed to require and as the interests of our citizens in a prosperous Europe seemed to justify.

Alternative Courses of Action on the Debts. As funded, the total amount of the principal owed to the United States by fifteen debtor countries is \$11,261,178,000. The debt holiday ended on June 30, 1932. Further payments to the United States on principal and interest are due December 15. Our government has received requests from the debtor governments for reconsideration of the terms of the debt agreements. It would seem, therefore, that our government is faced with the responsibility of deciding (1) whether the debts shall be paid, principal and interest, in accordance with the agreements; (2) whether further payments shall be postponed; (3) whether the refunding agreements shall be modified and the debts reduced; or (4) whether the debts shall be completely cancelled. I shall briefly discuss those propositions.

Shall the Debts be Paid in Full, Principal and Interest, in Accordance with their Terms? In considering that proposi-

[261]

tion it must be remembered that the debts are admittedly legal. They represent value received at the time they were made, and in principle the integrity of governmental obligations greatly outweighs any arguments that have been advanced in favor of cancellation. The Congress has already spoken quite definitely on the subject of cancellation and I submit it would be futile at this time to bring that subject again before the Congress. Personally, I see no sound basis for entertaining proposals for cancellation of the debts. That brings us to a consideration of the question:

Whether Further Payment Shall be Postponed? This subject cannot be dealt with on a general plan but must be carefully considered with reference to the ability of each country to meet its obligations. It is evident that certain of the debtor countries will be unable to meet payments presently falling due, and, therefore, it would seem that temporary postponement of payment of their obligations to the United States is necessary. On the other hand, some of the countries are able to pay in accordance with their agreements.

The subject involves a careful consideration of all the facts, with due regard not only to the conditions of the debtor countries but also with respect to the fiscal status of our own country. As I have already said, the burden of taxation upon our own citizens is now almost confiscatory, and postponement of the payment of \$250,000,000 a year by way of interest, aside from the payments on account of principal, necessarily increases the burden of our taxpayers to that extent.

Shall the Funding Agreements be Modified and the Debts Reduced? The same elements should be taken into consideration in deciding this question as those which must be considered in deciding the necessity of postponement. Every country is faced with the difficulty of balancing its budget, of meeting its obligations, of raising the needed taxes, of effecting economies in public expenditures, and of establishing and assuring the continuance of sound currency. Every country has been struggling to restore its economic activity and revive its trade. In 1921 the international trade of more than one hundred countries reached a total of about 43 billion dollars annually. This increased consistently until 1929, when it

reached a level of about 68 billions. For the fifteen countries that have funded their debts to this country, the total international trade grew from 15 billions of dollars in 1921 to 22½ billions in 1929. By 1931 the total dollar value of the international commerce of the world had dropped even below pre-war levels, or from the peak of 68 billions in 1929 to less than 40 billions in 1931. In addition, the wholesale prices in the world's chief markets went steadily downward in 1930 and 1931 until now they are below the 1913 levels. As the depression continued the financial position of many countries became more difficult. Resources diminished until finally Great Britain and twenty-one other countries were compelled to go off the gold standard.

Obviously, this had a very serious effect upon the trade of the United States with Europe. Nationalism became intensified, the European countries raised their trade barriers and put in all kinds of trade restrictions, such as quotas, licenses and so on. Then came the British Empire Conference at Ottawa, the result of which, it is estimated, will have a prejudicial effect on American exports to the extent of upwards of 200 millions of dollars a year.

Armaments. In considering the applications for postponement or reduction of debts, it is pertinent to consider the amount of money being spent by the debtor countries for armaments. This amount has substantially increased in all of the debtor countries since 1913. In that year the world expenditure for armaments was \$2,531,000,000. The amount expended in 1930 was \$4,128,000,000. It is now estimated that the amount of the annual expenditures for armaments throughout the world reaches a total of 5 billion dollars. The combined figures for the six great powers—Great Britain, France, Italy, Japan, Russia and the United States—show an increase of 65 per cent. Budgeted expenditure for national defense for the year 1932, per capita, was:

France	\$10.79
United Kingdom	6.77
Italy	6.72
Belgium	3.61
Poland	3.00
United States	5.69

The total amounts budgeted for national defense for the current fiscal year in the fifteen debtor countries amounted to 1,361 million dollars, or five times their debt service to the United States Government for that period. For example, the debt service of Great Britain to the United States was 6.35 per cent of its total expenditures, whereas the national defense expenditures were 11.43 per cent. For France, the figures were, debt service, 3.07 per cent and national defense, 22.51 per cent; Belgium, debt service, 2.73 per cent and national defense, 9.48 per cent; Italy, debt service, 1.47 per cent and national defense, 27.19 per cent. Since the debt-funding agreements, the payments by Germany on reparations account, with the exception of Great Britain, have more than covered the payments of those countries on account of war debts to the United States. Payments credited Germany by creditors on reparations account, from 1924 to 1931, inclusive, total \$2,480,000,000, or an average amount per annum of \$310,000,000, as against total receipts by the United States on intergovernmental account during that period of \$1,638,000,000, an average annual payment by the debtor governments of \$205,000,000. In 1930-1931 Germany paid France on reparations account \$214,726,000; France remitted to the United States \$35,000,000. Belgium received from Germany \$23,411,000 and paid to the United States \$7,000,300. Italy received on reparations account \$37,190,000 and paid to the United States \$14,821,000. The United Kingdom received from Germany but \$87,445,000, but, by reason of obligations owed to her by France and Italy, she received amounts more than sufficient to counterbalance her payment of \$159,940,000 to the United States. Her excess receipts in 1930-1931 amounted to \$15,000,000.

Relation of Intergovernmental Debts to the American Taxpayer and Business Man. The business man and taxpayer of this country are interested in four principal questions: (a) Will postponement or reduction of the debts help materially to restore world economic activity? (b) If so, will our increased foreign trade produce revenue to the United States sufficient to offset any loss of interest by postponement or loss of principal by reduction of foreign debt? (c) Can the debtors assure us that our exports will have fair competitive

access to their markets? This question is of particular significance in view of the action of several countries in placing restrictions upon our exports. (d) Will the debtor countries give assurance that they will cut their expenditures on armaments so that not only their citizens but our citizens, as well, may benefit in the reduction of expenditures for armament?

It goes without saying that if the answer to each of these questions is in the affirmative and we are given assurances that agreements thus made will be carried out, then in our interest and in the interest of world welfare we should negotiate further modification of the debt agreements. In other words, if the debtor countries can offer us the compensating advantages indicated in the questions thus stated, then I believe it to be in the interest of the United States to reconsider the settlements.

It is obvious that in dealing with the debt problems, as I have already said, each country presents a separate problem. Always there must be kept in mind the tax burden on our own country.

The time has come when the debt problem should be removed from the political field. I am convinced that it would be distinctly to the advantage of better international understanding, of world peace and of world economic welfare if political considerations were entirely eliminated from discussion of the international debt problems.

STEPS TOWARD RECOVERY

SIR ARTHUR SALTER, K.C.B., C.B.

Former General Secretary of the Reparation Commission, 1920-1922; former Director of the Economic and Financial Section of the League of Nations, 1922-1931; author of *Recovery—the Second Effort*

AT this moment the world is uncertainly poised between two fates. Whether we look to the Disarmament Conference, the Far Eastern situation, the general condition of international affairs, or the whole series of economic and financial problems that arise in connection with the world depression, we see that a crucial stage has been reached. In each of these spheres indeed, there are certain recent factors which indicate some hope of success if wise and collective policy seizes the opportunity. But in each certainly success is still uncertain and precarious.

There are, of course, many elements in this present world depression. Among them, underlying others, is the movement of a trade cycle such as we have seen in the past. Until recently the movement has been downward, and anything done in the way of a remedial policy has had to work against the downward movement. It seems to me that there are some signs, possibly illusory, certainly precarious, that now the purely natural movement of the trade cycle is perhaps beginning to turn upward. But it is certainly not turning upward so decisively that it cannot be, or would not be, fatally impeded either by unwise policy, or by an absence of deliberate decisions where decisions are definitely and urgently needed.

For the most part, in these last few years events have been allowed to drift. And at least as often as not, where definite policy has intervened, such as, for example, within the sphere of tariffs, it has not lightened but aggravated the situation. But there have been in the last year three notable exceptions, three cases in which deliberate and wise policy, taken by a particular country or countries, has definitely relieved the situation and been of advantage not only to the country or countries initiating that action, but to the whole world. One of these instances is American, one European, and one English.

[266]

The first is the monetary policy of the Federal Reserve System, of deliberately injecting new money by open market operations. I know that there are some who are skeptical of the success or wisdom of this policy. To them I would like to address this question: What would have been the position if, with the hoarding, the external drain upon gold, the panic of June 1932, the situation had not been relieved by this policy? Is it not clear that without this counteracting force, there would have been a formidable further deflation and a further downward movement of prices?

The worst dangers of the situation of June seem to me again—perhaps I speak rashly—to be now past. Mr. Lamont has said, with obvious truth, that the dollar is impregnable against external distrust or external strain or assault. The dollar could never be threatened except by internal distrust and “flight from the dollar” and whether or not there was ever danger of that, the moment of panic at least seems to be past, the hoarding has stopped, and the movement is reversed.

As I should read the situation as a detached observer, I should say that in June there were both pessimism and panic, whereas now the mood oscillates, in truer correspondence with facts, between a mitigated pessimism and a cautious hope.

We seem to have passed from the panic of June back to the depression, shall I say, of January, but with this difference, that you have gone through the panic. The situation is stronger because the panic has been passed through.

Nevertheless, it certainly remains true that some of the worst impediments to real and permanent recovery on a high level still remain in every sphere—in the world's currencies, the credit system, and the world's commercial policies. Certainly we need every resource of wisdom upon which we can call.

The ship of the world's finance has now to navigate in stormy seas through perilous reefs and shoals, and it has to do so under the great disadvantage that the ship answers to three helms and not one. There was a time when the seas were quieter, when there was one helm in the ship of the world's finance. Well, London has been partly displaced, but not completely replaced. Now there are the three helms of London, New York and Paris. The first, through the

[267]

snapping of a metallic connection, is not very securely fastened to the rudder, and tends to jog violently and intermittently the course of the ship, but it does not control it. The second helm, New York, with its volatile call rates and its Stock Exchange immediately responsive to every mood of hope or fear anywhere in the world, is perhaps too sensitive to the touch. The third, Paris, with its large accumulations of gold followed by no corresponding expansion of credit, and with none of the orthodox consequences following customary causes, is perhaps too insensitive to the touch. And under these difficulties, the ship has to navigate difficult and stormy seas.

Surely, if single and central policy is impossible, there should at least be coördinated policy. I fail to see how otherwise the ship can avoid disaster.

I venture to express the opinion that the world needs a world policy of controlled reflation, aiming to bring prices back to a point intermediate between the present level and that of 1928. I need not enlarge upon the enormous advantages of such a policy as a stimulus to enterprise, as a relief to indebtedness of all kinds.

The second act of constructive and deliberate policy which has beneficially controlled, to some extent, the drift of events, was the Lausanne settlement of reparations. You will remember that the Lausanne Conference met shortly before the termination of the Hoover moratorium. The first act of that Conference was to postpone payment during the Conference itself. The Conference then provided first temporary relief, and next the fixation of a total capital sum which was to be commercialized by public issue in such a way as to involve neither an impossible burden for the debtor country, Germany, nor an intolerable burden on the world's exchanges; in fact, as you will remember, the burden was so reduced that it can never exceed more than about a tenth of the annual burden implied in the plan made as recently as 1929 by the committee presided over by Mr. Owen D. Young.

The European creditors, in making this agreement, had in mind the increase in the real burden that resulted from the fall in prices; the diminished volume of Germany's external trade; the necessary cessation of the system of payment out of new borrowing; with the inevitable consequence that any pay-

ments must be made out of a surplus of exports over imports. And such a surplus, they thought, if not modest in amount, must involve both a restriction of Germany's purchases from abroad and also a forced export of her goods at cut-throat prices—which would both be fatal to world recovery. It was with those considerations in mind that the European creditors made a new reparations settlement. It was an act not of altruistic abnegation but of enlightened self-interest.

The third act of leadership to which I refer was the English conversion operation, which may not have all the results it was intended to have, but, if it does, will certainly be another real contribution to world recovery. The first object of that was, of course, to reduce the budget burden in England, but the second object was to give a lead towards a general reduction in long-term rates of interest for new borrowing in the world, a reduction which requires many other conditions, but, if it were possible, would quite obviously be of great assistance in many ways to world recovery.

Something, therefore, has been done this year, but we have ahead of us a series of problems not only in the sphere of monetary policy, but in the world's credit system, commercial policies, and international relations. The credit system presents a triple problem. (I am speaking of the general indebtedness of the world, not of the particular problem of intergovernmental indebtedness.) There is, first of all, the problem of dealing with the past, and there I notice with great pleasure some steps being initiated in this country with a view to the formation of a council of foreign bondholders. If such a council here, in conjunction with similar bodies in London and in Paris, could really do something to replace the succession of disorderly defaults by some kind of orderly arrangement, very great good would result, first of all, in diminishing the extent of the destruction of the debtor nations' credit, and, secondly, in avoiding a scrambling competition between the creditors for such resources as are available.

The second aspect of the credit problem is the encouragement, when it is possible, of a resumption of lending. Thirdly, the coöperation of the great issuing houses will be required to prevent future foreign loans from being as wastefully ex-

pended as some of them certainly were in the period between 1924 and 1928.

In commercial policy, the world is at the cross-roads. The choice is not between absolute free trade and protectionism. But are we going to move, however gradually, towards a system in which trade will be freer, or are we proceeding towards a system of closed and probably increasingly hostile economic units, whether national, imperial, or regional? In the long run I have no doubt plain economic necessities, the obvious consequences of the natural development of large-scale industry, with its needs for markets much larger than those comprised within national frontiers, must compel policy to create an order appropriate to that development. In the long run, yes, but, as Mr. Maynard Keynes so often says to the procrastinators or doctrinaires in my country, in the long run we shall all be dead. Though I hope our vision extends beyond our individual lives, we are all very considerably interested in what is going to happen during the remainders of our lives and during such a period it does seem to be really doubtful as to which direction the world is going to move in.

Yet one thing at least can be said: It is almost certain that the world will move in the one direction or the other more or less as a whole. The interdependence of nations is perhaps an overexploited idea in these recent years, but it means among other things this: That it is politically impossible, whatever may be economically desirable, for one part of the world to have a commercial system radically different from that of the countries with which it trades. Whatever the economists may say, you cannot persuade popular audiences over a period of years that it is fair or right to admit goods freely into your market from countries that obstruct your own goods by high tariffs. In the past my country attempted to lead the world in one direction. It is obviously not at the moment in as good position to give a lead as it has sometimes been in the past. The post of leadership is vacant.

If the world is to proceed towards greater freedom of trade, what should it do? In my view, it should look to see what forces are making for reduction of tariffs and try to encourage those forces. There are at least two such forces. The first is the movement towards regional reduction of tariffs.

That movement may result in very considerable abuses and difficulties, but under proper conditions it may result in a real improvement in the world situation. To put my proposal shortly, I should very much like to see the countries which are accustomed to have the most-favored-nation clause in their treaties, adopt a policy of encouraging and not discouraging such an arrangement as is desired now by Belgium and Holland, the principles of which are: (1) no increase against any country; (2) substantial, progressive decreases as between the two countries; and (3) an open invitation to any country in the world to come in upon equal terms. That kind of movement is in the nature of the case such as to tend to the reduction of impediments to trade and to be extensible to other countries.

There is one other force in many countries which are really protective and mean to remain protective. There is a feeling that some features of their tariff, if one knew just what they were, probably do a great deal more harm, on any theory of the tariff, than good. There is a desire to correct excessive and ill-judged features of existing tariffs.

The World Economic Conference could do great service in encouraging this movement by laying down certain principles to guide protective countries in their protective policy. It is not a question of asking a specific country to make such and such changes in its tariff. But the delegates of all countries might well be urged to go back and reexamine their own tariffs in the light of those principles. The reservation of tariff rates from the agenda of the World Economic Conference would not preclude consideration of such principles. With great respect, if I were going to advocate certain economic principles for the Conference to lay down, I am afraid the first I should try to lay down would be, if Mr. Strawn will allow me to say so, an explicit condemnation of the principle he has suggested, namely, the compensatory principle of equating differences of costs by a so-called scientific tariff.¹ What is the very basis of all international trade? Is it not surely this, that owing to natural advantages, better organization, greater skill, or even lower wage rates, some countries are able to supply certain

¹ Cf. *supra*, pp. 117-118.

articles more cheaply than others? Why does any one of us ever buy anything from abroad? It is only because we can get a given article cheaper or a better article at the same price, and the only reason we can do it is that some countries are able to produce them definitely cheaper.

Supposing you did comprehensively and with scientific precision exactly abolish this difference, what would happen? You would not impede world trade; you would destroy the very foundation of world trade. True it is there are countries which have the so-called scientific tariff and still do some world trade. Why? In the first place, because they do not apply the principle comprehensively. Neither this country nor England would think of applying a scientific tariff so high as to foster rubber production at home. In the second place, the tariff is not detailed or precise. A country may have a cost-equalizing tariff in regard to a large category of goods, and foreign trade will still creep in because the tariff does not render effective protection for specific articles. So-called scientific tariffs are as a rule not scientific in detail nor comprehensive in scope. If, unhappily, it were possible to frame tariffs that were both, we should have no world trade at all.

I should like to turn, in the few minutes that remain, to the framework of all economic and financial prosperity, which requires, as Lord Astor¹ has reminded you, a basis of secure peace and confidence in international relations.

You know the efforts that have been made in these last thirteen years, built partly but not solely on the Covenant of the League of Nations, partly on Locarno and on the Kellogg Pact, and on many other efforts. In the future what part is America going to take? Is she going to adopt a policy of political isolation, or is she going gradually to depart from that policy? Is she going to cooperate more and more closely with the rest of the world in establishing the machinery both for the settlement of disputes and for the preservation of peace? Doubtless prophecy is as rash as advice is impertinent, but perhaps prophecy is a more excusable fault than impertinence, and I will venture to express the very definite opinion, much more definite in this sphere than in regard to the problem of

¹ Cf. *supra*, pp. 111-112.

economic nationalism, that America will increasingly abandon a policy of political isolation and will continue to act with the world even more decisively in solving the world's problems.

And if you ask me why I have that faith, I would say for two reasons. It is because I reflect on the two greatest events in American external history and, as I understand them, the two main principles of external policy in the American tradition. The first of those is the principle of "no taxation without representation." For a nation like America, with her enormous investments and commitments and interests in every part of the world, all of which are dependent upon the framework of society within the countries where they are situated, all of which are risked by unwisdom of policy in those countries, what does political isolation mean? Surely it means a lack of political influence corresponding with the financial interest and responsibility—which is precisely "taxation without representation." A century and a half ago you fought against that principle. Surely you will not hug that principle to your breasts when nobody desires to fight about it.

And the second traditional principle of American policy, as I understand it, is, "no foreign entanglements." You may think it paradoxical if I say that the only way to avoid foreign entanglements is not to pursue a policy of political isolation; but I believe it is fundamentally true. Not a century and a half ago, but a decade and a half ago, you were entangled in a great war you had not made; we were all of us entangled in a great war we had not desired; because we had not collectively controlled the march of events that resulted in the outbreak of that war. In the modern world the only way to avoid being the slave of events is to be their master.

It is for these two reasons that I venture, rashly perhaps, to prophesy that America will certainly not continue a policy of political isolation, even if she and the whole world pursue policies of increasing economic nationalism.

I have mentioned certain international and external problems. I can only remind you in a word of the enormous range of the internal problems now perplexing every country and challenging the competitive system under which we have grown up. Whatever its defects—and patent indeed they are at this moment—that system has, after all, sheltered in com-

fort such multitudes as no other system the world has known has done; it has given to innumerable millions a standard of material comfort that before had only been known by favored classes in a few brief periods in a few restricted areas. I like to think of that system as best materially expressed in the soaring structures of this city, which seem to me to body forth in stone and steel the very conception of Energy Triumphant, as the Medieval Gothic embodied the conception of the Church Militant.

We all know that if this system is to be retained and made adequate for its task, it must be so reformed, perhaps transformed, that it will save us from the tragic paradox of poverty in a world of plenty, and of plenty apparently causing poverty. It must somehow or other be so reshaped that extra productive capacity at every stage will be (as it should be and as certainly it can be if we reform our own human organization) translated into corresponding extra purchasing capacity. But the task is a great one, externally and internally.

In the winter in which we now are, in the year which is about to come, events must certainly be anticipated which will need the mobilization of every resource both of constructive intelligence and of international good will.

It has been my privilege for many years now to be associated with one effort at Geneva to evoke and apply something of the constructive wisdom of mankind. I see, as all of those associated in that work see, that the entire work of which Geneva is part, is now at a most critical and crucial stage. It may be decisively strengthened; it may be fatally weakened.

You whom I address, through your personal influence, through the offices private or public which you occupy, are no inconsiderable part of the forces which direct events and policy in this country, and it depends largely, perhaps decisively, upon the policy of this country whether in the years ahead of us man is master of his fate, or its slave, whether he is the sport of circumstances or will control his destiny.

No other age in human history has ever made the same challenge to the constructive intelligence, the wisdom, and the collective will of man as ours has. For never until now have the nations' resources and man's knowledge and skill been sufficient to give the material basis of a rich civilization to the

[274]

whole of the world's inhabitants. Never before has a promise so rich been menaced by a danger so great.

It is defects in human organization alone that require to be remedied. I cannot believe that the response to that challenge, with the penalties of failure so great, and the rewards of success so incalculable, will be an unworthy one.

[275]

PROCEEDINGS
OF THE
ACADEMY OF POLITICAL SCIENCE

Volume XV

JUNE, 1933

[No. 3

TARIFFS AND TRADE BARRIERS

A SERIES OF ADDRESSES AND PAPERS PRESENTED AT THE SEMI-ANNUAL
MEETING OF THE ACADEMY OF POLITICAL SCIENCE
APRIL 28, 1933

EDITED BY
PARKER THOMAS MOON

THE ACADEMY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY
1933

COPYRIGHT BY
THE ACADEMY OF POLITICAL SCIENCE

CONTENTS

	PAGE
Preface	iv
PART I: TRADE BARRIERS IN THE WORLD DEPRESSION	
<i>W. Randolph Burgess</i> Introduction	1
<i>John H. Williams</i> The United States Tariff and Our International Financial Position	2
<i>James W. Angell</i> Exchange Depreciation, Foreign Trade and National Welfare	9
<i>G. R. Parker</i> Import Quotas and Other Factors in the Restriction of Trade	21
<i>L. J. Dickinson</i> The Relation of the Agricultural Problem to Tariffs	27
<i>George P. Auld</i> Discussion: Trade Barriers in the World Depression	35
PART II: PROCEDURE IN TARIFF MAKING	
<i>Shepard Morgan</i> Introduction	39
<i>John Lee Coulter</i> The Tariff Commission and the Flexible Clause	41
<i>James Grafton Rogers</i> Reciprocity and the Most-Favored- Nation Clause	52
<i>Edmund E. Day</i> Tariff Bargaining	62
PART III: INTERNATIONAL COLLABORATION	
<i>Jackson E. Reynolds</i> Introduction	69
<i>Sir Walter T. Layton</i> International Coöperation in the Economic Crisis	71
<i>Hans Luther</i> International Coöperation	85

PREFACE

ON the eve of a World Monetary and Economic Conference and at a moment when almost universal attention is focused on trade barriers, tariffs, quotas, and exchange depreciation, the hope may be ventured that this volume will be not only a solid addition to economic knowledge, but an exceptionally timely approach to the problem of the hour. The reader will find in these pages important statements by the experts who represented the United States in the Preparatory Commission for the world conference and by other very distinguished authorities.

In substance this volume is the record of the Semi-Annual Meeting (Fifty-third Year) held by the Academy of Political Science on April 28, 1933, at the Hotel Astor in New York City. The papers presented at the meeting and printed here represent, of course, the views of their respective authors, and for the divergent opinions expressed by them the Academy can obviously assume no collective responsibility.

In this place it is appropriate to acknowledge the profound debt of gratitude due to the speakers who addressed the Semi-Annual Meeting and likewise to the Committee on Program and Arrangements. The members of the committee were: Mr. John W. Davis (Chairman), Miss Ethel Warner (Director), and Messrs. Winthrop W. Aldrich, Frank Altschul, William C. Breed, W. Randolph Burgess, Joseph P. Chamberlain, Frederic R. Coudert, Paul D. Cravath, Norman H. Davis, S. Parker Gilbert, George L. Harrison, Alanson B. Houghton, Pierre Jay, Thomas W. Lamont, Russell C. Leffingwell, Samuel McCune Lindsay, Robert M. MacIver, Roswell C. McCrea, George O. May, Ogden L. Mills, Parker T. Moon, Shepard Morgan, George A. Plimpton, William L. Ransom, Jackson E. Reynolds, E. R. A. Seligman, Albert Shaw, Alfred P. Sloan, Thomas J. Watson, Louis Wiley, and Owen D. Young.

PART I

TRADE BARRIERS IN THE WORLD DEPRESSION

INTRODUCTION¹

W. RANDOLPH BURGESS

Trustee of the Academy of Political Science
Deputy Governor, Federal Reserve Bank of New York

THE significance of this meeting may be indicated in part by the fact that by truly prophetic insight our topics for discussion today are precisely upon one of the points which were emphasized in the joint statement by the President and the Prime Minister of England two days ago. You may have noticed the sentence in that statement: "Commercial policies have to be set in a new orientation. There should be a constructive effort to moderate the network of restrictions of all sorts by which commerce is at present hampered, such as excessive tariffs, quotas, exchange restrictions, and so forth."

Today's meetings, therefore, devote themselves to one phase of the matters which will be discussed at the World Economic Conference.

The first speaker this morning was one of two American delegates to the international committee arranging the agenda for the World Economic Conference. It gives me great pleasure to introduce Dr. John H. Williams, Professor of Economics, Harvard University, who will speak on "The United States Tariff and Our International Financial Position." Professor Williams!

¹ Introductory remarks at the First Session of the Semi-Annual Meeting.
[277]

THE UNITED STATES TARIFF AND OUR INTERNATIONAL FINANCIAL POSITION

JOHN H. WILLIAMS

Nathaniel Ropes Professor of Political Economy, Harvard University;
U. S. Representative on the Preparatory Commission of Experts
for the World Monetary and Economic Conference

THE world situation prior to the depression was characterized by two opposing tendencies, both carried to unprecedented extremes: on the one hand, a growing network of international financial relations and an enormous burden of international governmental and private debt, and on the other, a progressive increase in tariffs and quota arrangements. The first looks logically toward a freer movement of goods, the second endeavors to prevent such a movement. Though no simple or single explanation of the depression is possible, this conflict of international forces lies close to the heart of the problem.

The intensification of trade barriers had its origin in the war. In part it is traceable to that sheer exuberance of nationalism which war intensifies; in part to the need for revenue, which was greatly increased by the war; in part to the creation by the Versailles Treaty of new states, which proceeded at once to exercise their new-found sovereignty by raising tariffs against each other and everybody else.

More important, perhaps, has been the increased industrialization of the younger countries. Cut off from imports of certain goods from the warring nations, they proceeded to develop new industries at home, textiles in India, China, and Japan, iron and steel products in India and Australia, shoes, textiles, and other products in Brazil. With the aid of American capital and branch factories, Canada has experienced a rapid industrialization. To this development must be added the war-time expansion of productive capacity in countries already industrialized, particularly the United States. The new growth of tariffs has been in part an attempt to protect these new or expanded industries.

[278]

Another prolific breeder of tariffs has been depreciation of currencies. The war caused a collapse of the gold standard in Europe, and the depreciation of currencies after the war, together with the abandonment of exchange stabilization measures, produced a wave of protectionist sentiment all over the world. England responded with the key industries act, and the United States with its emergency tariff of 1921. We have witnessed this same relation between currency and tariffs in the present depression.

Perhaps more important than any of these causes of trade restrictions has been the condition of agriculture. The war reduced the European output of agricultural production by drawing off the population from the soil. This curtailment, together with war-time expansion of demand for raw materials, provided an opportunity to other countries to increase their output. For a time, in response to the shortages, there was some downward movement of agricultural tariffs in some European countries. But as European output was restored after the war, non-European output did not contract; and the rapid technical improvements in the industry further expanded total output.

The effects were intensified by the peculiarly inflexible demand-supply conditions to which agriculture is subject. As foreign markets are reduced by trade restrictions and prices fall, it is difficult for countries not possessing diversified industries to turn to something else. They endeavor to make up in quantity what they lose in price, and to push upon markets still comparatively open what is denied admission to previous markets. Such action invites further trade restrictions; and increasing quantity reduces prices further; but with inelastic demand the increased quantity sells for a lesser total sum. The pressure to increase exports is intensified by financial requirements. Such countries are usually borrowers of capital, and their seeming prosperity in the earlier part of the period, together with that in the lending countries—our own in particular—greatly increased the capital inflow. But as output continued to expand and the gap in European output disappeared the conditions were reversed, though international leaders were slow to perceive the change. The spread of the protectionist movement, the attempts to sustain prices by con-

[279]

trol schemes applied to many individual commodities, the appearance of Russia in the world's markets in 1928, our own stock-market boom, serving as a magnet for the world's short-term funds, the cessation of the flow of capital to the young countries, bringing upon their balance-of-payments position and their prices the full weight of the interest charges—all these factors assisted in converting the slow fall of agricultural prices, which had been in process since 1925, into an abrupt collapse. The collapse has produced a further intensification of trade restrictions, and created a great disparity of prices—amounting to as much as \$1.00 a bushel for wheat—between different markets.

Our special interest today is in our own policy. We have raised our tariff three times since the war—the Emergency Tariff of 1921, the Fordney-McCumber Act of 1922 and the Hawley-Smoot Act of 1930—and we have taken this action under entirely new international conditions. The war abruptly changed our position from the world's leading debtor to one of the two leading creditors. War-time exports of twenty-two billion dollars and imports of eleven billion dollars gave us an export surplus equal to the sum of our export surpluses in the preceding forty years. The partial payment by a billion dollars of gold was the first phase of the heavy gold flow to this country since 1914; but the principal means of payment consisted of the repurchase of our securities previously held abroad, and the extensions of credit by our government—the inter-allied debts. To these sums must be added the post-war exportation of private capital, which has made us the world's creditor, on private capital account alone, by an amount in excess of ten billion dollars.

It has been frequently pointed out, especially by European economists, that there is a logical conflict between a high protective tariff and an international creditor position; and our policy has been contrasted with that of England before the war. A nation whose international position calls for the receipt of interest payments on balance injures both herself and her debtors by interfering with the receipt of such payments in the form of goods. By her free-trade policy England received payment in foods and raw materials at low cost, and by offering to receive them freely she expanded her own market

for finished goods abroad. The policy was enormously beneficial to England and to her debtors. In contrast we, it is pointed out, have imposed an increasingly high barrier against goods; refusing to take goods, we have compelled payment in gold, on which there was no tariff, and by this process have at length smashed the monetary system, producing a world collapse.

This is a serious indictment. The correctness of the reasoning and the emphasis to be assigned to it in any analysis of causes of the present situation raise difficult questions. In the first place, whatever the merits, some account must be taken of the sheer rapidity of change in our own position and of the perhaps inevitable effect of such world-wide maladjustments as have occurred since 1914. Our protectionist policy has been a part of a world-wide movement. The change in England's position occurred gradually in the first half of the nineteenth century and was accompanied at all times by lively discussions about the tariff. Gradually England receded from her protectionist position and came out at the end of the half-century a creditor and a free trade nation. We have been called upon with great suddenness to unlearn one philosophy and to learn a new one.

In the second place, we have not at any time since the war been a creditor nation in the pre-war English sense of being required to receive an import surplus. Part of the reason is to be found in the dominance of capital items in our balance of payments year by year. Whatever the income account may have been, we have in fact exported capital on balance. This condition has continued even during the depression, taking the form mainly of withdrawals of short-term balances from our market. In consequence, there has been no direct and immediate pressure upon foreign nations to ship us goods on balance, for under these conditions the foreign exchange for interest and other payments due us is supplied, not out of the sale of a surplus of goods to our market, but out of our own capital exportation. German borrowing from us in the period prior to 1928 and its relation to her own reparation payments provide a familiar illustration. The problem is further complicated by the fact that even if we put on one side all the capital items in the balance of payments and look only at the

income items, there is no clear indication of a creditor position. Tourist expenditures abroad and immigrant remittances roughly balance incoming payments on account of interest, and in most years have shown an excess of outgoing payment.

Besides the incorrect appeal to the facts of our own case, the emphasis placed by the critics upon the trade-balance position seems to me to be exaggerated. Whatever the balance position may be, a high tariff undoubtedly interferes, item by item, with the ability of foreign nations to make interest and other payments in the form of goods and does divert payment into other media, including gold. There is, moreover, a relation between our protectionist policy and our capital exports. Much capital, for example, has gone to Canada, and there the connection is very clear. When we impose a tariff on Canadian goods we do one of two things: either we create a price-cost differential in favor of our country relative to Canadian prices and costs, or we induce a retaliatory increase in Canadian duties. In either case, there is a good reason for capital to move from our market to the Canadian market. Interference with the free movement of goods invites an alternative movement of the factors of production. The same point can be made, though with perhaps less force, with respect to our tourist expenditures. In so far as our tariff alters the terms of trade in our favor and renders more difficult the inflow of goods, the fall in foreign prices and costs relative to our level makes our money incomes go farther in a foreign country than at home. I would not push these points too far; what they suggest is that our tariff by affecting the terms of commodity trade has had also an influence on other items in the balance of payments, so that we are not in a position to know what our total balance would look like without a high protective tariff.

Perhaps the actual rates of duty, extreme though they are in many instances, are less objectionable than the principle on which they purport to be based. In 1922 we announced the cost-equalization principle. It sounds highly scientific; it is, actually, absurd. This principle says that in so far as foreign costs are lower than our costs, we are entitled to a duty to make up the difference. If rigorously applied it would work as follows: after the imposition of a duty our prices would tend to rise relative to foreign prices; as foreign prices and

[282]

costs fell a point would be reached at which particular imports could again occur; but such an occurrence would call logically for a further investigation of costs and a further increase of duty. In so far as it is applied, the principle amounts to saying that we do not believe in the receipt of goods from foreign countries.

The Tariff Act of 1930, in which we reaffirmed this principle, was super-imposed on duties already high. Begun as a means of increasing protection to agriculture, it developed characteristically into an all-round increase. The chief significance of the duties on agricultural products was not in their direct effects upon trade, since we are still mainly an agricultural exporting rather than an importing nation, but in the opportunity afforded to experiment, with unfortunate results, with the price mechanism in our own market. The industrial duties, since they were already in many instances prohibitive, probably had less direct effect upon trade than upon sentiment. Our action was enormously discouraging to the world and created a wave of animosity against us. Coupled with the act of 1922 it profoundly reinforced Europe's conviction that the American high-protectionist policy is a root cause of the world's difficulties. Personally, I have felt that this view contains much exaggeration and that the world would probably have had a very similar experience in the post-war period taken as a whole had all other factors operated as they did and the American tariff position remained unchanged after 1913. I have also felt that European tariffs and other trade restrictions have hurt Europe more than our tariff, because the European countries trade primarily with each other. But these are, after all, nice distinctions. It seems clear enough that our policy has been unsound in principle, extreme in degree, and bad in effect.

The situation that immediately confronts us is one of great emergency. The fall of world prices, particularly of agricultural prices, has greatly intensified an already unbalanced international situation and forced each nation to resort to defensive measures to protect its internal economy, which action has forced other nations to take like recourse. The accompanying condition of panic, leading to sudden withdrawals of short-term balances from the leading markets, has from time to time and particularly in 1931 greatly intensified the dis-

[283]

turbance and led to a new wave of trade restrictions. The result is a tangled network of defensive measures, which may be classified under four main types: (1) depreciation of currency, involving departure from the gold standard; (2) control of foreign exchanges, permitting a purely nominal adherence to the gold standard at a par of exchange maintained by means of restrictions upon the outflow of payment; (3) direct restrictions upon international trade by prohibitions, quotas, contingents, clearance agreements, licenses and similar devices; (4) indirect restrictions on trade by tariff rates.

It is important to recognize that these defensive measures, while differentiated in form, are essentially one in origin, purpose, and effect. It is also important to recognize that they are not in the main the result of deliberate voluntary action. But the general effect is that of destructive economic warfare resulting in a progressive strangulation of international trade, which in turn reacts disastrously upon domestic trade and employment. The total value of world trade is one-third of that in 1929 and the physical volume has fallen by at least 25 per cent, by far the largest decline on record. Meanwhile, stocks of a number of raw products are double those of 1925; world unemployment is estimated as at least thirty millions, exclusive of dependents; and national incomes have fallen by more than 40 per cent.

Under conditions like these it does not behoove us to enter into the refinements of commercial policy, theories of free trade versus theories of protection; they do not apply. What is required is a world solution for a world collapse. In the nature of the case remedial action cannot be undertaken by any one nation without supporting and compensating action on the part of others; to quote the language of the World Conference agenda, what is required is "a broad solution by concerted action along the whole front." The time has come to find out how much common sense there is in the world.

REMARKS BY THE CHAIRMAN

CHAIRMAN BURGESS: The discussion will be continued by Professor James W. Angell, of Columbia University, who has often addressed this audience before. He will speak on "Exchange Depreciation, Foreign Trade and National Welfare." I have pleasure in introducing Professor Angell!

[284]

EXCHANGE DEPRECIATION, FOREIGN TRADE AND NATIONAL WELFARE

JAMES W. ANGELL

Professor of Economics, Columbia University

WITHIN the last few weeks, the question of foreign exchange depreciation has taken on a new and vital significance for the people of this country. From 1879 until March 4 last, with the sole exception of the period of the World War, we were on the gold standard, and our exchanges were stable. The government bought and sold gold in return for currency at a fixed price, without limit on quantity, and the import and export of gold were entirely unrestricted. From time to time, other countries suffered from depreciation of their currencies in terms of the foreign exchanges, but not we. Other countries might abandon the gold standard, undergo the inconveniences and losses usually entailed, and then painfully clamber back to a stable base. We viewed their gyrations with some sympathy, more irritation, and perhaps a measure of satisfaction at our own superior arrangements. But what was involved was always a fluctuation of the foreign currency, not of our own. Our own currency, in terms of the standard measure, gold, remained stable.

Now the picture has become radically altered. Since March 4, 1933, and especially since April 19, American currency has become unstable in terms of gold. Gold exports are forbidden, gold is in fact not obtainable for internal use, and the principal foreign exchanges have moved substantially against us. For the first time in over five decades, except for the war period, we are viewing exchange depreciation from the other side. We ourselves are now one of the depreciated countries. The question of what happens to a country when its foreign exchanges depreciate, of what we may expect next, has suddenly become a matter of intense national concern.

[285]

THE GENERAL THEORY OF EXCHANGE DEPRECIATION

The general theory of the effects of a moderate depreciation of the foreign exchanges, so far as these effects can be separated from other contemporary phenomena, is familiar. At first, the depreciation gives a bounty to the exportation of commodities, since the same price as before, in terms of the foreign currency, now provides a larger yield than before in terms of the domestic currency. Other things equal, the current physical volume of exportation therefore increases. On the other hand, for analogous but opposite reasons, the physical volume of importation decreases; the depreciation operates like a general *ad valorem* tariff. But these changes are not permanent. A number of factors, usually substantially the same as the ones which caused the exchange depreciation to take place, are likely to produce a rise in prices and costs of production within the depreciated country. This rise reduces both the bounty on exports and the penalty against imports. If the original exchange depreciation was of only moderate severity, and if the exchanges are now held approximately stable at some new lower level, most classes of internal prices and costs will catch up with the exchange depreciation fairly promptly. The greatest part of the export bounty and the import penalty will then disappear. The country retains a permanent advantage in foreign trade only to the extent that certain kinds of internal costs of production, such as long-term interest and rent charges, and to a less extent various tax charges, are fixed in terms of money and fail to rise. A marked appreciation of the foreign exchanges, on the other hand, is supposed to set in motion substantially the opposite chain of events. But in both cases the uncertainties involved, the marked though usually temporary shifts in the channels of foreign and domestic trade, and the frequently enduring changes in the distribution of real wealth and income, are likely to leave the country less well off than before—to leave it with a smaller rather than a larger total of goods and services to consume. There is little in the deductions of general reasoning to warrant the expectation that inflation, for example, can permanently increase the real welfare of a country; on the contrary, real welfare is extremely likely to be diminished.

This general theory of the effects of moderate foreign ex-

[286]

change depreciation was borne out with substantial consistency by the actual history of the depreciated-exchange countries before 1914, and by the course of events immediately after the war. Analysis of the flood of post-war depreciations is of course complicated by the numerous other disturbing factors which were at work. Moreover, in a number of cases the depreciation passed rapidly to such extreme forms that internal economic activity came almost to a standstill; such was the result in Germany. To these latter types of situation, rather different considerations must be applied. In the main, however, the facts were in substantial conformity with the theory just outlined.

A second great wave of moderate depreciation in terms of gold began a year and a half ago, when Great Britain went off the gold standard. A dozen countries followed her example almost at once, and a number of others took similar steps somewhat later. The magnitude and scope of what has happened is without precedent in the world's peace-time history; it has been no less than a revolution. Among the large countries, until March 4 only the United States and France had remained on the unrestricted gold standard, though Germany and Italy had kept their exchanges stable; and now the United States has joined the group of depreciated countries. Hardly half a dozen nations of importance are today either on the full gold standard, or even on an exchange base which is stable in terms of gold. An appraisal of the actual effects of these recent depreciations on the depreciated-exchange countries themselves is therefore worth attempting, for the light it casts on what we may ourselves expect.

EFFECTS OF THE RECENT DEPRECIATIONS

The effects of the foreign exchange depreciations which have taken place within the last nineteen months are difficult to isolate and judge correctly. This is true for two principal reasons. In the first place, the depreciations developed in the midst of the steadily deepening depression of world business activity, which began in 1929; in large measure, they were of course themselves the product of this depression. In consequence, nearly all of the phenomena at issue must be measured in terms of a shrinking base. The question to be answered becomes, in most cases, not that of determining what increases

[287]

or decreases took place as the result of exchange depreciation, but of determining whether the actual decreases would have been greater or less, had there been no depreciation. In the second place, when the depreciations began to develop on a substantial scale nearly every country in the world, whether its own exchanges were stable or not, began to take direct or indirect measures to restrict imports from the depreciated countries. To the extent that these measures were actually effective, the temporarily stimulating effect of exchange depreciation on the exports of the latter countries was of course nullified.

