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NATIONAL ECONOMIC SECURITY

ARTHUR B. ADAMS

UNIVERSITY OF OKLAHOMA PRESS

NORMAN, 1936

NATIONAL ECONOMIC SECURITY

By Arthur B. Adams

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Set up and printed by the University of Oklahoma Press, Publishing Division of the University, at Norman, Oklahoma, U.S.A. First edition February 1, 1936

THIS BOOK IS DEDICATED

To all students of our national economic problems who place public welfare above special privileges.

PREFACE

CAPITALISM is not dead and should not die. The institutions of private property and of profit-making should be preserved, in my opinion, and individual initiative should be given ample opportunity to stimulate desirable productivity of our industrial system. But, under modern industrial and economic conditions, the nation cannot depend on the laissez faire policy to control the operation of our industrial system to the best interest of all the people. The so-called natural economic laws, which heretofore have been depended upon to control the distribution of the national money income (the net production of industry), have failed to distribute the national income in a such a way that our industries can be kept operating at full capacity. Neither have the natural economic laws adjusted the daily and weekly work hours of laborers to the technological progress made in the methods of production in industry in such a manner as to prevent unemployment. The nation cannot achieve permanent prosperity for all unless our government is able to formulate and put into operation economic regulatory policies which will remedy these glaring defects in the operation of our industrial system.

Since the beginning of the depression in 1929 the United States has been confronted with many grave national economic problems; as a people we must deal with these problems by the adoption of some kind of permanent national economic policy or policies. What should be the nature of these permanent policies? What are the strong and the weak points of the so-called New Deal policies, and how should these policies be revised to meet the national economic needs? If you individually do not agree with the conclusions in this book, you should have defensible reasons for disagreement with them. We, as intelligent citizens, should have well grounded opinions

concerning the methods of handling our pressing national economic problems.

I believe that this book contains a sound analysis of the present national economic situation and points out the correct basis for the formulation of sound permanent national policies to deal with the economic problems which resulted from the conditions. However, I do not anticipate that all readers will agree entirely with every analysis, conclusion, and recommendation made in it in reference to the defects in our present industrial system, or as to the fundamental nature of our various national economic problems, or as to how they should be dealt with by the Federal government. I have written the book, with the hope that it may be of value to our people in helping to point the way to the best policies for dealing with these problems. It is my sincere desire that this book may induce others to think more seriously and more deeply concerning the formulation of wise national economic policies to meet the present grave economic situation.

We are now groping for national prosperity. Temporary artificial prosperity for a few would be of little or no benefit to the nation. The American people want permanent prosperity for all. This book was written for the purpose of pointing out the principles upon which our national economic policies must be based in order to attain lasting national economic security.

I wish to acknowledge the valuable aid of Mrs. Georgia M. Byron and Miss Mildred Coston in the preparation of the manuscript of this book. They verified most of the reference and statistical data used in it, as well as typed the manuscript.

ARTHUR B. ADAMS

Norman, Oklahoma

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NATIONAL ECONOMIC SECURITY

CHAPTER ONE

CAUSES FOR RAPID ECONOMIC DEVELOPMENT OF THE UNITED STATES

IN ITS industrial development the United States has recently passed through a complete economic era or epoch, and has entered upon a new and vastly different one. The first era of our national industrial history was characterized by the growth of our industrial system with its great productive efficiency and capacity. This remarkable industrial system was built as a result of the exercise of individual initiative in the exploitation and use of our natural resources, the development of mechanized productive processes, and the saving and investment of large quantities of new capital funds. As our industrial system reached a more complete maturity in its growth, the distribution of the proceeds of production (the national money income) became more unequal, and, in proportion to the size of the national income, savings and investments increased and consumers' incomes decreased. However, the unequal distribution of the national income and the large savings, actually contributed to the rapid increase in productive capacity of our industrial system, as long as established industries could be expanded and many new ones developed.

By the end of the World War, largely because of the continued increase in the unequal distribution of the national income and the growing maturity of our industrial system, the nation reached a new economic era characterized by surplus savings, excess productive capacity for goods at prevailing prices, and an inadequacy of consumers' purchasing power. How and why this new national economic era developed and what kind of public policies should be applied to cope with the grave economic problems brought forth by it are the major

problems with which this book deals. But, before considering the development of the new economic era and its problems, we should examine the fundamental basis and principles upon which the growth of our industrial system was founded during this first era. In other words, we should know what caused the rapid industrial development of the United States prior to the World War.

During the period of time from the end of the Revolutionary War in 1783 to the beginning of the World War in 1914 the United States of America enjoyed an economic expansion more rapid and more general than did any other nation. In this period of 130 years, the country grew from one of thirteen sparsely settled agricultural colonies to a powerful industrial nation of forty-eight states with a population of more than one hundred million people. Our annual production and accumulated wealth increased more rapidly than did our fast growing population. Notwithstanding some notable exceptions, the standard of living of the average American was raised to where "the American standard of living" became the envy of many other peoples.