Despite these difficulties, however, a survey of the accessible general data enables certain conclusions to be drawn with a reasonable degree of confidence. Broadly stated, these conclusions are that, first, the appearance of exchange depreciation in terms of gold did not bring about a substantial revival of general business activity in any of the depreciated countries; but second, however, the appearance of exchange depreciation actually was associated with a decrease in the current rate of decline of business activity in some of these countries, and with a cessation of the decline in others; and, third, the countries which retained stable foreign exchanges suffered, as a group, substantially more rapid declines in business activity than those countries whose exchanges depreciated.

To interpret these conclusions correctly, it is necessary to elaborate them somewhat, and to indicate the factual basis on which they rest. In the first place, the period of the depreciations now in question has as yet been short, and the depreciations themselves moderate. Most of the depreciations from which the conclusions are derived date only from September, 1931, or later, and complete data on them are not yet available after December, 1932. The period which can be examined hence covers only fifteen months or less. Among thirteen major countries in this group, for which reasonably extensive information is available, the (unweighted) average foreign exchange rate in December, 1932, stood at 69.4 per cent of the gold par, with a range for the group between a low of 42 and a high of 91. To date, the scale of the depreciations in terms of gold has thus kept within fairly moderate bounds.¹

¹ The countries selected are Denmark, England, Norway, Sweden, British

In the second place, the adjustments of internal prices and costs which theory leads one to expect in the depreciated countries had gotten well under way by the end of the period, but had not yet had time for full development. In the ten principal countries retaining stable currencies, the average wholesale price level for 1932 stood at 89 per cent of 1931, and the average cost of living index at 93.¹ But for eleven of the depreciated countries, for which recent price data are available, the average wholesale price level in 1932 stood at 103 per cent of 1931, the cost of living index at 98.² This virtual constancy in absolute terms, appearing at a time when the countries with stable currencies were undergoing substantial price declines, can evidently be regarded as a relative *increase*.³ Had the average price index for these depreciated countries risen in full proportion to the average exchange depreciation, however, with prices in the stable countries taken as the base, it would have reached 128.⁴ The adjustment of internal prices to the new exchange levels, which usually appears in due course, was hence only about a third completed

India, Argentina, Canada, Chile, China, Japan, Mexico, Peru, Spain. The exchanges of Brazil were held stable after July, 1932; this country is hence not included. If we omit Chile and Japan, which in December 1932 had exchange rates standing at 49 and 42 per cent of par respectively, the average for the eleven remaining countries in this group rises to 74; and the lowest figure rises to 61. These last two countries are in a sense "unrepresentative" of the bulk of the present depreciations, since they have been undergoing marked internal inflations; and Japan has in addition been engaged in extensive military activity abroad.

The factual information used here and in subsequent paragraphs is taken from the League of Nations, *Monthly Bulletin of Statistics*.

¹ The ten stable countries selected are Austria, Belgium, Czechoslovakia, France, Germany, Holland, Italy, Poland, Switzerland, the United States.

² Price data for Argentina and Mexico are incomplete. Omitting Chile and Japan, the averages for 1932 both stood at 97 per cent of 1931.

³ This is a substantial part of the explanation of why England underwent no large change in prices after quitting the gold standard. Another part of the explanation, not inconsistent with this but standing on different ground, is stressed by various English students: namely, that England went back to gold in 1925 at too high an exchange parity, so that her prices were subsequently "too low"; the depreciation in 1931 merely adjusted her exchanges to her prices. It should also be observed that the quantity of English currency and bank deposits has remained remarkably stable.

⁴ Omitting Chile and Japan, 122.

by the end of 1932. We should therefore expect to find the effects on foreign trade and production which theory attributes to the first main phase of foreign exchange depreciation, still in actual operation during this period; and such is actually the fact.

In the third place, the depreciated countries came out decidedly better in foreign trade, during this first phase, than did the stable countries, and curiously enough came out better in imports as well as exports. To secure a broad base and to eliminate seasonal influences, I have compared the foreign trade figures in 1932 with the average of 1929 and 1931 taken as 100, using the same ten stable currency countries and the same thirteen depreciated countries as before.¹ In terms of money volume of trade, the (unweighted) average imports of

¹ The summary figures for foreign trade in the two classes of countries, showing the trade in 1932 as a per cent of 1929, of 1931, and of the average of 1929 and 1931, are as follows; figures in parentheses indicate number of countries available for each sample.

		Values		Weights	
		Stable (10)	Unstable (13)	Stable (7)	Unstable (4)
1932 imports as per cent of.....	1929	42	50	72	62
	1931	69	77	82	89
	Average.	56	64	77	75
1932 exports as per cent of.....	1929	40	51	66	78
	1931	60	85	78	93
	Average.	50	68	72	85
Unweighted average for total trade.....		53	66	75	80

The percent which the recorded relative levels of exports for 1932, measured against the average of 1929 and 1931, formed of the similar levels of imports, were for these countries as follows.

	Stable	Unstable
By value	89	106
By weight	93	113

[290]

the stable countries fell in 1932 to 56 per cent of the base figure, the imports of the depreciated countries to only 64 per cent. The exports of the stable countries, on the other hand, fell to 50 per cent of the base, the exports of the depreciated countries to only 68 per cent. Thus the decline was less in both categories for the depreciated countries; and whereas in the stable countries exports declined more than imports, in the depreciated countries exports declined *less* than imports. The available figures based on weights, which because of price declines show a smaller decrease than the money volume figures, reveal precisely the same relations. The differential advantage to exportation, which theory anticipates in the first main phase of exchange depreciation, thus developed in actuality for a large group of depreciated countries.¹

The data on physical production and on employment, so far as they go, tell a similar story. The (unweighted) average index of industrial production for eight stable countries in 1932, compared with the average of 1929 and 1931 taken as a base, declined by 32 per cent; the average for five depreciated countries fell only 11 per cent, and in the case of one of these countries actually rose a little.² Here again the first main phase of exchange depreciation was thus associated, if not with an actual revival of general business activity in the depreciated countries, at least with a much less rapid decline than in the stable countries. This too can evidently be described as a relative increase.

¹ Reference should be made here to the recent study by the U. S. Tariff Commission, entitled *Depreciated Exchange* (3 Parts: 1932), undertaken in response to Senate Resolution No. 156 (72d Congress, 1st Session). Also see the summary of this study in the *Annual Report* of the Tariff Commission for 1932, pp. 59-61. Concerning itself only with the effects of depreciation abroad on the foreign trade of the United States, covering only the period from October, 1931 to March, 1932, and using a narrow and base for purposes of comparison, the Commission found little difference between foreign stable and depreciated countries, with respect to the recent changes in our own foreign trade.

Also see W. O. Scroggs, "Depreciated Currencies and World Trade" (*Foreign Affairs*, April 1933).

² The countries for which current indices of industrial production were available are as follows. Stable countries: Austria, Belgium, Czechoslovakia, France, Germany, Hungary, Poland, United States. Unstable countries: Canada, Chile, England, Japan, Sweden. The index for Japan, measured on the indicated basis, stood at 101 for 1932.

[291]

The general course of events in the past year and a half has thus been comparatively favorable to the depreciated countries—or, to be more accurate, has been less unfavorable to them than to the countries with stable exchanges. Prices in the depreciated countries, with one or two exceptions, have remained nearly constant instead of falling; foreign trade and industrial production have declined less sharply than in the stable countries; and exports have declined less than imports. But it would clearly be quite erroneous to conclude from these facts alone, without further qualification, that exchange depreciation is a desirable thing in itself. The period covered to date embraces only the first main phase of depreciation, which is also the phase that is superficially most advantageous to the depreciating country. In the great majority of the countries considered, very little change has as yet taken place in prices or other internal costs, and in most of them there has as yet been little expansion of currency and credit—little internal “inflation”. If their internal prices begin to rise, as they very well may, the foreign trade advantage which these countries now enjoy in dealing with the stable countries will dwindle and disappear¹—unless they then depreciate their exchanges still further; and in that direction, as is all too familiar, lie only irreparable loss and disaster. Moreover, it is evident that even this temporary advantage which they now have is dependent on the maintenance of exchange stability, or at least of a lesser degree of depreciation, in foreign countries. Exchange depreciation is a purely relative phenomenon, not an absolute condition. If all countries were to “depreciate” their currencies equally in terms of the foreign exchanges there would be no actual exchange depreciation at all, and no foreign trade advantage.

Finally, the advantages which the countries with depreciated exchanges obtain are not, in a manner of speaking, absolute advantages, but are obtained dollar for dollar at the expense of the stable countries. The situation which stimulates the exports of the first group restricts *pari passu* the exports of the second group; and conversely for imports. In the last year and a half, the serious distortion of foreign trade channels and

¹ The same effect would be produced if prices in the stable countries fell to an equivalent extent.

the intensification of international competition, which widespread exchange depreciation has produced, have been a major factor in deepening the world depression itself. Until the present evils of fluctuating exchanges are ended, no general recovery of world trade can take place.

Taking the situation in the aggregate, it can safely be concluded that the countries which have allowed their exchanges to depreciate in terms of gold, in the last fifteen months, are not better off as a whole than they were before; in real terms, they are rather worse off. Their position seems relatively better now than that of the stable-exchange countries only because in the latter countries, for reasons having in the main rather little to do with the maintenance of the gold standard as such, the volume of business activity has been declining with even greater speed. To date, the depreciated countries have benefited from a relative expansion—to be accurate, from a less rapid contraction—of their export trade. They have also benefited, insofar as they are debtors on balance to foreign countries, from the fact that going off the gold standard has prevented the process of paying their foreign obligations from forcing further internal contractions of currency and credit. But these are in the nature of the case only temporary advantages. Meanwhile the depreciated countries are paying more than before for their imports; it is costing them more than before, in terms of goods and human effort, to meet their current obligations abroad; and insofar as their prices are rising, they are helping the profit-receiver within their borders at the expense of the creditor, the wage-earner and the salaried man.

THE PRESENT POSITION OF THE UNITED STATES

We come now to the position of the United States. Until March 4, the United States was on the stable-currency side of the situation, and suffered all the marked if presumably temporary disadvantages which attend that status. Our exports to the depreciated countries were seriously hampered, and our own manufacturers complained bitterly of the unnatural advantage which foreigners had acquired here—an advantage which not even our own remarkable tariff could wholly offset. The fact was overlooked that some of the imports which were most objected to came from countries with stable exchanges; and that the country as a whole was getting its imports sub-

stantially more cheaply than before. Now, however, we are on the other side of the same situation, and have ourselves become a country with depreciated foreign exchanges. What will happen, both to our foreign trade and to our economic position as a whole?

What will happen depends in largest part on what we ourselves do. Our recent abandonment of the gold standard was in many ways a phenomenon without parallel in economic history, and one whose wisdom many have questioned. Despite the world depression, we are still a country with a substantial excess of commodity exports over imports, with a substantial current income from foreign investments, and with no large obligations currently coming due abroad. The panic which compelled the closing of all banks for over a week in March also compelled a suspension of gold payments and gold exports, but the panic soon disappeared. When we abandoned the gold standard, we still had very large excess gold reserves; our discount rates were at comparatively low levels; the federal budget was being brought nearer equilibrium than in years; and there was no unmistakable evidence of any unmanageable pressure against our foreign exchanges. On the contrary, much reputable opinion holds that removal of the remaining restrictions on gold exports would have automatically dissipated such pressures as actually existed. Yet in the face of this basically favorable situation, we went off the gold standard, and went off without a struggle. The action is without precedent. Why was it taken? The authorities responsible appear to have felt that exchange depreciation abroad was exerting a depressing influence on the American price level, and desired to offset this influence. To some extent, the diagnosis was undoubtedly correct. But in the very nature of the case, as remarked before, this depressing influence could only be temporary in character; indeed, it had already begun to abate as the depreciated countries adjusted themselves to their new position. Nor can it easily be shown that the way to compensate for exchange depreciation abroad is to depreciate your own exchanges. It is rarely true, even in finance, that two wrongs make a right.

At least for the present, however, that water is over the dam. The abandonment of gold, while bitterly attacked in some

[294]

quarters, has been enthusiastically applauded in others, and in any event the step cannot be retraced quickly. It has already produced certain marked effects. Our exchange rates on leading foreign centers have depreciated by amounts which still vary from day to day, but which have run up as high as 15 per cent. This means that American exports are cheaper in terms of foreign currencies than before, and as a consequence certain export industries have already received increased orders from abroad. On the other hand, of course, our imports are costing us more than before,—such things as silk, rubber, paper, pulp, sugar, coffee, tin—and that can hardly be regarded as a national advantage. At home, the markets for securities and basic commodities have swung violently upward, in anticipation of measures of internal inflation which have not yet materialized; and on the same ground, there has been some increase in the real activity of business. It should be observed that these are of course the favorable initial effects which usually accompany the first main phase of an exchange depreciation.

If internal inflation does not in fact take place, however, and if prices do not increase substantially for other reasons, then the sole major effect of the abandonment of gold on our foreign trade will be to stimulate our exports somewhat, and to penalize imports. This really means that we shall then be giving a somewhat larger quantity of exports than before per unit of imports, and hence, though most of us will not realize it, that the terms of our foreign trade are really moving against us. But that situation is likely to prove temporary; if nothing else happens, our exchanges are likely to return to something like their former levels. If our internal prices do rise, on the other hand, then to that extent the effect of the exchange depreciation will be nullified. But in the present situation, any rapid rise in general prices is likely to come about only through deliberately inflationary measures undertaken by the federal government. Inflation may in fact be the only path out of the present depression, for us, but it is a path which I view with the gravest misgivings. Past experience, including our own, gives little ground for confidence in the success of inflationary measures, even when operated by the most astute politicians; and gives little ground for hope that, by so-called "control,"

[295]

it can be kept within predetermined limits. The usual course of inflation is first a substantial initial stimulus, such as we are now beginning to experience; then a period of disorganization and loss; and then either a painful struggle back to a stable currency base, or a tragic plunge into that vortex of rising prices and increasing quantities of money, which eventually destroys the currency itself. If there were any guarantee that inflation in any form would really revive business activity more than momentarily, and would bring back lasting prosperity, I would be the first to support it. As far as past history and general reasoning afford a guide, however, just the opposite is the case. Inflation, as a cure for business depression, simply does not work; at the end, it leaves the country only with a huge balance of net loss and suffering.

With such an outcome almost surely ascertainable in advance, it seems to me merely irrational to embark on that course of action. We have yet to explore the effects of reciprocal tariff reductions, of other forms of international coöperation, and of many sorts of internal adjustments which are now in process. Instead, we are helping to force the world and ourselves back to where we were in 1919; and the odds in our favor are rather smaller now than they were then.

The hope I see in the situation is the hope that quasi-dictatorial powers over currency and credit will be given to the Administration,¹ thus choking off the more irresponsible of the projects now before Congress; that the Administration will then make little or no actual use of these powers, unless for individual relief purposes; and that through patience, the working out of innumerable adjustments now taking place, and adherence to sane counsels, a way out of the present morass will be found. Shot-in-the-arm schemes are almost certain, in the long run, to do more harm than good; we cannot, by overnight magic, transport ourselves into the millennium.

REMARKS BY THE CHAIRMAN

CHAIRMAN BURGESS: Our next topic is "Import Quotas and Other Factors in the Restriction of Trade." The speaker will be Mr. G. R. Parker, of William B. Nichols and Company, New York. Mr. Parker is former President of the American Exporters' and Importers' Association. Mr. Parker!

¹ Effected by the Act signed May 12, 1933.

IMPORT QUOTAS AND OTHER FACTORS IN THE RESTRICTION OF TRADE

G. R. PARKER

Of William B. Nichols and Company, New York
Former President, American Exporters' and Importers' Association

IF it were true that words are given us to conceal our thoughts, it might be added that statistics are given us to obscure our objectives. I know of no more dreary way of attempting to prove a point than to approach it through the medium of massed tabulations and comparative figures. In the very simple and elementary remarks I have to make on a very broad and involved subject, it is my purpose to avoid any such procedure in coming to a timely conclusion.

The primary reason why the subject of international trade restrictions is so complex is that individual and universal welfare appear to be in conflict. Groups of people do what they know to be *wrong in principle*, but believe will benefit them. One is somehow reminded of the anecdote about the members of the congregation which gave a barrel of wine to the minister. As each received the cask to supply his portion, each poured in a pitcher of water, thinking that so slight a dilution would scarcely be discovered. The minister, who for the purpose of this allegory may be assumed to typify universal welfare, can scarcely be said to have profited. Yet each individual believed himself better off.

World society is today organized into a number of political units, the boundaries of which have been fixed by the accidents of history, rather than by economic or even wholly ethnological considerations. To quote Mr. H. G. Wells, a nation is a group of people, "which is either afflicted by or wishes to be afflicted by a foreign office of its own, in order that it should behave collectively as if it alone constituted humanity".

Now each nation, because it feels that it must foster its own industry, or protect its currency, or rectify its trade balance, and so on, has proceeded to place varying restrictions on its trade, principally on its imports, that is on the exports of other countries. The result of this widespread economic nationalism

is that merchandise is denied its natural market, or forced to artificial price levels. Goods cease to pay for other goods. Ships carry partial cargoes or rust at their docks. As a practical illustration let us trace the course of American foreign trade. In 1929 total American exports and imports amounted to \$80 per capita; in 1930 to \$58; in 1931 to \$37; and in 1932 to \$24. The rate so far this year is still lower. Putting it another way, the head of a family of five did business with foreigners in the amount of \$400 in 1929, and \$120 in 1931—a decline of about 70 per cent. To cite a single example of how this bears on domestic trade, let us recall that ordinarily out of every two bales of cotton grown in this country, one is sold to foreigners. And the manufacturers, the mail order houses, and others trying to sell goods in the South have a very vital interest in the bale which should be going abroad.

In places like China, we have the all too frequent spectacle of famine in one part of the country, while abundant harvests are being garnered in another. Here the explanation is simple. There is no adequate transportation system. And it seems to me that one of the major causes of the present world depression is in a broad sense much the same. The distribution system has broken down. Goods have been prevented from moving freely.

The progress of human civilization has been concurrent with the growth of trade. In the animal kingdom there is no trade. Each adult animal supplies its own wants. Savage society is much the same. It is when men begin to exchange the product of their labor that we note progress. It is still possible for the individual to get along with very little trading, but the result is a primitive peasant class, with little living margin over bare sustenance, and closely bound to the soil. Modern society, slowly evolving through the ages, has been developed by individual production in excess of individual needs, and trading the resulting surplus for the similar surplus of others. When trading ceases depression ensues.

There are of course intermediate stages. Thus if the producer is compelled to trade only with his immediate neighbors, there are definite limits to the surplus he can dispose of. As his trading horizon broadens, his capacity for the exchange of goods increases. In a word, his own purchasing power is greater, and his standard of living higher. It is therefore

[298]

almost self-evident that the greatest prosperity for the individual is achieved through the widest possible markets for the product of his labor.

In the face of this axiom it would seem logical in a period of world depression to seek a remedy through widening, rather than narrowing the avenues of trade. As far back as 1927, when there was as yet no hint of coming disaster, the World Economic Conference in Geneva declared:

The experience of the years since the war proves that import and export prohibitions, and the arbitrary practices and disguised discriminations which result therefrom, together with the obstacles of all kinds placed on the circulation of goods and capital, have had deplorable results by hampering the normal play of competition, by imperilling both the essential supplies of some nations and the not less indispensable markets of others, and by bringing about an artificial organization of production, distribution, and consumption.

Experience has shown, moreover, that the grave drawbacks of these measures have not been counterbalanced by the financial advantages or social benefits which were anticipated.

It is therefore important for the recovery and future development of world trade that the governments should forthwith abandon an economic policy which is injurious to the interests both of their own and other nations.

Let us see now what has happened in the very recent past. According to the United States Department of Commerce, during 1932 trade barriers were introduced or increased by no less than sixty-five commercially important countries without taking into account those restrictions incident to exchange control. In Europe general tariff increases occurred, ranging from the Netherlands increase of duties by three-tenths, to the Estonian imposition of a 15 per cent tax on all payments made abroad, in addition to its regular tariffs. In South America similar increases of import duties occurred, or what amounts to the same thing, larger percentages were imposed as consular fees.

Apart from tariffs, the effort to limit the decline in currency valuation in terms of gold or of foreign currencies has impelled many countries in Europe, Latin America and Asia to adopt some system of artificial exchange control. The effect is to discourage imports since it becomes difficult, in varying degree, for the importer to secure funds with which to effect payment. With the exception of Belgium, Finland, France, Lithuania, the

[299]

Netherlands, Poland and Switzerland, all European countries had by the end of 1932 put into effect a greater or less degree of exchange regulation. Apart from France, with its devaluated currency, nearly every commercially important country has now actually or practically abandoned the gold standard.

Finally and in addition to tariff and exchange barriers, the past year has witnessed widespread increase in the limitation of imports, through the adoption or extension of the quota system, and what is closely related, the regulation of importations through license requirements.

The quota is a wholly arbitrary device whereby the government declares that purchases of certain articles from abroad shall not exceed a fixed number or quantity. The total is then allotted in varying proportions to the producing countries. The license system provides that the importer shall be compelled to obtain formal consent, from some government agency, before bringing the particular goods into the country.

With the possible exception of the British Empire, which has so far not widely adopted it, the quota system is now to be found throughout Europe and other parts of the world. Its viciousness resides primarily in the opportunity provided for unfair and discriminatory practices. Quotas are of necessity arbitrary both as regards other countries as a whole, and as to the industries within these countries. For example, France establishes an import quota on radio receiving sets. Under this a certain quantity is allotted, let us say, to the United States. But it then remains for some body such as the American Chamber of Commerce in France to divide this quota among various American manufacturers. The probability of dissatisfaction and grievance is apparent. Obviously there is no scientific method of establishing a universally fair system. It is common to base a quota on past performance, as for instance the average imports of the article from a given country for the three preceding years. Clearly the effect is to perpetuate results of past conditions which may have meanwhile undergone radical change.

To visualize how this operates, let us assume that Latvia and Finland have been exporting mouse traps to Bulgaria. The latter decides to establish a quota on mouse traps based on a three-year average. The record shows that Latvia's exports for the preceding year, and for the two previous years were at

[300]

the rate of 2, 4 and 6 respectively per annum, or a total of 12 for the three years. The corresponding record for Finland was 5, 3, and 1, or a total of 9. Now evidently Latvia's three year average is 4, and Finland's 3. The quotas are now fixed in this ratio. As a result Latvia is allowed to bring in 33 $\frac{1}{3}$ per cent more than is Finland. Yet an examination of the figures shows at a glance that prior to the quota, Latvia's product was on the decline, while Finland's was increasing. In the competitive race for the Bulgarian mouse-trap market, Finland was in process of passing Latvia. Its product presumably had become cheaper, or better, or both. Yet Latvia with apparently declining efficiency and lower capacity to compete, is allowed the greater share of the business.

Having passed this inequality, how can any body representing the exporting country make any pretense of an equitable distribution of the quota among its own producers? The same problems have to be met in an equally unscientific manner.

The opportunities for real or alleged favoritism and discrimination are evident. National, racial and personal likes and dislikes can scarcely fail to jeopardize any semblance of unbiased determination.

Let us now examine for a moment the distressing picture as a whole. In the years since the war, and with rising crescendo in the immediate past, national governments throughout the world have set up barrier after barrier and restriction after restriction. Feverish nationalism, retaliatory action against others, and mistaken efforts to create islands of prosperity in an ocean of depression, have been the motivating factors.

At the same time and with the same purpose attempts have been made to distort the normal course of trade through sentimental propaganda, exemplified by such movements as "British Goods are Best" or "Buy American". One can scarcely be accused of specious casuistry in pursuing this to its absurd conclusion. Why not with equal logic "Buy New England"? Then "Buy Connecticut" and finally "Buy Danbury". Then the Danburyites may wallow in the prosperity engendered by a plethora of hats. Why allow Michigan-built automobiles to compete with local industry in Ohio? And should not patriotic Detroiters not only buy and use their own motor cars, but preferably drive them on their bare rims rather than import rubber tires made by Akron labor?

[301]

The end and goal of all these trade-restricting policies is clearly visible. It is the continual narrowing of trading areas, the reduction of the possible market for the products of labor, and resulting lower individual purchasing power and living standards. Theoretically at least, if logically carried through, it would mean a return of mankind to its earliest state, in which small groups, the family or the tribe, consumed what they produced. In such a society a surplus over consumption requirements is of no value, since it cannot be exchanged. It is in fact what in our more advanced civilization we choose to call overproduction. We must go back some hundreds, if not thousands of years to find the world's people eking out so bare and cheerless an existence. Yet it is precisely along this retrogressive road that the political and economic isolationists would drive us.

Happily there have been evidences here and there of an awakened national intelligence. The Stresa Conference of last year reached an agreement as to mutual preferences on agricultural products among the countries of the Danube basin. The Oslo Economic Convention, to which the Scandinavian countries, Belgium and the Netherlands are parties, provides against upward tariff revision. And the later agreement between the Netherlands and Belgium initiated positive tariff reductions. These and other isolated measures, relatively minor, and confined to limited areas, are nevertheless encouraging. If a system is good for a group of European states, if it is good for a group of North American states, it may one day dawn on the public consciousness that an integration of such systems might be logical. It is not too much to hope that the forthcoming International Economic Conference may be a step in this direction.

REMARKS BY THE CHAIRMAN

CHAIRMAN BURGESS: We turn now to another much discussed phase of the tariff problem, "The Relation of the Agricultural Problem to Tariffs." Senator Dickinson of Iowa was scheduled to present this paper; he is otherwise occupied today in the pressing business of the Senate. He sent word that he greatly regrets his inability to be present. He has sent his paper and it will be read by Professor Parker T. Moon, of Columbia, and the Secretary of the Academy of Political Science. Professor Moon!

[302]

THE RELATION OF THE AGRICULTURAL PROBLEM TO TARIFFS

HON. L. J. DICKINSON
United States Senator from Iowa

THE Association of Land-Grant Colleges and Universities in November 1932 reported that

the difficulties in which the world finds itself are related to (1) the monetary, credit, and trade policies followed during and after the World War, (2) the over-expansion of production and productive capacity in many industries, with an accompanying increase in the volume of indebtedness, (3) the unparalleled orgy of speculation in securities, (4) the trend toward economic self-sufficiency, especially among European nations. This trend resulted in considerable degree from obligations to pay war debts and reparations, and from efforts to escape the effects of falling prices and was manifested in trade barriers and import restrictions that retarded international trade and curtailed the foreign demand for products of this country.

The trend above noted was not directed in retaliation but was a program for self-preservation by our foreign neighbors. It is natural, when conditions are on the down-grade, for every nation to do whatever is possible to preserve its own interests, and that is the program that has been followed by the nations of the world since the close of the World War.

Nations naturally follow the disposition of the individuals. When the individual found that his income was being curtailed, he immediately retrenched. His house was left unpainted; his old automobile was driven another year; his old shoes were resoled. Every principal retrenchment curtailed his trade with his associates and his neighbors. Governments did exactly the same thing. It was not retaliation; it was self-preservation.

Many people are inclined to insist that the falling off of our world trade is due entirely to the tariff policies of our own country. In discussing the collapse of international trade, many contend that tariffs have destroyed such trade, and that it cannot be revived until these restrictions are removed. But Wallace B. Donham states:

[303]

In my opinion the collapse of international trade results mainly from serious over-production of raw materials, stimulated by competition among the industrial nations and followed by the sharp fall of commodity prices. This over-production and price collapse is the primary fact and trade restrictions are mainly a result.

The fact that the foreign trade of all countries has declined in about the same percentage as the general economic condition is convincing that tariff is not the cause. Free-trade countries have had a percentage decline similar to that suffered by protective countries.

Apparently, from the statement of Secretary Hull, we are to embark upon a new international policy. It is the theory that by lowering the American tariff and by negotiating reciprocal tariff agreements with other countries, we shall be able to increase our imports and expand our exports. If this can be done, it is of material interest to the farming population of the United States. It should be remembered that our main exports are wheat and cotton and pork products in the agricultural group, and automobiles, machinery, oil in the industrial group. In accepting an international policy of this kind we depart from the traditions of previous years that have served our country well.

Let me further suggest that 65 per cent of all of our imports are duty-free; that the list of articles on the free list includes practically all of the products not produced within our own border lines. Certainly coffee, tea, silk, rubber, etc., are non-competitive products. Foreign interests are at liberty to ship them here and exchange them at will.

It is, therefore, proper to ask on what items shall the tariff be reduced? Can we give a list upon which, with safety to home interests, a drastic reduction in the tariff rate can be made? No such list has been prepared or can be prepared. Every time we lower the tariff and allow the importation of a foreign product that can be produced in this country, we are depreciating the value of the capital investment engaged in the production of that product and putting American workmen out of employment.

Secretary Hull makes the suggestion that "a long list of American commodities could be profitably exchanged for foreign commodities that the United States does not produce

or produces in insufficient quantity, or produces in a manner not economically justifiable". Our industries here are in a position to produce every product for which the raw material is found within our boundaries. We have the labor available. What is to be gained by turning this trade to our foreign neighbors?

For this reason, the theory that we can expand our export trade, and that foreign debts can be paid thereby, is lacking in specification. Contributors to this view are among two classes of people: first, the economist or internationalist who believes that all trade barriers should be removed; second, those organizations, such as the automobile, farm machinery and tire concerns, that have reached the conclusion that they are in position to compete in the markets of the world. In contradiction to the first view, all of the countries of the world for the last fifteen years have adopted the reverse course. With reference to the ambition of the large corporations, it seems clear that this was largely due to the extreme expansion in the production of these commodities following the war and is not a practical program in ordinary times under keen competition.

Wallace B. Donham further states:

We must not delude ourselves. The only way we can maintain and increase our present exports is by increasing imports of manufactured goods which will in the main directly compete with established home industries. Shall we gain by shifting social groups now surrounding these industries into other areas and other industries whose exports may grow? Even with our relatively mobile labor such a policy will add social strains which may well overwhelm us.

But it is said that if the farmer produces a surplus of farm products, he must depend upon a world market for the surplus portion of his crop. This is true, and because of this perplexing phase of our farm marketing system, effort has been made for the past ten years to segregate the domestic consumption from the export portion of the farmers' crop.

The interest of the farmer in tariff can be best illustrated by the fact that all of the farm bills that have been proposed in Congress in the past fifteen years base their relief upon the protective tariff system. This is true of the debenture plan, the equalization fee plan, the allotment plan, and the plan now pending before Congress. On April 18, 1933, during the dis-

cussion of this legislation, Senator Smith, of South Carolina, stated: "Unfortunately, the principle of the high protective tariff is in this very farm bill raised to the n^{th} power, reaching to where it is an embargo, and yet we call ourselves Democrats." Also Senator Bailey, of North Carolina, on the same day, in talking upon the farm bill said:

We Democrats commit ourselves in this bill to a prohibitive tariff policy, being a party pledged against the existing tariff system. I have heard of paradoxes in my life, but that is the chief. In the very hour when we propose it, we see in every paper that comes forth the statement that the Secretary of State of the United States, and the President himself, are making overtures to the other nations with a view of readjusting the tariffs. We here build a wall to heaven in one moment and invite them to cut it down in the next. If that policy is sound, then we, in the enactment of this measure, are destroying that very policy.

The old slogans were: "Make the tariff effective on farm products" and "Give the farmers the benefit of the domestic market". The best interest of the farm population is, therefore, directed in three courses: First, a reduction of farm products until the surplus in excess of domestic consumption is not great. Second, a continuation of the protective tariff schedules on farm products to prevent imports from foreign countries from directly competing with our farm products in the domestic market (this will prevent low-cost production from interfering with our domestic trade). Third, the maintenance of a high industrial schedule in order that the American workman may retain his position as against the foreign workman working long hours and for low wages.

The present Administration has pointed out the desirability of reducing tariff duties on goods the farmer buys in order that foreign nations might trade goods of this type for farm products. In such a proposal consideration must be given to the question of how, if these goods that the farmer is to buy are to be imported, will the labor now employed in the production of these goods find other employment. On the other hand, if the farmer is to be deprived of the market for his farm produce that is consumed by the American workmen, and must run the chance of selling his farm produce in competition with other farm produce in foreign markets, the chances are that he will lose rather than gain. A European

workman may eat wheat produced in Russia, Australia or Argentina, but if the American workman is employed in an American factory, the chances are that he will consume American food products.

Kenneth W. Stillman, in *The Protectionist*, says:

To illustrate the action of bargaining tariffs, let us look at the automobile and cotton industries. Let us suppose we bargained with England to reduce its automobile tariff in consideration of a reduction in our tariff on cotton goods. The sale of English cotton goods would increase, and the Lancashire factories would expand operations and would require more help. But in the United States cotton prices would fall and many cotton producers would be forced out of business. Meanwhile the increased sale of American automobiles in England would have expanded operations in Detroit and more workers would be needed. Theoretically, the jobless cotton workers would be transferred to the automobile industry.

Who knows that the jobless cotton workers would be transferred to the automotive industry, either theoretically or actually? What probably would happen is that the English cotton operative would make a great deal more money and might be able to buy an automobile, but that automobile would, in all likelihood, be turned out by an English concern or one of the American plants in England. Both the cotton worker and the automobile mechanic would run great risk in the exchange. And while the owners of the motor industry might make more dollars, the cotton industry would be torn to pieces and suffer severe deflation.

On April 11, 1933, the *Washington Post*, in editorial comment upon the present Administration's tariff policy, stated:

If the United States is going to embark upon such an experiment, it ought not to do so blindly. It may be difficult for the average man to understand what advantages Americans as a whole would gain from a scheme which would close the American market to domestic output. Secretary Hull's theory of the world as a great economic unit is a myth. The world is no more an economic unit than it is a political unit. Wages in Japan, for example, are about one-sixth to one-tenth of what they are in the United States. Under present conditions a scaling down of tariff barriers would put Japan in the most advantageous economic position of any nation in the world. Unemployment would increase in the United States. Manufacturing would be transferred to countries paying cheap wages.

What barriers are we to remove? When Canada was first settled and developed, her wheat fields began to threaten ours. Then Argentina entered the lists and competed with our farmers on the world market with wheat, corn, meat and wool. Soon it became evident that we were no longer looked upon by the world as the only place where food could be produced in surplus quantities. Therefore, every agricultural schedule reduced puts our farmers in direct competition with cheap lands and low-paid labor in South America and Canada. If barriers are to be removed on the industrial schedules, may we ask what business is now making excessive profits or paying excessive wages? Every dollar you give to a foreign laborer must be taken away from an American workman.

What kinds of goods do foreign nations want to trade or sell us? Not all industrial commodities surely! There are few industrial nations, but many agricultural nations. What do you suppose Argentina wants to exchange with us? Not manufactured articles—she manufactures nothing. She wants to give us agricultural products. So also do Australia, Canada, Cuba, China, Mexico, Russia, India and a host of other agricultural countries. Do not let us be deceived on that score.

The kind of commodities foreign nations want to sell or "trade" with us is a matter of public record. The records are open for your inspection. Foreign nations have a right under our tariff law to protest against any rate in the 1930 Tariff Act, and the Tariff Commission must investigate the protested rate. What do you think was protested—iron, steel, sewing machines, automobiles or any other industrial product? No! Not one protest about industrial products. Every protest was on agricultural rates. Mexico complained about the tariff on live stock, milk and cream; Argentina against wheat, cattle, hides, wool, sheep, flaxseed and casein; China against dried eggs; Cuba against beans, okra, pineapples and other vegetables; France against cheese, mushrooms, and so on.

More than 80 per cent of all protests filed by foreign governments against the protective tariff have been against duties on agricultural commodities. These foreign agricultural nations want our market. Because of our higher standard of living, the American market is equal to or better than the combined markets of the world, and in the economic drive against this

country, the attack has been centered on agriculture. The fight has been bitter and forceful, and I am sorry to have to admit that it has been helped and abetted by certain groups of American financiers who seek to collect some of their bad loans by this method. But to you and to ninety-nine per cent of the industrial East, the loss of the American farmer's market spells plain disaster and ultimate ruin. For by the very act of tampering with, breaking down, or "trading" with the farm tariff, we would automatically destroy the buying power of more than 75 per cent of our population, and get in return for that great loss the dubious trade of foreign peasant farmers and great paid labor who do not buy automobiles, radios, electricity, or any of the other luxuries which are common to the American farm home.

It is agreed that there is a farm problem. We know it cannot be solved by putting the American farmer in direct competition with the foreign farmer. The American farmer pays taxes, buys industrial goods, and in every way contributes to the general welfare of the state and nation. The foreign farmer pays no taxes to help maintain our institutions, nor does he buy our industrial goods.

A protective tariff is the very foundation of farm relief. We cannot stand a foreign invasion of our markets without a violent reduction in the purchasing power of our farmers, now so cruelly reduced because of the world's financial difficulties.

We are passing through strange days and experiencing radical changes in the sub-structure of our national life. Changes are being made in our money values. How these changes will affect us in the future, no man can foretell. An agreement on world fiscal policies must come first. The present negotiations now going on in Washington may go to the heart of the fiscal problem. World agreement on currency is possible because finances know no boundary lines. Economic boundary lines have been recognized in tariffs since the beginning. Following an agreement on money, we can then feel our way into the economic field.

A sacrifice of our tariff schedules in our present plight would discourage everyone. With a world over-producing in every line, with workmen unemployed in every country, our problem is to find a way by which we can go forward. We cannot turn

our jobs over to foreign workmen. We cannot put our farms in direct competition with foreign farms. We must maintain the protection now afforded our agricultural interests if we expect to get back to the solid foundation of national security and happiness.

REMARKS BY THE CHAIRMAN

CHAIRMAN BURGESS: We now have half an hour for discussion. The discussion will be opened by George P. Auld, former Accountant General of the Reparations Commission, 1920-1924, and a partner in the accounting firm of Haskins and Sells.

[310]

DISCUSSION: TRADE BARRIERS IN THE WORLD DEPRESSION ¹

GEORGE P. AULD

Of Haskins and Sells;

Formerly Accountant General of the Reparations
Commission, 1920-1924

PRIOR to the historic event that occurred on April 19, 1933, the problem of the restoration of international trade appeared sufficiently formidable. In fact, it seemed for the time being insoluble. What effects the definite suspension of the gold standard by the United States has had on that complex of inter-related dislocations one may hesitate, at this short interval and amid the critical diplomatic conversations now going on, to attempt to specify. It seems likely, however, that the shock of that event will be found to have provided a solvent of some potency, under the influence of which things that have had a highly indurated appearance will be rendered more manageable.

Most or all of us are convinced that international trade is a good thing. The contrary thesis, which has received some thoughtful and a great deal of thoughtless support in this country, is that the home market for domestic products must be developed, and their export discouraged. The advantage claimed for a conscious policy of this sort is the attainment of a more complete national integration. Its adoption would imply the progressive curtailment of imports, and its results, the world over, would be, in fact, identical with the system of barriers which during the past two years have been piled up, more or less fortuitously, across all the pathways of trade.

Our view here doubtless is that the more complete domestic integration aimed at by a policy of economic nationalism could not be worth the distress caused by the attendant dislocations in our export industries. Only some future benefit of an importance so commanding and a certainty so clear as is rarely to be foreseen in this world, could justify or make bearable such disastrous dislocations as we and our neighbors are now with difficulty enduring.

More than that, and referring specifically to the situation of this country, we have the matter of our normal and natural export surplus to consider. After suffering the elimination of our export trade in amounts equal to the barred-out imports, what disposition would we make of the normal remaining balance—our normal excess of ex-

[311]

ports? We must sell that excess on the world market or face the creation of a permanent class of unemployed at home. But can any nation dedicated to the unneighborly, not to say uneconomic, policy of blockading imports expect to secure or to keep foreign customers? Perhaps least of all nations, with the exception of Britain, can we hope to serve the real interest of our producers by a policy of economic nationalism.

Now, the present blockades, with the possible exception of our own most recent tariff legislation, are not in the main expressions of conscious policies of economic nationalism. Import embargoes are clearly traceable, in most cases, to acute currency difficulties precipitated by the international panic of 1931. And being merely effects and not causes, it might be thought futile to try to deal with them at all. That is, of course, a mistake. For, of the many hundreds of millions of dollars of trade that have been cancelled out, exports against imports, as a result of the panicky embargoes of the past two years, it is obvious that by mutual agreement a substantial proportion could be reinstated on both sides of the international accounts, without affecting the exchange values of the currencies concerned. Here, then, the opportunity clearly exists for the nations to bring a little common sense into the conduct of international affairs. Here, plainly, is a chance for their representatives to discuss with each other, like ordinary rational human beings, conditions which are easily susceptible of correction by negotiation.

Such a reinstatement, by common consent, of self-balancing currents of trade has, however, definitely restricted possibilities of usefulness, except as to the general restoration of confidence that it should promote. Its limitations arise from the fact that on final balance of all international movements of commodities and services, every country is either an importing debtor or an exporting creditor. That final balance has to be moved, not in the main against gold shipments, as is the popular impression, but by international lending. And these movements of capital, if they are to be properly organized and free from the grave dangers associated with floating debt, must be in the form of long-term lending, which is now practically nonexistent.

The resumption of international long-term lending, then, is basic to full recovery, and it presents a problem of extreme difficulty. It is this country, as the great exporting creditor of the world, that must do a major part of that lending in order to move its own surplus. This is a painful and highly unpopular idea these days. But there is no doubt at all that neither we nor our neighbors can get very far on the way toward international economic stability and prosperity until we begin again to lend abroad. The difficulty, of

[312]

course, is to find those proper objects of international lending which can today command the confidence of our investors.

A second major limiting factor on efforts to reach international stability by negotiation lies in the apparently fundamentally weakened position of British industry. During the whole period of growth of the modern system, Britain has been the central fact in world trade. Since the war she has not been holding her own, and her struggles to maintain her position exercise a profoundly disturbing effect on world economic conditions. Having to buy her food abroad, she is vitally dependent on the export of her manufactures, but whereas in 1913 she had over 15 per cent of the world export trade, her share progressively declined to about 12 per cent in 1930, representing the very substantial shrinkage of one-fifth of her original share, a shrinkage which was in effect somewhat more than a fifth when account is taken of a small increase in her proportion of total world imports.

At present Britain, and consequently to an extent the rest of the world, is dominated by a school which believes that monetary manipulation is the great economic panacea. On this theory one need not be greatly concerned directly with the fundamental mechanism of society, which is industry and production, but may count on salvation through monetary management, and in particular, so far as present international aspects are concerned, through the massing and maneuvering of gold stocks in and out of the foreign exchange markets.

The real position of sterling is today obscured by these maneuvers and by transfers of funds reflecting speculation and fears of repudiation of the dollar. The underlying position of sterling, in my view, is dubious. It has for long been the leading currency of international trade. Its preëminence and that of British finance generally were founded on the former preëminence of British industry. No currency can, in the long run, be maintained artificially or in any other way than on the foundation of a vigorous and healthy system of production. It is, therefore, reasonable to suppose, if the decline of British industry continues, that the whole system of international exchanges built up through the centuries around sterling will be subject to continued or recurrent strains incident to its gradual reconstitution.