The two fundamental conditions upon which real economic progress depends are: (1) A consistent increase in the annual production of economic goods and services per inhabitant of the nation; and (2) An increase in the *real incomes* of each economic class (particularly that of the low income receivers) pro rata with that of the growth in the per caput production of the nation. Both conditions are necessary before general economic progress can become an actuality. Prior to the World War, the United States enjoyed a substantial increase in the annual production of economic goods and services. Also, in the face of a growing inequality in personal incomes, the national income was distributed in such a manner that practically all economic classes received progressively larger *real incomes.*

We should be able to give a satisfactory answer to the question: Why did this nation experience such a notable industrial and economic growth up to the beginning of the World War? Why were we able to increase our per caput production rapidly, and at the same time to distribute among the people the fruits of that production in such a manner as to advance the general

welfare of the different economic classes? There must have been certain outstanding forces and factors present in our economic situation which were responsible for this remarkable achievement. What were the causal forces?

At the time of the original settlement of this country the legal institution of the individual's right to acquire, own, and dispose of property (commonly referred to as the institution of private property) was transplanted from the European countries from which the settlers came. Also, the institution of the right and freedom of the individual to make private contracts, which, if not illegal, will be enforced by the government, was brought from Europe and established as an American institution by the original settlers. All of our economic progress up to the present time has been made under the institution of the private ownership of property; in fact, our whole economic system is based on that institution. The United States, however, is not peculiar in this respect, for the economic systems of all capitalist nations are based on the institution of private ownership of property. Neither is the institution of the individual's freedom to make and enforce legal private contracts peculiar to the United States: the same institution exists in all capitalist nations as a necessary adjunct to the maintenance of the institution of private ownership of property.

The only respects in which this country has differed from the European countries in regard to the individual's freedom to make and enforce private contracts, is in reference to the character and kind of legal restrictions placed upon the freedom to contract. On the whole, we have thrown around private contracts fewer legal restrictions than have other countries. Few restrictions have been placed on the making and enforcing of private contracts, on the ground that certain kinds of contracts would result in undesirable or injurious public or social consequences. During the period of our great industrial development we proceeded largely upon the theory that the individual would best serve the public interest by best serving his personal interest in the use of his property and property rights in business transactions. In this respect, the United States probably has extended more "freedom of contract" than has any other nation.

The exercise of individual initiative in economic activities is restrained necessarily by the legal limitations placed upon the freedom of contract. While legal restraint on the freedom of contract is only one of several factors which today prevent the individual from freely exercising individual initiative in his economic activities, the placing of many legal restrictions on private contracts during our great period of economic development would have imposed a powerful curb on the exercise of such initiative. All kinds of business regulatory measures imposed by the government place restrictions on the freedom to make private contracts; such public regulation restricts the exercise of individual initiative because it restricts the freedom of contract. For these reasons, "freedom of contract" and the freedom to exercise "individual initiative" in business have come to mean one and the same thing to many people.

In the past few years much has been said and written about the large part that freedom of contract and free exercise of individual initiative have played in advancing the economic development of this nation. Unquestionably, under the frontier conditions which existed up to a comparatively short time ago, self-reliance, rugged individualism, and the free exercise of individual initiative did play an invaluable part in the economic growth of the country. Economic life under such conditions was necessarily an individualistic one; personal success and welfare depended more upon the settler's ability to exercise individual initiative in providing for self and family than upon his ability to co-operate with others in economic endeavors. The free exercise of the acquisitive instinct on the part of each settler was a powerful force in converting the wilderness into farms, homes, towns, and cities. Certainly, the settlement and economic development of this country would have proceeded at a much slower rate than it did if its settlement had been carried out under any kind of a publicly regulated and controlled plan. The uncurbed privileges of taking advantage of opportunities for personal gain offered by this rich country induced our people to exercise a maximum amount of individual initiative and energy in exploiting and developing it.

The governmental policy of selling very cheaply or giving away the public lands and resources to individual citizens who

wanted to appropriate and exploit them was another public policy which played a large part in the rapid economic development of the United States. The money received for the public domain disposed of prior to the Civil War by the states and Federal government was not sufficient to pay the public expenses of acquiring and disposing of it. The Homestead Act of 1863 provided for giving away all the remaining desirable lands in the hands of the Federal government. So long as a plentiful supply of public lands and resources was available, our land policy assured an ample supply of cheap land and resources for ownership and development.

During the period of its settlement and exploitation, no other country offered the opportunities of great rewards for the exercise of individual initiative that this country afforded. The United States was blessed with an abundant supply of free natural resources which might be appropriated privately and exploited for personal gain. If it had not been for the great bounties of nature with which this continent was blessed, the history of its economic progress would have been vastly different from what it actually was during the nineteenth century.