On the other hand, if we were to witness a thoroughgoing reconditioning of British industry, which, according to a leading British exponent of rationalization, would require a capital expenditure running into many millions of pounds, sterling and the international exchanges could be expected to regain and maintain a natural stability. And if this reconditioning were to be effected in part by Ameri-

[313]

can capital, the problem of finding a proper object for American lending would be solved. For British credit meets all the necessary tests.

As to the world-wide bases of international credit, which urgently require regeneration before international lending generally can be resumed, it is hardly susceptible of denial that they may best be repaired by the political and moral appeasement which would flow from a settlement of the problem of intergovernmental debts and from some measure of success in present efforts to deal with the problem of disarmament.

[314]

PART II

PROCEDURE IN TARIFF MAKING

INTRODUCTION¹

SHEPARD MORGAN

Vice-President, Chase National Bank;

Former Finance Director, Office for Reparation Payments, Berlin

THE topic for discussion this afternoon is "Procedure in Tariff Making." The Academy of Political Science tackles, as a rule, only one problem at a time. Considering the state of the world and of the United States at this moment, it is fortunate, I think, that we are not attempting to deal with monetary stabilization, price stabilization or kindred topics, or we might continue our conference for weeks, months, perhaps even years. We are, however, dealing with a topic which is next door to the question of currency stabilization, the solution of the problem of intercourse between nations.

This afternoon, we deal with the technical phases of that topic. We are to discuss procedure in tariff making. We are fortunate in having three distinguished speakers who can deal with this subject from standpoints of authority. I desire to announce thus early that the fourth speaker, Sir Vincent Massey, who was former Minister from Canada to the United States, will not be with us. He told us this morning, to our great regret, that in his judgment the conversations now pending between Prime Minister Bennett and President Roosevelt were of such a nature that he felt it wiser for him to make no expressions of opinion during their pendency.

The first speaker on the afternoon program is John Lee Coulter, Commissioner of the United States Tariff Commis-

¹ Introductory remarks at the Second Session of the Semi-Annual Meeting.

sion. Mr. Coulter is a Westerner. He comes from a part of the United States which has a preponderant interest in export, rather a small interest in import. That in itself makes the comments that we will hear from Mr. Coulter this afternoon of great interest. In addition, we have the assurance that we will learn the results of his service on the United States Tariff Commission. Mr. Coulter!

[316]

THE TARIFF COMMISSION AND THE FLEXIBLE CLAUSE

JOHN LEE COULTER

Commissioner, United States Tariff Commission

ASIDE from its duties in connection with "unfair competition and unfair acts in the importation and sale of articles of commerce" and in connection with "discriminations by foreign nations against the trade and commerce of the United States", the most important duties of the Tariff Commission are prescribed by Sections 332 and 336 of the Tariff Act of 1930, which carry forward similar functions from the Act of 1922. Section 332 requires the Commission to be in constant touch with all tariff problems pertaining to all commodities in international commerce and the tariff policies and acts of all nations, so as to be able on a moment's notice to serve the President and the Congress. Section 336 is the so-called "Flexible Clause" of the Tariff Act, which I have been invited to discuss as a part of your program dealing with "Procedure in Tariff-Making".

Perhaps I should make clear at the outset that under this section the Tariff Commission is distinctly not a policy-making body. Under our government, the determination of public policy is a matter of general legislation participated in by the President and the Congress, and may not be delegated to a board or commission. In 1922, the party in power, in the light of the complete change in the international commodity price structure during the war and the partial deflation between 1920 and 1922, not knowing what further changes might take place, which would throw individual tariff rates out of line from the general policy of protection which it had established, and wishing to provide machinery for the review of individual rates of duty, classifications, etc., deemed it wise to add to the duties of the Commission the quasi-judicial or scientific task of reviewing individual rates of duty (upon request of the President, either House of Congress or committees

[317]

thereof, representatives of domestic or foreign industries affected, or upon its own motion), to determine whether the rates prescribed in the Act approximately carried into force and effect the policy intended by the Act. The Commission was commanded to report its findings in each case to the President, who was authorized to put the findings into effect by proclamation provided they fell within certain limits as to changes in rates of duty, reclassification of articles, or changes in value basis for the assessment of ad valorem rates.

Three major problems presented themselves: (i) The limitations as to the scope of the Commission's duties; (ii) The measuring stick to be used by the Commission; and, (iii) The method of putting the findings of the Commission into effect. I shall deal briefly with each of these in the order named.

I. LIMITATIONS AS TO THE SCOPE OF THE COMMISSION'S DUTIES

The Commission was not permitted to transfer articles from the dutiable to the free list, or vice versa; nor was it permitted to change the form of duty—for example, a rate of duty from specific to ad valorem, or the reverse; further, it was not authorized to specify maximum or minimum ad valorem limits in cases of specific duties, or to specify maximum or minimum specific limits in cases of ad valorem rates. Maximum changes in rates were limited to increases or decreases of 50 per cent from the rates provided in the Act itself, except that in certain cases where ad valorem rates were provided the value basis upon which the rate was applied might be changed from foreign invoice value to American selling price, provided, however, in such cases the rate itself could not be increased if the value basis was changed. Authority also was given to reclassify dutiable items either by subdivision of basket clauses, price groups, or more definite description of articles.

II. THE MEASURING STICK TO BE USED BY THE COMMISSION

The Tariff Acts of 1922 and 1930 more definitely than heretofore set forth the basis for rates of duty imposed. The

[318]

basis defined or described was the difference in costs of production in the United States and the principal competing country of like or similar articles laid down in the principal market or markets of the United States. The measuring stick was made much more definite in the 1930 Act. This sounds like a very simple and a very practical measuring device until it is analyzed. It will then be recognized as very practical and simple in some cases, but a very difficult rule to apply in many cases and not at all applicable in others. In addition to cost differences the Commission was charged with the duty of evaluating other advantages or disadvantages in competition. Supplementing the research work carried on by the Commission in each case, provision was made for a public hearing at which interested parties were given an opportunity to appear, present evidence and be heard.

During the ten years 1923-1932 inclusive, the Commission had cases where no basis had yet been worked out by economists, statisticians, accountants, or other experts for ascertaining costs of production. Thus, in the investigation pertaining to hides and skins, it was possible to measure the quantity of domestic and foreign production, international trade, supply and demand, prices paid, etc., but not costs of production. Who could tell whether it cost more or less per pound to produce the hide on the animal's back than the different classes of flesh or the bones or other parts of the carcass? At one moment, or in one country, the price of the hide might be higher than other parts of the carcass, or again, it might be lower. Also there are scores of grades and conditions of hides. The cost-of-production measuring stick just would not work. From this extreme we ran the gamut to investigations where the measuring stick worked perfectly. So far as I know, nobody has yet made a study of the thousands of different grades, sizes, values, etc., of the different items or articles listed in the Tariff Act, or broken down basket clauses and attempted to classify all as to whether cost difference is a practical or impractical basis for measuring the competitive impact. It should be said, however, that in a great many of the investigations conducted by the Commission a working basis for obtaining costs of production was developed.

Another important problem which confronted the Commis-

[319]

sion was that of finding like or similar domestic and foreign articles in direct competition. While there were, of course, great numbers of staple or standard articles such as wheat and flour, butter, milk, cream, etc., which were like or similar except for minor differences in grade, etc., there were also great numbers of cases where domestic production would be largely in one price group, or one grade or class of the product, and imports in another. In the case of ad valorem rates of duty, the duties imposed often are not burdensome on the low-priced group, but practically prohibitive on the high-priced group; while in the case of specific rates of duty they are often not burdensome on the high-priced group, but practically prohibitive on the low-priced group. Where there is no domestic production of the class or grade or price group imported, or no imports of the class, grade or price group produced in this country, a problem presents itself, which has not yet been successfully solved, although some approach has been made to the problem in a number of cases. In some important cases, however, the Commission did not find a practical basis for a definition by grades, classes, or price groups, and while it found the rates of duty either excessively high or extremely low as to portions of the commodity, it was unable to provide a remedy under the flexible provisions of the law.

While the law requires the Commission to compare domestic costs with costs of the commodity produced in the principal competing country, it sometimes happens that one country sends us more in quantity of one grade or class, and another country more as measured by value; or two or more countries may be nearly equal but may be shipping different classes of goods, or to different American markets, or at different seasons. While this is a difficult problem to handle, it is believed that in general it has yielded to reasonably practical conclusions.

We come now to the problem of the principal American market or markets. Inland farms, factories, fisheries, or forests may have a great advantage in inland markets but great difficulty in reaching coastal markets on account of high rail rates versus government-subsidized water rates on imports. In contrast, coastal producers and importers may have an even break, both in coastal markets and inland markets. This is one of the most difficult sets of problems which confront the

[320]

Commission,—i. e., the problem of transportation and of principal market or markets.

Of somewhat the same nature is the problem of regional and seasonal competition. Imports may have distinct advantages in some regions as imported anthracite coal has in New England; or in some seasons, as winter vegetables from Cuba and Mexico have in some areas. Since the Tariff Commission may not prescribe different rates for different ports or areas, or for different seasons, but only for different grades, classes, price or other groups of articles, the only equitable solution in cases reviewed to date has been to base the duty on weighted averages, which, however, have left domestic products predominant in some areas and imports in others, and domestic products predominant at some seasons and imports at others.

Another difficult problem which has confronted the Commission during the last four years has to do with a representative period of time for cost comparisons,—bearing in mind that cost differences must be an analysis of past performances and new rates of duty proclaimed must project us into an unknown future situation. It must be evident that a factory operating at full capacity and producing 100 units in 1929, would have a unit cost vastly different from that prevailing when the plant was operating at 20 per cent of capacity in 1932, but with the same taxes, imputed interest on fixed assets, depreciation, repairs, and general overhead expense, even if costs for labor, raw material, etc., remained the same. Add to this picture declining wages, salaries, costs for raw materials, etc., and you will see the difficulties of this particular problem. Here it is well to call attention to the fact that as prices decline, specific rates of duty mount higher and higher in ad valorem equivalent. Thus, if the duty on an article valued at \$1.00 in 1929 was 30 cents, it was a 30 per cent duty; if the article has declined in price, in 1932, to 60 cents, the same duty of 30 cents is now a 50 per cent duty. When the price of Cuban 96° sugar was \$2.00 per 100 pounds, and the duty was 2 cents per pound, the duty was 100 per cent; when the price fell to 50 cents per 100 pounds, and the duty remained at 2 cents per pound, the ad valorem equivalent was 400 per cent. On the other hand, when prices are advancing, specific duties grow lighter. In contrast, when prices are fall-

[321]

ing, ad valorem rates of duty decline in specific equivalents. Thus, on an article valued at \$1.00, a duty of 30 per cent has a specific equivalent of 30 cents; if the price falls to 60 cents, the 30 per cent duty is now equivalent to a specific duty of only 18 cents. Of course, the opposite is the case when prices are advancing. This has led some students to the suggestion that specific duties should have definite maximum and minimum ad valorem limits, and ad valorem duties definite specific limits. Of course, these phenomena are only characteristic of periods of rapid price changes and perhaps the more practical solution of this problem lies in the field of stabilizing prices. It is none the less one of the most serious problems in any attempt to adjust tariff rates in a period of falling or rising prices.

We come now to what is probably the most serious problem of all. Having found a domestic commodity in competition with a like or similar imported article; having established the principal competing country and the principal American market or markets; having decided upon the representative period of time to be covered; and having worked out all seasonal, regional and other problems and any "other advantages or disadvantages" in competition; how shall we arrive at representative domestic and foreign costs in those cases where cost methods are applicable? There is the question of high cost and low cost farms or factories, well located, or badly located. How many factories or farms shall be costed to be truly representative of the industry? What if the foreign factories do not choose to give access to their records? Shall invoice prices be taken as an evidence of costs? Do the imports come from low or high cost factories, and do invoices include an element of profits, or are articles being imported at prices under the cost of production? If the domestic industry is largely mechanized, and uses very little but highly paid labor, how shall it be compared with a foreign industry only slightly mechanized but employing many laborers at low wages? How shall we segregate the costs of a given article or grade or class of article, if a factory makes a hundred or a thousand different articles or grades of articles, losing money on some and making satisfactory returns on others? These are only a few of the questions which come before the Commission. It

is well known that few farms keep cost records and generally the more efficient enterprises have the best records.

Needless to say without a capable staff of economists, statisticians, accountants and technical men and women, the Commission would not be able to do its work efficiently. The policy for a hundred years and more was to invite interested domestic producers and importers to file their claims before committees of Congress, examine import statistics, and then "agree" upon a rate of duty. Frequently, interested parties overstated, or understated, or misstated their claims for consideration. The turbulent scenes in Congress were an evidence of the difficulty in "agreeing".

In spite of the many problems which I have presented which confront the Tariff Commission, I believe it may be said that great progress has been made toward a sounder and more accurate basis for adjusting rates of duty than the hundred-year-old methods. I am not discussing the question whether this country should have a low-tariff or a high-tariff policy, or whether emphasis should be placed upon the amount of revenue, or the amount of protection, or the importance of international trade. These are matters of public policy to be determined by the Administration in power—by the President and the Congress. This having been decided, the problem before the Tariff Commission is one of testing or verifying rates of duty, classifications, bases of value, etc.

It should be added here, in view of the subjects of the three addresses to follow mine, that during the sixteen years of work by the Tariff Commission in conducting surveys and the ten years of adjusting rates of duty, a body of information and a small staff of experts have been built up which will be of invaluable assistance to the government either in future tariff revisions or in negotiating reciprocal trade agreements, whether the policy is chiefly to build up our foreign commerce, to protect American industry, or to produce revenue, or whatever the policy.

The long list of problems which present themselves in the administration of the flexible tariff provision may lead some to conclude that the provisions are impossible of application. Whether the theory of difference in costs of production should be the basis of tariff rates is a matter of high public policy to

be decided by public opinion and enacted into law by the Congress, but the experience of the Tariff Commission in the past few years indicates that some yardstick or measure of tariff rates can be applied to particular industries, even though it is the somewhat inflexible stick of cost differences. For want of time, detailed discussion of even the more important investigations cannot be made but perhaps some bare figures will give an impression of the extent of the Commission's work in recent years.

Since the Tariff Act of 1930 became effective in the middle of that year, that is to say, during a period of about thirty months, the Commission has given consideration to approximately 225 applications for action under the flexible provisions and related clauses of the Tariff Act. These 225 documents are not mere pieces of paper in the Commission's files, but the problems raised by each of them have received the careful consideration of the Commission and its staff, in some cases involving several weeks of work of one or more men to determine whether or not the Commission was justified in spending public money in a full and formal cost investigation. These applications have been worth every dollar of expense put upon them by informing the Commission of the conditions in the industries regardless of what subsequent action may have been taken.

Of the 225 applications, nearly 75 have been dismissed without prejudice after a careful examination of the facts involved. On the other hand, a total of about 135 investigations, or more than one per week, have been ordered, of which about 30 were under the general powers of the Commission; that is to say, the Commission decided in these cases that the public interest would be best served by a broad rather than a narrow study of the problems raised in the applications. Going back to the entire number of formal investigations, namely 135, more than 90 of them, or one every ten days, have been disposed of in one way or another, and the majority of the 90 have resulted in formal reports to the President, together with the Commission's findings.

So much for the bare statistics of investigations and reports. Back of these lies more than the mere count of items on which duties were increased or decreased. Probably the more im-

portant consideration is the intimate knowledge which the Commission and its staff now have of many basic industries, as a result of its investigations, both from the point of view of the domestic producer and of the import trade. For example: for the first time in the history of tariff legislation, we shall be in a position to tell, among the hundreds of varieties of cutlery, what types and grades are truly and sharply competitive as between imports and domestic production; what types are predominantly produced in the United States but not imported under prevailing conditions, including the duty; and what types are largely imported with small domestic production. These facts will be of great value in tariff bargaining.

Another by-product, so to speak, of the Commission's investigations is the friendly relations which the Commission has developed with the domestic, the importing, and the foreign producing industries. Not only do importers and foreign producers regularly come to the Commission's public hearings to present their case, but under the flexible provisions, for the first time, the foreign manufacturers have an opportunity to present in a confidential manner the intimate details of their costs, which in the past have been largely minimized rumors. The surprising thing is that they not only have the opportunity but take advantage of it in almost all cases where the Commission's agents have made contacts with them. Both the domestic and foreign producers seem to say, "Now, at last something can be done about a rigid tariff system. We do not have to wait for the periodic general tariff revision to get changes in particular rates". Whether their hopes and expectations have been justified in the past is not under discussion, but at least in the past ten years there has been some hope of "doing something about it" in cases of serious maladjustments.

III. THE METHOD OF PUTTING THE FINDINGS OF THE COMMISSION INTO EFFECT

I come now to one of the most controversial problems in connection with the work of the Tariff Commission under the so-called flexible provisions of the Tariff Act. After the Commission has completed a case and finds that an increase

or decrease in duty, or change in classification or value basis is warranted, (a) shall the Commission proclaim the result (with right of appeal of interested parties to the Courts); or, (b) shall the conclusions be certified to the President, who may reject the findings, or change them, or approve and proclaim them; or, (c) shall the conclusions be reported back to the Congress, and if reported to the Congress, shall they become effective if not actually disapproved by one or both Houses, or remain merely a recommendation until affirmatively acted upon by Congress and the President? These are the principal proposals which with minor modifications have received much study. Which shall be the law is a matter of high public policy to be determined only by public opinion and enacted into law by the Congress with the approval of the President. It would not be useful for me to express an opinion on this subject without a detailed analysis of the philosophies involved and an historical study of past experience. Time does not permit this discussion at this time. It is even then a question whether a member of the Court or Commission should engage in a discussion of the controversy, although it would be highly useful for him to give expert testimony of the workings of the different approaches to the subject. Suffice it to say that under the present law, the conclusions of the Commission are filed with the President, who may return them to the Commission without action, or approve the findings; and if he approves, he issues a proclamation putting them into effect at the expiration of thirty days. The Supreme Court has declared this procedure constitutional, without, of course, indicating whether in their judgment this is the wisest method of procedure.

[326]

REMARKS BY THE CHAIRMAN

CHAIRMAN MORGAN: We are grateful to Mr. Coulter for this very lucid analysis of the intricacies of the work of the Tariff Commission. It occurred to me, in the course of his talk, that perhaps we might write an epitaph on tariff legislation to this effect, paraphrasing the well-known childhood maxim:

What a tangled web we weave
When first a tariff we conceive!

It has been my duty often to go to Washington and sometimes I have gone to the State Department. Walking down the corridors there, I have seen on the door the name, James Grafton Rogers, Assistant Secretary of State. I have always said to myself, "There is a fellow I want to see!" Then I would talk to one of the other Assistant Secretaries and he would say, "Oh well, Jim Rogers is the man you should see but he is so terribly busy I am afraid you can't." So it is a pleasure to me this afternoon to have Mr. Rogers under my thumb. At last he is going to talk to us, for at least twenty minutes, and we are going to learn from him a great deal. Mr. Rogers!

[327]

RECIPROCITY AND THE MOST-FAVORED-NATION CLAUSE

JAMES GRAFTON ROGERS

Dean of the Law School, University of Colorado
Former Assistant Secretary of State

THE nations of the world are in recent years strangling the flow of international trade between them by governmental measures. These measures are in part, tariffs; in part—and progressively more so—other more direct impediments such as embargoes, quotas fixing the amount of goods allowed to be imported, restrictions of means of paying for imports, and other more involved regulations. The motives for the measures are chiefly three: (1) the policy of artificially protecting a nation's own industry by barriers against competition from abroad; (2) the desire for the revenue easily collectible from import trade; (3) currency protection, that is to say the preservation of a nation's currency from depreciation on the international exchange and prevention of the withdrawal of gold from national reserves to balance excess demands for payment abroad. These are all familiar facts. The disastrous results are notorious. International trade has fallen off at least a third in commodity quantities since its crest four years ago and these measures share some considerable responsibility.

The simple general impression that high tariffs are the cause for the decay of international trade is wrong, for the height of tariffs is not the critical factor and there are other causes for our dwindling trade statistics quite as significant as any and all the artificial barriers. We can, however, blame some of our difficulties on the governmental checks against free flow. That topic we can discuss. There we can to some extent control events.

The man-made impediments to trade, such as tariffs and embargoes and quotas, fall in a rather specialized field of human experience. The men who have studied this field are

[328]

few; those who have real experience in its practical problems fewer still. The lore is confined mostly to some experts and public men in governmental service, some few international traders, various research men in public institutions and a number of academic scholars. The literature of the subject is dull, diffuse and dusty beyond compare. Yet the topic is one in which great popular impulses and national sentiments are active and predominating and the principles developed are rather few and simple. What I have to suggest today will seem rather meager fruit of two years' daily exposure to the practical problems of international commerce in our Department of State.

There are three rather well defined policies in operation as respects the regulation by modern governments of trade between nations. Two older policies have disappeared or dwindled to insignificance. Of the older policies, one was called mercantilism. This was the aggressive maneuvering, grasping and management of opportunities for trade abroad by a nation acting as a merchant might, to seize, monopolize and exploit a field for selling his goods. This policy still threatens the world sporadically but is, I think, faded or fading from the scene. Another older policy was free trade, the attitude of non-interference by governments with the natural currents, the ebb and flow of commerce. This, too, is gone. Every important government and nearly all the lesser units are actively intervening today. The nations today are all hampering, levying on and manipulating trade and the policies now in operation are simply three different attitudes in which nations approach the treatment of trade from and to other countries by agreement as to policy. All three attitudes lead to forms of treaties which are expected to govern the impediments to trade.

The three schools may be called the school of equality of treatment, usually known as the most-favored-nation policy, the school of special bargaining, which tries to gain trade opportunities by buying and selling concessions or special privileges to other nations, and the school of group or area agreements, which tries to get outlets for trade by joining with several other nations in a regional or multilateral compact for lower national barriers. The United States has

[329]

pretty consistently clung to the equality school. The present-day French and Spanish policies are of the special bargaining color. The recent British policy, represented by its Empire Preference agreements, and such experiments as the Ouchy agreement between Belgium, Netherlands and Luxembourg to reduce their tariffs as between themselves, illustrate the school which tries to pull down the dikes by regional or multilateral compacts. These three plans, the equality practice, the special bargaining policy, and the multiple regional scheme represent the real thought and practice of the world today. It will be noticed that they all assume the existence of trade barriers on international boundaries and differ only as to how they treat, accept or struggle to reduce those barriers with an eye to the opportunities of their own people.

With these policies in mind, and accepting them as the only known procedures available for practical statecraft at this given hour, recognizing the need for some alleviation, assuming the opportunity for it developed by world-wide dissatisfaction with the weeds that choke our paths, what can this country, the United States, chart as a wise course? Let us for a moment examine the three policies.

The equality school repudiates the efforts to drive special bargains with other nations, reserves to itself freedom of action as respects the dikes it pleases to build on its own frontiers but offers its neighbors a guarantee against discrimination if they will reciprocate, each in turn, by the same guarantee. This guarantee is made by a treaty for typically five or ten years or by a revocable *modus vivendi* in which each nation pledges to give the other most-favored-nation treatment, that is to say, to give the other as low tariff rates and as friendly a reception in general as is accorded anybody. The phrase gives the name to the policy. It is essentially a device to produce equality, for such it accomplishes in direct ratio to the prevalence of the agreements. This has been the American plan on the whole throughout our history. We have today, it is true, a preference arrangement with Cuba, which is based on political grounds and the maintenance of which is recognized in our other international contracts. The Cuban exception is not a real one, as special instances of this sort exist elsewhere and are well established in world precedents.

[330]

We have, of course, special arrangements also for our possessions, the Philippines, Porto Rico and so on, but these are intra-family cases. We had once for twenty-five years a preferential agreement with Hawaii which preceded annexation. In the Civil War period there was reciprocity with Canada and efforts to restore some such status have been made and are today under discussion. In the 'nineties we made some efforts at other preferential arrangements. The Argol agreements, so called, were small-scale bargains which lasted a few years. The Kasson agreements, about the same period, were a series of wider efforts which came to nothing. In 1904 we got preferences with Brazil which survived until 1922. The deviations are all those worth mentioning in three generations. The United States has practiced equality of treatment. It is today committed to this policy by treaties with many of the important nations but most of these agreements are short-time arrangements or will be revocable within a few years.

Our policy has been determined in this direction by a variety of causes. The general rise in favor of the equality school during the last century has been one of the elements but in my judgment a minor one, as American attitudes have been little swayed by Old World political thinking. In the beginning this country was much influenced by the tradition against foreign entanglements. It is and has been true that special trade agreements are seldom uncontaminated by political features. In later years the need for preserving freedom to carry on the high protective policy which is so ingrained in our public thinking and also the wide diversity of our own industries and exports seem to have been the determining factors. A bargaining policy in the true sense means some breaches in tariff walls. It is also a difficult procedure for a nation which produces everything, wants to sell everything and everywhere and cannot make concessions for a bargain without exposing some branches of its own industry. To put it abruptly, a bargain with Australia to lower the barriers against American refrigerators in exchange for lowering our own barriers against Australian wool, which might be a typical bargaining treaty, is difficult when the only interested advocates are our small percentage of refrigerator manu-

[331]

facturers and we meet the opposition of as large a representation of constituents who grow wool. Nations with specialized export, or both export and domestic, industries are in an altogether different position from the United States. These and other factors have undoubtedly controlled our policy — the political dread of entanglements, the tradition of protection and the wide variety of our own production. In recent years the policy of equality has steadily gained ground in professional opinion, due in part to the growth of certain political ideas and the rise of the smaller nations, as well as to expert observation. It can be said that prevailing opinion here and at large is in its favor. Personally, I have little doubt that the United States must and will maintain the general principle.

The chief alternative offered in the past century, once free trade was abandoned, has been resort to the special bargaining school. The history of France, the recent experiences of Spain and the older records of Europe give us a vivid picture of its operation. To a nation with a highly centralized political control, able to change its tariffs by executive decree, without resort to a legislature, a country specialized in its export commodities, not too much committed to preserving domestic protection and rather keenly concerned in preserving alliances and groups for military or political purposes, the policy offers many attractions. Indeed only a country with a flexible government and a specialized production ought to find some advantages. Some or all of these conditions seem essential to success. Even then the results are transitory. Nations like politicians do not stay bought when they are purchasable. The policy leads inevitably into political consequences. France uses it avowedly for other than commercial ends. The practice degenerates easily in the hands of men who are exposed to the influence of strong industrial groups on the one hand, or to preoccupation with political as well as purely trade problems. Preferences soon produce antagonisms and tariff wars. All in all, the special bargaining school seems to me peculiarly unsuited to American conditions and traditions. Our experiments under the McKinley Tariff of 1890 and the Dingley Tariff of 1897 confirm this doubt. Let us make it clear, however, that these observations apply only in part to the practicability of reciprocity with border countries like Canada

and even Mexico or Caribbean nations. There special considerations make easier the path. Reciprocal agreements of this type, founded on geographic and racial proximity or even on a geographic basis alone, surrounded as they are by other than purely commercial ideas, are not in any sense representative of a general bargaining policy.

A more promising opportunity is offered by the school I have referred to as experimenting with group or areal multilateral compacts to reduce trade barriers. It is quite possible that the strangulation of trade by economic nationalism may be broken by the growth of relatively free custom areas through this technique. The Ouchy plan, still really uncompleted, has at least a flush of promise. Under it three countries agreed to reduce their tariffs as against each other ten per cent a year for five years, or fifty per cent in all. They offered the benefits and obligations of the agreement to any other nation that cared to adhere. The British Empire agreements are vastly different. There internal walls were lowered as between the members of the Commonwealth, but new and higher walls were erected against the world. Except as the agreements show a tendency to breaking the deadlock by grouping, the arrangement is not representative. It is besides on obviously precarious footing and a rather specialized proceeding. There are some other movements toward regional concessions. The Oslo convention is an example. Others such as the Danubian project and ideas suggested elsewhere are yet unfashioned. An American regional agreement is not at all fantastic in conception if this country is willing to venture any concessions at all in its tariff ramparts. At least the multilateral plan deserves attention. Its coördination into a general scheme of equality of treatment is suggested by the right of adherences established in the Ouchy document. International law can find a way to meet the technical difficulties if the scheme furnishes a real road to relief.

The belief already expressed in the long-time wisdom of equality, the critical attitude assumed toward the bargaining school and the rather untried nature of the regional scheme may seem to leave us without any forward-looking plan. This is not the case. There is under the equality policy and within the framework of the most-favored-nation treaties a possibility

of barrier reduction by agreement which is relatively simple and easy if the American public is willing to do anything at all to lubricate international trade. The possibility is well recognized among students and a detailed examination of trade figures shows the practical opportunity.

The most-favored-nation treaties, in essence, provide that the parties shall be given the benefit of any bargain given to others. The agreement is not to give nations equal advantages, or even to make tariff walls of the same height for both parties. The agreement is only that commodities of every character shall be admitted under the same conditions as those afforded to other nations for like commodities.

It is lawful under the agreements and just under their principles to reduce by agreement with Brazil the tariff barrier on coffee into the United States in exchange for reduction of Brazil's rates on our potatoes into Brazil. If both nations are bound by most-favored-nation treaties with third governments, say Brazil with Chile and the United States with Germany, Brazil must now let Chile import potatoes at the reduced tariff into Brazil and the United States must let Germany import coffee at the new rates into this country. The concession may not interest Germany but it need not anger her as a preference would do. She has lost nothing; Brazil has gained. The United States has made no great concessions except to the coffee-growing countries, Brazil and one or two others. She has gained potato trade to offset. This process of generalizing concessions under equality treaties has been employed on a considerable scale in Europe. It preserves equality, lowers tariff barriers and, if wisely pursued, is a practicable path.

The practicability of this procedure of making mutual reductions of tariff barriers on a small list of commodities of special interest as between ourselves and any one nation and then generalizing the new rate to all who give us equality of treatment is of course dependent on some special conditions. They seem to me chiefly as follows:

First. Is it possible to pick out for each individual trading transaction a set of commodities which will especially interest the other country and yet not interest others sufficiently to destroy the trading possibilities with them in turn? To illustrate, can we give concessions to France on cosmetics,

[334]

cordials and dress models for instance, and yet not destroy our opportunity to drive a bargain with Spain on olive oil and cork? It would so seem. The opportunities are really considerable. A rough survey of our trade with the thirty principal nations shows that each is the leading producer of certain articles which constitute from fifty to over ninety per cent of its dutiable exports to this country. Thus, for example, wool constitutes normally nearly all of Australia's shipments to America and a concession to Australia on wool would to her be of great value and yet of relatively little importance to other countries. My judgment is that this condition applies to at least twenty nations and that in these the industry which could be favored would have the political strength to mature the bargain.

Second. Are concessions to be granted the United States on specific products of our own selectable on the same basis? This problem is more difficult, partly because we now face a matching problem, but it seems to me practicable in at least a dozen cases.

Third. Would the concessions bought for America in each case be sufficient to offset the resistance exerted here by industries exposed to less protection by our own reciprocal lowering of barriers? Here is the crux. The concessions desired from us by other nations are mostly in behalf of agricultural or land products. So far as they consist of items like coffee, rubber, tea, tropical vegetable products like drugs, cork and so on, the reductions in tariffs will only affect minor industries. But most countries want to sell us items like bacon, butter, hides, meat, tulip bulbs, wines, wool and so on which compete directly with domestic producers. We must never forget and yet we constantly do forget that we can sell more only as we buy more. At least we cannot sell without reciprocal spending or lending. The only program practicable in my judgment would be simultaneous negotiations covering enough countries and enough items to promise comprehensive results and enlist widely scattered public support. We cannot, in view of our history, trade the American dairy farmer for the benefit of the American electric light industry or vice versa.

Fourth. Is the negotiation of such agreements practicable in view of our political machinery? It is in my judgment

[335]

worth trying only if Congress is willing to entrust the President with wide power to negotiate firm agreements for terms of years and to lower our tariff barriers in return. Authority to lower barriers to a given percentage on a wide range of articles would at least be essential. It is well to remember that our Congress has power to destroy the effective operation of a treaty for a term of years by legislative act. Experience also indicates that the submission of a series of treaty bargains to the Senate, as in the case of the Kasson treaties, gets us nowhere. The program implies wide power, great courage and much prestige in the Chief Magistrate.

Fifth. Is it practicable to liberalize our regulations and administrative machinery as well as to lower tariffs? The authority to negotiate should include this subject on both sides, for tariff rates are only part, indeed the lesser part of the grounds for complaint. The complaints are based in part on matters of law and regulation, in part on elements of spirit and sympathy. The United States is only following examples abroad when we find the Departments of Agriculture and the Treasury applying their own little theories of protection in the guise of sanitary, fiscal and inspection regulations, but they are bad examples.

Finally, it must be pointed out that the lowering of tariff barriers here and abroad is no general solution for the demoralization of international trade. We cannot sell more unless we buy more. It is also evident that trade is languishing in part because of the recent wide establishment of general-manufacture in countries which formerly produced little but raw material. England's exports of textiles, for example, are now affected by the growth of cotton mills in India and China. Finally, the height of tariff walls is not, in spite of all the propaganda, the most critical factor in impeding trade. Import and inspection regulations are of growing importance, and uncertainty about tariff levels is as great a threat to trade as their altitude. We can look with favor on a policy of reciprocal negotiation primarily because it promises a breach in the vicious circle of retaliatory restrictions to international trade. We should and can avoid the entanglements, uncertainty and antagonism of a loose bargaining policy.

[336]

REMARKS BY THE CHAIRMAN

CHAIRMAN MORGAN: I have hidden from you one revealing fact about the last speaker. For a year or two, he was a reporter on the old *New York Sun*. At a somewhat different time, I also was a member of that amiable company. I think if I hadn't known it, from the lucidity and vigor of his speech, I would have recognized the fact.

We have heard thus far from Mr. Coulter about the operation of the tariff administration as we have it. We have heard from Mr. Rogers about the possibilities of applying the principles of reciprocity under the traditional tariff policy of the United States, that of most-favored-nation practice.

We now come to a third phase. Mr. Day, who is Director for the Social Sciences of the Rockefeller Foundation, was one of the American representatives on the Preparatory Commission of Experts for the World Monetary and Economic Conference. The subject which he is going to speak to us about is "Tariff Bargaining." Any of us who have ever attended or observed international conferences know that these things go on sometimes under the guise of bargaining, sometimes horse trading, sometimes playing poker. Mr. Day will, I am sure, take the more dignified course and discuss this process as bargaining. Mr. Day!

[337]

TARIFF BARGAINING

EDMUND E. DAY

Director,
U. S. Representative for the Social Sciences of the Rockefeller Foundation;
Member on the Preparatory Commission of Experts for the
World Monetary and Economic Conference

THE present government of the United States has committed itself to a policy of tariff bargaining. Two broad questions arise: first, to what extent does the policy now adopted by this action: first, to what American tariff practice; and, second, what conditions are likely to determine the success or failure of the new program. In the brief time available this afternoon, only in bare outline, but these questions will be dealt with only in bare outline, but these questions will serve to bring out some of the important issues that are involved.

For more than a century tariff legislation in the United States has clung tenaciously to a number of basic principles. From time to time certain deviations have appeared, and large, these have proved shortlived and have introduced no important changes. The new policy will throw some of these earlier principles into sharp relief.

The most conspicuous and best known feature of tariff policy in the United States is the persistent and cumulative protection of American enterprise against foreign competition. Grounds for adherence to this policy have shifted from time to time as political exigencies have required, and occasionally the trend toward higher duties has been interrupted, as in the acts of 1833, 1846, 1894 and 1913. But in effect the ideal of protection has been consistently pursued since the very beginnings of the government and opposition has rarely accomplished more than a moderation of the excesses to which the principle has at times been carried. No element of American economic policy appears to be more deeply rooted nor is any less likely to be completely abandoned.

Another widely recognized feature of tariff legislation in the United States is its strongly political color. The con-

[338]

ling forces which have put the long series of tariff acts upon our statute books have been predominantly self-interested and partisan. Administrative or expert counsels—even since the establishment of the Federal Tariff Commission—have played a relatively unimportant rôle. As early as the Act of 1789 the Congressional representatives of the two states of Massachusetts and Pennsylvania set the precedent. Ever since that time tariff legislation has been dominated by highly organized and powerful pressure groups operating through Congressional channels. Party against party, section against section, industry against industry, manufacturer against raw material producer—the forms of opposition may have varied; but, underneath, the unrelenting play of producer interests has tended to fix the level of the duties finally imposed. In no line of governmental action have the sordid effects of lobbying been more evident. In none has it been more difficult to secure effective representation of the general public interest. Appeals to take the tariff out of politics have proven entirely futile. Tariff legislation despite its highly technical character has always been a creature of political forces.

In another respect tariff legislation in the United States has a consistent record: it has been uniformly autonomous in the sense that its adoption has not been contingent upon the passage of related legislation in other countries. Doubtless from time to time American policies have been affected by the action of other nations. But—aside from certain abortive attempts at reciprocity—there has been no important intergovernmental bargaining. In this field as in others, the American policy has been neither to give nor to seek corresponding favors.

Closely associated with this phase of policy has been long-sustained adherence to the principle of non-discrimination among the foreign countries. The rule has been to apply American customs regulations and duties uniformly to all imports whatever the country of origin. Of recent years provision for unconditional most-favored-nation treatment by all countries has been another and closely related feature of American policy. Results in this direction, however, have been disappointing. Even provision for extreme penalties against discriminations by foreign countries—such as is found in Section 338 of the Tariff Act of 1930—has failed to bring other

[339]

nations into line with American wishes on this point. In the eyes of other countries non-discrimination has little virtue if maximum rates are applied to all.

Review of American tariff legislation over more than a century discloses thus at least four striking features: consistent and cumulative protectionism; purely political controls of the system; autonomous application of the laws without inter-governmental bargaining; and avoidance of discrimination among the many differing nationals affected by the imposition of the rates. To what extent will the contemplated bargaining tariff policy break with this record of the past?

Most obviously a fundamental change will be introduced with respect to the conditions under which any new legislation will take effect. Hereafter action on the American side will be contingent upon related action by one or more foreign powers. Autonomous tariff legislation presumably goes into the discard; or at any rate, if used at all, it will be supplementary. In the main, bilateral or multilateral negotiations will lead to conventions which will become operative only when necessary formal approvals have been secured from all the governments concerned.

To what extent will the tariffs thus adopted be made discriminatory as between the nations within and those without the specific conventions? On this point opinions appear to differ. In some quarters it is apparently held that there is an inherent conflict between effective tariff bargaining and an unlimited extension of the concessions to all parties whether or not they are directly involved in the conventions adopted. On the other hand there is impressive expert authority for the opinion that adherence to the principle of most-favored-nation treatment is entirely consistent with satisfactory bargaining. It is to be hoped that the latter view will prevail among the Washington authorities, at least until a thorough-going test has been made of its practicability. Mr. Rogers has already given a lucid explanation of the several lines along which this attempt should be made. Doubtless there should be limitations upon the scope of most-favored-nation treatment. Certain desirable exceptions to the rule have been noted in valuable studies conducted through committees and conferences under the League of Nations. But that unconditional most-favored-

nation treatment should constitute the basic principle is generally admitted. Otherwise a network of discriminations will develop that will almost certainly breed ill-will and in time may bring a serious setback in the promotion of more amicable economic relations.

It is the avowed intention of the present administration to obtain from the bargaining tariff policy a lowering of existing tariff barriers. How far substantial progress can be made in this direction remains to be seen. The record of earlier years, as already noted, is not encouraging. But that certain underlying developments in the American economic situation during recent times improve the chances of some moderation of the traditional high protectionism is quite evident.

It is probable, however, even under present conditions, that if genuine and substantial reductions of prevailing duties are to be effected a change must be made in the legislative processes by which duties are fixed. So long as the tariff remains as largely in politics as heretofore, so long as the fixing of rates is subject to Congressional dictation or lobby interference, a considerable and permanent reduction of existing duties is bound to prove exceedingly difficult, if not impossible. Delegation of authority to the Chief Executive to negotiate tariff reductions within stated limits and to give effect to these reductions by presidential proclamation would seem to be of the essence of the new policy. Even then the undertaking is bound to be one of enormous complexity.

So much for the points at which the new bargaining policy breaks with the past: what are other factors which are likely to determine its success or failure? A considerable number of them might be listed. Only a few of the more important, however, will be mentioned. Some of these derive from the extraordinary world conditions now prevailing; others are of a more durable character.

International political relations, of course, have a fundamental bearing upon the possibilities of effective tariff bargaining. As matters now stand, some clearing of the political atmosphere is indispensable. War clouds are no setting for forward-looking commercial negotiations. Until real progress is made toward military and naval disarmament, national policies, economic as well as political, will be dominated by narrow

ideals of defense and security. Assurances of a durable peace are an essential preliminary to the restoration of normal world trade. Suspicion and animosity no more make for satisfactory business arrangements among nations than they do among individuals. Successful tariff bargaining rests at bottom upon general confidence and this can only be established when political relationships provide the necessary guarantees. No considerations cut more deeply than these into the prospects of the new trade policy.

Measures of economic warfare, equally with the means of aggressive armament, must be scrapped before satisfactory commercial negotiation is practicable. Under present conditions international trade is checked in every direction by arbitrary restrictions and prohibitions, by exchange controls, by depreciated currency fluctuations. Tariff bargaining presupposes a substantial degree of stability in the fields of money and credit; it cannot make substantial headway in the midst of financial disorder. Moreover it is impeded by the extremes to which governmental intervention has gone in fixing both the direction and the volume of trade in some countries. In general, bargaining will probably tend to settle on the level of the most rigid forms of regulation represented among the nations undertaking to negotiate. Until currencies are stabilized and numerous arbitrary trade discriminations and restrictions are abandoned or at least moderated, the new tariff policy will make no great headway.

Another factor of supreme importance in determining the success or failure of the new policy is an adequate definition of objectives. Tariff bargains must be articulated in a more comprehensive economic program, the parts of which are appropriately interrelated. The period of the 1920's amply demonstrated the absurdity of promoting exports and stimulating foreign investments without regard to the means by which foreign purchasers and debtors were to make payment, either on the current items or on obligations previously assumed. The Hawley-Smoot Tariff Act in many respects further added to the absurdity of the total situation. In general the economic policies incorporated in the war settlement and in a host of post-war measures may be said to have constituted unintentional economic suicide: they have been crowded with

[342]

basic contradictions and inconsistencies. If the American Government is to engage in tariff bargaining it should do so with a view to the probable consequences of all parts of its economic program and in such a way that the total program makes economic sense. That this will be difficult is, of course, to be admitted. But this is merely one of many points at which difficulties must be squarely faced. Failure to define adequately the objectives of the bargaining policy threatens ultimate failure of the entire undertaking.

A danger to which tariff bargaining is peculiarly subject is an exaggerated emphasis on the purely direct and bilateral effects of negotiated arrangements. Such slogans as "Buy from those who buy from us", are so plausible that even government officials may be led astray. It is difficult to keep sufficiently in mind the fact that many of the most sound and profitable international trading relationships are multi-cornered. Any tendency to reduce trade conventions to purely bilateral terms is almost certain to be a step backward. Multilateral agreements or the simultaneous negotiation of two or more related bilateral conventions would seem to be the way to avoid this particular danger. A further safeguard is to be found in more general recognition of the fact that trading which takes advantage of differences of comparative cost among the producing nations is still sound, though somewhat old-fashioned, economic doctrine.

Another factor which will play an important part in the new policy is the willingness and ability of government to make genuine concessions. Certain reductions of prevailing rates on the American side should involve no very serious interference with American business interests, at least directly. Certain articles, which are given high protection under our present Tariff Act, are produced, nevertheless, only in slight measure in this country. While the problem of substitutes arises and doubtless there will be competitive sensitiveness, some imports may be more freely admitted without destructive effect on any enterprises of large proportions. Possibilities of this sort, however, are limited. Sooner or later in the bargaining program, the Government will have to face the fact, plain and unvarnished, that concessions cannot be made without injecting material foreign competition into certain sections of the

[343]

American market. The procedure will then necessitate not only nice negotiation, but a large measure of political courage. At this stage, the sailing will not be smooth even if the total result is unmistakably in the public interest. How far the Administration, even with the best of intentions, can get concessions out of our prevailing American processes of treaty-making and legislation is uncertain. As noted before, unless provision is made for a substantial delegation of power to the Chief Executive, the possibilities appear to be closely limited.

Finally, it is of the utmost importance that there be infused into the contemplated bargaining a spirit of underlying co-operation. The nations of the world must work together if satisfactory conditions are to be restored. If the projected commercial negotiations fall to the level of the huckstering of the market-place, if they incite a striving for petty and minute gain, if they exhibit an unwillingness to yield anything without a manifest, direct and completely offsetting advantage, they will not get far. Negotiations are bound at best to be exceedingly complicated. They will tax the patience and goodwill of those who participate. Unless there can be a note of common purpose, there is an unmistakable risk of more ill-will and of more barriers to international trade than exist at the present moment. To suggest that tariff bargaining should be friendly is no counsel of perfection, but one of necessity. American tariff policy in moving into its new phase will tax the resources of the new Administration in many directions. But no other form of action at the moment promises as much in the way of better tariff readjustment on the American side. Moreover, measurable success in the undertaking will work a change in American commercial policy of extraordinary significance.

[344]

PART III

INTERNATIONAL COLLABORATION

INTRODUCTION¹

JACKSON E. REYNOLDS

Vice President of the Academy of Political Science
President of the First National Bank of New York

MEMBERS of the Academy of Political Science and Guests: I know that I voice the regret you all feel that the President, Mr. Houghton, is not here this evening to introduce our guests with one of the charming and interesting addresses he always provides for us. It devolves on me, therefore, as Vice President, to act in his stead.

Our British guest is a Trustee of the Academy, and he is known to a great many of us as a teacher, a writer, a statesman, and an editor. My own acquaintance with him goes back to about four years ago when we were associated together as members of the committee for the organization of the Bank for International Settlements.

The Statutes of that Bank, I think, are the most lucid and terse documents I have ever read and most of that is due to the work done by our guest as the head of what we flippantly called the polishing committee. I complimented him at the end of our session there on this quality of succinctness and brevity in the statutes and he very modestly agreed with me that they were the best documents of the kind he had ever seen (laughter), but he made one reservation. He said he agreed except as to Article IV. That article he did not write nor polish. I did that myself. (Laughter.)

Our guest is one of the few liberals left in a most illiberal world. He is an exponent of liberalism not only as a profession of faith but also as a canon of behavior, and his behavior

¹ Introductory Remarks at the Annual Dinner Meeting.

is shown when you are his adversary; he is always liberal with you and, if you omit or state inadequately your own position, he is so fair that he does it for you.

Another quality which he exhibits, and one which makes him a useful citizen of the world today, is his outspoken belief in the advantage of a world economy. This comes in part from his broad knowledge as a trained economist and in part, I think, from the happy fact that he stands in that center of international affairs and trade which is London. That quality in him has found expression in his passionate devotion to the League of Nations and his evangelistic zeal in opposition to all trade barriers at all times. For these and many other reasons we welcome him and his message this evening.

I have the privilege of presenting Sir Walter Layton.

[346]

INTERNATIONAL COÖPERATION IN THE ECONOMIC CRISIS

SIR WALTER T. LAYTON, C.B.E., C.H.

Editor, *London Economist*

Chairman, *London News Chronicle*

MR. CHAIRMAN: With your permission I should like my first words tonight to be a tribute of respect and affection to the memory of two distinguished members and staunch supporters of this Academy, both of whom were present when I addressed you last. I refer to Dwight Morrow and Roland Boyden. To America, their loss, particularly at a time like this, is very heavy indeed, and their place will be difficult to fill; their loss is no less grievous to the nations of Europe whose problems and idiosyncrasies they both understood so well.

I hope, Mr. Chairman, that I shall be as succinct as you have indicated that I was at Baden-Baden, but I am not quite so confident myself. I had intended to speak tonight solely on the question of tariffs. But while we were still at sea, we heard the sensational news that the gold standard had been thrown overboard by the United States; so my carefully prepared notes — together with a great many preconceived notions — went overboard, too.

The background of the crisis, however, has not changed, and it may be well at the outset to remind ourselves of the appalling dimensions of the problem with which we are faced.

SCALE OF THE CRISIS

The International Labor Office recently estimated that the number of industrial workers unemployed in the chief nations of the world was from thirty to thirty-five million. Taking dependents into account, this means that there is a population

[347]

of some hundred million—not far short of the population of the whole United States—whose bread-winners are standing idle and producing nothing toward their upkeep. Primitive people, they say, cannot count above five, and figures like those I have given you are extremely difficult for anyone to understand, but it may help to illustrate the magnitude of this great unoccupied population, if I present it in this image: that if they were arranged in file, at intervals of a yard, they would stretch twice round the world. If we are to generate the driving force that is needed to grapple with this great problem, we must make the effort to conceive what these figures mean in terms of human suffering, baffled ambition, and resentment resulting from despair.

Let me give one other illustration which appeals more perhaps to a seafaring people than to a nation mainly inhabiting a land continent. There are today thirteen million tons of shipping laid up and rusting in the ports of the world, a figure considerably greater than the total shipping losses incurred during the whole of the Great War. Equally striking figures could be given of the 50 per cent or 66 per cent drop in international trade, of budgets unbalanced through falling revenue and shrinking production.

I will give only one further statistic, which will epitomize for this audience all the rest. The national income of the United States was estimated to amount in 1929 to \$85,000,000,000; last year it was estimated at \$40,000,000,000—less than half. That is all that was available in the United States last year for wages, salaries, profits, rents, interest, taxes, and all forms of payment. Similar figures could be given for the national income of other countries and in every case it will be found that a large part of the shrinkage is due to the tremendous slump in prices.

If prices remain at their present low level, we are faced with the almost inconceivably difficult task of scaling down all payments, whether wages or fixed charges, to this new low level, for it really is unthinkable that some of us should continue to receive an unchanged amount of a national income so diminished, while others scramble for the rest. Little wonder, therefore, that universally it is recognized that one of the conditions of recovery is a rise of prices.

[348]

AUTARCHY OR AN INTERNATIONAL WORLD

Let me hasten to add, however, that this baffling situation is, to my mind, by no means purely a monetary question. The power of the world to produce has never been greater than at present, but a grave disharmony between this power of production and the unsatisfied demand of millions of potential consumers has been brought about by a great variety of causes both political and economic, some of the most important of which were under discussion at Washington this week.

Before we can formulate sound policy on these matters, we must be quite clear what sort of world it is that we are trying to re-create. Many nations have been acting as though they thought it possible to build up their own prosperity regardless of or even in spite of other countries' interests. The doctrine of self-sufficiency, or autarchy, makes a very strong appeal to those who take a cynical view of the possibility of international coöperation; and let us not close our eyes to the fact that the tide has been setting very strongly in this direction in recent years. Without arguing the matter here, I venture to state my opinion that the policy of autarchy must lead to universal impoverishment and a prolonged and far-reaching setback to the whole standard of modern civilization.

But if we are to turn in the opposite direction and seek to rebuild an international world, we must face all the implications of that decision and promote one another's prosperity by mutual accommodation. It is useless to will the end unless we are prepared to will the means.

EFFECTS OF "GOING OFF GOLD"

One of the questions that is in everybody's mind is whether the new situation created by the dramatic events of the past week in this country will help or hinder the process of recovery and the restoration of a world such as I have suggested.

My own first reaction on hearing the news was one of relief that someone had at last had the courage to do something, that the ball had been set rolling, and that great events had been set in train. There seemed to be a sense that we were being moved off a dead center. Further, I realized that the American Administration, backed to an exceptional degree by the public opinion of this country, was evidently determined

[349]

to act, by heroic measures, if necessary, to stop the fall of prices and start the movement in an upward direction.

Is it possible by the measures proposed to achieve this? It is perhaps rash for an outsider to talk about these subjects of current controversy, but it does really seem to me that the urgency, the deep-seated nature of the difficulty with which we are faced, is such that we must take our courage in both hands and say exactly what we think.

What can we learn from past experience? Germany and other countries in Europe, for political and economic reasons arising directly or indirectly out of the war, passed through a phase of currency depreciation which it proved impossible to control. The results were in most cases disastrous to the economic and social life of the countries concerned. Perhaps Dr. Luther will have something further to say regarding this episode in modern history. I will only observe that it impressed the world with the extreme difficulty of keeping inflation under control, and inspired all the nations of Europe with a determination that, if possible, they would prevent its recurrence.

It was one of the tenets of early Bolshevik doctrine that you could utterly destroy the social system of a country, if only you tampered sufficiently drastically with the currency, and experience seemed to confirm this.

The British episode, on the other hand, was of a very different kind. In September, 1931, the only recent experience of currencies "off gold" was that of the countries to which I have referred, and with that experience in mind it was natural enough that a great national effort was made to insure that the pound sterling should remain "as good as gold." We failed. The immediate cause of our failure was the withdrawal of foreign balances on a tremendous scale while our foreign assets were frozen and could not be realized. We were in the position in fact of a banker on whom the depositors make a sudden call but whose assets are unrealizable. But that is only part of the story, for behind this capital flight was the fact that during the preceding years our national trading account had been getting more and more out of balance (and if I speak of our trading account, you will, of course, realize that I am talking of the foreign payments of all kinds, that we have to make to foreigners and the payments to be made to the coun-

try concerned, including everything that comes into the current year's trade, for goods or services, interest, and so forth).

For a number of reasons — one of the most important of which was that we were almost the only remaining free-trade country in the world, surrounded by a ring of tariffs which were rising higher and higher—we were buying more than we could sell. So long as capital flowed freely toward Great Britain, that is to say, while we were borrowing the means of paying for our imports, we could carry on; but as soon as the tide of capital stopped flowing, it became imperative to balance our current account, which meant that by some means or other our imports must fall or our exports increase. There was no other possibility.

One way of doing this would have been to do what I have just suggested as the almost incredibly difficult task which would face us today if we were going to cut down all incomes and salaries and every other payment in the country to the present level of wholesale prices. We could, in theory, have attempted by scaling down everything in Great Britain and by universal deflation to increase our exports, but even if it had been politically possible to do it, there was no time. When once the storm had burst in Central Europe, the only alternative was adjustment through a depreciation of the currency.

The pound fell in no sense as the result of internal inflation either actual or anticipated; indeed there was no inflation. We went off gold with a soundly balanced budget. We were driven off gold as the result of external pressure and a lack of balance in the trading account between Great Britain and the rest of the world. When the pound fell, it settled down after a while at a level which has gone a long way toward restoring equilibrium in our balance of payments.

It is, however, hardly necessary to add that though we may be solvent internationally in the sense of paying our way and balancing our account, both our incomes and outgoes are extremely low and we are faced with the problem, as everybody else is faced, of raising the general level.

I will make only two reflections on this story. They are these: First, the level to which the British exchange fell was largely determined by the level of the tariffs and the severity of other restrictions which were existing against British trade.

If you are forced to make your imports and exports balance, which they must do when capital ceases to flow, if you still can't get out enough exports, or if you are still taking too many imports, your currency must fall. If the ring of tariffs which were opposed to our trade had been still higher than they actually were, the depreciation of the pound would have had to be greater; if the tariffs had been less obstructive, the fall in the pound would have been less.

My other comment is, however, that while the fall in the pound had the effect of checking the fall of our exports and restoring the balance of British international trade, it unquestionably introduced a disturbing element into the international economic situation and, by so doing, at first at all events, it increased the general depression for us as well as for others. Though Great Britain clambered a little higher onto the raft, we pushed the raft a little lower in the water. From the world point of view, it caused more deflation. I believe, however, that in the latter half of the period since September, 1931, the comparative stability of the pound and of our economic situation has been and is a helpful influence.

In this connection the reproach is made against Great Britain that we have kept the pound too low and are striving unreasonably to maintain a competitive advantage. But what I have said indicates that, in my opinion at all events, the level to which the pound fell and about which it fluctuated in the past period of twelve months, is a level determined for us by the existing situation of international trade barriers and all the concomitant series of conditions which determine trade. It was, therefore, not a level which we chose but, in a sense, a natural level. Having got there, we believe (certainly I believe), that it was an international benefit for us to prevent exchange from fluctuating up and down whenever speculative influences, waves of capital, or anything else, tended to push the pound up and down, and that the equalization fund was created for a purpose which was an international benefit.

AMERICA'S MOTIVES

But I must return to America. America's recent action is in strong contrast to that of the United Kingdom inasmuch as it is the result, as I understand it, of extreme internal, not

[352]

external pressure, the internal pressure being the compelling necessity for a lift of prices.

If I am right, and unless there is a flight of capital due to lack of confidence at home, there is no reason for the United States to fear a foreign drain such as that which drove us off gold. A large part of the foreign balances in America has been repaid, while America's balances abroad are large. Though in your case as in ours both imports and exports are low, your international payments as shown by the figures published this morning in the newspapers, are reasonably balanced; indeed, if account is taken merely of your current trading position, there is no reason why the mere act of suspending gold payments abroad should cause any fall at all in the exchange value of the dollar. The currency of a country that is off gold is free to fluctuate, but this is not in itself a reason why its movement should be downward.

America has not abandoned gold, however, through any distrust of the gold standard, but with the definite idea of raising the internal price level.

It would be out of place for me to attempt to discuss the specific methods or merits of inflation—or perhaps I should use the word “reflation”—which are under discussion today in this country, but I will venture to state one or two propositions which seem to me to have a bearing on the situation from the international point of view.

First, the United States plays so great a rôle in the commodity markets of the world that an upward movement here should help more than anything else to start the ball rolling. I think that everyone who has considered the international monetary situation has been looking for and hoping to see a movement of prices in this country. We feel in Great Britain, for example, that whatever steps we might have taken to urge or stimulate a movement in Great Britain, could easily be neutralized, would almost certainly be neutralized, by anything like a contrary or adverse movement in this country.

But, to secure a higher level of prices is not so simple as it sounds. Experience has shown that merely to create the means of payment whether in the form of bank money or of currency has no magical effect. The present trouble is not that there is insufficient currency or credit in existence, but

[353]

that it does not circulate. There are today in the hands of the public of this country, in circulation, far larger quantities of currency than in any period of the boom. Clearly, if the currency circulates and the credit circulates, there is enough currency in America to carry a much higher level of prices than exists today. But, the level will rise only if somebody spends. A revival of spending either by private individuals or by the government may start a general upward movement; but unless there is general confidence and unless conditions are ripe for a uniform improvement all along the line, experience has shown (and effort after effort in recent years has illustrated this) that one act of spending may merely give rise to a momentary lift which will quickly fade away, while the currency and the bank credit return to the banks and lie idle once more.

This uncertainty as to the effect of inflation exists whether it is achieved by expanding bank credit, by printing paper money, or even by devaluing the dollar in terms of gold. True, it is so often presumed that if the gold content of the dollar were reduced by half, prices would at once be doubled. I believe that to be an illusion. Such a measure would encounter precisely the same difficulties as the other methods of inflation to which I have referred in particular, the difficulty of getting a uniform general upward movement of prices. You have got to get all incomes marching forward more or less *pari passu*.

But there is a special problem of getting an upward movement which must be borne in mind, for if there is to be anything like a uniform advance of prices in the United States, there must be recovery not merely of domestic purchases but of foreign buying, i. e., the international trade level must rise; for clearly you cannot secure and maintain a higher price for such commodities as cotton, wheat or copper if you are getting an expansion only in the home market.

Whether an expansion of foreign buying will happen or not depends to some extent on the effect of inflation in America on the foreign exchanges. What will that effect be? If a rise of prices were to take place in the United States unaccompanied by any price movement abroad, it is to be presumed that ultimately, in the long run, there would be a fall of the

dollar exchange to something like an equivalent extent, and when things had settled down, there would be no advantage or disadvantage to the United States in international competition.

But we all know that in the meantime, while things were adjusting themselves, considerable uncertainty would prevail in the exchange market, while a flight of capital, which might quite readily occur, would tend to drive the dollar below its natural level. Both these factors would have a deflationary effect abroad, similar to that caused by the fall of the pound, and this would increase the international depression. This, in turn, would spread back to the United States. There is real danger that efforts to stimulate prices internally may be neutralized unless very great care is taken to avoid harmful repercussions on the general state of the world.

The moral is that while everyone agrees that efforts must be made as far as government or bank policy can do it, to foster an upward movement of prices, we can be sure of gaining the maximum advantage only if the movement is international and all the different countries endeavor as far as possible to keep in step with one another. Further, the upward movement must be orderly and not violent, because we may be practically certain that if violent movements occur, the harmful reactions which are just around the corner, as it were, will more than neutralize the beneficial effects.

But, if we must look to general coöperation among the nations to secure higher prices, why is it that Great Britain hesitates to agree forthwith to stabilize the pound on a suitable parity and join in an effort to produce something like international reflation? The answer to that question is contained in the communiqué issued on Wednesday in which it was indicated that there must be simultaneous action in commercial as well as in monetary policy.

The mere stabilizing of the exchanges, even if accompanied by an upward movement of prices, would not suffice to insure an international system which we could be certain of maintaining. The economic nationalism of the last decade has created such changes and disturbances in the normal course of trade that unless we restore a much greater freedom in the movement of goods and enable trade to flow in its normal

channels, we cannot be certain that a new international financial system would be any more enduring than that which we set up and maintained between 1924 and 1930.

Autarchy is incompatible with an international monetary system. The mistake that we made in 1924 was to endeavor to set up an international monetary system without first making sure that the economic background was right, and we in Great Britain feel that that mistake must not be repeated.

TARIFFS

The experience of the depression has gone a long way toward driving home the lesson that there is no country in the world which can insure its own prosperity while the rest of the world is depressed; but there are still many illusions on the question of tariffs and their effect. It is still, for example, widely believed that a lowering of tariffs would involve a lowering of the standard of living. It is, indeed, obvious that, in practice, tariffs have not saved any country from a disastrous fall in the earning power of its people, for in the depression difficulties have overwhelmed both protectionist and low-tariff countries alike; but it is perhaps worth while to point out that in Europe's experience countries that have the highest standard of living are precisely those countries which have the lowest tariffs, while those with high tariffs have the poorest standard of living. The United States shares with Brazil, Spain, Hungary and Poland, the distinction of having the highest tariffs in the world. England and Holland are still among those countries that have the lowest.

Again, both in America and the British Dominions the idea is prevalent that a tariff which balances the cost of production at home and abroad has some scientific justification and puts competition on an even keel. But surely this is the most fatal of delusions. Foreign trade takes place because country A can produce goods more cheaply than country B, and obtain in exchange something which country B can produce more cheaply than country A. If you penalize trade by a tax precisely equivalent to this difference in cost, you abolish the whole benefit that would otherwise be gained by foreign trade, and, if you were to carry the policy to its logical conclusion (fortunately no country has ever done so) it would bring all

[356]

international trade to an end. This criticism is not merely a theoretical argument but is confirmed by practice, for this principle has been most vigorously applied by precisely those countries which have, as I said just now, the highest tariffs in the world and have most seriously impeded the flow of trade.

In this and many other respects a change of sentiment must come about if there is to be a change in the policy which has produced the present economic blockade. I would only add to this negative criticism one positive doctrine which is peculiarly pertinent at the present moment and which I think is now widely realized; it is that creditor countries must frame their commercial policy in such a way as to accept a position in regard to international trade in which they have a surplus of imports. Unless creditor countries accept this position, debtors must default, with all the harmful results to international credit that default involves.

Moreover, I do not believe that this conclusion regarding the need for creditor countries to accept an import surplus can be escaped by assuming that for a long period of time, let us say for the next decade, the situation will be taken care of by the resumption of lending on a large scale. German experience has shown in a striking object lesson that the method of continuous lending without the possibility of repayment by means of increased exports merely leads to the piling up of a mountain of foreign debt which is bound sooner or later to come tumbling down.

This German experience means, as I believe, that investors before investing abroad again will need to be satisfied that the countries concerned can maintain a positive balance of trade so that they can pay their debts by legitimate means.

There has been talk of a tariff truce in the last few days. Clearly something of that kind is obviously needed during the Conference; but it is only a suspension while the statesmen talk; for it is worth emphasizing that if we are to do anything in regard to trade, it is useless to stabilize the *status quo*. It is the *status quo* which has brought us into this situation. It is essential to secure much freer movement of goods than we have been enjoying in recent years. For unless there is a substantial reduction of the barriers to international trade, it will be impossible to restore the equilibrium of the world.

[357]

I said just now that if we will the end, we must will the means. That is going to prove a hard saying, for the questions we have to answer are precisely those I have been posing. Are creditor countries prepared to accept a situation where they will have an import surplus? Are we content to lower trade barriers to such an extent that we shall, in fact, become (and this perhaps applies more to Europe than to America) more interdependent? Do we really believe that we can safely move along those lines, or not?

I need hardly add that if we are to do so, political conditions must also be of such a kind that we can confidently count on peace at all events between the Western and industrialized countries of the world. These political conditions include disarmament and all that it implies. Nevertheless, we must realize that political appeasement is the first item in the time-table, for until it is achieved, the nations will not move along the road to greater interdependence.

WAR DEBTS

Before I sit down, I will refer very briefly to a subject which I have so far left on one side, namely the question of the War Debts. We cannot envisage the future adjustment of international trade without considering this matter, but, as it is still under official discussion both in Washington and London, I do not propose to discuss how it should be settled.

I will, however, venture two observations. The first is that when America is considering the future of her trading account (and I have urged that you should think of the situation in terms of actuality), the surplus of imports over exports requiring to take care of the normal private inflow of interest owing to American citizens will inevitably have to be increased by whatever amount may be paid in respect of the War Debts, while the exports of England and of France must be similarly increased.

The second is that this necessity cannot be avoided by arranging for payments in gold or even in silver, for England, at all events, produces neither of these metals and can acquire them only by a trading surplus. Nor does the increase in our holdings during the last few months refute this contention from the point of view of the immediate future. The way

[358]

our gold has been seen to be piling up in recent weeks seems to support the view that the June payment can be taken care of and there is almost enough in the till for December. But this is a superficial view; for our trading position, though nearly balanced, is still in deficit. This means that the gold which is flowing to England, if our figures are right, has not been earned in the way of trade, but has come to Great Britain as a result of an inflow of capital which for a number of reasons has recently been taking place. If and when that capital is withdrawn, the gold will flow out again.

If, in the meantime, we use the gold to pay the War Debt, the War Debt payment will not depress the pound at once, but we shall only have postponed the evil day, for when we are called upon to pay the private deposits which the gold represents, the pound will fall if our gold and foreign exchange holdings have been used up. That inflow is the counterpart of a capital movement; it is not an indication that we are earning a surplus which can be handed over to pay the debt.

There is no escape in the long run from the economic necessity which dictates that in the end international debts can only be paid from a trading surplus.

Mr. Chairman, I have touched on controversial questions; I hope I have not been indiscreet.

Sixteen years ago in April, a British mission, of which I was a member, quickly followed by a mission from France, set sail for the United States to organize coöperation for war. This April a series of missions has also crossed the sea. On this occasion there is no conflict of purpose between the nations nor are they divided into rival camps. They have come with one common aim, the aim of organizing a strenuous campaign against the forces of world depression and despair.

In physical warfare no army could hope to succeed if each division planned its movements independently and advanced and retired whenever it thought fit. The same is true of the present fight on which we are engaged. The secrets of success are the coördinating of action and the allotting to each of his appropriate task. The peoples must understand that, if we pursue what appear to be our individual interests at the expense of other countries, our self-seeking will most certainly recoil on our own heads. If we don't hang together, we shall

[359]

hang separately. But if our statesmen have courage, as your President clearly has courage, and also have the breadth of vision to grapple with the situation as a world-wide problem, there is no reason why we should not organize an advance along the whole front at once which will enable us to break through to prosperity.

REMARKS BY THE CHAIRMAN

CHAIRMAN REYNOLDS: We have another guest this evening who has just arrived from overseas, the representative of Germany. He has become known in his own country as the man who can do everything. He has been a mayor, several times a cabinet minister, twice Chancellor of the Reich, and once President of the Reichsbank. I happen to recall no Ambassador who has come to us in recent years with broader experience.

His first responsibility as a cabinet officer was in charge of the organization of the national food supply at the time that the great German cities were on the verge of starvation as a result of the extreme phases of currency inflation. It is said that whenever his associates in the cabinet asked him about the food situation, he countered with embarrassing interrogations about the currency situation. His associates became so annoyed at this persistent and uncompromising attitude that one day on about five minutes' notice they catapulted him into the job of Finance Minister and told him to do it himself.

As the Minister of Finance he filled a conspicuous rôle in the stabilization of the currency, and that led quite naturally to his becoming the President of the Reichsbank.

Some of you whose acquaintance with mayors is limited (laughter) may think that being a mayor is a poor school for diplomacy; all of you who are acquainted with bankers will be positive that banking is a poor school for diplomacy; but in his two terms as Chancellor of his country, our guest had the advantage of a good school of diplomacy and a great mentor in Dr. Stresemann. It was during that period that the foreign offices of Europe were engaged in framing the Treaty of Locarno, and our guest had much to do with that undertaking which has since resulted in inestimable contributions to the stability of Europe.

I have great pleasure in presenting Dr. Hans Luther.

[360]

INTERNATIONAL COÖPERATION

DR. HANS LUTHER

German Ambassador to the United States

Former Chancellor of the Reich and Former President of the Reichsbank

TO ADDRESS this gathering of the Academy of Political Science is both an honor and a pleasure to me. I know from my activity at home in Germany that the importance of the Academy of Political Science is nowise limited to the boundaries of America. The number of prominent personalities in the society, the weighty subjects that distinguish its meetings, and the abundance of general intellectual, and especially political, impulses launched by it, gave the organization long ago a fame that is world-wide. I thank you most sincerely, for this reason, for affording me the opportunity, now that I have entered upon the duties of Ambassador of the German Reich at Washington, to discuss before you a key theme such as "International Coöperation".

Before I develop my personal views, let me, please, preface my exposé by assuring you of something. No government in the world is more ready for international coöperation than is the German. The German Government is surpassed by no other in its eagerness for international coöperation.

I realize that this assurance may meet with some skepticism. Stating the case with moderation, a flood of criticism has in recent weeks been poured over Germany in foreign countries. But I am fully convinced that in a group like yours, thoroughly averse to slogans, disfiguring of the truth is clearly perceived, and the distinction readily drawn between the policy and volition of a government and the occasional effervescence of the youthful vigor and enthusiasm which have ever accompanied revolutions.

For this fact has to be taken into account: A revolution has occurred in Germany—bloodless and even within the forms prescribed in the pre-revolutionary Constitution, and, therefore, in accordance with them, something which no other revolution heretofore has accomplished. The present Government

[361]

of the Reich was given special legislative powers by a new Reichstag. This Reichstag conferred these special powers by the two-thirds majority necessary for changing the Constitution. And this Reichstag was elected by voters who, it may be said, sensed that this would be the issue. The election of this Reichstag resulted from the application of a general, equal electoral franchise and of proportional representation.

Now concerning the meaning and aim of this revolution. It is the national rebirth of a people; it is, according to the belief of the majority of the German people, the final fulfillment of a thousand-year-old wish which not even the Bismarckian Empire had been able to fulfill completely. The other great peoples have long since completed the process of becoming a nation.

It is only another aspect of the national renaissance of Germany that she directed the power of her national will against certain anational or anti-national movements which only through a rather inexact but universal way of expression are called international. These anational or anti-national movements threatened to disrupt the body of the German nation. Internationalism is something positive, while what I mean by anationalism is purely negative. Thus Germany has defended herself against such anational communism, and in doing so has rendered, I think, a service to the future of the whole world. The highest law for Germany both as a state and as a nation now is to secure and solidify the inner stability of her state and social organism. The German people, however, will never cease to be the bearer and augments of the intellectual and cultural values of her own past, of which she is proud. Grown together into a nation, the Germans are still the old German people.

The process of the German revolution had been going on long in the German people, assuming also the form of reaction to administrative and social ailments and disturbances of the social equilibrium during the post-war years. I am sure to find in this country, which justifiably has been judged to be the refuge of liberty, understanding of the necessity of meeting disturbances of the social equilibrium with wise government and popular policies, especially when these disturbances are as large as they were in Germany.

[362]

If to some of you, ladies and gentlemen, any of the happenings in Germany seem too rapid, or too evident, or exaggerated, pray do not forget that these developments took place in Germany under the terrible and unnatural pressure of the situation created by the Treaty of Versailles. This excessive pressure curtailed the sphere of life of the German people to such a degree that those who were not in the possession of positions that guaranteed spiritual and material existence passed into a state of material and spiritual distress in which self-preservation and self-maintenance by extraordinary means were forced upon the German people.

But what is now the attitude in questions of foreign policy of the new German state? What is its disposition toward international coöperation? How will it act? In foreign countries frequently the German Government is not considered a national government, as is its own rating of itself, but a nationalist government, that is, one which in an exaggerated measure keeps its eyes solely on the political, economic and other interests of the nation. Such a statement does the German Government an injustice. In his declaration on the Government's program before the Reichstag on March 23, Chancellor Hitler noted expressly: "The national government is ready to extend its hand for a sincere understanding to every people that is willing once and for all to terminate as a matter of principle the sorry past"; and again: "The German people want to live in peace with the world"; and further on: "Ten years of sincere peace will do more for the welfare of all nations than thirty years of running amuck by the victors and the conquered nations". All declarations of the German Government run in the same direction, and its applied policies follow the same course. Chancellor Hitler only recently, at a meeting of the National Socialist Labor Party, professed these concepts of foreign policy and declared that Germany's policy was one of peace, which Germany needs and which she wishes to maintain—"a peace with equality". The attitude of the German Government is thus made clear.

But what in principle, and generally, is the relation of the national to the international? That, indeed, is the core of my subject. National sentiment and international coöperation are not antithetical; the national is indeed necessary to the inter-

[363]

national. No great, liberating, people-uniting, and in the highest order productive, international idea is possible unless it has for its supporting base a free nation, conscious of and caring for its national individuality.

He who would promote internationalism without a national foundation is as foolish as he who believes that to develop the state the family has to be destroyed. Internationalism not reared on nationalism is like a tree without roots. Such internationalism would be anationalism, it would be a mere fiction, and upon fictions a political reality can never be built; on the contrary it is indeed dangerous to try to do so.

Let us do without similes and consider the actual reality. Where are to be found any forces other than state-national forces on which international solutions could be rested? I see none on the entire globe. In the same way that sound private economic relations between members of different nations are necessary, and that individual energy in private business is necessary in the affairs of mankind, so without the state-action of nations a new and sound internationalism cannot be constructed.

A solution of world problems—an international coöperation—is possible only when based on nations. This connotes nations with equal rights. The genuine equality of nations must again become the source of international thought and action. Where there is no equality, one nation will not develop full confidence in the honesty and reliability of another. Successes in a partial domain will remain partial successes. The vital organs of a whole, such as is formed by the community of nations, can be deprived of their normal blood circulation politically as little as economically without the whole body falling sick and staying so.

To show in what respects Germany is not the equal of other nations entails going into many details and examining the general tendency of the Treaty of Versailles. Allow me to remind you of the disarmament promises which, despite a great deal of good will in other countries, are yet unfulfilled. The position of Germany, Germany's struggle for equality in armament, with its aim at sweeping and general limitation of armament, is well known.

Besides the task of disarmament, at which the Disarmament

[364]

Conference has now labored for fifteen months, general attention is now directed with the greatest devotion to the tasks of the Economic Conference, which, by means of international coöperation, is to ease the world-wide distress of the hour. I will refrain from asserting, retrospectively, how great a share of this distress was caused all peoples by the Treaty of Versailles and the subsequent agreements. Now it behooves us to help in the future. Germany will participate in the Economic Conference with the strongest will for international coöperation imaginable. Germany welcomed in the warmest manner the decision of your President, resulting from his profound statesmanlike judgment, to have preliminary conversations on the World Economic Conference in Washington, so that in this manner the way would be paved for the understanding which would make the realization of this great labor certain instead of problematical.

Not a few countries had long been surrounded by high tariff walls when Germany, only a few short years ago, decided hesitatingly to follow this example. But there is also a difference between prohibitive tariff walls and those which merely aim at an equitable equalization of advantages: To give an instance, a southerly sun bestows upon a soil more than fertile, certain advantages which are denied to the scanty soil of another country, despite the greatest industry of its population. To equalize such advantages is the sole aim of a few agrarian emergency measures taken by Germany in recent times; and this view could hardly be characterized as economically unjustified, internationally destructive, or vulnerable from the angle of political morality by any unprejudiced point of view. These customs measures, though late, did nevertheless raise some dust, but they need not prevent Germany's being a good buyer in the future in the American market. For many years now almost twice the number of millions have wandered to the United States for imports into Germany as have moved in the opposite direction for exports from Germany to the United States. Germany must draw attention to this. But it does not do this with the feeling that it is proper on principle to buy from a country only as much as it will buy from you. World economy would be a wretched thing, condemned to never-ending ailment, if the tendency persisted of checking up with

[365]

the pencil the trade between two countries by such a system of control, instead of, as once upon a time, putting at the disposal of our fellow nations commodities from the entire world with the consciousness that the finally necessary economic balance would not be struck by only two states but within the whole family of nations.

You as a creditor nation know certainly that paying debts due the United States is possible only in the form of dollar remittances or the importing of goods. When a debtor country like Germany wants to open a market for the export of commodities to foreign countries, no artificially devised prerequisite for a function in world economy within the scope of international coöperation is in question but, I might say, an imperturbable fact born of the simplest logic. It is precisely truths of this sort which in recent times have often been buried by landslides. Let us hope that little by little they will rise again from the débris of muddled theory and inorganic thinking.

Regarding the other questions which must be solved by the World Economic Conference or in connection with it, I will limit myself to a mere hint. Among them is found the compelling necessity for the reestablishment of firm value relations between the different currencies which will make the merchant's computation possible. This subject is so actual at present, also in the United States, ladies and gentlemen, that the mere touching upon it by me unleashes the whole complex of thoughts connected with it.

Generally speaking, I would like to express my conviction in regard to the World Economic Conference that without sacrifices by each participant it will hardly work. Should the Conference reach a global result, however, it will be shown that the sacrifices demanded of everybody are only seeming sacrifices because the gain by all in a revived commodity and credit traffic between the nations will represent a much greater advantage than the total of sacrifices made will be a loss.

To hold that times of comparative poverty are the most suitable for the spiritual and cultural progress of peoples is a high-minded idealism. A grain of truth is surely hidden therein. At the same time I am of the opinion that in our world today a certain average prosperity of peoples is neces-

[366]

sary to progress. There is hardly another country that has developed this to the degree that yours has. The general living standard in the United States is recognizedly high, when we overlook the present confusion.

Still more important for international coöperation than thriving economy and flourishing culture is mankind's far more precious and all-embracing gift, the preservation of peace. It is especially Germany, which suffered so much from the consequences of the war, and which is now conscious of the geographic handicaps of its situation, that longs for this ardently. What Chancellor Hitler said on this subject I have already quoted. Please, do not believe the gossip that in Central Europe lives a people feeling anything else but the desire for a just peace with all the world, as the best basis for international coöperation.

I would like to close, so as not to make an unreasonable demand upon your time. Since I deemed it proper to express at the outset my gratitude to your highly esteemed society for this invitation, I would like to conclude by expressing the fact that it is a great satisfaction to me to have been entrusted with the post of ambassador at Washington. If international coöperation, as I have attempted to sketch it here, be the prerequisite to world recovery, then I dare to express the hope that I shall be successful in developing still further the international coöperation between the United States and Germany, which in many respects has long been in existence. International coöperation cannot be furthered in a vacuum, but only by practical individual work between state and state, people and people, man and man.

Allow me to close with the confession of faith and confidence that international coöperation will be a blessing for both countries: America and Germany.

[367]

PROCEEDINGS
OF THE
ACADEMY OF POLITICAL SCIENCE

Volume XV

JANUARY, 1934

[No. 4]

CURRENT PROBLEMS OF UNEMPLOYMENT
AND RECOVERY MEASURES IN OPERATION

A SERIES OF ADDRESSES AND PAPERS PRESENTED AT THE ANNUAL
MEETING OF THE ACADEMY OF POLITICAL SCIENCE
NOVEMBER 8, 1933

EDITED BY
PARKER THOMAS MOON

THE ACADEMY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY
1934

COPYRIGHT BY
THE ACADEMY OF POLITICAL SCIENCE

PREFACE

BECAUSE of its immediate interest as a symposium of authoritative and expert views on the problems of national industrial recovery, the present number of the PROCEEDINGS has been rushed through the press and is issued in advance of the regular publication date. In these pages the reader will find not only a discussion of national recovery by the officials and advisers who are guiding the National Recovery Administration in the United States, but also a critical appraisal of unemployment problems and recovery measures by some of the ablest American and British economists and by several of the foremost leaders of industry.

The papers and the discussion here printed will constitute the record of an exceptionally well attended and stimulating Annual Meeting (Fifty-third Year) of the Academy of Political Science, held on Wednesday, November 8, 1933, at the Hotel Astor in New York City. The Academy is deeply indebted to the distinguished speakers who took part in the meeting and to the Committee on Program and Arrangements, a list of whose members follows: Mr. Gerard Swope (Chairman), Miss Ethel Warner (Director), and Messrs. Winthrop W. Aldrich, John B. Andrews, William C. Breed, W. Randolph Burgess, Joseph P. Chamberlain, Raymond B. Fosdick, Walter S. Gifford, Alanson B. Houghton, Thomas W. Lamont, Sir Walter T. Layton, Sam A. Lewisohn, Samuel McCune Lindsay, Roswell C. McCrea, Wesley C. Mitchell, Parker T. Moon, Shepard Morgan, William L. Ransom, Jackson E. Reynolds, E. R. A. Seligman, James T. Shotwell, Thomas J. Watson, Louis Wiley, Leo Wolman, and Owen D. Young.

(iii)

CONTENTS

	PAGE
Preface	iii
PART I: CURRENT PROBLEMS OF UNEMPLOYMENT AND RECOVERY MEASURES IN OPERATION	
<i>Owen D. Young</i>	1
<i>Leo Wolman</i>	3
<i>Sir William H. Beveridge</i>	10
<i>Stanley King</i>	17
<i>Donald R. Richberg</i>	25
<i>George A. Sloan</i>	33
<i>Edward A. Filene</i>	
<i>Sir William H. Beveridge</i>	
<i>Louis C. Marburg</i>	
<i>George A. Sloan</i>	
<i>George Sands</i>	
<i>Donald R. Richberg</i>	
<i>J. Leo Honigman</i>	
PART II: SCIENTIFIC PROGRESS, THE SHORTER WEEK AND UNEMPLOYMENT	
<i>Walter C. Teagle</i>	44
<i>Harold B. Butler</i>	51
<i>Sumner H. Slichter</i>	63
<i>Henry I. Harriman</i>	76
<i>Harry L. Hopkins</i>	81
PART III: LONG-RANGE PLANNING	
<i>Gerard Swope</i>	84
<i>Daniel C. Roper</i>	91
<i>Sir Arthur Steel-Maitland</i>	101
	(iv)

PART I

CURRENT PROBLEMS OF UNEMPLOYMENT AND RECOVERY MEASURES IN OPERATION

INTRODUCTION¹

OWEN D. YOUNG

Chairman of the Board, General Electric Company

THE ANNUAL MEETING for the fifty-third year of the Academy of Political Science will be in order. I emphasize "political science," for if it be the function of science to discover the principles and to formulate the rules by which we may interpret what is going on in the world or by which we may forecast what will go on, then I think we may well ask ourselves this morning, after a half-century of existence, whether there be such a thing as political science. Whatever catastrophe may have happened to political science, it is at least fair to say that the Academy and Miss Ethel Warner, its Director, still survive.

Whatever the distortion which may have come to that term "academy" in our day, for the Greeks at least it was "a pleasure ground" where Plato taught philosophy. This morning I welcome you who are here and you who are listening in, to that kind of place, a pleasure ground, not a musty cell where scholastics insulated from the world discuss attenuated theories. This is a football field, sparkling with life, where everybody, particularly now, is intent on watching the ball. Few see it, some fumble it, but the spirit of all is to advance the ball.

To govern the play we must have rules. They may be changed from year to year and from generation to generation, but for the purposes of the game these rules are more important than the exact sciences, say, of physics and chemistry which govern the make-up of the ball.

¹ Introductory remarks at the First Session of the Annual Meeting.

This is an academy not so much of an exact science as it is one in which temporary rules governing the play are considered. It is not and ought not to be a dark and solemn place, and I am sure it will not be so this morning, but a bright, cheerful, and stimulating place where competent observers tell us about this quickly moving spectacle which is now on.

The topic of this meeting of the Academy is: Current Problems of Unemployment and Recovery Measures in Operation. This morning we shall ask what rules should one adopt in this contest with unemployment. Scholars are taking part in this game, not old men with long, gray beards, but young ones who have moved out from the cloisters to the arena. We welcome their appearance on this field of action and they now have the opportunity to demonstrate to a watchful and sympathetic audience their ability to advance the ball.

So I bring you first this morning a scholar who is a player in the game, Dr. Leo Wolman, Professor of Economics at Columbia University, who is Chairman of the Labor Advisory Board of the National Recovery Administration. He will talk to you on the "Progress and Possibilities of Unemployment Insurance in the Codes."