From the earliest settlement, the abundance of natural resources in proportion to population made it possible for the United States to have a large production per laborer employed in producing agricultural products and raw materials. While production per acre has never been great in agriculture in the United States, because of the large size of our farms, production per farm has always been large. Also, because our country possessed an enormous quantity and a great variety of rich natural resources which were either free or very cheap in price, our production of minerals per laborer employed has been much larger than has such production in any other country. As a result of the fact that our natural resources were plentiful and cheap and our labor supply was scarce and dear, our per caput production of raw materials of all kinds always has been high. Consequently, during Colonial times and the early period of our national history, our people devoted most of their economic activities to the production of the materials of nature.

In the earlier part of our economic history, the high per caput production of the materials of nature and the wide opportuni-

ties offered to appropriate free natural resources placed laborers in a position to demand and to receive high wages. If a laborer was not satisfied with the wages he was offered by a prospective employer, he could take up a free farm for himself. The abundance of free natural resources afforded each individual, regardless of his economic status, an opportunity to exercise individual initiative in advancing his own economic welfare. As long as that opportunity was open to all there was a fairly equitable distribution of the proceeds of industry among all economic classes in the country.

Under conditions of rapid exploitation of our abundant resources, the sparsity of population caused a constant shortage of labor, except during a few short periods of business depression. Because of the scarcity of labor, the high production per laborer, and the freedom of choice of laborers, the wage scales in this country were very high, even in Colonial times. As a result of high wages and the scarcity of labor it was necessary to economize in the use of labor. For this reason the handicraft industries, based largely on human labor, did not develop to any considerable degree in the early period of our history. As already indicated, we first developed those industries which depended largely upon our natural resources, and in which labor was a comparatively small factor.

In point of time, the United States was far behind England in the development of manufacturing. Only a few of our basic manufacturing industries were well established by the beginning of the Civil War. But from 1860 to 1907 we led all other nations in the development of the manufacturing industries. Our undertaking of manufacturing was characterized by the invention and application of machinery to production to a much greater extent than it was in any other nation. The outstanding reason we led the world in the application of machinery to production was because of the relative scarcity of labor and the relatively high prevailing wage rates. In the development of American manufacturing it was necessary to substitute mechanical power and process for human labor wherever possible in order to compete with the manufacturers of Europe, who were able to secure a plentiful supply of laborers at low wages. Therefore, the high cost of labor in this country was the greatest cause for

making and using automatic machinery to displace laborers in production. Because of this necessity to economize on labor, we proceeded at a much more rapid rate to mechanize production in all fields of economic endeavor than did the people of any other nation. The "American inventive genius" was called forth, if not generated, by the relative shortage of labor and its high unit cost. The fact that there were few well established handicraft industries developed in this country prior to the mechanization of manufacturing made the building of our factory system easier than it was in the European countries where it was necessary to supplant the handicrafts with machine production.

For many years after we began to apply natural power and mechanical processes to production, the resulting labor economies created no serious economic problems for us. There were still many natural resources to be exploited and new manufacturing industries appeared every year or so. The rapid growth of our industrial system required the employment of almost all of the native laborers and of many foreign laborers who migrated to this country. Displacement of laborers by machinery in the various industries only increased the supply of labor available for building new industries and the expanding of old ones throughout the nineteenth century and the first decade of the twentieth. Therefore, while we were building our industrial system, it was not possible to displace a sufficient number of laborers with machinery to create a great surplus of labor.

The extensive use of machinery in production was the underlying force which enabled the country to continue to increase both the general per caput production of the nation and the specific production per laborer employed. General use of labor-saving devices worked hand in hand with the bountiful supply of natural resources to increase the productive capacity of the country. As long as there was no permanent or consistent surplus supply of labor in the nation the employed population received a share of the increase in production which resulted from the use of the labor-saving devices. The growth in production due to the use of machinery enabled employers to pay higher wages, and the continual scarcity of labor forced them to do so. Consequently, the extensive mechanization of production from

the Civil War to the World War was the principal force responsible for our rapid economic progress during that period.

In order for the United States to achieve this progress, it was necessary to accumulate the capital required to build its industrial system. This was done, and could be done only, by consuming less than was currently produced and investing the surplus production in capital (productive) equipment. Because of the generally high per caput production, saving by a considerable portion of our population entailed not a great personal sacrifice on their part. The utilization of the rich natural resources and the development of many new industries enabled many of our citizens to receive large surplus incomes. Most of these surplus earnings were re-invested in new capital for the industries from which the earnings came, or invested in capital for new industries.