[370]

THE OUTLOOK FOR UNEMPLOYMENT INSURANCE IN THE CODES

LEO WOLMAN

Professor of Economics, Columbia University; Chairman, Labor
Advisory Board, National Recovery Administration

NONE of the hundred or more codes of fair competition which have been signed by the President of the United States contains any provisions for unemployment insurance. Nor has there yet been any serious discussion within the Recovery Administration of the policy of broadening the terms of the codes so that they may include measures, in the form of unemployment insurance, for the prevention and relief of unemployment. The movement for insurance legislation which only twelve months ago showed unsuspected vitality and promise in many of the state capitals of the country, and even in Washington, has meanwhile wavered before the impact of the mass of national labor legislation initiated by the National Industrial Recovery Act and stands now uncertain and fearful of the future.

Whatever may be the eventual fate of unemployment insurance, the reasons for its present neglect are quite clear. In the first place, the task of carrying codes through to completion is much more formidable than anyone not closely acquainted with the details of the operation could possibly imagine it to be. In addition to the many rules affecting trade practices, the labor provisions of the codes have already gone far beyond the few and simple items contained in the law. The mandate to establish minimum rates of wages has been elaborated to cover geographical variations in the minimum wage, exceptions for special classes of workers, special wage provisions for learners and apprentices, limitation of the number of apprentices and learners, formulae designed to ensure the maintenance of satisfactory wage differentials between unskilled, semi-skilled and skilled labor, and in a number of instances the establishment of scales of wages for nearly all grades of labor employed in the industries in question. The determination of

[371]

maximum hours of work has, likewise, in practice involved the fixing of daily and weekly maxima; making provision for emergency and seasonal employment; distinguishing between average and maximum hours, and, where average hours are provided, determining the method of averaging, as in the recent case of the Ford automobile company; establishing the rate of wages paid for overtime in excess of the maximum hours; and adjusting the wages paid for the longer work-week to the reduction in hours. A fair number of the codes legislate as to labor representation on the code authority and as to the method of handling industrial disputes. Over and above these features, all codes impose restrictions on child labor, make rules with respect to employment in hazardous occupations, and specify various and sundry administrative principles and devices which, in each instance, are deemed essential to the effective enforcement of the terms of the code.

When it is remembered that the Recovery Act was passed by Congress on June 16, last, that in the four and one half months since the bulk of American industry, from manufacturing to retailing and the hotel business, has come under codes of fair competition, and that, within the same period, the President's Reemployment Agreement was launched and administered, it is obvious why so specialized and extraneous a question as unemployment insurance has to this time received such scant attention in the councils of the Recovery Administration. It is, in fact, hard to recall any instance in the history of modern industry when so universal and complex a body of labor legislation was formulated and adopted in so brief a space of time. There have been parallels for this sort of thing in war time. But even during the World War, the volume of labor legislation of both the Federal and state governments was infinitesimal compared with what at this time has been accomplished by means of the codes in less than six months, and, what is more important, the changes in labor standards during the war were, by comparison with the present, the result of a slow process influenced and directed mainly by the trend of basic economic conditions, and hardly at all by the terms of legislation.

The second and probably ruling factor responsible for the prevailing apathy toward unemployment insurance is to be found in the theory underlying the National Industrial Re-

[372]

covery Act. Everyone familiar with the origins of this legislative measure knows that it is rooted in the widely accepted belief that unemployment can be immediately reduced by shortening the work-week and that the volume of business activity can be augmented by raising wages and thereby increasing the purchasing power of millions of wage-earners and salaried employees. While this belief is not new in the annals of economic theorizing, its general and enthusiastic acceptance by innumerable business men and labor leaders, and the conduct of a vast experiment in public control under its influence, is, to say the least, an unusual event in modern business history. When, moreover, there is added to this view the equally widely held opinion of business men that stability of production and employment can be achieved through the right of business to combine to regulate prices and output, and to perform other similar regulatory functions in industry, the system of ideas relevant to the experiment conducted under the NRA is presented at least in bare outline. Whether this doctrine is true or untrue, sound or unsound, is a question whose full exploration falls beyond the scope of this paper. But the fact remains that faith in its efficacy has acted, for the present at any rate, to emphasize the elements of business recovery in the program, and to subordinate the problems associated with an expedient like unemployment insurance.

Practical tests of the effectiveness of a complicated economic program are, unfortunately, always hard to discover and, when found, harder to interpret. On the face of things there has been, as is well known, a marked and, to many, an unexpected increase in both employment and payrolls which in a general way synchronizes with the progress in code-making. From the low in the middle of March to September 15, employment in American manufacturing industries increased 35 per cent; and over the same period manufacturing payrolls advanced by 60 per cent. From the time, also, when the codes and the President's Reemployment Agreement became effective until the present, full-time weekly hours have been reduced by 10 to 20 hours a week, and in extreme cases by as much as 30 hours a week. Wage-rates, likewise, although here the statistical evidence is not yet fully available, rose substantially and with more than customary rapidity.

[373]

When, however, these data are subjected to further analysis and to comparison with similar phenomena elsewhere, the case is far from clear and the relation of cause and effect turns out to be by no means certain. Thus, while employment expanded by 35 per cent from March to September of this year, 13 per cent of the increase took place by June 15, before either codes or reemployment agreements were used; whereas, also, the total increase in payrolls from March to September amounted to 60 per cent, half of this advance or 29 per cent occurred by the middle of June. Quite obviously recovery began with the climb of business out of the trough reached during the banking moratorium of March. And much of the rise in employment and payrolls from that time until mid-September may easily be attributed to this initial stimulus which, together with the effects of well-known speculative forces of the period, antedated the adoption of the wage and hour provisions of the codes. It should also be noted that the rise in both payrolls and employment until the middle of the summer was associated with a very considerable recovery in business activity and in the volume of production. Since then business has been clearly declining and we appear now to be approaching the point, if we are not already at it, where the increase in employment due to the shortening of the work-week and the increase in payrolls due to the raising of wage rates may be expected to be more than balanced by a drop in both employment and payrolls due to the decline in the volume of industrial production.

There is, in this connection, much in the foreign experience with employment and unemployment during the last twelve months which throws light on the probable character of American business developments in the same period. English unemployment, for example, has dropped approximately 20 per cent between August 1932 and September 1933; and Canadian employment improved 16.5 per cent from April 1933 to September of this year. The apparently large discrepancy between the rate of reemployment in England and Canada, on the one hand, and in the United States, on the other, is mainly attributable to two factors in the American business situation in the first months of the present administration. The gold embargo, the decline of the dollar, and anticipation of a high and rising price level produced considerable speculative buying by both producers and consumers and unquestionably con-

tributed powerfully to some of the expansion in business. At the same time the base from which American reemployment and wage increases started, reflecting as it did the virtual paralysis of business in the first quarter of 1933, was so much lower than the prevailing levels in either England or Canada, that the rebound when it came was almost certain to be more striking in the United States. It is, indeed, a fact worthy of the most careful consideration that at the depth of the depression in this country, the recorded unemployment rate here seemed to be from two to two and one half times as great as the highest unemployment rate of England.

Statistical evidence such as this, meager and unsatisfactory as it may be, seems to me to support the conclusions of economic analysis and to confirm the truism that the chances for continuing improvement in employment depend upon the prospects for continuing improvement in business. The fixing of minimum standards of employment through the NRA, particularly in this country where labor legislation has lagged far behind the labor law of Europe, has already served as an indispensable measure of social reform and has gone a long way to raise conditions of work in the sweated industries to levels approaching comparative decency. But as an instrument for promoting and perpetuating business recovery, the regulation of wages and hours and the variety of controls over trade practices provided in the codes of fair competition hold not nearly so much promise of success. The continued lack of balance in American business processes, the disparate changes in costs among industries during the past months, and the importance of fundamental elements of uncertainty in the business situation point to the persistence of a large volume of unemployment far in excess of the rate of unemployment customary in this country before the depression. This unemployment may for some time to come be particularly heavy in the construction and capital equipment industries, precisely where the recovery has been least noticeable during the past months. While governmental intervention, in the form of public works or like measures, may seem temporarily to mitigate the severity of the problem, the chances are that it will hardly serve as a solution.

How to provide adequate care for the unemployed during these next years and how to prepare them for slow reabsorption into industry is the outstanding problem before this country.

The steps we have already taken in building up our elaborate and effective machinery of Federal relief will probably never be retraced. We have learned, like the countries of Europe before us, that for so many-sided a problem as unemployment, there is no single, simple solution. Failing the adoption of economic policies calculated to generate prolonged business activity and the consequent return of the unemployed to their jobs, neither unemployment insurance, nor public employment offices, nor public works, nor regulation of wages and hours constitutes an adequate, effective unemployment policy.

In the United States, as in England during the past decade, a satisfactory public unemployment program will involve the administration of public relief so as to afford fair and decent standards of life for the unemployed; the creation of provisions for the reeducation and retraining of labor; the establishment of machinery for the transfer of surplus labor from dying industries into new fields of employment; devising means for equitably distributing the burdens of cost of such a program among those best able to bear them.

In this program, compulsory unemployment insurance must be an essential element. With the growing realization that the volume of American unemployment will for some time continue to be unusually large, the pressure for state unemployment insurance legislation is bound to grow and to lead shortly to the passage of laws in several of the industrial states of the country. If this happens we shall repeat in the United States many of the mistakes made by other countries and raise knotty problems which we might otherwise avoid. The form of organization created by the codes of fair competition makes possible experiments with unemployment insurance along new and more hopeful lines. Already there have been developed in America legislative proposals for "unemployment reserves" which, unlike the so-called "insurance" schemes, are based upon funds established by individual industries or companies. Such reserves set up under compulsory state legislation will dovetail harmoniously with similar future developments in the industrial codes. Reserves for unemployment, designed to cover the employees of an industry and jointly administered by employers and labor under the supervision of public agencies, will solve the problems of interstate competition which have always retarded the advance of social legislation in this

[376]

country; will ensure greater efficiency and flexibility in administration; will avoid the subsidizing of dying industries by more prosperous ones and thus hasten the solution of the problem of unemployment in declining industries; will strictly limit insurable risks and thus separate the unemployed who must receive relief from those who will be recipients of unemployment insurance benefits; and will encourage experimentation with methods of prevention and devices for reducing the amount and frequency of unemployment.

REMARKS BY THE CHAIRMAN (MR. OWEN D. YOUNG):

The next speaker is a representative of the Brain Trust of England. I heard him say recently that he didn't know what the "Money Trust" was. Perhaps he doesn't even know what the Brain Trust is, but I suspect from watching its operations in this country that we have hoarders and spenders in both the Money Trust and the Brain Trust, and we like the spenders over here because we like to keep brains and money in circulation. It is very fortunate that as the exchange of goods between these two great nations has diminished, the interchange of ideas, at least, has held its own; perhaps it has increased. These two great English-speaking nations have not yet joined the ranks of those who bar ideas from without or limit the free expression of them from within. I hope they never will.

So we welcome not only with open minds but with hungry ones, this distinguished Englishman; educated in the law, and escaping from the rigors of its practice, he is more concerned in seeing what the law should be than what it is. With a legal education built on a preparation at Charter House and Balliol, with high honors in mathematics, the classics and in literature, he not only knows what ought to be, but he knows how to tell us what ought to be and why.

As Chairman of the Unemployment Exchange Committee and of the Board of Trade, as Director of the Labor Commission, as Secretary in the Ministry of Food, as Member of the Royal Commission on the Coal Industry, he knows about labor and its problems first hand. He not only knows how to tell men about these things but, as the author of an anthology of thoughts on woman, he ought to be able to tell you ladies as well. Difficult as these subjects are, they are only fun for him, because I am told that his principal recreation is hill walking.

I welcome Sir William H. Beveridge, the Director of the London School of Economics and Political Science, to the arduous task of telling this Academy and its guests something about the British experience with unemployment.

[377]

LESSONS FOR THE PRESENT FROM BRITISH EXPERIENCE WITH UNEMPLOYMENT

SIR WILLIAM H. BEVERIDGE
Director, London School of Economics

THE first lesson is that we had unemployment in Britain for many years before we agreed officially to recognize its existence. All through the second half of the nineteenth century the British trade unions had been paying unemployment benefit to their members, sometimes less and sometimes more, according to the state of trade, but till well into the twentieth century, we still had people talking as if nobody need be unemployed, as if all the unemployed were unemployable. We still had a Poor Law in which the only regular provision for the able-bodied was an offer to enter the work-house; a Poor Law based on the simple principle that if relief to the able-bodied was made sufficiently unpleasant, they would and could get work. Chiefly as the result of an exhaustive examination of our Poor Law system and of distress through unemployment, made by a Royal Commission between 1905 and 1909, our official view was changed. We set up permanent machinery for dealing with unemployment, through employment exchanges and insurance; we got to recognizing unemployment as an integral part of our economic system. Twenty-five years ago, we in Britain got our heads out of the sand at last in this matter of unemployment. Possibly you in this country are passing through the same stage today. It is only natural that you should come to that later than we did. Your industrial expansion began later and has lasted longer.

My second lesson is that just about the time that we came to recognize the reality of unemployment as an economic problem, we came also to a conclusion about one of the possible means of relieving distress from unemployment. We came to the negative conclusion that what we call "Relief Work" and what you call "Work Relief" was not a good general method of trying to help the unemployed. During the years from

[378]

1905 to 1909 we tried many experiments in making work for the unemployed. Nearly all those experiments turned out badly. By "Work Relief" I do not mean the putting in hand at times of depression of useful public works on which men are employed on ordinary commercial terms, and only those men are employed who are used to the work and can earn their wages there. "Work Relief", for which men have to be selected irrespective of their capacity for the particular work and from which they cannot be discharged (since they are in need of relief) simply because they are unable to do the work as well as others, is something different from work. It tends to become sham work, more expensive and more difficult to organize, and in the end more demoralizing than money payments with no pretense at work at all.

From this negative conclusion against "Work Relief" as a means of preventing distress through unemployment, we came to the positive conclusion that the best way of preventing distress was through a system of unemployment insurance, such as had been practiced for fifty years by trade unions for their own members, which we decided then to extend under a national compulsory system to people who could not or would not join a union. We began a system of unemployment insurance for a few industries in 1911 and we extended it to all industries in 1920. It applies now to every form of employment except in agriculture and domestic service. For every week of employment, the employer has to buy an insurance stamp representing his own and the workman's contribution and affix it to a book carried by the workman; he deducts half the value of the stamp from the workman's wages. For an adult male the stamp is now 20d., so that employer and workman each contribute 10d., roughly 20 cents; the national government adds a third 10d., making 30d. or 60 cents altogether. The workman when unemployed goes to an employment exchange and gets benefit, now nearly 30s. a week—\$7.50 for a man with three children.

This system has gone through a great deal of criticism and a variety of changes. I think I can say that now there is no serious person in England who would seriously propose to abandon it. The essence of the insurance system with us is its connection with a nation-wide system of employment ex-

[379]

changes. Insurance benefit for unemployment is not and should not be paid merely because a man is not working; one must be satisfied also that he could not work if he wanted to—that there is no job for him, not only in his own town but elsewhere, which he can reasonably be expected to take. The only way of making sure of that is to have a complete register of all the jobs available. The employment exchange is there to register the jobs as well as the men. In unemployment insurance the employment exchange is as essential as the doctor is in sickness insurance. The doctor both issues a certificate of sickness and helps the client to get well. The employment exchange both certifies that the client really needs benefit because there is no job anywhere that he ought to take and helps him to any job that there is.

To start unemployment insurance without employment exchanges would be like starting sickness insurance without doctors. But if unemployment insurance is connected with an efficient organization of employment exchanges, our experience shows that there is no serious danger of individual malingering, of men getting benefit who could get jobs.

The great bulk of people in our country, as in yours, would much prefer work to benefit. The few who would not, can be prevented from abusing the insurance system by the employment exchange system. Fear of individual malingering is an imaginary danger.

But there is one real danger in unemployment insurance which, particularly in your country, calls for a warning. The volume of unemployment in a country depends, among other things, on the wage policy adopted by those who in that country determine wages. The contract of employment is a contract for the sale of labor and, as in every other sale, if the price is beyond what the market will bear, the goods will not be sold. It is possible for wages to be too high for the market, to cause unemployment. That is an unpopular thing to say anywhere. In this country it may seem particularly out of place, for the people of this country, more than any other country, have been sold to the idea that high wages are a cause of prosperity.

Every country has its own favorite economic theory, its pet delusion. Ours in England is or has been the lump of labor

theory; the idea that there is only a limited amount of work to be done, so that if by a machine you save labor you necessarily create unemployment; by that delusion, by not mechanizing enough, we in Britain have lost more trade than we need have lost in the world. Your favorite theory in this country is the high wage theory, the idea that pushing up wage rates by itself creates prosperity. By that idea, I believe that at this moment you are making recovery in some ways slower than it need be. You must not mind my saying that; for I honestly and regretfully believe it. Of course I have not a word to say against prohibition of wages so low that they amount to sweating. If an industry cannot exist except by paying wages below the level of subsistence, the country is better without it. And above that subsistence level it should be the aim of every employer to pay as high wages as he can afford; the object of economic effort in civilized society is not the enrichment of the few by high profits, but the solid comfort of the many. But the payment of high wages is a sign of prosperity, not its cause. In America as in every other country of the world, the payment of higher wages than the market will bear means the payment of higher wages than the market will bear means the unemployment, so that the adjustment of wages to what the market will bear is one of the most responsible tasks in our economic system. The people who have that task under collective bargaining are the associations of employers and the trade unions. Any scheme whether of insurance or of relief for unemployment which makes either of those groups careless about the creation of unemployment is a social danger of the first magnitude.

Frankly, I believe that we came very near to that danger in Britain since the war. Our recorded experience of unemployment falls into two parts. Before the war our unemployment ran between 2 and 10 per cent and averaged about $4\frac{1}{2}$ per cent; in those days the trade unions, which controlled wage policy, themselves paid for unemployment through their insurance systems. Since the war, our unemployment has run between 10 and 20 per cent and has averaged about 13 per cent; during that period the trade unions had lost much of their direct responsibility for the unemployed; we have had insurance, and have at times got near to making benefit under our insurance scheme run on indefinitely; we have provided

the benefit partly by direct taxation, partly by a flat rate of insurance contributions — a tax on employment — falling indiscriminately on all industries, steady and fluctuating, high wage and low wage, and therefore not felt specially by any one of them. We have had money wages sticking up while prices fell.

Let me say at once that I don't believe any one can definitely prove that the higher level of unemployment in Britain after the war was directly due to wages being too high. There were too many other possible causes of unemployment at work; there was general disturbance of our economic life after the war. But it is clear that the divorce of control of wage policy from responsibility for unemployment was there, as a possible cause of unemployment. If, as we in Britain recover from this depression, we do not get back to something much nearer the prewar level of unemployment, there will be ground for believing that the danger which I have mentioned has become real and active; that by insurance we are keeping wages higher than the market will bear.

I hope that we shall in fact have reformed our insurance scheme enough to get rid of that danger; reformed it in the direction of distinguishing again firmly between unemployment insurance and the relief of destitution; reformed it by making our insurance benefit limited in duration and based upon actuarially calculated premiums, while providing in some quite different way for those who exhaust their claims to benefit and still need relief because they have not recovered employment.

Of course you may ask what is the real distinction between insurance benefit and relief, if each is just a money payment to the unemployed person. The distinction is that insurance benefit should be paid as of right, on the certificate of the employment exchange that the workman is unemployed and that there is no job for him, without any inquiry as to his other resources, the earnings of his family or his savings. It is a well as over the time when he is standing by as can and should draw with no more loss of self-respect and no more hesitation than he draws his wages. But if he runs through this insurance claim and comes upon relief, then it is

[382]

probable that he needs something more than a mere money payment; as likely as not, he will have been demoralized, physically or otherwise, by long idleness; he may need reconditioning, fitting for a new kind of career, physical rebuilding. The payment to him should take account of all his other resources and should be given not as of legal right but by administrative discretion. I believe that that is the solution to which we shall be working in Britain, though I hope also that we shall be able to make our insurance benefits so generous, that the great bulk of the unemployed will not need to run through their benefit.

That is the one real danger in a scheme of unemployment insurance, the risk of divorcing the control of wage policy from responsibility for its possible consequences in management. I have felt bound to mention this possible danger, not because I am against insurance, but because I am strongly in favor of insurance. But I cannot advise any one to take that road without pointing to the rock ahead. If one sees the rock, one can see the way around it. The way to avoid the danger that I have named in regard to wage policy lies in observing two conditions: First, that the insurance benefit shall be definitely limited in duration; second, that the cost of insurance shall be thrown both upon employers and upon workmen, in such a way as to bring home to the leaders in each industry the facts of unemployment in that industry. This condition does not mean that no contribution should be made to insurance from public monies; it does mean, I think, that contributions should be made by workmen as well as by employers, and that the contributions paid in different industries should be different.

Let me add one final lesson from British experience. One of the standing difficulties in getting the problem of unemployment dealt with seriously is the shortness of human memories. "When the devil was sick, the devil a saint would be; when the devil got well, the devil a saint was he." In a trade depression people are ready to do all sorts of things about unemployment; as soon as the depression passes, they forget all about it and do nothing, till the next depression comes and finds them unprepared. We had many depressions of trade in Britain before 1908; we forgot about each of them as soon as it was over and did nothing to prepare for unemployment. At

[383]

last, by a fortunate combination of persons and politics, we did out of the depression of 1908 get the employment exchange system and unemployment insurance for a few industries. But when in 1916, at the height of the war-time boom, I tried to get insurance extended to other industries, to cotton and wool and leather and many more, so as to be ready for the depression that might come after the war, I found employers and trade unions alike solidly against it. Their ears were plugged tight by prosperity; they said they wouldn't have any unemployment after the war and if they did they could look after it themselves. Four years later, at the end of 1920, we got insurance for all industries just as the depression was upon us; we got a worse scheme than we need have had and the scheme itself never had a fair chance; it was swamped by relief. We were like the man who tries to take out a policy against fire, just as his house has got well alight.

That is my last lesson and the most important one. Don't forget about this depression the moment that you recover from it, as before long you will recover. Put in some solid planks of reconstruction now, among them something permanent to take care of unemployment.

REMARKS BY THE CHAIRMAN (MR. OWEN D. YOUNG):

At least the Brain Trust in this country is not narrow-minded in its recruiting. It not only selects its people from university halls but it occasionally reaches down into business for a man. It is an honor to them who invite and to him who accepts. I have the privilege, ladies and gentlemen, to introduce to you this morning an old friend of mine, long a co-actor with me at the bar and in business, whose distinctions there, great as they were, are now displaced by another and higher title. He is President of Amherst College.

Ladies and Gentlemen — Dr. Stanley King, who will speak to you on the subject of "Unemployment Reserves and Insurance Programs."

[384]

UNEMPLOYMENT RESERVES AND INSURANCE PROGRAMS

STANLEY KING

President of Amherst College
Chairman, Massachusetts Commission on Stabilization
of Employment

AFTER listening with you to the matured wisdom of Sir William Beveridge, ripened by many years of experience in this problem of unemployment insurance in Great Britain, I confess that I feel very much like a schoolboy in the presence of a revered and learned professor, for while, sir, I have been thinking about this problem for thirty years, you have been dealing with it.

The problem of unemployment is the most serious challenge faced today by American industry. For the past four years the American people have witnessed a tragic demonstration of the breakdown of our older methods of dealing with men and women who are out of work through no fault of their own. The fundamental case for unemployment protection lies in the fact that under a democratic form of society we are forced to prevent any large-scale starvation. Funds must be provided somehow. Gathered during times of stress, through taxation and by gifts, they tend to make conditions worse. It is practical sense to build a system which will gather the funds in good times and disburse them in bad times. This simple theory underlies all formal proposals for unemployment insurance, for unemployment reserves.

Some ten European countries now have some kind of unemployment insurance, covering a total of forty-five million workers. Most of these countries are poorer than the United States; their commerce and industry were more severely dislocated by the war; and their populations are now more burdened by taxes. In spite of this, ten of the industrial countries of the Western world outside of North America, have courageously attempted to solve the major social problem of our time.

[385]

Meanwhile, the question is receiving the serious study of our own people. An interstate commission appointed by the governors of six Eastern industrial states (Massachusetts, Connecticut, New York, New Jersey, Pennsylvania and Ohio) has made a report. The American Association for Labor Legislation has made a comprehensive study and recommended a program. State commissions have been at work in Wisconsin, Massachusetts, Ohio, New York, California, Minnesota and elsewhere. Senator Wagner has proposed a bill for the District of Columbia. And the able and far-sighted woman who is Secretary of Labor in the President's cabinet has publicly approved a program of unemployment insurance. At the same time a number of large employers, most notable among them the General Electric Company, have initiated voluntary programs along this line. In spite of this really imposing development of opinion, however, it still seems to be true that the employers of the country as a whole maintain their traditional attitude of opposition to any legislation in this field.

Let us examine the concrete proposals that have been made. The Ohio bill, drafted by the Ohio Unemployment Insurance Commission, passed by the Assembly but killed in the Senate, is deliberately an insurance measure. It assumes that unemployment insurance is sound in theory and feasible from an actuarial point of view. It aims primarily to provide compensation for losses incurred, to relieve distress resulting from unemployment. A fundamental principle of the Ohio plan is that the cost of insurance be shared by employer and employee. The sponsors of the plan would apparently favor a contribution also from the state treasury, raised by taxation, but they do not include this proposal at present, because they believe its inclusion would destroy the possibility of passage of the Ohio bill. In scale of benefits the Ohio plan is more generous than other scales proposed in this country. It allows 50 per cent of wages, with a maximum of \$15.00 per week, for a period of sixteen weeks, after a waiting period of three weeks. The Ohio commission felt that a 3 per cent charge on payroll (2 per cent from the employer and 1 per cent from the employee) was all the traffic would bear at the beginning, and so fixed this rate of contribution. But the actuary for the Ohio commission recommended a charge of 4 per cent on payroll so as to permit

the increase in the duration of benefits from sixteen weeks to thirty-five or forty weeks.

The Ohio bill pools all the contributions from all the employers in the state in a common fund, from which benefits are paid. Provision is made, however, apparently more as a concession to opposing theory than from conviction, for classification of risks and adjustment of premium rates to comparative unemployment hazards after the experience of some years has been accumulated. Under this provision the rates for the employer may be varied between 1 per cent and 3½ per cent instead of the flat 2 per cent.

The Ohio plan follows the British procedure; is based, perhaps, largely on British experience; and is perhaps not so much a new contribution to our thought in this field, as an adaptation to our needs of the experience of Great Britain. It frankly attempts to guarantee to the worker a definite benefit; and then it levies such a tax upon industry as may be necessary to meet the bill. Its sponsors are candid in expressing the belief that state contribution to the unemployment insurance fund is desirable, but at the moment impracticable. This Ohio program will undoubtedly be urged not only in Ohio but before the legislatures of most of our industrial states, and we may expect a vigorous campaign for its adoption.

Happily, we have an alternative proposal, equally definite, the result of equally thorough study, and sponsored by equally competent authority. The Wisconsin commission, the Massachusetts commission, the American Association for Labor Legislation, as well as five of the six state representatives on the interstate commission (Massachusetts, Connecticut, New York, New Jersey and Pennsylvania) have made proposals, which differ in detail but are similar in their essential provisions.

The Wisconsin-Massachusetts plan is based on a philosophy which differs fundamentally from that implied in the Ohio program. Our proposal is significant, I think, because we lay emphasis on preventing unemployment as well as relieving it. We recognize the danger pointed out some time ago by Sir William Beveridge when he said: "The real danger of unlimited relief of unemployment lies, not in the fear of demoralizing the individual worker, but in the fear of demoralizing

Governments, employers, and trade-union officials so that they take less thought about the prevention of unemployment." We who have studied the matter in Wisconsin and Massachusetts believe that unemployment is to a substantial extent preventable, that the assumption to the contrary is unsound and dangerous, and that our first duty is to frame a program which will give the maximum incentive to prevention, while at the same time providing relief to those out of work.

The American Association for Labor Legislation, which has been studying the problem for more than a decade, has made a recent report which is a genuine contribution to the subject. Its Special Committee was broadly representative and included employers, representatives of labor and the social agencies, as well as economists.

Its report contains an outline proposal for legislation and I have seen no clearer or more lucid exposition of the subject. The report proposes an American attack on the problem along new lines. Its essential provisions are not unlike the proposals put forward by the commissions of Wisconsin and Massachusetts.

The Wisconsin bill, which was the result of prolonged study in that state, was enacted into law about a year ago. It contained a provision that it should become effective only when the industrial indices reached a certain level, and has therefore not yet begun to operate. Meanwhile, a Special Commission, containing a representative of industry, a representative of labor, and Professor Raushenbush of the University of Wisconsin, is engaged in working out the details of administration which will be involved.

The Massachusetts proposal was submitted to the legislature last winter by the Massachusetts Commission on Stabilization of Employment, after a study of eighteen months. It came up for consideration by the legislature at the time when the legislature was engrossed with the problem of beer, and at the time when the banks in Massachusetts were closed. The legislature met the issue by extending the life of the Massachusetts commission for another year and asking it to consider further not only its own bill, but all other bills which had been submitted to the legislature in this field. As the essential provisions of the program of the American Association for Labor Legisla-

[388]

tion, the Wisconsin law, and the Massachusetts bill are similar, I shall discuss this with particular reference to Massachusetts, with which I am most familiar. The Massachusetts commission was made up of two of the leading employers of the state, two representatives of labor, the Commissioner of Labor and Industries of the Commonwealth, President Compton of the Massachusetts Institute of Technology, and myself. Our proposal received the unanimous assent of the Commission.

We recommend establishment of compulsory unemployment reserves to which employers of ten or more persons, except in agriculture and certain special employments, shall be required to contribute 2% of the payroll of all employees except those who received more than \$1,500.00 during twelve months prior to unemployment. The employer's payment is to be made monthly or oftener to an unemployment reserve fund deposited with the Treasurer of the Commonwealth for account of the employer and his employees, each employer's deposits to be kept in a separate account. It is not to be drawn upon by any other employer or by the employees of any other employer, or for any purpose except for benefits during unemployment and for such administrative expenses as are chargeable against the account.

Our proposal also provides that:

The employer may substitute his own voluntary plan, providing the benefits offered are at least equivalent to those required by the bill, subject to approval of the Department of Labor and Industries.

Under our proposed plan, benefits from each employer's account are to be paid eligible employees laid off more than four weeks or dismissed for no fault of the employee, providing the employee is unable to find suitable employment by the end of four weeks. The amount of the benefits is to be one-half the normal wage or salary of the employee, but not to exceed \$10.00 per week. Benefits are to be paid for not more than ten weeks in any twelve months.

Each employer's liability is limited to the amount of his unemployment reserve account and to the 2% contribution described above. He cannot be required to pay more. When his account becomes exhausted, his unemployed workers draw no further benefits.

When an employer's unemployment reserve account amounts to \$50.00 per covered employee, he is required to contribute only 1% of his payroll, as long as the account remains at or above this level. When his account reaches \$75.00 per employee, no further contributions are to be required as long as his account does not fall below that level.

The cost of this plan to the employer is limited to the cost of the 2% contribution. His employees must still bear, if unemployed, the loss of all wages during the first four weeks, of all unemployment beyond the ten weeks' benefit period, and of all unemployment after

[389]

the employer's account in the unemployment reserve fund is exhausted, together with half or more of the wages lost during the benefit period.

This heavy cost still remaining upon the out-of-work employee is one reason for requiring that all the contributions to the unemployment reserve fund shall be made by his employer.

An equally important reason is the probable effect of the contribution in stimulating the employer to reduce as much as possible the number of lay-offs and dismissals in order to keep his unemployment reserve at the \$50.00 or the \$75.00 level and thus reduce the amount of his contribution.

Our intimate acquaintance with industry in Massachusetts leads us to believe that the best point of attack on unemployment is the individual enterprise. Hence we recommended an individual company reserve financed solely by the employer. Thus the burden of compensating men who are laid off is placed squarely on the shoulders of the employer who laid them off. And as a corollary, the employer who operates his plant steadily is protected from supporting the unemployed workers of his less efficient neighbor. By this device we give an immediate pecuniary incentive to each individual employer to stabilize his own operations and impose a penalty on each employer who fails to do so.

We believe that this is sound social accounting. It places the cost of unemployment on the concern responsible for it. It brings into higher relief the fact that irregular employment is expensive, increases costs; and that stabilized employment is both more efficient and socially more desirable. It gives a pecuniary premium in competition to the socially sound employer and a pecuniary penalty is placed on the socially inefficient employer. Where can one find a more potent pressure toward the goal society desires to reach?

The problem of investment of unemployment reserves will become serious if and when a number of large industrial states enact such legislation. Reserve funds will be accumulated and invested during periods of prosperity and will be sold mostly during periods of depression. It is highly probable, therefore, that the investment of reserve funds in the usual type of bonds would result in a net increase in unemployment. Our Massachusetts proposal, therefore, recommends the investment of state funds in the short-term obligations of the United States Government and in deposits in the Federal Reserve System.

It should be noted that the Ohio plan, which is frankly an insurance proposal, guarantees benefits to unemployed workers within limitations and then assesses the cost, whatever that may be, on industry and on employees, with the obvious possibility that a portion of it might be borne by the state. One may doubt whether it is wise to impose on industry today this unlimited liability. The Wisconsin-Massachusetts proposal, on the other hand, is in essence a proposal of industrial reserves. It fixes the contribution of the employer and thus attempts to limit his liability, and avoids the dangers inherent in a contribution from the state treasury. These differences are fundamental. Which proposal one accepts depends upon one's underlying philosophy.

We should recognize that every proposal thus far made in this country, so far as I know, except the recent proposal for dealing with this matter in the codes, calls for state legislation. No commission, so far as I know, believes that the solution of the problem can be left indefinitely to voluntary action on the part of liberal-minded employers. No commission recommends a Federal law; for the Federal Constitution seems to be an impediment to Federal legislation in this field unless it is accomplished through the codes.

It is easy to criticize the detailed provisions of any bill for unemployment compensation. These are essentially of less importance and can be modified from time to time as experience may indicate. My experience with this problem in industry dates back nearly thirty years, when I worked under the leadership of William H. McElwain, a Massachusetts shoe manufacturer. In an industry which at that time was working only 270 days a year on the average, McElwain succeeded in stabilizing his production and operating his plants, which at that time were the largest producers of shoes in the country, on a basis of 306 days in a year. McElwain's untimely death in 1908 was a great loss to industry, but since that time other employers in this country both in that line and in other lines, have made remarkable progress in stabilizing employment.

Our proposal is to stimulate such efforts by placing a pecuniary incentive before all employers looking toward the stabilization of their employment.

President Roosevelt has publicly said that unemployment insurance is coming in this country just as definitely as workmen's compensation came. Our own studies would make us believe that that is true. In a time of emergency like the present, I would hope that the employers' associations in our industrial states, working in coöperation with associations of labor, might coöperatively draft bills to submit to the state legislatures. In that way I believe we would secure the soundest procedure in this field, but if the employers' associations in our industrial states continue to maintain their traditional policy of opposition, my own judgment is that public opinion will force legislation in this field and that the employers will find themselves operating under laws which they had no share or participation in drafting.

REMARKS BY THE CHAIRMAN (MR. OWEN D. YOUNG):

The next speaker on this program is a graduate of arts in the University of Chicago, and in the law from Harvard. Unlike Sir William Beveridge and Stanley King, he has never escaped from the practice of the law. There he has achieved distinction, not behind the bulwarks of established precedent, but by courageous advances from the firing line into no man's land.

As Chief Counsel for the railway unions in the government injunction suit in 1922, as General Counsel for the Railway Labor Executives Association since 1926, in sustaining trial by jury in labor contempt cases before the United States Supreme Court, as co-author of the Railway Labor Act passed by Congress in 1926, he has established himself as an authority not only on the problems of labor but on the rights of labor. This required him to be also familiar with the problems of capital and the rights of capital; problems of both capital and labor as component parts of industry are the same, but in the division of the income of their joint endeavor, the rights of one begin where the other ends.

It was natural, therefore, that one with this experience should be chosen, and I think it was a fortunate choice, as General Counsel of the National Recovery Administration.

Ladies and Gentlemen, I have the honor and privilege of introducing to you Mr. Donald R. Richberg, who will speak to you on "Progress Under the National Industrial Recovery Act."

[392]

PROGRESS UNDER THE NATIONAL INDUSTRIAL RECOVERY ACT

DONALD R. RICHBERG

General Counsel, National Recovery Administration

IN that bygone era when we were enjoying the illusion of prosperity it was my part to appear occasionally on programs of the Academy of Political Science as a critic of those who seemed to be too well satisfied with the existing economic order. Today I might entertain myself, but probably no one else, by reviewing a few of the suggestions offered at such times as constructive measures to promote a more stable and more evenly distributed prosperity, and to prevent the inevitable breakdown of an undisciplined, uncoördinated control of the business enterprises upon which our freedom and security depend.

But I shall yield to this temptation only long enough to restate the philosophy of the present recovery program in terms of some of my earlier criticisms which have been validated by subsequent events. Under the terms of Title I of the National Industrial Recovery Act we are now seeking to bring about a purposeful, planned organization of trades and industries, so integrated and coördinated that the continuous production and exchange of necessary goods and services may be assured. The basis for such an assurance is being sought, not in the exertion of a political control over business, but by encouraging and sanctioning measures of self-discipline that will provide a genuine self-government of industry.

This program is now being subjected to certain widespread criticisms which arise out of either misunderstanding or misinterpretation of both the means employed and their objective. Men who are either ignorant or careless of the facts talk glibly about the "regimentation" of industry and describe an essentially democratic and individualistic endeavor as the product of the socialistic doctrines of Karl Marx.

[393]

The President and officials of the National Recovery Administration have spent long exhausting weeks persuading the representatives of practically all our basic industries to agree upon codes of fair competition, which are being carried out through the voluntary coöperation of the privately selected directors of industry. Yet these patient, persuasive efforts are now being denounced as the establishment of a presidential dictatorship over industry! When the facts are marshaled to confound some of these critics they have resorted to the explanation that underlying these apparently democratic measures of free coöperation are the sinister purposes of those who in their hearts are plotting an economic dictatorship and a socialistic state.

As one of the draftsmen of the law, who has been engaged ever since its enactment in its interpretation and administration, I am so frequently accused of participating in this "socialistic plotting" that it comforts me now and then to reread an address made before this Academy in the year 1928. It is true that I said that the ideas of eighteenth-century individualism no longer fitted our needs. But at the same time with equal emphasis I said that the ideas of nineteenth-century socialism never did fit our needs; and that the twentieth century demanded genuine coöperation between property men and labor men in developing a common program for their common benefit.

In this same address I went so far as to suggest that it was a serious impediment to social progress to have the minds of financiers and business leaders impregnated by socialists with the doctrine of the inevitable class struggle, which, fortunately, the vast majority of American workers had never accepted. I even suggested jokingly that the writings of Karl Marx and his disciples should be expurgated from our libraries so as to prevent American business men from being led astray and learning to look upon the workers as a hostile class of society.

Having held these ideas for many years it would be very embarrassing for me to discover that I was participating in a national movement to establish a socialistic dictatorship. And every time I have a talk with General Johnson, the Administrator for National Recovery, and listen to the forceful expressions of his highly individualistic and competitive theories

[394]

of political economy, and to his explosive comments upon the vicious influence of government bureaucracies, I shudder to think of his rage if he were ever to discover himself promoting state socialism!

The fountain head of the recovery program is the President; and it would surely be difficult for anyone to find either in his conversations or his writings any affectionate sympathy with the dogmas or programs of Karl Marx. In fact his utterances have abounded in such statements as these: "We must get back to first principles; we must make American individualism what it was intended to be—equality of opportunity for all, the right of exploitation for none." "The task of government in its relation to business is to assist the development of an economic declaration of rights, an economic constitutional order. This is the common task of statesmen and business men." And when the President sought in a speech to redefine individualism in modern terms, he said that "business leaders are now expected to assume the responsibilities which accompany power."

Now being reassured myself, and having, I trust, reassured my audience that my individualistic views are not out of line with the Administration program, let me quote one further paragraph from that address made to this Academy in 1928:

The managers of industry today ought to be statesmen, because the welfare of the country rests upon their larger decisions. Not merely physical well being, but social policies and social ethics are determined by those whose power over the standards of daily living is greater than that of government. But it is democratic statesmen we need, not dictators. Does any man here doubt that the forces moving in modern life and the powers available for human direction are too great and too complicated to be safely controlled by any one man or any small group of men? Does anyone think that any sane man or any small group of sane men would aspire to dictatorship in the modern world? A would-be dictator must be inspired by delusions of grandeur, willing to seize the thunderbolts of Jove, reckless of when or where he may unloose a storm to devastate the land.

The National Recovery Administration is not seeking to establish a dictator or a group of dictators of industry, but is in fact moving in precisely the opposite direction.

The Recovery Administration is seeking to establish such self-governing organizations of business men as may prevent the rise of any more irresponsible dictators of industry such

[395]

as those who guided the American people along the road to ruin in the years before 1929, and continued to lead them downward into the valleys of despair as long as their self-serving powers survived and they could exercise bad judgment unrestrained by any first-class economic or political intelligence.

The American people do not yearn for any more such dictators—neither petty autocrats in control of the lives and fortunes of communities nor industrial Caesars ruling the destiny of the nation. They do not want any dictators whether privately or publicly selected. The worthy leaders of industry and politics have come to see clearly that the anarchy of an undisciplined and uncoordinated private control of all essential business enterprises, free from enforced responsibility to serve the public interest, is no longer a tolerable economic system, when the daily subsistence and welfare of the entire population depend upon the continuous and beneficent functioning of these agencies for the exchange of the products of human labor.

Those who study the course of events throughout the world cannot help observing that, in every nation in the world where a stubborn resistance to the necessary development of new economic controls has brought about a political revolution, some form of state socialism has been the outcome; that is, a political control of business primarily in the interest of certain classes, although nominally in the interest of all the people.

It has been amply demonstrated that the individualism of a pioneer people cannot be preserved in a modern industrialized state. But it has not yet been proved that the only alternative is to surrender to state socialism and make the best of it. Many nations of the world developed from principalities and kingdoms into empires, while the American colonies were creating and strengthening a republican form of government unifying in a national federation the self-governing units of the states.

Russia, Italy, Germany and other nations may now have found it necessary to coördinate the production and exchange of goods through the exercise of dictatorial powers by the state. But here upon this continent, where our ancestors devised a new variety of political government which has developed lustily for over 150 years, we may have the courage and vision to develop a new variety of industrial self-govern-

ment, along similar lines, as another great contribution to civilization.

Observers in other nations may view our efforts with sympathy, with skeptical amusement or downright hostility. The Tories and the ultra-radicals within our borders will do their best to make our efforts fail—the first group because they feel we are going too far in the direction of public restraints upon individual freedom—the second group because they feel we are not going far enough. Perhaps there is no half-way house. Extremists can always produce very logical arguments, to which the principal answer is that life is not logical—or consistent—but is an eternal compromise between utterly opposing forces from the cradle to the grave.

It is my personal belief that there is a half-way house—a house of democratic coöperation and self-discipline—which lies between the anarchy of irresponsible individualism and the tyranny of state socialism. That is why I am so deeply concerned with misrepresentations of the spirit and purpose and methods of the National Recovery Administration. Intelligent criticism is both inevitable and helpful. But the extremists of either the conservative Right or the radical Left who may sincerely believe that there can be no permanent middle ground, are not fair, and frequently not sincere, when they deny that the Recovery Administration has laid the foundations of its program in that middle ground.

It was John Stuart Mill who long ago said: "The social problem of the future we consider to be how to unite the greatest individual liberty of action with a common ownership in the raw material of the globe and an equal participation of all in the benefits of combined labor." He stated his conviction that all classes of society "must learn by practice to combine for generous, or at all events for public and social purposes, and not, as hitherto, solely for narrowly interested ones." He ventured to assert that "the deep rooted selfishness which forms the general character of the existing state of society is so deeply rooted only because the whole course of existing institutions tends to foster it."

The temporary phases of the Recovery program call for speeding up action and shortening deliberation in order that the emergency needs of millions of idle workers and impover-

ished farmers may be satisfied in a short period of time. But in the very process of providing emergency relief there is a well-considered and conscientious effort to lay the foundations of deliberative, self-governing institutions for the permanent improvement of industrial conditions.

The emergency program and the program for the long pull of economic recovery each deserve separate appraisal although today they are closely interwoven in the activities of the Recovery Administration. And the effort to establish the half-way house of democratic coöperation deserves the sympathetic aid and encouragement of all those who still have faith in the ideals of our democracy.

If the half-way house cannot be established we may soon find that we have reached the end of democratic institutions of government; because trade and industry must become responsive to public obligations; and there must be set up somewhere a government of industry adequate to insure a nation against mass starvation in the midst of plenty and against the paradox of millions of willing workers living in forced idleness while billions of capital investments also lie idle.

If a machinery for the self-government of industry cannot be created and operated then control by political government is inevitable. That is the final issue of the recovery program. Every disputed item of that program presents the same choice.

Cut-throat competition, in the anarchy of private business operations, prevented any concerted move to shorten the hours of labor so as to absorb the unemployed—or to fix minimum wages on at least a subsistence level, so that industries need not be supported by public taxation for the relief of their underpaid workers. And so it was necessary for the government to fix in the codes maximum hours and minimum wages. Many powerful employers, resentful of any interference with their individual and unrestrained control of labor relations, have fought against any responsible self-organization of their employees—even to the extent of carrying on years of civil warfare with perennial outbursts of violence and bloodshed.

But millions of wage earners, citizens of a democratic government, cannot be deprived permanently of any voice in determining the terms and conditions of their employment. Either they must be allowed to participate in industrial self-

[398]

government or they will demand the extension of the control of industry to the political government in which they still have the power of a free ballot.

The employer who is still devoting his best energies to preventing his employees from exercising the right of collective bargaining is the best ally whom the left-wing Socialists or Communists have in this country. Such an employer is simply driving his employees and the unemployed to the ballot box, or to even more direct means of using political power, not merely to control, but to destroy, the economic power with which they are being repressed.

If the extremists of either the Right or the Left had written the American constitution in 1787 they would have given us institutions, not of self-government but of class government, which could hardly have endured. Today we face a similar problem and prospect in our efforts to write the constitution of self-government in industry. If we can write into that constitution a representative form of government, based on a free choice, a free functioning of the representatives of all interests, using the sanctions of political government merely to enforce the considered judgments of the majority, we may devise a method of industrial self-control which will last long after the present experiments in political control in other nations have disappeared.

Our desire to try our hand at solving this problem in our own way does not indicate an ignorance of what has happened elsewhere, or an arrogant assurance that we know more than any one else. It may mean only that we prefer to make our own mistakes instead of copying the mistakes of others. It may mean particularly that, since we did not lead the other nations into a world war, but only followed them, and then followed them into a world depression, our people have a certain natural inclination to try to find their own way out.

Surely the experiment upon which we are embarked is well worth making. Surely it is appropriate that America again should seek to find a new method of human coöperation, to deal with new phases of world-old problems. Without undue confidence that we shall succeed, we may feel that this is at least a high adventure, worthy of the best that we can give of patience and self-sacrifice and devotion to a common cause.

[399]

REMARKS BY THE CHAIRMAN (MR. OWEN D. YOUNG):

The first Code approved by the President was that of the Cotton Textile Industry. I am told that it was presented on the day that the National Recovery Act was signed. The preparedness of that great industry certainly could not be matched elsewhere unless it be in another industry which is now ready for a change in the law. It is fitting that the spirit and courage and breadth of view of the cotton textile industry be recognized by asking the President of its Institute to participate in this program, so I am going to ask Mr. George A. Sloan to speak next.

[400]

A NECESSARY FOUNDATION FOR STABILIZED EMPLOYMENT

GEORGE A. SLOAN

President of the Cotton-Textile Institute, New York

MR. CHAIRMAN, I am sure that I bespeak the sentiment of the members and guests present when I express to Mr. Swope and to Miss Warner our gratitude and admiration for the splendid program which they arranged for our fifty-third Annual Meeting.

Much has been said here today about the revolutionary changes that are taking place in working conditions. In considering the improvements that have come about, the average person is apt to think only in terms of shorter working hours and increased wages. He has suffered so much from the depression and has heard so many explanations of its causes that he is perfectly willing now to embrace the benefits of the NRA and to leave the rest to the code makers. I doubt very much if he is aware that many codes, like the Act itself, have their inception in a recognition of the age-old law of supply and demand—that they contain fundamental provisions which tend to preserve a balance of productive activity with consumption requirements and that these provisions, on account of their prevention of destructive industrial warfare, are the very foundation for the benefits that have come, and will continue to come, to the working man and woman.

There are three basic provisions in the Cotton Textile Code:

1. *Working hours.* The limitation of working hours to 40 hours a week was directed toward reemployment so that the industry might take care of the same force for which it provided employment prior to the depression. This objective has been more than accomplished. The number of workers has risen from 320,000 in March to 465,000 on September 1, which raises employment to substantially higher figures than pre-depression levels.

2. *Wages.* Minimum wage levels were established and pro-

[401]

vision was made so that in grades of employment receiving more than the minimum, the traditional difference in wage rates would be preserved and, further, that the shorter hours should not result in less pay in the shorter work week. These objectives have been accomplished. The established minimums have been observed but they have not become the maximums. The traditional differences in the higher occupational groups have been preserved and exceeded. The effect of increased wages, plus the necessary addition to working forces under the Code, have altogether led to an increase in cotton-mill payrolls of 74 per cent from May, when the Code was being formulated, to the end of August.

A recent survey indicated that the employment and payroll gains noted in late August were being maintained on October first.

3. *Limitation on Over-Capacity and Overproduction.* This chronically depressed industry went through the boom years of 1928 and 1929 without relief from its chronic disorders. Its enormous over-capacity, resulting from the abnormal demands of the Great War, the development of night work and other causes, necessarily prevented healthy, normal competition. Consequently the most vital provision of the Cotton Textile Code for effectuating the policy of the National Industrial Recovery Act by rehabilitating this industry, is the provision for the limitation of the operation of spindles and looms to 80 hours a week. This has the effect of reducing over-capacity to an approach to a reasonable balance between productive capacity and the demands for consumption. Without this fundamental provision the industry could not have undertaken the other steps and the heavy burden of increased costs which are involved in shorter hours and increased wages.

Important as are the provisions for working hours, important as are the provisions for wages, this last provision is the cornerstone of the Cotton Textile Code. It has gone far to remove the threat of overproduction. Stocks which reached the lowest point in several years during the middle of the summer have not increased materially. No improper burden has been placed upon the consumer. The industry is getting back the dollars which it puts into the production of the goods, and in the main, something for depreciation and in some branches something

[402]

for interest on investment, but, by and large, nothing beyond that. It has been able to secure the necessary working capital to meet the demands made upon it by other provisions of the code and by the Agricultural Adjustment Act in the estimated \$125,000,000 tax imposed upon the processing of its raw material.

In the cotton textile industry there are approximately 30,000,000 spindles in place. A demand for consumption of cotton goods such as that of 1929 could be satisfied by the operation of one-half this number if run six days a week without any limitation upon hours of operation. This over-capacity is somewhat mitigated by the fact that many of the mills are so located that there are no housing facilities to accommodate employees for continuous operation. But the over-capacity, making allowance for that situation, is enormous. This over-capacity resulted largely from conditions during the war which led to a great development of new facilities to meet abnormal demands and the fact that the industry during the same period, due to the same pressure, changed over very largely from one-shift to two-shift and, to some extent, to three-shift operations.

The devastating effects of over-capacity are interwoven with the causes and effects of the great depression through which we have been passing and the national emergency which it has produced. Efforts by provisions in codes of fair competition for the various industries to check these devastating results by dealing with the problem of over-capacity are just as closely interwoven with the national effort which is now being made for economic recovery.

A marked over-capacity in an industry is destructive of fair competition in that industry. Where the productive capacity of an industry is reasonably in balance with the demand for consumption, there exist conditions for normal and fair competition. Buyers are competing actively among themselves to obtain their requirements; sellers are competing actively among themselves to dispose of their products. It is essential to the protective functioning of the competitive system that there be both this active competition among buyers and active competition among sellers. The system breaks down when the reasonable balance of this duality of active competition is lost or destroyed. Such balance is destroyed when there is an

[403]

overhanging over-capacity. In that situation, there is an acute pressure on each unit in an industry to seek as large a share as possible of the inadequate demand. The overhead based on capacity runs on. There is not enough business to keep all busy and the pressure to reduce overhead by volume drives the seller into panic selling, whereas the buyer, knowing the over-capacity and ever-present threat of overproduction, holds off in the knowledge that his demands can be more than amply satisfied and on his own terms whenever he gets ready to buy.

The inevitable result of this situation is the scramble of sellers for orders in order to secure volume and a cutting of prices for that purpose without regard to costs. The result is reflected back on the wage earner. There is a steady pressure on the employees to accept lower wages in order to make it possible for the plant to keep operating. There is a tendency to eat up the working capital in continuing to do work below cost in the desperate effort of the concern to keep operating. In this situation some concerns go under. But the factory and machines are not destroyed—they merely afford a temptation for others to buy them in for a low figure and to increase the destructive competition by operating them at fixed charges that are far less than those which are properly attributable to the amount of capital involved.

During the past seven years I have observed the destructive operation of these inevitable results of over-capacity in the cotton textile industry, which incidentally is the largest manufacturing industry in our country from the standpoint of the number of employees. This factor has made it a chronically depressed industry which was generally unable to earn profits even in the boom period of 1928 and 1929. These conditions in our industry and in certain other chronically depressed industries, such as coal, resulting from over-capacity, have merely become general in the period of depression.

With the great shrinkage of consumer demand, with the great shrinkage in purchasing power, which set in in 1929, industries in which there was normally a fair balance between facilities for production and the demand made upon those facilities by consumers, lost that balance. For the time being, there came to be this overhanging over-capacity in almost every industry, with the accompanying destruction of the

normal protective functioning of the competitive system. Prices and wages could not have been forced down more ruthlessly by the monopolization of all buying power into a single hand to accomplish that purpose. What was the immediate necessity of each producer, namely, to cut his price, to increase his volume, to try to reduce his overhead by getting a larger share of the inadequate demand, was diametrically opposed to and destructive of the interest of the industry and the interest of the public. The whole country, except for a few favored industries dealing with necessities which had to be purchased, was caught in a vicious spiral of lowering prices, lowering wages and continued inroads into fixed and working capital. Credit, which is the most important part of our monetary structure, contracted and withered. Borrowers could not be expected to borrow when there was every prospect that the downward spiral would make it impossible to get a dollar back out of their operations. Lenders could not be expected to lend to concerns which were caught in the grip of this economic maelstrom. It was no help to the consumer to get something for nothing by buying below cost, when his employment and earnings were being destroyed by this very practice.

No individual concern, no matter how clearly it saw the devastating effects of what all were doing, could make any impression on the situation. The pressure of over-capacity on each unit to get as large a part of the inadequate demand as it could, in order to keep going at all, drove each along a course which obviously was collectively disastrous. Concerted action to check these destructive forces was the only way in which the situation could be met in this national emergency and this was the reason and justification for the National Industrial Recovery Act.

A great effort such as this by a nation to stem the tide of disaster necessarily means an adjustment in the lives and in the businesses of particular individuals in order that the rules laid down may be applied universally. In the cotton industry the limitation of machine hours meant the shortening of hours of operation for numerous mills, particularly the largest ones, whose two-shift or three-shift operation very materially exceeded the eighty-hour limitation. It also meant some shifting of employees from plants engaged in three-shift operations

to other plants, but the reduction in working hours so increased the opportunity for employment that the hardship to particular employees in making the shift was undoubtedly far less than if the industry and the country had continued on its downward course. Concerns which had been operating two long shifts or three shifts necessarily had to make an immediate adjustment of their operations, but against this they have the indirect benefits of the codes in increased purchasing power, increased demand and the release of the industry from the destructive effects of over-capacity.

Unlike some laws which are required in times of emergency, while this one brings some difficult readjustments to certain persons, it carries with it certain corresponding benefits to the same persons, as well as to all others.

Dealing with over-capacity in this way does not mean any lessening or limitation on actual production. The restraints must always permit, as they do under the Cotton Code, the fullest measure of production that consumption can be stimulated to absorb. But the public must realize, if the NRA is to succeed, that uncontrolled over-capacity, in times of depression, is Public Enemy Number One to capital, labor and the consumer alike.

[406]

DISCUSSION: CURRENT PROBLEMS OF UN- EMPLOYMENT AND RECOVERY MEASURES IN OPERATION¹

THE CHAIRMAN (MR. OWEN D. YOUNG): Now the meeting, under the rules, is open for discussion. I referred at the beginning to the fact that the Academy was like a football field. I don't want you to take that too literally. The meeting is open for discussion if anyone wishes to discuss or ask questions which the speakers may or may not be willing to answer.

MR. EDWARD A. FILENE (President and Chairman of the Finance Committee, Wm. Filene's Sons Co.; founder, Twentieth Century Fund): In order to give Sir William the reception he expects from us Americans, I want to challenge him to make good his thesis that high wages are dangerous. I will give him a thousand dollars for his institution, which is one of the best in the world, if he will show that there isn't a greater field for lowering costs by reducing the waste in any industry than by lowering wages; and he can pick his industries. I leave it to him with all his knowledge of industry and long experience of this sort of thing.

CHAIRMAN YOUNG: Here is a chance, Sir William. If you don't take it, some of us will.

SIR WILLIAM BEVERIDGE: I never said that high wages were dangerous. What I said was that it is possible for wages to be so high that they cause unemployment; that, I think, is quite undeniable so long as you have a wage contract at all, which is a contract for the sale of labor.

MR. FILENE: That thousand dollars is good if you prove that.

SIR WILLIAM BEVERIDGE: Well, I have no hope whatever of getting that thousand dollars from you in the time that is likely to be available.

MR. FILENE: You can have three months.

¹ This is an abstract of the discussion at the close of the morning session, following the addresses by Mr. Owen D. Young, Dr. Leo Wolman, Sir William Beveridge, Dr. Stanley King, Mr. Donald Richberg and Mr. George A. Sloan.

[407]

SIR WILLIAM BEVERIDGE: Oh, no, no. I will merely ask you to show what mysterious dispensation of Providence there is which makes the law of supply and demand not apply to labor. I would agree with you that there is probably no industry which cannot, given time, reduce costs and ultimately pay higher wages. Man's power over nature is progressing. It is going to progress and we are going to get richer and richer; but if you say to me, not only are we ultimately going to get richer, but we are always so rich already that we can always afford to put up wages without causing unemployment, then I say I simply and wholly disagree with you.

MR. FILENE: I am saying we can't afford not to put up wages because we are so poor.

SIR WILLIAM BEVERIDGE: Then I am afraid I can only disagree with you.

MR. FILENE: There ought not be a debate here, but I should like to get this point, because your statements will go all over our country and be quoted again and again, through many years, because you are a well known man, a man we listen to. We have a lot of people out of employment. The only way that we can get them back in employment is by buying the goods, the surpluses, as we call them, that they produce, so there will be demand for more production and more distribution. We keep ourselves at work by our purchases. If we haven't got wages high enough to buy as much as we produce, we put ourselves out of work; and that, in my shopkeeper's judgment, is the cause of the depression now.

SIR WILLIAM BEVERIDGE: Will you allow me to give you one alternative way of increasing the prosperity of wage earners and reducing unemployment which does not depend upon raising wages? It is the way which we happen to have adopted in England in this depression, of reducing the rate of interest. That doesn't sound as if it helped any workman, does it? Nevertheless in England it has made building, ordinary house building, far more possible than it ever was before. The building industry is booming. People who want to build, and not with government help, are borrowing money to build, and immediately they borrow that money, they pay it out in wages and it becomes real purchasing power, not sham purchasing power. That is the alternative.

CHAIRMAN YOUNG: Are you depositing that thousand dollars with the Chair, Mr. Filene?

[408]

MR. FILENE: I will deposit it with you.

CHAIRMAN YOUNG: Very good, sir.

MR. LOUIS C. MARBURG: May I ask Mr. Sloan a question in connection with the very interesting subject he raised regarding limitation of capacity? As I understand it, there is nothing in the Textile Code which would prevent modernization, installing more efficient machinery for old-fashioned machinery. I am wondering about the difficulty of substituting a modern machine for an old one. If the modern machine has twice or three times the capacity, must three old machines be put out of operation? Furthermore, as I understand it, there is no possibility of selling the old machines second-hand because probably nobody would get permission to operate them. Is that correct?

MR. GEORGE A. SLOAN: In my statement, I did not attempt to cover the matter of limitation on machinery but rather confined my remarks to limitation on machine jobs. As you know they are entirely different subjects. The former was covered recently in an amendment to our code. But as you have indicated the amendment does not provide a rigid control. Answering your last question, that would depend a great deal on the state of repair of the old machinery and the purpose for which it would be used. Permission would be granted promptly to operate second-hand machinery, as well as new machinery, if the particular installation was to be made for replacement or balancing purposes. Under the code it is permissible to add spindles to balance looms or vice versa. And indeed it would be possible under this provision even to build a new mill if the need existed.

MR. GEORGE SANDS: I should like to ask a question about high wages. Are not high wages a result of increased business, and isn't the idea of producing prosperity by paying high wages a new idea, and would it not take very long to work out?

CHAIRMAN YOUNG: I take it you are classifying Sir William Beveridge and Mr. Filene, one as an antiquarian and one as an ultramodernist.

MR. SANDS: Exactly so. It is not entirely clear to many minds. Can any light be thrown on it?

SIR WILLIAM BEVERIDGE: May I very briefly try to answer that? I personally am one of the people who live by trying to sell to the public the idea that economics is a science. If it is a science, some of the old ideas in it are still sound.

[409]

I don't want to say—I have never said—that high wages are a danger as such. I think that the American idea that the employer should aim at paying the highest possible wages he can is a very good idea and it is an improvement on the idea of many English employers. That doesn't alter my conviction that at the time of depression the pushing up of wages is more likely to slow down recovery than to hasten recovery, and for this reason, that in a depression what you haven't got is enough real purchasing power in circulation, and merely rewriting wage rates doesn't increase purchasing power. What does increase purchasing power is getting somebody to draw money from the banks or borrow money and use it in setting people to work. That can be done by encouraging the individual employer, as we have done in England, by lowering rates of interest; it can be done, as I am delighted to see that you are also doing in this country, by borrowing money by the government to start public works. I want to say that because I certainly don't criticize—I strongly support—that policy.

CHAIRMAN YOUNG: I just suggested to Mr. Richberg that he might like to say a word in moderation.

MR. DONALD R. RICHBERG: Whether I can serve as a moderator of this high wage discussion or not, I am inclined to try to agree with both parties here. It seems to me the whole question involved is one of relatives; high wages are high in the sense of the exchange value, we will say, for the products of other labor.

One of the great difficulties that it seems to me we have been striving to overcome is the utterly irrational disparities in wage scales. I don't think Sir William will disagree that this effort is a healthy policy because it makes for a broader and more healthy consuming market. As one who has had to do with wage scales from the standpoint of those who have tried to raise them from time to time, I would be the first to admit that it is entirely possible for the wage scales of a certain group to get so far out of line with other wage scales that, as a matter of fact, they destroy the markets for their own products. But, on the other hand, what we have started toward in this country particularly is an effort to prevent great fields of industry from operating on an absurdly low wage scale. Such a wage scale in fact permits of a large number of excess services which could be done away with—the wastes of which Mr. Filene speaks—and if you force the raising of those wage scales those who desire to sell the products to dispose of some of those wastes which are superimposed upon them.

[410]

MR. J. LEO HONIGMAN: I believe everybody is convinced that the original cause of unemployment came from the subsidence in the production of capital goods. The people present might be interested to hear a word from Mr. Richberg, taking advantage of his presence here today, and if it is not improper to direct the inquiry to him, as to what the chief impediments are to the distribution into circulation of a good part of the three-billion-dollar appropriation that has been put at the disposal of the public works administration.

MR. RICHBERG: Of course, I could shrug my shoulders and say that the Administration of Public Works and the National Recovery Administration are separate entities, but I should like to say one word in answer to your request. I think that the major cause in the lag of the public works program is unavoidable. It is simply the amount of time which it takes to bring about the operation of a public works program. I believe, if I remember correctly, in Washington the other night Sir William Beveridge was giving me some comfort as to similar efforts abroad; the inevitable lag is due to the fact that you can't put a public works program into operation overnight, in two weeks, or four weeks, or five weeks. It may take six months to get an adequate public works program going sufficiently so as to have its secondary effects upon the general welfare. In addition, under our form of government we have to face the difficulty of the separation of sovereignties, and the fact that although the Federal government is supplying the money for the public works, the greater part of the public works program was intended as a state program. Coöperation between the Federal government and states is required, but it is obstructed by other factors of delay, the greatest of which probably is politics. We expected too great speed of action in a public works program. I can't say that for myself, because the first time I had the opportunity to see the President after his inauguration, I did urge strongly the inauguration of a public works program on the very ground that it would take a comparatively long time to get into operation. The experience here has not been one of undue delay but of the ordinary delay which might have been expected. The hopeful thing in the situation is that the public works program is beginning at the present time to go into actual operation and not merely allocation.

[Limitations of space preclude publication of the continuation of this discussion. Mr. WILL ECKSTEIN, JR. questioned Mr. RICHBERG regarding the possibility of effective action against design piracy. By suggesting that the breakdown of distribution and of consumers' purchasing power, rather than any overproduction, was the real difficulty, Mr. JAMES H. CASE, JR. elicited from Sir WILLIAM BEVERIDGE a reaffirmation of his opinion concerning high wages.—ED.]

[411]

PART II

SCIENTIFIC PROGRESS, THE SHORTER WEEK AND UNEMPLOYMENT

THE RECOVERY PROGRAM IN OPERATION¹

WALTER C. TEAGLE

President, Standard Oil Company (New Jersey); former Chairman of the Industrial Advisory Board, National Recovery Administration

MEETINGS of this Academy are always noteworthy, yet I doubt if it has ever held sessions comparable to this gathering in possibilities of benefits to follow. This because we are passing through an unprecedented era of political and sociological experiment. We need more clear thinking and frank discussion. Those equipped by training or special opportunities to keep informed can render a great service to the rest by giving us the benefit of their views. Never has so large a portion of our people been seriously interested in public affairs. I am quite certain that there never was a time when they were so anxious for guidance.

Some of the reasons for the public's confusion might be set forth briefly here without prejudice to the speakers who are to follow.

The eighth month of a new Administration, elected by an overwhelming plurality on the platform of giving the people "a new deal" has just ended. No one can say that the promise has not been fulfilled. Momentous changes have tumbled over each other's heels. President Roosevelt was inaugurated in the very hour that our principal bulwark of business stability, confidence in the banks, was crumbling. For more than three years we had seen liquidation, reduced manufacturing and commercial activity, disappearing employment, and loss of faith — panic and its aftermath. The electorate

¹ Introductory remarks at the Second Session of the Annual Meeting.

decided that it was time to change the pilot and try a new course, even though it led us into uncharted seas.

So, in a period of a few months, we have thrown overboard theories of government, business and finance, which have been followed so long as to have achieved the dignity of fixed laws of conduct. Structural changes in the political economy of the United States are still being made, and it is too early to comprehend their full purport. With these intentional changes, taking place more or less according to plan, are others, some of them just as serious, which are consequences. They are by-products of the experiment, unforeseen and even less understood, and when their effect is felt still other changes must be made to counteract them.

Let us recall some of these new departures. We abandoned the gold standard, and made possession of more than \$100 in gold illegal. We paid farmers government millions to plow back their ripening crops. We made it both profitable and patriotic to destroy a percentage of our great Southern export staple—cotton. We killed hundreds of thousands of pigs that they might not fulfill their destiny and become hogs.

We have appropriated thirty-three hundred millions of dollars for public work, the need for which was not apparent but had to be created, and then set about persuading communities to ask for this money and discover ways of spending it. We passed a stringent law to control new security issues. We have legalized beer and voted repeal of the Prohibition Amendment. We set up agencies to protect home-owners from foreclosure under mortgages, and to coördinate the railways. No invention has been rejected if it promised to make for recovery. Granting immunity from the anti-trust laws, we have invited community of action by industries. The NRA has asked business to set up codes of fair practice and to agree as to how much to produce, how long to work and how much to pay employees.

And who can say as yet which of these measures is sound and which unsound? We were going to pieces waiting for events to shape themselves for our salvation; we have made some marked gains, notably in employment and business activity, since we began struggling against the forces that were pulling us under. So far, so good.

No one can foretell ultimate consequences of our venture into the socialization of business. We are on a new road, a one-way street by which we can never return. Fortunately we are not bound permanently to those things which time may demonstrate have been mistakes. We can modify policies, and undoubtedly shall as the need develops, but we can never go back to the positions we abandoned under the New Deal. Our economic Humpty-Dumpty of 1929 has been pushed off the wall, and all the king's horses and all the king's men can't put him together again.

Our struggle to reorganize production and distribution so that all men may earn a living in agriculture, in the professions, in railroading, in finance and industry, or in whichever of the countless activities the people engage, must succeed, and to succeed the recovery effort must command universal support. The new program is not a porous plaster which, laid on the afflicted spot, will drive out the depression aches. It is not enough for the physician to prescribe. The patient should not only take his medicine, but make a real effort to get well. If business is to run itself, as contemplated in the act, then business men must take the initiative in regulating their own affairs, to the end that interference by government may be restrained to the minimum.

Those who are becoming impatient with accomplishments to date must understand that the program is incomplete. General Johnson said at Chicago that the President had gone about twenty-five per cent of the way in bringing us up from the March fourth low. In the background of all our troubles is the need for a more equitable distribution of the rewards of industry. Our productive capacity over the past three decades has run ahead of consumption because purchasing power has not broadened sufficiently to take in all classes. Farmers and the lower-paid wage earners should have participated more liberally in the enjoyment of benefits from the release of manpower by the machine.

Revamping a nation's distribution to bring about such ideal results is a gigantic and slow-moving task in economic reorganization. In the process we must avoid half-thought-out departures from the established order, but we must not oppose change merely because it inconveniences us. I am convinced

[414]

that Washington does not want to run private business. It cannot favor measures that would destroy individual initiative and standardize all producers.

The President has the determination to drive ahead on lines that many critics told him were dangerous. He will have the courage to recede from positions that are untenable. He has sanctioned the inauguration of price-fixing in the petroleum industry unless, as I am confident will be the case, it is shown to be economically unsound and even dangerous in the public hearings which start next week. He himself recognized the hazards in price-fixing when he refused in clear and logical terms the demands of five Western governors for rationing and price-fixing for agricultural products. Of course, we cannot have price-fixing in one industry and artificially stimulated profits, without appeals from every other industry for like subsidies. It is apparent that President Roosevelt is feeling his way by trial and error to a more equitable distribution of the national income, and more power to him! It is the one ultimate insurance of human welfare and community prosperity.

While there have been some setbacks, there is not sufficient reason in anything that has transpired to date to make us discouraged at our inability ultimately to achieve success.

If I speak of the setbacks, it is only the better to emphasize the constructive accomplishments of the NRA program. Under the pressure for action there had to be mistakes. It could not have been otherwise. The wonder is that there have been so few, and those not more serious.

Remember that there was no Federal department already staffed and running smoothly to take on the tremendous task of administering the NRA. A complete organization had to be assembled, instructed and placed in positions practically overnight. While the NRA was still nothing but a law and an idea, the public expected an almost immediate end of troubles which had been accumulating for four years. Disappointment naturally followed.

Commanding the situation in NRA, working as I doubt if any leader ever worked before in time of peace, meeting new problems of magnitude each hour, combating opposition from the ablest advocates of every contrary proposal, was the man selected to direct the recovery program. I am glad of an

[415]

opportunity to pay tribute to the courage and energy of General Hugh S. Johnson.

Probably the two most general criticisms of the NRA are:

First—that it has brought about price advances that have outrun the gain in individual incomes, and

Second—That it has been conducted largely for the benefit of organized labor.

There seems to be ground for argument as to whether prices have outrun increased earnings, if we consider aggregate earnings rather than individual cases. If they have, I do not see how it could have been prevented. We could not provide a fund for new wages for more than three million men and women long out of work, without taking it largely from those already in jobs, or adding it to the prices of goods produced. If a business, without enjoying any increase in volume, adds more workers, it will either have to spread the cost of the additional labor over the old payroll, or add the wages of the newly employed to prices. No doubt prices have gone up too rapidly, and too far in some cases—a situation which will be corrected eventually by competition even under code requirements. As business recovers the lag in earning power behind living costs should disappear.

As to the second criticism, we must bear in mind that a well organized minority obtains more than an unorganized majority, and that all workers did not share in the success of industry in the good years. An important provision of this act gives labor a voice in questions concerning its own welfare. The much discussed paragraph 7-A specifically provides for collective bargaining. There exist only two important agencies for this. One is the trade unions, with something over 4,000,000 members already firmly established in many industries. The other is industrial representation, or self-government by employees who ballot for the election of their own representatives to meet with management. Something like 1,500,000 workers have been operating under this plan. It will be seen that the total of those in labor unions and those under representation plans is but a small part of the nation's workers, so that if the others should have occasion to indulge in collective bargaining they would have to create an organization or enroll under the already existing trade union of their craft. The

American Federation of Labor seized the opportunity for the organization of workers in hitherto non-union plants. No one could reasonably object to this.

It is regrettably true that a consequence of the misunderstanding of 7-A has been an epidemic of strikes. These resulted in most instances from over-eagerness to experience the benefits promised. In some instances, the enforced reduction in hours brought about loss in weekly pay. In others, hastily formed local unions made immediate demands to demonstrate their existence and their strength; when these were not immediately complied with, the local leaders precipitated strikes.

This situation led to the creation of the National Labor Board as a tribunal and board of mediation to facilitate adjustment of differences. In almost every case submitted there was not a real occasion for a strike because the troubles were of a character which a correct understanding of the 7-A section of the act could have ironed out. As an employer, I believe that management has been wrong as often as labor, in precipitating lockouts and strikes. A proper concern for the rights of the workers and the maintenance of some form of contact through which they could bring their problems to management would have been in most cases the means of keeping disagreements from reaching formidable proportions.

Labor troubles, discontent in the agricultural sections, protests of consumers over price increases and delays in completing codes are all symptoms of the difficulties of readjustment. They do not prove it a failure. We must meet these troubles and strive to correct them, without mistaking their correction for the larger objective of a better planned and balanced industrial system under which we can build for the future.

REMARKS BY THE CHAIRMAN (MR. WALTER C. TEAGLE) :

On several occasions we have been privileged to see our United States through the eyes of a friendly, if critical, British cousin. Mr. Harold Butler has paid us three visits before this one. He came first as Secretary General of the First International Labor Conference, back in 1919. Again in 1926 he was here to be amazed at our prosperity. His third journey was made in 1930 and the condition of the United States at that time was reflected by the title of his report, which was "Unemployment Problems in the United States."

Mr. Butler was Under-Secretary to the British Ministry of Labor during the War. From 1920 to 1932 he was Deputy Director of the International Labor Office, which, as most of you know, is the Labor Bureau of the League of Nations. Last year they dropped "Deputy" from his title and made him Director.

It is a piece of very good fortune that Mr. Butler could come here today to speak to us on the human and social effects of mechanization. Mr. Butler!

[418]

SOCIAL ASPECTS OF SCIENTIFIC PROGRESS

HAROLD B. BUTLER

Director of the International Labour Office

IT is characteristic of the strange times in which we live that at the meeting of the British Association last September, Sir Josiah Stamp, who is not only an eminent economist, but also a leading figure in the ranks of big business, should have chosen for the title of his address: "Must science ruin economic progress?" Imagine the shock that such a title would have given to his Victorian grandfathers!

In the nineteenth century both economists and business men devoutly believed that science was the source of all progress, and most of all of economic progress. They would have rubbed their eyes in blank bewilderment at the idea that science could possibly thwart the advance of material prosperity. Nothing in their experience had ever occurred to suggest such a possibility. They had seen the steady growth of wealth and well-being gradually extending, if in very unequal measure, to the whole population. They had seen the burden of grinding manual labor progressively relieved by mechanical invention. They had seen the means of transport and communication revolutionized by the application of steam and electricity.

All these and many other gifts had been bestowed by science upon humanity. What reason could there be to suppose that this beneficent process would not continue indefinitely? How could science check, let alone ruin, economic progress?

Even thirty years ago such a paradoxical idea would have appeared fantastic to most people. It was still believed, and on the whole believed rightly, that the constant change produced by scientific invention was a self-adjusting process. Though the hand-weaver might be displaced by the power-driven loom, he would soon find another job, probably as a weaver, or if not, in some other of the numerous occupations called into existence by the progress of material civilization. Though temporary unemployment no doubt existed, until the

[419]

last years of the nineteenth century it had not attained sufficient dimensions to become a recognized social problem. Broadly speaking, scientific progress moved evenly forward without producing any marked social dislocations or disturbances. Its benefits to society in the shape of expanding wealth and comfort were so obvious and so widespread that in the eyes of reasonable men science and economic progress were naturally regarded as indissolubly and eternally linked.

What has occurred, then, to induce discerning and well-informed people like Sir Josiah Stamp and many others, not merely to doubt that science and economic progress necessarily go together, but even to suggest that they may be mutually incompatible?

In seeking an answer, we may perhaps begin by taking a simple but significant fact. During the last three years there has been a decline in the average standard of living in most industrial countries. There are various indications which suggest this conclusion—the huge number who have been unemployed and reduced to a bare subsistence level, the fall, not only of nominal, but also in many cases of real wages of those still at work, and the drop in national incomes wherever they have been measured.

Until the present depression set in, the world as a whole and almost every individual country had become accustomed to expect a steady expansion of the national income and with it a more or less rapid improvement in living standards. This meant that labor conditions were being lightened, hours of work reduced, the opportunities for leisure increased and the means to enjoy it made available, as wages left a growing margin above the level of mere subsistence.

During the last three years there has been a serious decline in the national income of most countries. In Germany and the United States it has, according to recent calculations, been nearly cut in half. Great Britain and other countries have suffered very substantial losses. There is, in fact, no doubt that the general standard of living throughout the world is considerably lower than it was three years ago.

Why is this? How is it possible that this disastrous and unexpected regression should come about just at a time when science is making tremendous strides in every field, when

[420]

mechanical invention is cheapening and facilitating every kind of production, when the use of newly-discovered methods of cultivation, breeding and seeding has greatly enhanced productive power in every department of agriculture? Is it in spite of science that this disastrous check to economic progress has occurred? Or is it in some mysterious way *because* of science? That is the puzzle which we have to solve.

We may perhaps get some light on the problem if we begin by considering the effects of scientific discovery upon economic life. Its most far-reaching consequence has been to convert first industry and later agriculture from a placid stream to a rushing river, or if one wishes to use the correct jargon, from static to dynamic processes. If one harks back to the ages before scientific discovery began, one realizes that in the old days there was little fluctuation in economic affairs. Each community was largely self-sufficing. It grew nearly all its own food and manufactured nearly all its own products. The general level of comfort of the mass of the population varied little from century to century. A bad harvest might bring them temporarily near starvation, but no permanent improvement was likely to occur over any short period of time. A few additional luxuries might become available to the upper strata of society, but there was very little economic or social progress. In Egypt the peasant is using the same primitive implements and methods of irrigation that he used in the time of the Pharaohs, and his standard of living is probably about the same. The artisans are weaving and pressing cloth, hammering iron and copper, in precisely the same way as they did a thousand years ago. As a result, none of them enjoy plenty or leisure, though very few are acquainted with actual want and practically none with unemployment. Last year I visited an Egyptian town of 30,000 inhabitants without a single European or a single bank, but also without a single man out of work. The primitive standards and the primitive economic organization of the Middle Ages had resisted the depression, while in the cities the European factories were running short time and hundreds were unemployed.

The introduction of science has converted the slow even flow of economic life into a tearing torrent. In the industrial countries, standards of food, housing, leisure and intelligence

[421]

have changed beyond recognition in a few generations after remaining at a consistently low level for centuries. Only two hundred and fifty years ago, as Macaulay puts it, "farmers and shopkeepers breakfasted on loaves, the very sight of which would raise a riot in a modern workhouse", and "men died faster in the purest country air than in the most pestilential lanes of our towns". During the last eighty years since Macaulay wrote, we have, as he foresaw, gone further ahead to an extent which we hardly realize. Progress born of science has continued to drive forward with ever-increasing velocity, but contrary to the assumption on which we have been hitherto explaining the process, we are now painfully discovering that there is a speed limit. While it remains just as true as before that science is the source of economic and social advancement, it appears that the *rate* of transformation which it produces cannot be indefinitely accelerated. If the *tempo* of change becomes too rapid, economic progress may become self-arresting instead of self-adjusting; and the social benefits of increased productivity may be destroyed by counter-vailing social evils. Perhaps I may be allowed very briefly to suggest how this has happened.

It is obvious that with every change the economic structure becomes more complex. When new powers of production are put into use, whether they be derived from power-driven machinery or improved fertilizers or some other utilization of scientific method, an economic equation is destroyed and a new balance has to be struck between production and consumption. More of some kind of product can be produced than formerly, but this additional production is useless unless additional consumption is forthcoming to absorb it. As new wealth is created, it must be passed into circulation, if it is to be fruitful and reproductive.

At first, industrial development required readjustments within the community, but it soon overflowed national boundaries and gradually built up an infinitely complicated network of international exchanges. The maintenance and extension of this network was the condition of further progress. In other areas, which enabled living standards to be raised and consuming-power to keep pace with intensified production. Thanks

[422]

to quicker and more extensive methods of transportation by land and sea, it became possible to extend this process to the world at large. What we now call "world markets" were opened up; that is to say, the creation of wealth and its redistribution soon became a world-wide instead of a merely nation-wide process.

The system of international exchanges became more and more elaborate. It depended for its stability upon a delicately balanced system of international finance and the observance of certain rules for the proper regulation of the flow of credit and commerce. In fact, there is now no country which does not depend in a greater or lesser degree on the buying power of every other country, with the result that any serious dislocation of the machinery of wealth distribution and exchange produces not a national or a continental, but a world-wide disaster. It is from just such a dislocation that we are now all suffering. Until the system of international exchanges is restored at its old level, we shall not regain our old level of prosperity, but we shall inevitably drop back to lower standards of life.

It would, however, take me much too far to attempt any general analysis of the causes of the depression. I am mainly concerned with causes of disequilibrium in industry itself. Here it is plain that the increased facilities of production which science increasingly offers are a barren gift, unless the power of consumption grows in a corresponding measure. Through the application of innumerable inventions put at the service of the production by the engineer, the chemist, the physicist, the botanist and so on, we have reached the point when enormous quantities of the same articles can be rapidly and cheaply produced and at the same time an infinite variety of types and qualities of article. Each of these inventions necessitates some measure of readjustment if equilibrium is to be preserved. The spread of mass production requires a parallel spread of mass consumption to render it a paying proposition. What were luxuries produced only for the opulent few a generation or two ago, can now be manufactured by the million; but it cannot pay to do it unless the millions have the money with which to buy them.

When we talk about "overproduction", therefore, what we usually mean is that more is being produced than people can

[423]

buy, not more than they want. It is of course fantastic to talk about the "overproduction" of wheat and coffee, when there are millions previously accustomed to eat bread and drink coffee daily who are now unable to afford either. It is equally absurd to speak of the "overproduction" of boots and clothes, when there are millions who are unshod and half-clad.

The real truth is that consumption has failed to keep abreast of production. The redistribution of the new wealth created has not taken place smoothly and swiftly enough to maintain the balance. We have somehow failed to adapt the economic system sufficiently rapidly to be able to exploit successfully all the new facilities which science has placed in our hands. The result has been a breakdown. We are now trying to patch up the machine by various expedients. Let us very briefly look at some of these expedients.

In the first place, attempts are being made to restrict production by national or international agreements. We are trying to slow down the output of all kinds of necessary things. We are telling the farmer and the manufacturer that it is no use of their trying to produce all the things that people want, because they just can't buy them.

Such measures are probably necessary as emergency measures, but they are no final solution of the problem. Ultimately we have got to increase the purchasing power of those who want things, so that they can buy everything that the farmer and the manufacturer are equipped to produce. The new balance must ultimately be struck at a point of higher consumption and not of lower production, if economic and social progress are to be maintained.

It is in that direction that the thoughts of statesmen and economists are more and more consistently turning both in the United States and in Europe. They start from two fundamental facts, which demonstrate beyond question the state of that wealth is not circulating freely; the second fact is widespread unemployment. These two facts are, of course, not unconnected. They are different aspects of the same problem; but for the purpose of convenience we may consider them separately.

Although it is difficult to form any precise estimate of the

[424]

amount of money lying idle in a particular country at any given time, this is generally admitted as being one of the marked features of the present depression. Anyone in touch with the stock exchanges of the principal countries knows how widespread is the nervousness of investors and how reluctant they are to venture their money under present conditions. There is no doubt that in most countries with large capital resources there are considerable reserves of credit at present unused. The Preparatory Committee of Experts reported to the World Economic Conference that "available credit has not disappeared; on the contrary, there is an abundant supply but it is not being used".

As long as a large part of the wealth of a country is lying idle, it is obvious that business must remain slack and the level of unemployment high. In Europe during the last six months there have been distinct signs of recovery in most countries. More money has been moving. The exceptionally fine summer no doubt played a considerable part in tempting people to spend on holidays and travel cash that would otherwise have been hoarded. But investment is still at a low level. There is not enough confidence to induce people to risk their money in new enterprise, with the result that unemployment, though reduced, is still high and millions of men who would be buyers were they earning wages, remain idle and consequently a drag on the recovery of business. It is to meet this situation that here and in many European countries large programs of public works have been drawn up, usually financed by public borrowing.

In Italy, something like two billion lire (\$153,239,430) a year has been expended on public works during the last four years on electrical development, land reclamation and so on.

In Sweden the government has arranged to spend about 290 million kronor (\$67,394,360) during the present financial year, which it hopes will secure employment, directly or indirectly, for about 100,000 out of the 150,000 workers who are out of employment.

In Great Britain, loan expenditure on electrical and telephone development, road construction etc. has amounted to sums ranging from 100 to 150 million pounds (\$456,338,000—\$684,507,000) a year during recent years, and public authori-

[425]

ties are now being encouraged to raise loans for the purpose of slum clearance.

In Germany, an elaborate program providing for the expenditure of 1,200 million marks (\$414,084,500) has been approved this year, in addition to other schemes already under way. The program of public works includes schemes of agricultural colonization, allotments, repairs to public and private buildings, water, gas and electrical development, and so on. Similar schemes have been undertaken in many other countries, including Australia and Japan.

The object of these operations is to pump money back into circulation which would otherwise lie sterile and unproductive. As the attractions of private investment do not provide enough steam to work the pumping machinery, as they would in normal times, the state has to supply the power. This expedient for restoring balance is really being systematically tried for the first time. It has long been advocated by the International Labour Organisation and was strongly urged by its representatives at the World Economic Conference, where they found themselves in entire agreement with a resolution on the same lines put forward by the United States delegation.

The Conference decided to appoint a committee to study the whole question internationally, but in the meanwhile vigorous efforts are being made in the U.S.A. and in many European countries to institute large public works programs with the object of getting money back into circulation and incidentally restoring large numbers of idle men to useful work and effective purchasing power.

But this expedient, though fruitful, will not by itself redress the balance and solve the unemployment problem. The tremendous pace of scientific progress has set up more profound dislocations in the industrial structure, which will not be removed in any short space of time by purely financial measures. Even when the upward movement of prices and employment is once more in full swing, we shall certainly find that there are still further readjustments to be effected before we once more return to an even balance between producing and consuming power, between the desire for work at good wages and the need of industry for workers. When the depression has lifted, we shall inevitably find that the weight of technological un-

[426]

employment is still on our shoulders. In a country like Great Britain, where the rate of technical change has probably not been so rapid as in the United States or in Germany, the Prime Minister stated not long ago that when trade and industry recovered their normal momentum, there would in all likelihood still be two million persons, or about one-sixth of the wage-earning population, out of work on the average. There is no reason to expect a more favorable situation in other countries, allowing for variations in the intensity of their mechanization and industrialization. It was reckoned that in Germany at least 1,000,000 of those out of work last winter had been displaced by technical improvements introduced in the last few years.

It is unnecessary to cite the abundant evidence which now exists to show that in the last decade technological displacement has, on the whole, proceeded more rapidly than reabsorption into new or expanded industries. In other words, we have not succeeded in keeping pace with the changes which science has brought about. As Sir Josiah Stamp says: "Every scientific innovation alters the centre of gravity of collective demand". In the end human life can and will be richer, "but the pain and waste of the disturbance has to be debited to the gain before the net balance is progress". We are at present out of gear. Our economic and social development has lagged behind our technical achievement. Still further expedients are needed to reconcile human happiness with our mechanical progress. Unless that reconciliation takes place, not only will no new balance be struck, but political upheavals may still further derange the system which we have built up. In the long run, a society equipped with every conceivable comfort and convenience of civilized life cannot stand, if any large section of its citizens are still haunted with the fear that they may not be able to procure the elementary necessities of life. For that reason, the discovery of the new balance is not only an economic but also a human or social problem.

We may therefore look at some of the further expedients now in the way of adoption. It is evident on all hands that less human labor is progressively required to produce a greater volume of goods and services. This means that humanity is

[427]

not only able, but forced to enjoy longer periods of leisure. The question is whether that leisure is to be demoralizing or profitable, whether it is being rationally or irrationally distributed. There is plainly no need for men to be idle, while children are prematurely harnessed to toil and are deprived of their full education. In most civilized countries the age of employment has been gradually raised during the last hundred years to fourteen years. Under the Industrial Codes, the United States has taken a great step forward and fixed the age at sixteen. I believe that in time that example will be generally followed. It is only another step forward along the road we have been following since the dawn of the industrial era.

The length of industrial life is also being shortened at the other end. Most of the evidence available shows that when the elderly worker is displaced, his chances of fresh employment are increasingly precarious and that if he gets a job, it is usually on a lower level. Moreover, the age of efficiency is being lowered in proportion as the skill and speed required by the machine become more exacting. The man of fifty is now too old for many occupations, which were still within the compass of the man of sixty a generation ago. Hence the rapid extension of systems of old-age pensions.

This year we drew up an international convention on the subject at Geneva and we found that there were already fifteen countries that provided insurance against old age. Medical science is prolonging the average span of human life just at the time when mechanical science is curtailing the years of industrial efficiency. These twin consequences of scientific progress present a social and economic problem of undeniable difficulty and magnitude, but its solution is an indispensable element in that readjustment which we are now undertaking. We have to learn how to make the leisure won by the machine pleasant and profitable instead of painful and degrading.

Finally, it is becoming clear that the old daily and weekly limits of work are becoming out of date. As a British industrialist expressed it recently: "We are not yet in sight of a technocratic sixteen-hour working week, but there is never again going to be full-time for all". That fact is being slowly and more generally recognized. The question is whether all

are to work part of the time, or whether some are to work all the time, leaving the remainder in idleness.

It is not really a new problem, but again only a further step along an old road. In the last hundred years, hours of work have been progressively reduced from 12 to 14 hours a day to something round about 8. That progressive reduction has been one of the corollaries of scientific progress, which is now pushing us to the next stage. A year ago the International Labour Organisation took up the question of a shorter working week. We had a first discussion at our conference in June, and next summer we shall see whether the time is not ripe to establish a shorter working week by international agreement.

In the meanwhile, a bold lead has been given in this country. The logic of the present situation has been courageously faced, and a shorter week prescribed for every branch of American industry. There are great difficulties to be overcome, but I believe that they will be overcome, and I doubt whether the old working hours will ever be restored. To establish shorter hours internationally will be even more difficult, as there are wide differences between the conditions prevailing in different countries; but I believe that the change will come, perhaps gradually and piecemeal, but in the end inevitably.

Such, very summarily stated, are some of the expedients which are now being tried to remove the dislocations of the economic machine which the speed of scientific progress has produced. This process of readjustment is not a finite but an unending process. If we are to avail ourselves of the new powers and possibilities which science is constantly putting within our reach, we must become accustomed to thinking of our social and economic system not as something fixed and immutable, but as requiring indefinite elasticity in order that it may be progressively adapted to the changes which crowd upon us. To quote Sir Josiah Stamp once more: "We have no adequate technique of change. We treat life as mainly static with occasional and exceptional periods of change, whereas we must learn to look upon it as continuously changing with occasional and abnormal periods of rest—and we have to secure all the changes of social outlook implied by that reversal of view". The need for such a new outlook is perhaps the great lesson of this depression. In so far as we

acquire it, we shall succeed in carrying through the profound readaptation of our social and economic organization, which will alone enable us to harness the achievements of science to the service of human progress.

REMARKS BY THE CHAIRMAN (MR. WALTER C. TEAGLE):

Some fifteen months ago, as a result of my advancing my views too vigorously, a group of business men handed me a very difficult job. This was to popularize the idea that the way to relieve unemployment was for employees to go upon a shorter week. The idea was regarded as highly revolutionary and met with strong opposition from many employers; nevertheless, it made such headway as to create openings for about a million who had been out of work.

Within the last three months it has been gratifying to see many of the large employers who were adamant in refusing to go along with the short week idea, enthusiastically enrolled under the Blue Eagle and putting all of their workers on a forty-hour week or less. Obviously such a drastic change in working conditions has certain significant economic implications. What they are I do not believe many of us have determined. One gentleman, however, has followed this through and it is with anticipation of great enlightenment that I introduce Sumner H. Slichter, Professor of Business Economics at Harvard University, who will discuss this most important new phase of industry. Professor Slichter!

[430]

IMPLICATIONS OF THE SHORTER HOUR MOVEMENT

SUMNER H. SLICHTER

Professor of Business Economics, Harvard University

I

THE severity and duration of the present depression have made the problem of absorbing the unemployed more urgent than ever before. The principal purpose of the shorter working week is to accelerate the absorption of the unemployed. How effective is it likely to be in accomplishing this purpose?

During the last six months unemployment has been reduced by about 3,500,000. Rough estimates indicate that perhaps half of the gain in employment is attributable to the reduction in working hours. Consequently, the shorter working week has already made a major contribution to the reduction of unemployment. At the present, however, restrictions on hours, either by codes or the President's Reemployment Agreement, are in fairly universal effect. The prevailing limitation is 40 hours a week. It is safe to say, therefore, that the effect of a 40-hour week upon employment has been pretty completely exhausted. And yet probably 7,000,000 employable men are without jobs.¹ These 7,000,000 can be absorbed only by still

¹ Accurate information in regard to the volume of unemployment is not available. It is clear, however, that the absorption of the unemployed by the springing up of thousands of small business enterprises during the depression has been large. The growth of such enterprises is not reflected in the current indexes of employment. Furthermore, many thousands of persons are making a living by going into the taxicab business or trucking, or by opening small coal mines or returning to farming. The number of jobs created in these various ways may well exceed a million, but data for making an accurate estimate are not available. Much of the employment obtained in these ways may be regarded as emergency employment because the earnings are meagre and most of the persons engaged in it intend to shift back to other work as soon as business revives sufficiently.

[431]

further reductions in the working week or by a revival of business.

No one would challenge the possibility of absorbing large numbers of unemployed by reducing hours, provided the question of wages were not also involved. The National Recovery Act, however, is based on the principle that wage earners shall be compensated with higher wages for at least a part of the reduction in hours. And quite aside from the law, wages are inextricably linked with hours, for reductions in hours without some compensating wage advances would produce labor trouble. Indeed, the rapid spread of labor organization during recent months is partly attributable to the fact that for many thousands of wage earners the reduction of hours has meant another cut in earnings. Because of the close connection between wages and hours the question of how far jobs can be increased by reducing hours becomes a question of industry's ability to bear a further increase in operating costs.

The National Recovery Act, however, is based on the theory that higher wages do not interfere with the creation of employment. On the contrary, higher wages are said to increase the number of jobs by raising the demand for goods. This view is reflected in a speech by Senator Wagner, Chairman of the National Labor Board, before the recent convention of the American Federation of Labor in which he said that the large volume of unemployment requires that code hours must be reduced and code wages raised. It is also reflected in a recent interview of the Secretary of Labor in which she stated that unless independent forces accelerate recovery, hours would have to be further reduced and wages raised.

I wish that it were true that all one needs to do in order to increase employment is to raise wages. Most of our economic troubles could then be easily banished. But the Lord took only six days to make the world and He seems to have left it imperfect in many respects. At any rate, it appears to be true that in a given state of demand the quantity of goods which an enterprise can afford to make, and consequently, the amount of labor which it can afford to buy, diminish as labor becomes more expensive. In addition, the volume of spending by business enterprises depends in large measure upon the success of business men in discovering profitable ways of changing

[432]

methods or products. Subject to certain exceptions, it may be said that the higher the cost of making changes in methods or products, the greater difficulty business men have in discovering changes which can be profitably made. Perhaps it is a grave indictment of our economic institutions that the demand for goods drops and millions of men lose their jobs whenever business men discover fewer ways of making money. Nevertheless, this is the kind of economic system we have and in judging the possibility of increasing jobs by reducing hours and raising wages, we must face the fact that wage advances which do not reflect increases in the demand for goods are almost certain to diminish employment.

I say "almost certain" because under some conditions employment may not be diminished. The relation of wages to the demand for goods is more complicated than economists have been wont to assume and depends upon more variables than they have been accustomed to take into account. Consequently, I am not able to agree with those who are certain that the National Recovery Act, which sought to bring about business revival by increasing the cost of doing business, was a crazy attempt to raise ourselves by our own boot straps. To be sure, under ordinary conditions cost might well be regarded as madness. But conditions in the early spring of 1933 were most extraordinary. Confidence had sunk so low that enterprises were buying virtually nothing which was not immediately needed. As a result, the turnover of balances owned by business enterprises had become very low. Furthermore, more labor forces had been cut to a point where the demand for labor had become inelastic and where higher wage rates might not seriously diminish employment except possibly by putting firms out of business. Because of these very special conditions and because of them alone, there was a gambling chance that the total demand for goods might be raised by compelling business enterprises to pay higher wages. Under these circumstances higher wages might mean larger disbursements to labor which in turn would mean the diversion of money from the holders of idle bank balances into the hands of persons who would spend it promptly. But, of course, the experiment was bound to be a gamble because no one could

[433]

foresee its results. We decided, however, to take a chance and so we engaged in one of the most gigantic communistic operations in history. By government fiat, we decided to compel thousands of business enterprises to hand over a large part of their idle bank balances to wage earners. Paradoxically we engaged in this piece of communism for the purpose of saving capitalism.

As a matter of fact the theory of the Recovery Act has not been put to a test. Probably this is fortunate, because in attempting to halt the downward spiral of deflation by imposing higher costs on industry the government was playing a desperate game. At any rate, thanks to the threat of inflation and to world forces making for recovery, business began to revive before the codes saddled business with higher costs. Consequently, by the time that the President's Reemployment Agreement and the codes were imposed, most enterprises were doing a sufficient volume of business to enable them to meet the higher costs quite comfortably. This is shown by corporate income statements for the third quarter—a period when most enterprises were operating under either codes or the President's Reemployment Agreement. A compilation of the statements of 107 industrial companies for the third quarter shows that these companies made an aggregate profit of \$97,000,000 against \$78,000,000 in the preceding quarter and against a loss of \$11,000,000 in the third quarter of 1932.

One might infer from these figures that the recovery is proceeding rapidly enough so that industry will be able to bear the higher costs of still shorter hours and still higher wages. But the picture has another side. Although industrial production in the third quarter was fairly high, it was steadily going down. The Federal Reserve Board index of physical production undoubtedly has a bias which causes it to exaggerate the short-term fluctuations in output. Between July and September, however, the Reserve Board index dropped nearly 12 per cent. During the same period, the wage bill of factories increased over 15 per cent. Profits during the third quarter were increased by speculative bidding up of prices to levels which probably will not be maintained. In the immediate future many enterprises will be compelled to accept losses on inventories purchased at third-quarter prices. Finally, of the

[434]

107 companies tabulated, almost one-fourth lost money even during the third quarter. During the second quarter, which was almost as good as the last quarter of the present year is likely to be, over 40 per cent of the companies tabulated operated at a loss. Here is perhaps the most disturbing aspect of the present situation. The higher costs of doing business can not be confined to the enterprises which are making money. Consequently, even if higher wage rates increase the sales of enterprises which perform finishing operations on consumers goods, many other concerns feel the higher cost of doing business, but experience no gain in demand. The danger is that these firms will be so compelled to reduce their buying that the total demand for goods and the total volume of employment will drop.

This brief analysis indicates that for most lines of industry it would be folly to revise code hours downward and code wages upward until business improves. In other words, for the time being, the reemployment possibilities of the shorter work week are exhausted. Furthermore, if and when hours are further reduced and wages raised, the changes must be confined to the industries where the great majority of employers are making money. The analysis also seems to justify some conclusions concerning the National Recovery Act. As I said a moment ago, the theory of the Act has never been put to a test. It is plain, however, that as the Act is operating today, it is a relief act rather than a recovery act. It presupposes recovery rather than creates it. It has performed exceedingly valuable service in accelerating the absorption of the unemployed and in distributing the benefits of revival more promptly and widely among those who have suffered most from the depression. There is grave danger, however, that in our eagerness to help the unemployed we shall saddle industry with higher costs than it is able to bear. In that event, not only should we interrupt the recovery and add to unemployment but we should precipitate widespread price slashing and wage cutting, the very things that the Recovery Act is designed to prevent. Let us remember that no code authorities, however competent and efficient, can prevent an unrestrained struggle for survival with wholesale violation of the codes if the costs imposed on industry are too burdensome.

[435]

II

Although the shorter working week was intended primarily to accelerate the absorption of the unemployed, it is producing other results of considerable importance. One of them is to reduce the differentials in weekly hours (and also in rates of pay) which have existed between certain industries, especially between the North and the South and between the large cities and the small towns. Whether or not enterprises which have grown up in part as a result of large differentials can quickly adjust themselves to the new conditions of competition remains to be seen. In view of the haste with which many codes were inevitably made and the incomplete data upon which they were necessarily based, one must expect that some readjustment of differentials will be required in order to avoid driving too many plants out of business. The amount of relief that is needed will depend upon how rapidly business revives.

Another effect of the shorter working week has been to keep down weekly earnings. The advances in wage rates during recent months have been almost exactly offset by reductions in hours per week. As a result, the average weekly pay envelope of factory workers has scarcely changed since July and it is only about one dollar more than a year ago. This has important implications for the revival of business. It indicates that, for the immediate future, gains in demand will be confined largely to goods in the lower price brackets. Merchants call this resistance to higher prices a buyers' strike, but examination of weekly pay envelopes shows that it is only a matter of arithmetic. For the recovery to proceed on a sound foundation, profits must be obtained by selling an increasing volume of goods at low prices and at a small margin.¹ It was quite natural that the inflation policy of the administration in the early spring and summer should have misled business men into believing that they could market goods at considerably higher prices. Accordingly, they stocked up with inventories which

¹ This statement should perhaps be supplemented with the further observation that the rise in prices should occur by small increments. In other words, prices should at no time be permitted to get very far away from quotations which have already been tested in the market and which have proved able to move goods in volume. Large price changes are likely to provoke lack of confidence in the price structure and a consequent postponement of commitments by business enterprises.

in many instances will have to be sold at a loss. This accounts in part for the difficult period through which we are passing.

The dislocations produced by a depression as long and as severe as the present one are bound to produce a large number of men who for one reason or another are unemployable. The shorter working week will facilitate the absorption of the employables, but unfortunately the higher wage rates which accompany the shorter week will increase the number of the unemployables. In the past, the salvation of the men in the twilight zone between employable and unemployable has been the inefficiency of hiring practices. Careless hiring has permitted these men to support themselves by more or less intermittent work and thus has gone far to prevent them from becoming a social problem. Higher wage rates will compel enterprises to select their men more carefully than ever before. This will sharpen the dividing line between the employables and the unemployables and will push many men over into the latter class. A carefully planned social program to provide for the unemployables is urgently needed.

Depression stops the training of skilled specialists in many occupations with the result that revival may reveal a scarcity of some kinds of labor. This is particularly likely to happen after a long depression. The shorter working week will help produce labor shortages. Indeed, local compliance boards are already being compelled to exempt a few groups of specialists from the hour limitations in the codes. Active bidding for scarce types of skill will affect wages and by so doing it will influence the course of labor organization because it will make the scarce specialists conscious of their superior bargaining power and, consequently, more anxious to go it alone without the encumbrance of the less skilled workers. In a word, the shorter working week will accentuate craft consciousness and retard somewhat the drift toward organization along industrial lines which exists among factory workers.

III

Reduction in working hours is said to be needed in order to offset the effects of technological progress which, it is said, has been particularly rapid during the depression.¹ This sugges-

¹ As a matter of fact, there is no way of knowing whether or not this is

tion is often made in such a way as to imply that technological progress is in large degree futile and that unemployment can be avoided only by offsetting the gains in efficiency by reductions in hours. This amounts to saying that with industry organized as at present no increase in productive efficiency is possible except by reducing employment—an obvious untruth. Complaints concerning technological unemployment principally occur during periods of stationary or falling prices. Wages are a sluggish price and, consequently, become relatively high when the price level falls. Because labor becomes expensive, an unemployed surplus develops. This surplus is called technological unemployment. It might equally well be called "price-inflexibility unemployment," for it is the result of the impact of technological changes upon a more or less rigid price structure and is attributable to the rigidity of prices just as much as to the rapidity of technological change. Complaints about technological unemployment are little heard during periods of rising prices when wages lag behind the general price level and when labor is relatively well employed. Flexible reactions against technological unemployment. But the country appears to be headed toward institutional arrangements which will make prices more rigid rather than less so. If flexibility cannot be obtained in prices, it must be obtained somewhere else and this somewhere else may be in employment. Reducing the working week from time to time may perhaps be a useful device for converting into leisure the unemployment produced by the conjunction of technological changes and sluggish prices.

IV

But the displacement of labor which is likely to be most troublesome in the future is not displacement by technological changes. Rather it is displacement by the slowing down in the rate of industrial growth. In fact, *the effect of technological changes will probably be to reduce displacement rather than to increase it*, because technological changes will help sustain the demand for capital goods. Indeed, from the standpoint of true. The mere fact that hours worked have apparently declined more than factory output means little because dropping one-half or one-third of the force would itself raise the average efficiency tremendously.

[438]

maintaining employment, technological changes are likely to come too slowly rather than too rapidly in the immediate future.¹

Industry in the United States is organized and equipped for an extraordinarily rapid rate of growth. This is a natural result of the fact that we have been occupying a vacant continent and that the growth of population has been accelerated by a large flow of immigration. Now it appears that the economic development of the United States has reached a momentous turning point. Our natural resources are pretty well developed and the flow of immigration has ceased. Unless the growth of industry receives an unusually strong stimulus from technological discoveries, we may expect that industrial growth in the United States will be slower in the future than in the past. This means a difficult period of adjustment because the rate of growth cannot drop (except under very special conditions) without displacing labor in the capital-goods industries. But you ask: "Will not the drop in employment in the capital-goods industries be compensated by the rise in employment in the consumers-goods industries?" Eventually, yes, but unfortunately labor cannot shift quickly and immediately from capital-goods industries into consumers-goods industries, because the first effect of a drop in the demand for capital goods is a drop in the demand for consumers' goods. The reason is evident. When employees in the capital-goods industries lose their jobs and when the owners of plants in the capital-goods industries receive smaller dividends, they must reduce their purchases of consumers' goods. Incidentally this analysis sheds light on the problem of industrial overdevelop-

¹ This statement represents in some measure a change from the position which I took in my paper, "Technological Unemployment, Lines of Action, Adaptation and Control," before the American Economic Association in December, 1931. On that occasion, I stressed the dislocating effects of technological changes and expressed the view that automatic corrective forces cannot be depended upon to keep down the waste of technological changes. I see no reason for abandoning these views or reversing the opinion or expression "that we face the basic problem of developing economic institutions which will work reasonably well in a society which is highly dynamic." But the view that our society is likely to become even more dynamic in the future I have abandoned. In addition to the problems created by change, we are faced with additional and perhaps even more difficult problems created by the slowing down of the rate of change.

[439]

ment. Overdevelopment is a phenomenon which appears whenever the rate of change or the rate of growth slows down. Let business men experience greater difficulty in finding profitable ways of changing or expanding operations and instantly there is a shrinkage in the demand for goods that depends upon change or growth. This shrinkage in demand causes industry to appear to be overdeveloped in all departments. In other words, overdevelopment does not mean that industry has been changing too rapidly or growing too rapidly but rather that it is not changing or growing fast enough. There is danger that the code makers in Washington, through failure to understand this point, will make overdevelopment worse by permitting the codes to embody restrictions on change and growth.

Will a shorter working week help us make the adjustment to a slower rate of growth? Again we encounter the complicating issue of wages. If wage rates were not affected by changes in hours, one could assert with confidence that the shorter working week would help us absorb the men who will never again be needed in the capital-goods industries. In the long run it is probably true that labor will receive the same compensation in relation to its hourly output regardless of whether the working week is long or short. It happens, however, that the problem under discussion is not a long-run problem. Adjustment to a slower rate of growth must be made in the years immediately ahead of us. Furthermore, it is probable that labor possesses sufficient bargaining power to exact partial compensation in wage advances for every reduction in hours. This means that the effect of the shorter working week upon employment will depend upon the size of the compensating wage advance and the elasticity of the demand for labor. If the percentage reduction in the working week is greater than the percentage increase in wage rates times the coefficient of the elasticity of the demand for labor, at least part of the unemployed will be absorbed.¹ Otherwise they will not. Because the

¹ Thus if a 1 per cent increase in wage rates results in a 1.3 per cent decrease in the quantity of labor demanded, a decrease in the working week will produce a gain in employment provided the percentage decrease in working hours is greater than 1.3 times the percentage increase in wage rates.

demand for labor is at least moderately elastic, the percentage reduction in hours will have to be substantially greater than the percentage increase in wages to produce a substantial effect upon employment, unless it happens that technological changes raise the productivity of labor and hence the demand for it.

V

The foregoing analysis indicates that the shorter working week is likely to be of little assistance in helping us become adjusted to a slower rate of growth. Furthermore, if the higher wages made necessary by the shorter working week result in fewer hours worked, they will mean a reduction in the physical output of industry. Absorbing the unemployed by reducing the output of industry seems an unnecessarily costly procedure. Is there not a more effective and less costly way of making the adjustment to a slower rate of growth? The "new deal" is said to represent the inauguration of a policy of economic planning. Here is a problem for the planners. Cannot the introduction of the shorter working week be so managed as to increase simultaneously wages, employment, and the physical output of industry?

I believe that this is within the range of possibility, at least for many industries. In place of the 35 or 40-hour week of one shift, let us adopt the plan of operating plants with two six-hour shifts. This would mean a 36-hour week for the employees (almost as much as in the present plan of 40 hours) and 66 or 72 hours for the equipment.¹ Two-shift operation would permit both an increase in jobs and an advance in wages because it would enable labor to be concentrated upon operating the most up-to-date equipment where it would be most productive. For the same reason, two-shift operation would make possible an increase in the total output of industry and a rise in the standard of living. Quite aside from these general

¹ In order to preserve the Saturday half-holiday, it would probably be desirable to operate only one shift on Saturday. This would make a 66-hour week. By alternating the two shifts, each working in the morning one week and in the afternoon the next week, the division of work between the two could be kept equal. Eventually, a transfer to a 30-hour week for both shifts could be made. In view of the present low productivity of industry, however, a 66-hour week for machines would be desirable for a few years.

effects, two-shift operation would help offset the drop in the demand for capital goods and thus would facilitate the adjustment of industry to a slower rate of growth. In the first place, two-shift operation would lead to the retirement of the less efficient equipment and would cause the remainder to be worn out faster because it would be operating 72 hours a week instead of 40. This would increase the replacement demand for equipment, at least for a number of years. In the second place, the more intensive use of machines made possible by two shifts would make machine methods more economical in relation to hand methods. Machinery would be economical in many operations where it does not pay today. This would help sustain the demand for machines. Please do not infer, however, that I believe that two-shift operation of industry would be sufficient to keep the demand for capital goods in the future as large as it was during recent decades. So great was the impetus to growth given by a vacant continent and by the huge flow of immigration that only a rapid rise in the rate of replacement will prevent a decline in the demand for capital goods.

When the operation of two shifts is proposed, some people become alarmed over markets. Where will an outlet for the increased output be found? As a matter of fact the increase in output would not be spectacular because it would be limited by the reduction in the hours of labor. But the problem of the market would not differ from the case of the introduction of any other cost-saving method of operation. Expenditures saved in one direction become the demand for goods in other directions. This does not mean that there are no difficult short-run adjustments to make. It does mean, however, that the very reduction in cost at one point eventually makes possible a greater demand for goods at many other points.

Of course, if prices are not permitted to adjust themselves to the new level of costs, if throughout all branches of industry production is restricted in order to peg prices, then two-shift operation will be of little use in helping industry become adjusted to a slower rate of growth. It will be of use only if savings in cost are permitted to result in lower prices and a larger volume of output. This indicates the danger in the particular kind of industrial organization which is being

fostered under the codes. Innumerable special groups are being encouraged to organize for the purpose of promoting their own special interests. Each of these groups is intensely interested in keeping the price of its products high and the supply small. By various regulations, some perhaps rather indirect in their effects, many trade groups may be expected to place impediments in the way of the efficient and aggressive concerns which seek to enlarge their markets by translating lower costs into lower prices. And yet freedom to do precisely this is needed more than ever in order to offset the decline in the rate of industrial growth. It would be childish to imagine that a consumers' advisory board alone can protect the public against the kind of organizations which we are deliberately fostering in hundreds of industries. If the codes become permanent, as I hope they will, a carefully planned program will be needed to protect the community against organized restriction of output. Perhaps a tax might be imposed on idle productive capacity. Or unemployment funds might be created which would require each enterprise to pay for its own labor reserve and which would penalize it for laying off men. In any event let us remember that what some people regard as the problem of overproduction or overcapacity but what in the main is the problem of a drop in the rate of growth is only made worse by organized restriction of output.

REMARKS BY THE CHAIRMAN (MR. WALTER C. TEAGLE):

Is Mr. Hopkins in the audience? Apparently not. It seems that Mr. Hopkins has been unavoidably detained.¹

It is a source of much pleasure to me to welcome the next speaker. We have been associated together in Washington for the last four months as members of the Industrial Advisory Board, and in addition to that this gentleman occupies a high position in business and has accredited himself with great honor as President of the United States Chamber of Commerce. Mr. Henry I. Harriman!

¹ See below, p. 81. Ed.

DISCUSSION: RECOVERY MEASURES IN OPERATION

HENRY I. HARRIMAN

President, Chamber of Commerce of the United States

I WAS asked to open the discussion with a ten-minute talk with reference to the papers which you have heard.¹ Since I did not have an opportunity to read those papers in advance, it will be exceedingly difficult to discuss them with the care and the thoughtfulness that they deserve.

Dr. Butler showed you the very real problem that is raised by the remarkable acceleration in scientific advance and in mass production. Professor Slichter was a friendly critic of the NRA. Both of them have contributed much to the discussion of the problem.

Many years ago Wendell Phillips was asked to name his price for delivering a talk. He replied that if he discussed abolition his charge would be \$50; if he discussed any other problem it would be \$150, but in any event, the talk would be the same.

I think that applies in my case, for whatever might be the particular subject assigned me, my interest is so profound in the great industrial problems with which the NRA and the AAA are struggling, that I should inevitably turn toward them and a consideration of what they are doing for the country.

I realize that in giving you any statistics of what has happened, it is unfair to attribute those gains or losses to any particular legislative act. As Professor Slichter has pointed out to you, when the Industrial Recovery Act was passed and put into effect, there was an extraordinary shortage of goods which aided materially in the apparent success of the act; nevertheless, I think it may be of interest to point out a few figures of what has happened in the industrial world, whether they are due to natural causes, whether they have been accelerated, or whether they have been retarded by the legislative program that we have had.

We cannot deny the very serious situation which confronted us on the first of March. Steadily, for three and one-half years, almost without a break, national income and the activity of business had lessened. We had seen the national income fall from \$84,000,000,000 to about \$40,000,000,000. We had seen the number of the unem-

¹ The addresses by Mr. Walter C. Teagle, Dr. Harold B. Butler and Professor Sumner H. Slichter, which are printed above.

ployed rise from a normal of two or three millions to more than twelve millions. We had seen our whole banking structure shaken to its very roots.

Obviously, if such a condition were allowed to continue, we might have faced very real and very great disaster, and so, I think, one of the good features that we attribute to the President's program, whether it be entirely right or entirely wrong, or partially right or partially wrong, is the fact that it very materially changed our psychology and our way of thinking.

When we examine the figures we find in the farm situation a very substantial improvement. The index of farm prices rose from 49 at the end of last winter to 76 during the summer and dropped again in October to 70. Of course, the farmer is primarily interested not so much in the price that he gets as in what he can buy with the money that he receives from his crops and other farm products, and, based on his purchasing power, compared with the period that he likes to call parity—the period from 1910 to 1914—we find that in February his farm products would only purchase 50 per cent as much as they would in the parity period, and that by October they would purchase 60 per cent. There had been a substantial increase in the farmer's purchasing power.

If we turn to industry we find there the industrial activity curve, based on 1923-25 average as 100, rose from 60 in March to over 90 throughout the summer, dropping back at the present time to about 84. We find that retail sales, as reflected by department store figures, which are a fair index of what the people are actually buying, rose from about 60 to 70. Turning now to the stock market, we find that the corporate bond values rose in this period from below 65 in the spring to above 75 in October, and the value of stocks from 45 to 70. These figures show you that there has been a very substantial increase and improvement in our business situation.

Employment has been given to about four million men, according to the best indices that we have. Unfortunately there are no absolutely accurate figures dealing with unemployment, but from the best records that we could get, it looks to us as if the number of the unemployed had dropped from about 12,200,000 to somewhat under eight millions.

If we can continue those gains, if we can so wisely guide our economic life that we do not slip back, that we at least hold our own, and that we gradually go ahead, then I think it may well be said that the program which we have been following, whether it is directly responsible or not, has brought much good to the country. At any rate, in my opinion the time has not come to prophesy the collapse of the recovery measures which Congress has passed. Rather, it is

proper to consider them carefully from the standpoint of a friendly critic, to see what the reactions really are, and where we can point out mistakes.

The first mistake is a perfectly natural one. It was the error of labor in assuming that too much could be acquired quickly. We have had too many strikes and they have seriously disturbed the situation. Again I think that a mistake has been made in the determination of wage differentials based on districts, such as the North and the South, and in saying that those were the only differentials which should be recognized. There is a very real differential between the cost of living in the small town and in the big town, and this differential should have been more generally recognized in the codes.

The workman or the workwoman in the big city must pay at least a dollar a week in carfare. The workman cannot go home, as he can in the small town, to his lunch. The result is that he buys a lunch. That must cost him fifty cents a week more than if he went home.

We know that labor costs for building are greater in a great city than in a small city and consequently rents are higher, and I believe that it could be proved by statistics that the cost of living in a town of 10,000 population is at least two or three dollars a week less than in a larger city. Failure to recognize this is causing a vast deal of discontent in the small towns of the Middle West and, in fact, throughout the country.

I think there is a difference between the big industry and the small industry. Big industry has built up its reserves. Small industry frequently has no reserve with which temporarily to meet increased costs. This, also, was not recognized in the formulation of the codes.

As I have traveled around the country, I have met men in many lines of business sympathetic with the principles of the Recovery Act, yet stating that it is costing them the very life blood of their increases have come.

Mistakes are inevitable. I am not surprised that they have been made. I should be vastly surprised if they hadn't been made, and in pointing them out to you, I am doing so as the sincere friend of the Industrial Recovery Act and of the Farm Act.

I believe that the time has come when we should carefully consider and weigh these acts and see whether in our eagerness to push forward suddenly, we have not gone too fast and too far and have not increased our costs to a point beyond what industry can stand. This is not a criticism of the fundamental principles of the Act but merely

[446]

a suggestion that zeal may have pushed us too fast on the road toward even deferred recovery.

Just one more point before I close the discussion: A great deal has been said in the country about curtailing production. We have unmanageable surpluses in many lines, and I thoroughly believe that as a temporary expedient it has been wise to reduce production and as a temporary expedient it has been wise to reduce production and to balance production and consumption on the basis of what we are now consuming, but I would point out that the real road to recovery lies in putting these idle men and women to work in making more goods that we all want. That is extremely difficult to bring about.

Just to point out what it means: The Research Department of the Chamber of Commerce recently made a study of the increased labor and the increased demand for goods which could come if in some magic way we could raise the average family income (taking five as the number in the family) to a level of \$2,500 or \$3,000, that is, raise those families that are now receiving less than \$2,500 or \$3,000 to that level. We took as our basis a rather careful examination of what a family with an income of \$2,500 would actually buy. We found that if that increase of income could be made, there would be, among other consequences, an increase of 60 per cent in the amount of vegetables that would be consumed; an increase of about 50 per cent for fresh fruits and about 20 per cent for milk, 40 per cent for poultry and 16 per cent for eggs. When we came to the clothing line, we found the gains were very large. We found, if I remember the figures correctly, that we would have to increase the output of men's suits by about sixty million a year. When we came to examine the list for the ladies we found that the figures become absolutely astronomical.

When we considered what would happen to our homes, we found that the population of the United States had approximately one room per capita. That, to put it on the basis of a family with an income of \$2,500 or \$3,000, would mean that we would have to increase our rooms by over one hundred millions—not quite double the present space but easily double if you took out the slums and the poor places which are a disgrace to our civilization. When we came to ask what that meant in the line of labor, we found that for a ten-year period it would add to our output of lumber nearly thirty billion feet; it would add nearly twelve billion to the number of bricks that we would have to make each year; about one hundred and fifty million to the square feet of glass that our homes would require.

I might go on indefinitely telling you of the great market that lies before the country if we could simply raise our standard of living to the very modest standard of a family with an income of \$2,500 to \$3,000.

[447]

How this can be brought about is not simple. I do not know. I am not going to try to answer that problem, but I am going to point out that there is a great sphere of need which we haven't filled, that, without getting into the realm of luxury, simply remaining in the realm of decency and fair living, there is a task ahead which, in my judgment, would keep every man, woman, and child who wants employment at work for the next ten years.

REMARKS BY THE CHAIRMAN (MR. WALTER C. TEAGLE):

I know you will all be very glad to find that I was wrong when I stated that we probably weren't going to have the pleasure of hearing from Federal Director Hopkins. He has just arrived and will now address you on the subject of unemployment.

[448]

UNEMPLOYMENT RELIEF AND THE PUBLIC WORKS ADMINISTRATION

HARRY L. HOPKINS
Federal Administrator of Emergency Relief
Civil Works Administrator

MY friends, I had a perfectly good speech this afternoon which was knocked into a cocked hat by the President a couple of hours ago, so I am going to talk really about a new plan which has been announced, and after I tell you about it, you will know that I have no business being in New York this afternoon.

Before I tell you that, however, I want to go over briefly some of the things that we face. I have told a good many audiences that we had 4,500,000 families on relief last winter, about 21,000,000 people, and somebody very carefully kept it dark. Nobody could find out how many people were on relief in the United States; in fact, one person in six in this country was on relief. Those rolls have decreased from 4,500,000 families until today there are 3,000,000 families on relief and every month since March we have seen a decline in the number of families. In the month of September alone, a million people who had been on relief were taken off the relief rolls of the United States.

But even for three million families relief is no child's play. There are fourteen million people in those three million families who have got to be taken care of. You can't take care of three million families in this kind of economic situation, especially considering the kind of people they are, except by direct action methods, really giving them decent relief. Have they been getting decent relief? They have not. The average amount of relief per family in the United States has been about fifty cents a day per family. Well, that is a nice how-do-you-do to have fourteen million people (twenty-one million people last winter) living on fifty cents a day! It is ridiculous and it is absurd. It can't be tolerated. We don't intend to toler-

[449]

ate it. We are not going to give relief to people on any such basis as that.

This morning we sent out orders that thirty million dollars' worth of clothes had to be bought at once for these families in the next week. We are going to take food surpluses off the farms. We are going to spend \$150,000,000 or \$200,000,000 for these surpluses, get them right away and put them into the kitchens of the unemployed.

However, some of us are getting awfully sick of it, of these millions of people being on relief. Well, they are coming off. That is the essence of the President's new plan. Two million families are coming off relief a week from today, and they are going to be given real jobs; and two million more families are going to be given jobs within thirty days. Four million American men are going to be put to work within thirty days on real jobs.

How are we going to do it? Well, we are going to do it. We have two million men in the United States on work relief, in every town, city and county in the United States. These two million men get in work-relief wages an average of about \$20 a month—more in the great cities, less in the rural areas. They are working on every conceivable kind of public project, most of them good ones.

The Public Works Administration is going to give to me as the Civil Works Administrator—I was appointed to that office this morning by the President—\$50,000,000 a month for these two million families, and we, the Federal government, the states, the cities and the counties are going to continue to put in the \$65,000,000 a month that we are now spending for wages and materials. The additional \$50,000,000 is to be applied mainly in wages, so that in addition to the \$20 average that they are now getting, these two million families will now get an average of \$25 a month more. We propose at one stroke to take those fellows from work relief and put them on public work under a Civil Works Administration where they will have real jobs and be hired and fired like anybody else.

Second, we propose to organize in thirty days additional public works projects which will not be done under contract, but under what is known as force account in cities all over the United States, to put another additional two million men

[450]

to work. We propose to pay the prevailing rate of wage in local communities. We propose to do it on public projects where in the main the cost of materials will be about 20 to 30 per cent of the total cost of the project.

The Public Works Administration is prepared to give to us \$100,000,000 a month and we believe that we can get \$50,000,000 a month additional from counties, cities and states throughout the United States so that we will have \$150,000,000 a month to spend on public works projects.

It can be done; in fact, it is going to be done. This is a great day! It is a great day because it opens up to us the possibility of wiping out this relief business. No matter how well it is done, relief is a pauperizing, demoralizing affair that has no place in American life.

So, this morning, about half-past ten or eleven o'clock, the President created the Civil Works Administration of the United States. We are going to transform the machinery which was built up for relief purposes (much of which has been devoted to work relief) into a civil works administration. This afternoon all over the United States civil works administrations are being appointed and next Wednesday we are going to have a great meeting in Washington not only of these administrations but of all other people in America who can aid and help in this business of really getting people back to work.

That is the plan and that is what is going to be done. To be sure, we shall make some mistakes; but we are devoted to a cause, and our aim is to give these unemployed American men work on decent jobs, public service jobs. The President of the United States did it!

[451]

PART III

LONG-RANGE PLANNING

PLANNING AND ECONOMIC ORGANIZATION¹

GERARD SWOPE

Chairman, Executive Committee, Business Advisory and Planning Council
for the Department of Commerce; Member of the Industrial
Advisory Board, National Recovery Administration

MEMBERS of the Academy and Distinguished Guests: It is a great pleasure to welcome such a magnificent audience this evening, and to tell you also that the attendance at the meetings today has been remarkable in number and in quality. You might think that this great audience has been attracted possibly by our array of distinguished guests or even by the subject matter of the day's discussions and the evening's program, but that isn't so. You may think you have come here of your own free will, but you haven't. You have come here because of the great executive genius of your Director. I am not permitted to mention her name, but her name is on the program. What the Academy of Political Science would be without this directing genius, I don't know, but we who have come in contact with her, seen her great driving force, her ability, and her zealous devotion to the affairs of the Academy, all bow down before her with great respect and admiration.

I am going to inflict upon you one more and possibly the last of my talks for some time in regard to planning, and with reference especially to the situation of industry and commerce in this country today. The only thing I can say about it is that it won't be long and I therefore ask your indulgence and your patience.

¹Address delivered by Mr. Swope as presiding officer at the Annual Dinner Meeting of the Academy of Political Science.

[452]

The present depression is different from all its predecessors that I know anything about, not in being more widespread or having gone further or lasted longer, but in that it has aroused a greater determination not only in the more serious-minded groups, but also among people generally, to find a way if not of avoiding depressions altogether at all events of making them less severe and of ameliorating the conditions of those upon whom they fall most heavily.

The National Industrial Recovery Act was conceived and enacted to put an end as soon as possible to the present depression. I hope our work and thinking will not end until we find a program that we are willing to inaugurate for the future. The desire to prevent such a catastrophe in the future is the basis of all the talk that one hears and all that one reads in regard to long-range planning. If one has had even a small amount of experience as an executive in business or industry, he will appreciate that this is more easily said than done, and especially when our problem is so far-flung, our needs so many and our agricultural, commercial and industrial structure so complicated—made up of thousands of units largely dominated by the individualistic philosophy of our democracy, to which we owe so much of the progress we have made. While recognizing the tremendous difficulty of the problem and the need therefore to exercise the greatest care, I still think an effort to find a solution should be made. We should seek to have the best thinking brought to bear on this problem and draw wisely not only on our experience but on that of others. Simply to decide that these cyclical variations, with all their attendant miseries, are inevitable and that we gain nothing from experience is, as Senator LaFollette has said, "the counsel of despair".

Over two years ago, in October 1931, I was requested to appear before the Committee on Manufactures of the United States Senate, which was considering a bill for the establishment of a National Economic Council. I stated then:

I am in entire sympathy with having a National Economic Council, but I need hardly call to the attention of the Committee that this would be creating a new organization in the Government, when already there are several dealing with the subject-matter of the bill in the various departments. The bill is intended to cover "industrial, financial, agri-

[453]

cultural, transportation and labor interests of the United States." Industrial and commercial interests are now covered by the Department of Commerce and the Federal Trade Commission, which have built up large staffs, including able and trained economists; financial, by the Federal Reserve Board; agriculture, by the Department of Agriculture, which has built up an extensive data gathering bureau; transportation, by the Interstate Commerce Commission, and the public utilities are now under the regulation of Public Service Commissions in the various States; and labor, by the Department of Labor. The bill would give to this Council a very large problem, to coordinate the work of all the various departments above enumerated, so large that I question whether there would be any practical results.

Furthermore, it seems to me that this would be working from the top down, that even if you could get the ablest men, and the scope of the work was not too broad, you would be providing a superstructure resting upon the present chaotic conditions. It therefore would have no stable foundation. It undoubtedly would give much interesting academic information, but it seems to me would lead to no practical results, except, possibly, over a long period of time.

I should think it would be much better to start from the bottom and build up; that is, each industry should study the elements that enter into such an industry, to give the best service to the public, fair treatment to its employees and a reasonable return to its stockholders.

Trade Associations in America are the natural organizations to study the economic elements of each particular industry. Each Trade Association should hold itself responsible for the coordination of production and consumption to stabilize its industry, with the consequent benefits to the employees and to society. The organization and furtherance of the work of Trade Associations should be encouraged.

The Trade Associations, working out their problems in the stabilization of industry, would then be the foundation stones upon which to erect the superstructure of the National Economic Council. This might then be created by bringing together the officers, or duly elected representatives, of these various Trade Associations, to select from their number, or from the outside, a National Economic Council, to study the needs of industry as a whole. Such a Council would consist of men who have come up through the various industries, know those industries and their needs, who would work with others to find a solution to their common problems, and be able to deal with them not only more intelligently but in a more practical and expeditious manner, so that definite, concrete and constructive results might be expected.

In June 1933 the National Industrial Recovery Act was signed. It has often been stated that industry was responsible for the fearful situation in which we find ourselves and might have done much better even before the passage of the Act. It should be recognized that industry was limited by at least

[454]

two restrictions, now modified by the NRA—namely, the variations in the factory acts in the different states and the anti-trust laws. When the President signed the NRA, he issued a statement containing the following: "It is a challenge to industry which has long insisted that given the right to act in unison, it could do much for the general good, which has hitherto been unlawful. From today, it has that right."

Under the provisions of the National Industrial Recovery Act, commerce and industry are organizing into compact units and drawing up codes of fair competition, under which data will be collected which with intelligent study should lead to a better coordination of production and consumption. My point is that it is here, in each of these trade groups, that this study should start, not at the top of our fearfully large and complicated structure but at its base. Then mobilize these trade and industrial groups into the larger unit which I outlined last week in the proposed organization of a National Chamber of Commerce and Industry. When such a program, or some other, is accepted, to make permanent many of the essentials of the NRA, enabling coöperative work on the part of competing units in commerce and industry, a first but a very important step will have been taken.

But our vast social structure is not served only by industry—it requires labor in two principal directions. In addition to industry or manufacturing for clothing and shelter, perhaps its most fundamental need is agriculture for food and certain raw materials; then commerce and transportation for distribution, and finance to assist all of these activities. A beginning has been made in their reorganization, and assuming that these efforts will be fruitful of practical and beneficial results, it may now be the time to consider the creation of a National Economic Council for long-range planning, and the following is offered as such an outline, recognizing that the number of representatives of each interest may be subject to change. Of course, the entire program is subject to change and is simply put out for the purpose of stimulating thinking and discussion.

The National Chamber of Commerce and Industry, referred to above, shall elect four members to a National Economic Council. In addition, the Secretary of Commerce of the United States may be a member, or appoint one member to the Council.

[455]

Workers engaged in commerce and industry, covered by the above, shall elect, through their national organizations, four members to the National Economic Council. In addition, the Secretary of Labor of the United States may be a member, or appoint one member.

The national agricultural organizations shall elect four members to the Council. In addition, the Secretary of Agriculture may be a member, or appoint one member.

The transportation interests, including railroad, marine and air, shall elect four members to the Council. Workers engaged in rail, marine and air transportation shall elect, through their national organizations, four members to the Council. In addition, the Federal Coördinator of Transportation may be a member, or the Interstate Commerce Commission appoint one member to the Council.

The Federal Reserve Banks shall elect four members to the Council. In addition, the Secretary of the Treasury of the United States, or the Governor of the Federal Reserve Board, may be a member, or the Secretary of the Treasury may appoint one member to the Council.

The President of the United States shall appoint five members to the Council, representing the public at large.

The National Economic Council so constituted of thirty-four members—five government officers; five representing the public, appointed by the President; eight representing labor; and four each from commerce and industry, agriculture, transportation and finance—shall elect its officers. The Council may appoint an economic board of such number as it deems best, either from among its own membership or from outside.

The members of the National Economic Council shall serve without compensation, but their expenses will be borne by the Association which elects them.

A secretarial staff and offices shall be provided in Washington by the National Chamber of Commerce and Industry. The expense of such secretarial staff and offices shall be met by a prorata assessment on the National Chamber of Commerce and Industry, on the banks of the Federal Reserve System and on the agricultural and transportation interests.

Data collected, tabulated and analyzed by these various bodies, namely, commerce and industry, agriculture, labor,

[456]

transportation and finance, shall be made available to the National Economic Council, with any recommendations these bodies care to make. The National Economic Council may also initiate and ask for any other data and information from these units. The National Economic Council will also study the various data-collecting bureaus of the government, in the effort to unify and simplify this work, and make its recommendations to the President.

It shall be the province of the National Economic Council to study economic changes, advise the President and the Congress in regard to economic trends and make recommendations.

The various units of the Council will direct their work and studies so that the violent upheavals that we have experienced in the past, which have led to so much unemployment and misery, shall be diminished, and also study ways of alleviating the hardships attendant on such cyclical changes as, after the best of human study and experience, will still remain. Other studies tending to provide security and regularity of employment and peace of mind of the workers, shall be undertaken by the Council.

Even if these steps fall short of realizing the high ideal we have set, such correlation, coördination and conscious study should lead us to other steps and nearer to the goal we seek.

[457]

REMARKS BY THE CHAIRMAN (MR. GERARD SWOPE):

I am sorry that I can't introduce the first speaker on the program. When your Director suggested the subject of this evening's meeting of the Academy, "Long-Range Planning," I knew the natural person to introduce the subject, of course, would be General Hugh S. Johnson, the Administrator of the National Industrial Recovery Act, who has also given much thought to long-range planning.

When I asked him to speak, he accepted readily, as he esteemed it a great honor and especially fitting to address this distinguished academic body. But much to our regret, his duty as a soldier, which he always is, has called him West to allay the misunderstandings there. To show the speed of his movements, yesterday evening he spoke in Minneapolis, this noon in Des Moines, and tonight he speaks in Omaha. I have a telegram from him from Des Moines reading: "Had so many speeches to write couldn't finish paper until last minute for air mail and then snow storm blocked mail service. Please express my sincere regret but could not possibly have done otherwise."

I am sorry that he could not be with us this evening. I have the greatest admiration for General Johnson's ability, dynamic and irresistible energy, his unsparing and whole-hearted devotion to the NRA, day and night, in the sick room or in his office, and I am very sorry, indeed, that I cannot present him to you.

Our first speaker in the flesh hails from the sunny South, South Carolina, where he was born, educated, and has practiced law, and, curiously enough in these shifting times, has retained his home there, moving only occasionally to Washington and back to South Carolina.

His interests are broad, educational, legal, political, domestic and international commercial problems. It was he who suggested an original method of getting statistics in cotton. He is experienced and wise, and it is fitting that he should be one of the President's trusted advisers.

He is Chairman of the Cabinet Committee of the National Recovery Act, is interested in long-range planning, especially in the philosophic concept underlying that which may remain as permanent under the Act.

The Secretary of Commerce, the Honorable Daniel C. Roper!
[458]

LONG-RANGE PLANNING

THE HON. DANIEL C. ROPER
U. S. Secretary of Commerce

IT is a real pleasure for me to be with you tonight and to join this splendid assembly of men and women in a study of national economic and social recovery measures. The Academy of Political Science, with more than a half-century of experience, spanning several periods of economic disturbances in our national life, can supply knowledge valuable for the wise charting of our country's future.

Reference to the program of this annual meeting for 1933 shows that your earlier discussions of today have related to the emergency problems of unemployment and industrial readjustment for the primary purpose of safeguarding against immediate social disturbances. This is as it should be, but the study of emergency problems should also endeavor to determine the causes responsible for the 1929 cataclysm, thus providing a basis for efforts in planning to prevent the repetition of economic disasters in the future. The tragic imprint of this depression on the minds and hearts of our people should be an eloquent and lasting appeal to all of us to discover and put in motion such policies as will in the well-thought-out opinion of this generation safeguard the next against our experiences of the past four years.

Much consideration is being given to comparative statistics that show the staggering total of depression unemployment, the precipitous drop in commodity prices, the tragic losses in domestic and foreign trade, the drastic declines in national income and purchasing power. These are important comparisons, forcefully illustrating the severity of this depression. Such statistics, however, serve as measurements only of what has already happened. The real task for sound economic thinking is to interpret intelligently these figures, along with other historical data, and to ascertain what forces and factors have been working within our economic system to bring about the greatly increased disruptions and dislocations of our day.

[459]

REMARKS BY THE CHAIRMAN (MR. GERARD SWOPE):

I am sorry that I can't introduce the first speaker on the program. When your Director suggested the subject of this evening's meeting of the Academy, "Long-Range Planning," I knew the natural person to introduce the subject, of course, would be General Hugh S. Johnson, the Administrator of the National Industrial Recovery Act, who has also given much thought to long-range planning.

When I asked him to speak, he accepted readily, as he esteemed it a great honor and especially fitting to address this distinguished academic body. But much to our regret, his duty as a soldier, which he always is, has called him West to allay the misunderstandings there. To show the speed of his movements, yesterday evening he spoke in Minneapolis, this noon in Des Moines, and tonight he speaks in Omaha. I have a telegram from him from Des Moines reading: "Had so many speeches to write couldn't finish paper until last minute for air mail and then snow storm blocked mail service. Please express my sincere regret but could not possibly have done otherwise."

I am sorry that he could not be with us this evening. I have the greatest admiration for General Johnson's ability, dynamic and irresistible energy, his unsparing and whole-hearted devotion to the NRA, day and night, in the sick room or in his office, and I am very sorry, indeed, that I cannot present him to you.

Our first speaker in the flesh hails from the sunny South, South Carolina, where he was born, educated, and has practiced law, and, curiously enough in these shifting times, has retained his home there, moving only occasionally to Washington and back to South Carolina.

His interests are broad, educational, legal, political, domestic and international commercial problems. It was he who suggested an original method of getting statistics in cotton. He is experienced and wise, and it is fitting that he should be one of the President's trusted advisers.

He is Chairman of the Cabinet Committee of the National Recovery Act, is interested in long-range planning, especially in the philosophic concept underlying that which may remain as permanent under the Act.

The Secretary of Commerce, the Honorable Daniel C. Roper!

[458]

LONG-RANGE PLANNING

THE HON. DANIEL C. ROPER
U. S. Secretary of Commerce

IT is a real pleasure for me to be with you tonight and to join this splendid assembly of men and women in a study of national economic and social recovery measures.

The Academy of Political Science, with more than a half-century of experience, spanning several periods of economic disturbances in our national life, can supply knowledge valuable for the wise charting of our country's future.

Reference to the program of this annual meeting for 1933 shows that your earlier discussions of today have related to the emergency problems of unemployment and industrial readjustment for the primary purpose of safeguarding against immediate social disturbances. This is as it should be, but the study of emergency problems should also endeavor to determine the causes responsible for the 1929 cataclysm, thus providing a basis for efforts in planning to prevent the repetition of economic disasters in the future. The tragic imprint of this depression on the minds and hearts of our people should be an eloquent and lasting appeal to all of us to discover and put in motion such policies as will in the well-thought-out opinion of this generation safeguard the next against our experiences of the past four years.

Much consideration is being given to comparative statistics that show the staggering total of depression unemployment, the precipitous drop in commodity prices, the tragic losses in domestic and foreign trade, the drastic declines in national income and purchasing power. These are important comparisons, forcefully illustrating the severity of this depression. Such statistics, however, serve as measurements only of what has already happened. The real task for sound economic thinking is to interpret intelligently these figures, along with other historical data, and to ascertain what forces and factors have been working within our economic system to bring about the greatly increased disruptions and dislocations of our day.

[459]

REMARKS BY THE CHAIRMAN (MR. GERARD SWOPE):

I am sorry that I can't introduce the first speaker on the program. When your Director suggested the subject of this evening's meeting of the Academy, "Long-Range Planning," I knew the natural person to introduce the subject, of course, would be General Hugh S. Johnson, the Administrator of the National Industrial Recovery Act, who has also given much thought to long-range planning.

When I asked him to speak, he accepted readily, as he esteemed it a great honor and especially fitting to address this distinguished academic body. But much to our regret, his duty as a soldier, which he always is, has called him West to allay the misunderstandings there. To show the speed of his movements, yesterday evening he spoke in Minneapolis, this noon in Des Moines, and tonight he speaks in Omaha. I have a telegram from him from Des Moines reading: "Had so many speeches to write couldn't finish paper until last minute for air mail and then snow storm blocked mail service. Please express my sincere regret but could not possibly have done otherwise."

I am sorry that he could not be with us this evening. I have the greatest admiration for General Johnson's ability, dynamic and irresistible energy, his unsparing and whole-hearted devotion to the NRA, day and night, in the sick room or in his office, and I am very sorry, indeed, that I cannot present him to you.

Our first speaker in the flesh hails from the sunny South, South Carolina, where he was born, educated, and has practiced law, and, curiously enough in these shifting times, has retained his home there, moving only occasionally to Washington and back to South Carolina.

His interests are broad, educational, legal, political, domestic and international commercial problems. It was he who suggested an original method of getting statistics in cotton. He is experienced and wise, and it is fitting that he should be one of the President's trusted advisers.

He is Chairman of the Cabinet Committee of the National Recovery Act, is interested in long-range planning, especially in the philosophic concept underlying that which may remain as permanent under the Act.

The Secretary of Commerce, the Honorable Daniel C. Roper!

[458]

LONG-RANGE PLANNING

THE HON. DANIEL C. ROPER
U. S. Secretary of Commerce

IT is a real pleasure for me to be with you tonight and to join this splendid assembly of men and women in a study of national economic and social recovery measures. The Academy of Political Science, with more than a half-century of experience, spanning several periods of economic disturbances in our national life, can supply knowledge valuable for the wise charting of our country's future.

Reference to the program of this annual meeting for 1933 shows that your earlier discussions of today have related to the emergency problems of unemployment and industrial readjustment for the primary purpose of safeguarding against immediate social disturbances. This is as it should be, but the study of emergency problems should also endeavor to determine the causes responsible for the 1929 cataclysm, thus providing a basis for efforts in planning to prevent the repetition of economic disasters in the future. The tragic imprint of this depression on the minds and hearts of our people should be an eloquent and lasting appeal to all of us to discover and put in motion such policies as will in the well-thought-out opinion of this generation safeguard the next against our experiences of the past four years.

Much consideration is being given to comparative statistics that show the staggering total of depression unemployment, the precipitous drop in commodity prices, the tragic losses in domestic and foreign trade, the drastic declines in national income and purchasing power. These are important comparisons, forcefully illustrating the severity of this depression. Such statistics, however, serve as measurements only of what has already happened. The real task for sound economic thinking is to interpret intelligently these figures, along with other historical data, and to ascertain what forces and factors have been working within our economic system to bring about the greatly increased disruptions and dislocations of our day.

[459]

When we study the "forces behind the figures" we find that the *economics of balance* can no longer be depended upon to restore economic equilibrium. Recovery periods following previous depressions have been largely self-regenerative. In those eras it was only a matter of awaiting the completion of what were accepted generally as business cycles. Nations managed their affairs on the theory that natural economic forces in themselves eventually bring about harmony and balance. Heretofore, the laws of supply and demand have been depended upon to regulate conditions. It was contended that an efficient producer would succeed and that an inefficient producer would fail, thus keeping the productive power of the country in general line with the consumption needs. However, beginning with the World War, and continuing until the collapse of 1929, excessive industrial expansion, especially in productive capacity, stimulated by the demands of a warring world, created the necessity of an "Economics of Organization" to replace the old "Economics of Balance."

Now, in this new era when our thoughts are so much engaged in charting the future, it is necessary to be careful in the use of descriptive terms. Much is being said about self-government of industry. We all need to understand what is implied by this term. No one will contend that it means that all regulatory control by the Federal government should be removed and that business proceed without any coöperation from the government. There is no important unit of business that would desire this extreme. It would be approved only by such as the bootlegger, or those minorities in business that pursue a cut-throat policy by using unfair methods to reduce their costs and thereby are enabled to undersell legitimately conducted business. Self-government in business does mean that business will be permitted to do those things which business can do as well or better for itself than the government can do for it. If a greater measure of government regulation than this is necessary for the public safety and welfare, and in order to prevent another world economic calamity, such governmental regulations will be sought by the representatives of good business.

Neither must we forget the significant position of the ultimate consumer in the solution of our major problems. It is

[460]

evident to all that the national recovery program cannot be enforced successfully without the support of public opinion, which is crystallized in the ranks of the consumer. As an illustration of what might be done to educate the consumer and enlist his intelligent support, we may consider one element in the question of prices which is so fundamental to the success of the recovery program. Price increase must follow rather than precede purchasing power. Can this be safeguarded without getting the government into the dangerous field of price fixing? I suggest this experiment to that end: Set up in the NRA a study that will furnish the public at proper intervals information on extra costs for a long list of basic articles, as these costs result from the administration of the National Recovery Acts. With such facts, the purchasing public would be correctly guided in determining when prices are too high and thus enable purchasers to create such protests to their merchants and supply agencies as this information and other circumstances suggest and warrant. This would enable the public to unite against exorbitant prices. The NRA Research and Planning Division is now making certain cost studies relative to various industries that have adopted codes, and the next development in this field of study might well be along the lines I now suggest.

It is equally important that we select our terms carefully in defining conceptions of long-range planning and leadership. Students in this field must begin with a sympathetic frame of mind prompted by a revised vision of conditions, and guided by well-digested experiences from the immediate and remote past. Wisdom suggests that we look forward with open minds, willing to adjust to changes in conditions, rather than with a crystallized determination to preserve at all hazards the status of the past. Our planning studies must take more account of the consumer's psychology than of the producer's psychology. Plant capacity must be adjusted not to what we wish to produce but to what customers require and desire under their own conditions and ideals of civilization.

In the absence of long-range vision and planning, our entire commercial system naturally increased in complexity and sensitiveness. Maladjustments in one part of the system had more and more effect on the functions of other parts. Safety

[461]

REMARKS BY THE CHAIRMAN (MR. GERARD SWOPE):

I am sorry that I can't introduce the first speaker on the program. When your Director suggested the subject of this evening's meeting of the Academy, "Long-Range Planning," I knew the natural person to introduce the subject, of course, would be General Hugh S. Johnson, the Administrator of the National Industrial Recovery Act, who has also given much thought to long-range planning.

When I asked him to speak, he accepted readily, as he esteemed it a great honor and especially fitting to address this distinguished academic body. But much to our regret, his duty as a soldier, which he always is, has called him West to allay the misunderstandings there. To show the speed of his movements, yesterday evening he spoke in Minneapolis, this noon in Des Moines, and tonight he speaks in Omaha. I have a telegram from him from Des Moines reading: "Had so many speeches to write couldn't finish paper until last minute for air mail and then snow storm blocked mail service. Please express my sincere regret but could not possibly have done otherwise."

I am sorry that he could not be with us this evening. I have the greatest admiration for General Johnson's ability, dynamic and irresistible energy, his unsparing and whole-hearted devotion to the NRA, day and night, in the sick room or in his office, and I am very sorry, indeed, that I cannot present him to you.

Our first speaker in the flesh hails from the sunny South, South Carolina, where he was born, educated, and has practiced law, and, curiously enough in these shifting times, has retained his home there, moving only occasionally to Washington and back to South Carolina.

His interests are broad, educational, legal, political, domestic and international commercial problems. It was he who suggested an original method of getting statistics in cotton. He is experienced and wise, and it is fitting that he should be one of the President's trusted advisers.

He is Chairman of the Cabinet Committee of the National Recovery Act, is interested in long-range planning, especially in the philosophic concept underlying that which may remain as permanent under the Act.

The Secretary of Commerce, the Honorable Daniel C. Roper!

[458]

LONG-RANGE PLANNING

THE HON. DANIEL C. ROPER
U. S. Secretary of Commerce

IT is a real pleasure for me to be with you tonight and to join this splendid assembly of men and women in a study of national economic and social recovery measures.

The Academy of Political Science, with more than a half-century of experience, spanning several periods of economic disturbances in our national life, can supply knowledge valuable for the wise charting of our country's future.

Reference to the program of this annual meeting for 1933 shows that your earlier discussions of today have related to the emergency problems of unemployment and industrial readjustment for the primary purpose of safeguarding against immediate social disturbances. This is as it should be, but the study of emergency problems should also endeavor to determine the causes responsible for the 1929 cataclysm, thus providing a basis for efforts in planning to prevent the repetition of economic disasters in the future. The tragic imprint of this depression on the minds and hearts of our people should be an eloquent and lasting appeal to all of us to discover and put in motion such policies as will in the well-thought-out opinion of this generation safeguard the next against our experiences of the past four years.

Much consideration is being given to comparative statistics that show the staggering total of depression unemployment, the precipitous drop in commodity prices, the tragic losses in domestic and foreign trade, the drastic declines in national income and purchasing power. These are important comparisons, forcefully illustrating the severity of this depression. Such statistics, however, serve as measurements only of what has already happened. The real task for sound economic thinking is to interpret intelligently these figures, along with other historical data, and to ascertain what forces and factors have been working within our economic system to bring about the greatly increased disruptions and dislocations of our day.

[459]

When we study the "forces behind the figures" we find that the *economics of balance* can no longer be depended upon to restore economic equilibrium. Recovery periods following previous depressions have been largely self-regenerative. In those eras it was only a matter of awaiting the completion of what were accepted generally as business cycles. Nations managed their affairs on the theory that natural economic forces in themselves eventually bring about harmony and balance. Heretofore, the laws of supply and demand have been depended upon to regulate conditions. It was contended that an efficient producer would succeed and that an inefficient producer would fail, thus keeping the productive power of the country in general line with the consumption needs. However, beginning with the World War, and continuing until the collapse of 1929, excessive industrial expansion, especially in productive capacity, stimulated by the demands of a warring world, created the necessity of an "Economics of Organization" to replace the old "Economics of Balance."

Now, in this new era when our thoughts are so much engaged in charting the future, it is necessary to be careful in the use of descriptive terms. Much is being said about self-government of industry. We all need to understand what is implied by this term. No one will contend that it means that all regulatory control by the Federal government should be removed and that business proceed without any coöperation from the government. There is no important unit of business that would desire this extreme. It would be approved only by such as the bootlegger, or those minorities in business that pursue a cut-throat policy by using unfair methods to reduce their costs and thereby are enabled to undersell legitimately conducted business. Self-government in business does mean that business will be permitted to do those things which business can do as well or better for itself than the government can do for it. If a greater measure of government regulation than this is necessary for the public safety and welfare, and in order to prevent another world economic calamity, such governmental regulations will be sought by the representatives of good business.

Neither must we forget the significant position of the ultimate consumer in the solution of our major problems. It is

[460]

evident to all that the national recovery program cannot be enforced successfully without the support of public opinion, which is crystallized in the ranks of the consumer. As an illustration of what might be done to educate the consumer and enlist his intelligent support, we may consider one element in the question of prices which is so fundamental to the success of the recovery program. Price increase must follow rather than precede purchasing power. Can this be safeguarded without getting the government into the dangerous field of price fixing? I suggest this experiment to that end: Set up in the NRA a study that will furnish the public at proper intervals information on extra costs for a long list of basic articles, as these costs result from the administration of the National Recovery Acts. With such facts, the purchasing public would be correctly guided in determining when prices are too high and thus enable purchasers to create such protests to their merchants and supply agencies as this information and other circumstances suggest and warrant. This would enable the public to unite against exorbitant prices. The NRA Research and Planning Division is now making certain cost studies relative to various industries that have adopted codes, and the next development in this field of study might well be along the lines I now suggest.

It is equally important that we select our terms carefully in defining conceptions of long-range planning and leadership. Students in this field must begin with a sympathetic frame of mind prompted by a revised vision of conditions, and guided by well-digested experiences from the immediate and remote past. Wisdom suggests that we look forward with open minds, willing to adjust to changes in conditions, rather than with a crystallized determination to preserve at all hazards the status of the past. Our planning studies must take more account of the consumer's psychology than of the producer's psychology. Plant capacity must be adjusted not to what we wish to produce but to what customers require and desire under their own conditions and ideals of civilization.

In the absence of long-range vision and planning, our entire commercial system naturally increased in complexity and sensitiveness. Maladjustments in one part of the system had more and more effect on the functions of other parts. Safety

[461]

valves effective in other recovery periods no longer sufficed. Of course, the old fundamental economic forces still apply to a certain extent, but the magnitude of the machinery to be kept in balance was so great under new developments that the length of time necessary to bring about equilibrium under these expanded conditions was too long for nervous masses and might easily have resulted in revolution, even riot and bloodshed. The fundamental change in economic approach from former times convinced us that new, immediate and even startling methods and measures were necessary for this period, if we were to control immediate emergencies and secure sustained recovery. Thus it is that we must recognize that the lamp of past experiences is not sufficient to guide our way in this new emergency. To that experience we must add correct knowledge of the new conditions and patience with gradual approaches to results.

Five years ago, as I came from a session of the League of Nations at Geneva, an English resident of Geneva said to me: "Do you not and does not the United States realize that this League is an utter failure?" I answered, "If you are going to limit your vision to the results of the brief period of efforts that has so far taken place you cannot hope to see a permanent solution in your time. I am unable to say whether the League in its present form is even the proper medium for attaining a solution to the problems of war. But let us not forget that the League members are trying to change a situation that is coexistent with civilization. We should not expect to correct, in a brief period of ten or twenty years, a condition that has been in existence for centuries. It may take a century to prove the full value of the League. We should under no circumstances be too impatient with beginnings to solve such a deeply rooted problem as war. However, when I see men of contending nations placing their cards on the council table before them and freely exchanging information on their mutual problems, I gain hope that through a common understanding thus gained we can hail the beginning of a brighter era in human conduct."

This same principle applies with equal force to our present needed relationship to national problems in our economic recovery. We must not forget that in every one of the six

[462]

major depressions in the last fifty years, the period of recovery has been long and tedious. In these previous periods our people have been concerned, well-nigh exclusively, with the restoration of prosperity. Their concern has rarely taken any other form.

In our present situation, conditions are quite different. The number of people affected in this depression has been so great that industrialism and capitalism, as heretofore interpreted, came under attack and the problem of recovery involved a major responsibility for actually saving our civilization. Under these startling circumstances, new methods with drastic procedures had to be undertaken; something had to be done and done quickly.

President Roosevelt's recovery program, which thus came into being, represents the most important and far-reaching attempt in history to distribute the benefits of recovery among all classes and thus to apply coördinated and coöperative economic planning to the complete economic and social structure of the nation. This is not for the sole purpose of dealing with existing emergencies but also for the purpose of creating safer conditions for the future. With conditions so tragic, so extensive, it had to be expected that progress would be slow and that there would be of necessity experimentation. This, the President freely and early admitted.

It is also inconceivable that any sweeping plan of economic and social reform could move forward faultlessly and with uniform progress all along the line. Mistakes were to be expected, and mistakes have been made. Considered fairly, however, in the light of all the accomplishments, success has very much outweighed mistakes. For example, considering the long history of conflicts in the soft coal industry covering many years and frequently entailing bloodshed, the fact that a code for these mines could be worked out at all is a noteworthy accomplishment. If the NRA accomplishes nothing more than bringing together the many groups and segments of business around a common table of discussion, it would have a right to be recorded as one of the most constructive endeavors ever initiated in our country or in the world. For the first time in our history, the representatives of the consumer, of labor and of capital, many of whom previously were as far apart as the

[463]

poles in their thinking, have had an unequalled opportunity of understanding one another's problems and viewpoints.

Never before have the attention and efforts of all our business men been directed toward the objective of solving the entire country's economic problems. They have been mobilized on their own will, thought and action, as in war times. They have thought through their own problems and into the broader problems of the entire nation. Mutual objectives can be crystallized and made effective only through a plan that defines the responsibilities of each in coordinating toward a proper goal for all.

The business expansion that took place in the decade preceding 1929 created in men's minds a fear of what economists term "a planned economy". It was insisted that planning and freedom are incompatible. It was pointed out by some that individualism could not be preserved if we practiced the principles of central planning. But as the severity of the depression increased, and no united front was presented to stop the relentless attack of its destructive forces, it became increasingly evident that we would have to bring ourselves to the acceptance of the idea of coöperative economic planning, as an instrument of national salvation. The philosophy back of this idea is the fact that the "Economics of Organization" must replace the "Economics of Balance."

On November 1, the Business Advisory and Planning Council for the Department of Commerce, of which your chairman tonight, Mr. Gerard Swope, is chairman, met in its second full session. This Council was formed on June 26 of this year to advise with the Secretary of Commerce on immediate policy, study and long-range economic planning for the Department of Commerce. Foremost in our minds is the preservation of the industrial initiative that has so distinguished American business, and at the same time assistance to good business by regulation in protecting itself against the recalcitrant and sometimes destructive minority.

Few experiences in my life have given me greater encouragement and inspiration than I have received from meeting with these business men, big enough to think for themselves and for others, and fine and gracious enough to coöperate unselfishly in attaining objectives for the common good.

[464]

Gathered around the conference table last week were forty-five of the outstanding business and industrial leaders of this country, who had come to Washington at their own expense and with great personal sacrifice to attend this Council meeting. The major recovery problems were placed on the discussion table, and these men with their wealth of experience and knowledge discussed these problems freely and constructively. The members of this Council, without exception, expressed their confidence in our country's ability to fight its way steadily forward to greater heights of progress. But it was their unanimous belief that such a goal could not be attained without a soundly conceived and properly executed program of economic planning of industry generally. Their deliberations gave full evidence that coöperative thinking must replace individualistic thinking.

Any present-day approach to planning must first consider certain things that lie back of sound planning—blueprints and techniques constitute the second phase. Our starting point must be an effective and rationally foresighted leadership culminating in philosophically sound thinking. And plans made through foresighted leaderships, cognizant of the scope and interplay of economic causes and effects, cannot be successful if leaders lack an appreciation of the problems of business as related to civilization. Or, if they fail to develop the modes and habits of thought necessary to educate and enlist the support and understanding of the people behind such plans, they can hardly hope to avoid failure.

Broadly interpreted, the first requirement of a planned economy is a coördination of information which reveals the interplay between economic forces, and economic data that may be depended upon as a rule or which is immediately set aside as an exception. A factual basis and background is first necessary in order to give all groups an understanding of how the national organism works, so that each may comprehend how it fits into the whole operation, and how it is related to all other units within the national economy.

It seems incredible that the directing intelligence of the political and economic life of the United States did not sense in advance the on-setting power of forces which culminated in the 1929 débâcle and led to four years of depression. If

[465]

leadership does not take the responsibility of thinking ahead and perceiving what the actions and reactions of economic causes and effects may be, it is not worthy of the name. Leadership does not mean unerring prophecy, but it does require logical and intelligent foresight.

The question, "What is statesmanship?", is difficult to answer. Edmund Burke, the great English statesman, said: "A disposition to preserve, and an ability to improve, taken together, would be my standard of a statesman." The real statesman is one who understands change and knows how to adjust social and economic institutions to that change. He must foresee that certain inevitable results will grow out of a certain combination of circumstances. But no matter how clearly the statesman may see what should be done, he is powerless to make any progress unless he has vision to see life in its larger segments, and a willingness to think and work for others. He must then seek the truth throughout all of these segments of economic and social life. Then he must be able to assemble behind this line of leadership the public opinion and support of the country.

One of the greatest problems of any planning program is, therefore, largely a question of the most effective utilization of present leaders and statesmen. The principles and powers of leadership must be developed in the younger men of today, and dependence must be placed upon our schools and universities to do their part in training more and more of their students for the broader responsibilities of leadership and statesmanship. They must be surcharged with a zeal for service, rather than with inordinate desire to hold office. But education must not alone create leaders, it must create followers—those who have an enlightened understanding of what leadership is trying to accomplish and who, through this understanding, are eager and willing to give it their full support.

It seems that the greatest task of education today is to relate the individual to the broader picture, and instill in him the satisfying pleasure of clean and effective public service. Greater emphasis must be placed upon methods of doing and thinking as they apply particularly to wisely controlling, for the common good, the changes of a changing society. Change is viewed more today from the angle of how it affects group

[466]

welfare than individual welfare. What we now need is interest in the entire mass of our people.

We are passing today through one of those unusual periods in the history of the race which come at long intervals and which are the result of forces long accumulating—a period such as the fall of the Roman Empire, the Renaissance, or the political revolutions in France and England. It is very rare in the course of human experience that men can definitely put their fingers upon great opportunities in life. We generally see them in retrospect. Today presents one of the greatest opportunities this nation has ever had for economic statesmanship and leadership. We must have an intellectual leadership that is able to find and establish the right goal for our educational efforts.

Today the political and business leadership of this country have a joint appointment with destiny, and this appointment must be jointly met. We cannot afford to have the dangerous situation of political leadership pulling in one direction and constructive business leadership pulling in another. All approaches must lead, as the spokes of a wheel, along different lines to a common center. The hub is the unified objective which holds the various methods and activities together in one major program.

Thus the desired results require that the American statesman, the producer in field and factory, the distributor and the consumer work coöperatively in appreciation of the fact that each and all have responsibilities as well as rights in plans for stabilization and in maintaining a fair, equitable and desirable future social structure. We need here to reflect on the impressive words of George Washington at the 1787 Constitutional Convention, when he said: "Let us raise a standard to which the wise and the honest can repair; the event is in the hand of God."

[467]

REMARKS BY THE CHAIRMAN (MR. GERARD SWOPE):

Thank you, Mr. Secretary, for your very clear statement and comprehensive grasp of the problems that you have laid before us.

I want to call attention, before I introduce the next speaker, to how fortunate we have been at this meeting of the Academy in having not only the next speaker, who has come to us from England, but also Sir William Beveridge, who spoke to us this morning, and Mr. Butler, who addressed the meeting this afternoon. It was a signal opportunity, for these gentlemen, who have seen the depression in their own country, to come over to see near at hand what we are doing to retrieve ourselves from the situation in which we find ourselves.

Our next speaker is one of many whom I like to think of in England, a classical scholar and a public servant, a graduate of Balliol at Oxford, and an honor man, an athlete, rowing on the Oxford crew against Cambridge, entering into public life, becoming a public servant and later becoming Minister of Labor.

He has just recently come over to this country—he has been here before—to study our adventure in national recovery. He has been in Washington, the center of all this activity, the “hub,” as the Secretary speaks of it, and has talked to many.

It is a rare privilege to have him talk to us this evening, because of his background and experience. He may possibly speak to us critically—I hope so—but always with sympathy, because he believes in the objective toward which we are striving. It is a great pleasure and honor to introduce the former British Minister of Labor, the Right Honorable Sir Arthur Steel-Maitland.

[468]

LONG-RANGE PLANNING

THE RT. HON. SIR ARTHUR STEEL-MAITLAND
Former British Minister of Labor

OCCASIONALLY we may come upon something, whether it be a product of human making, or nature's handiwork, like a flower, which, though it comes latest in time, is yet most favored, and “like the last taste of things” is sweetest last, writ in remembrance more than things long past. I do not think however that could ever be said of a speech that comes like mine after such an interesting address as we have had from Secretary Roper, and after that long series of interesting papers which we heard this afternoon and this morning at the two meetings of the Academy. If, therefore, at this time of night you get tired in listening to another speech, just let me take shelter behind the Chairman.

Let my fate be like that of a young farmer in Scotland who was asked to sing a song at a farmer's dinner. He had no more voice than a crow, but he stood up and he sang. It was a ghastly performance and when he sat down again, he turned to the man next him and said, “I am afraid that wasn't much of a song, was it?”. His neighbor turned to him and said, “No, indeed, it wasn't, young man; but I don't blame you; you did your best. But I should like to break the neck of the man who asked you to sing.”

If therefore the speeches are too long, kindly turn your attention to the Chairman afterwards who will be able to deal with my would-be aggressors, however numerous, and let me get safely away.

But at least there is something that can be done at the end of an interesting day like this and that is to gather up some of the threads of what has gone before. We have heard today of the dislocation caused by the rapid advances of science. We have heard today references to the great depression through which we are passing, and to the misery created by it, of which as an old social worker myself I am only too conscious;

[469]

of industrial measures taken to mitigate it, and there again, as an old business man in another capacity, I can both appreciate the difficulties, and at the same time realize that those difficulties were made to be surmounted. And then this afternoon we heard the news of public works that are to be developed upon a large scale.

If I am to say a few words about long-range planning, I should like to approach it from a very practical standpoint. I will deal with a concrete instance, and then, if there be a minute or two to spare, say something of the general inferences that can be drawn from it.

This afternoon I think everybody who listened must have been greatly interested in the statement that was made by Mr. Hopkins, the Administrator of Civil Works, and in the expenditure which is contemplated upon them in the very near future. From the financial point of view it seemed to me to be a pronouncement of great moment. It may, and I trust it will, result in giving activity to industry. It means the creation of a great body of purchasing power and if that purchasing power proves active and effective, it is just that fillip, which in one form or another, as history has often shown, has started the first movement in lifting a country out of a state of depression and putting it on the path to recovery.

But, of course, a great program of public works is also of value in the employment that it gives. I have no doubt that those who are going to direct it will get the best possible value out of those public works. Speaking, however, as I do tonight on the subject of planning, I ask you—and I do so in no spirit of criticism—how much happier you would have been here in your country or we would be in ours, if before we tried to carry out a policy of public works we had a proper plan of them; if we had known precisely those works which were really most needed in the various great states and cities and communities, and if the necessary plans, designs and estimates had been ready prepared so that they could have been undertaken at once, at the time when expenditure upon them would have been most effective and of the greatest service to the community.

I say again, let no one take this as a criticism. It is not a criticism of this administration or of a past administration here, or of an administration in my country or in any other country.

There never really has been an attempt at such planning before, though it has been sometimes discussed. But, I ask you tonight to consider whether in the future there ought not to be such an attempt, so that if ever a crisis comes upon us, even if it is not so great as the present one, yet we should be ready to meet it instead of having to extemporize a program in the face of the emergency itself.

The truth of what I say can be seen if anyone will study the actual kinds of works for themselves. Like a practical man, I have been through a volume, and a most interesting volume, giving an analysis of the state of affairs in one of the foremost American cities, Philadelphia. It is by an able young American economist, Mr. Loucks. There one can see some facts that stand out quite clearly to the least active imagination, and they are these: Plans of this kind, of works that a city or a countryside most needs, take a long time in preparing. The very engineering side of a big project, as I know from my old experience in mines, may occupy a year before the matter can be examined in all its aspects, and a proper scheme prepared. Then it reaches the stage of public examination and criticism. There are often some ten to thirteen stages in the City Council to go through. That is notorious. In a country like this, where the Federal government, and the state government, may perhaps contribute a share of the expenditure, there are long series of negotiations which have got to be taken in hand. Then there may also come delays in negotiating the purchase or acquisition of real estate if it is required.

All that means that much time may be taken and very often many months must elapse before the first inception of a project of this kind, and the time in which effective work can be done upon it. Therefore, I say to you, would it not be wise, if possible, that we should think out our schemes in advance and have our plans ready beforehand?

If anyone studies these works and analyzes as Mr. Loucks has done in the case of Philadelphia it becomes clear that they can be foreseen. It is also clear that though it is in times of prosperity that people are naturally more inclined to carry them out, yet in most cases they can be postponed. Postponing them means that you are left without some new accommodation which is very desirable and would be very convenient.

to have. To postpone these, therefore, means need for some self-restraint. But if they can be postponed, think how much good would come of that postponement when the time of depression comes!

Of course the policy which I commend to you depends on the assumption that we know enough of these trade booms and depressions, to be able to say when we should postpone public works, and when we should put them in hand. I go to a class much abused at present, and I think in many cases unfairly abused, the economists. Some of the economists, in my opinion, are men in whom anybody would rightly put trust in a matter of this kind. According to the best opinion that I have known on this subject it would be possible to recognize the time at which you ought to put these works in hand, in order to give a timely fillip to industry in a period of depression. Think what that means!

At the present moment—and I am sure everyone in this country who has studied this depression must realize it—what is wanted is to give a spurt—a spurt to capital works, to those businesses dealing in building or other capital goods. It is the stagnation in the capital goods industries which for the moment has been making the recovery hang fire. The actual volume of works normally put in hand by public authorities of all kinds, Federal, state and municipal, is quite enormous. In an ordinary year in this country it transcends several-fold even the vast volume of public works which are contemplated at the present time. Yet in the present year the orders for the execution of such works have been at the lowest ebb instead of at the maximum. If the plans for them could have been prepared, postponed and kept ready to use, it would be an engine in the hands of any government which would be of the utmost value in an emergency like the present.

I do suggest to you that these are matters to which really scientific thinking should be directed. They can be coupled with other measures also which restrain the ardor of the upswing so as not to make it go to such a speculative height, when business is prosperous, and to mitigate its fall when the turn comes. The postponement of public works on the upswing, has a deflationary effect and prevents so great a height being reached. By taking them in hand on the downswing and by