During the eighties and nineties, monopolistic tendencies appeared in several of the major industries; nevertheless, on the whole, all kinds of business enterprises were profitable and the annual savings for new investments were large. But, because of the extraordinarily rapid rate of our national industrial growth up to 1907, the demand for new capital funds was generally in excess of the supply of new investment funds derived from current savings. At various times during the period of great industrial growth, the deficiency in the supply of current investment funds was made up by borrowing abroad and by the temporary expansion of bank credit. Our various business depressions prior to the World War were due largely to the excessive expansion of bank credit in order to secure desired current capital funds which could not be supplied immediately from current national savings. Regardless of the sources from which new investment funds came, their investment in productive enterprises generally returned substantial profits to the investors. Therefore, the prevailing high returns from capital investments stimulated people to greater savings for new investments.

In Colonial days and during the early part of our national history, most of our business enterprises were comparatively small and were individually owned and operated. Generally, the larger enterprises were organized as partnerships. The cor-

porate form of organization of business enterprises prior to 1840 was used only for banks, insurance and transportation companies (such as fire and life insurance, canal, pike and railroad enterprises), and for a few mining enterprises. With the growth of the railroads and of machine production in manufacturing and mining, it became necessary to bring together larger aggregates of capital than could be supplied by any individual or by a few partners to launch the necessary business enterprises. Mainly for this reason, the corporate form of organization became general for all large manufacturing and mining businesses, as well as for the financial, transporation, and communication enterprises.

While many grave abuses later originated in connection with the managerial operations of business corporations, the adoption of the principle of joint ownership of business enterprises was a necessary step in the development of the factory system of production. Only through such a scheme was it possible to bring together the necessary mass of capital and to give the enterprises perpetuity separate from the lives of individuals forming them. The corporate form of business organization offered to all investors a broader opportunity to invest their funds than they would have had under the individually owned or partnership enterprise organization of business. The corporate form of organization facilitated the accumulation and investment of savings in those business enterprises which were largely responsible for the building of our industrial system, and but for it, our national economic progress would have been much slower than it was.

The adoption of the constitutional provision which gave the Federal government control over interstate commerce and prohibited the states from levying import duties on the goods from other states played a major part in industrial and commercial development. It insured to each producer and to each seller a free and open *national market* in which to sell goods. As a result of the adoption of this constitutional policy the United States offered to the American producer what developed into the largest free market in the world for home producers. There is no such free market available to the home producers of any other country. Since the beginning of the

twentieth century, the American people have purchased more economic goods and services than have the peoples of all the nations of Western Europe. There is no free market as between the different European nations; but there is a free market as between the different states of the United States. This market is available to all American business enterprises.

Without the accessibility of our great free domestic market to American business enterprises, the development of modern mass production with automatic machinery could not have occurred in this country as it did. The development of mass production depends upon mass sales; mass sales require a large free market in which to dispose of the goods produced. Tariff walls around the boundaries of each state would have made impossible the growth of such a large free market. With the existence of this free national market our volume of production, and the technique employed therein, has not been restricted greatly by a limited market for the products of our major industries. On the other hand, our large free national market has encouraged the making of standardized goods produced by standardized mechanical methods. Also, because of the existence of this great free domestic market, American producers have been induced to mechanize production at a more rapid rate than have the producers of other countries. Our mass production, which developed partly as a result of the possibility of securing mass sales for the products, was the principal force which made possible our great increase in per caput production after 1890.

Of course, the building of the means of transportation and communication was another essential factor in our economic and industrial growth. During our earlier national history the settlement of the West was dependent on the development of transportation facilities to such an extent that rapid settlement was made possible only through the development of railroad transportation. Where and when there are no transportation and communication facilities, there can be no commerce or trade among the settlers. The growth of the national market was limited by the growth of both the transportation and communication facilities of the country. The establishment of the great American railway systems and the building of our means of communication (postal service, telephones, and telegraph)

were necessary adjuncts to the building of our factory system.

The United States was fortunate in being settled at the particular period of time it was settled. During Colonial times, because of a European shortage of agricultural products and raw materials, there was a strong European demand for our raw materials and surplus agricultural products. Then, for almost a century following the Revolutionary War, the European demand for our natural products was strong. We supplied a large part of the cotton and tobacco they used and they bought all our surplus food products at good prices. We had little competition from the other countries of the Western Hemisphere in selling these surplus natural products because they had not yet developed as great raw material and agricultural countries. As a result of our large importation of manufactured and capital goods, we had an unfavorable balance of trade up to about 1884. But because of the largeness of our exports and the favorable prices we received for them, our unfavorable balance of trade was never large during the time we were building our industrial system.

The American people have had the ingenuity and energy to make good use of the favorable physical and economic situation in which they were placed. Some writers would have us believe that our economic progress has been due largely to the superiority of the personal qualities of our people, such as intelligence, initiative, daring, efficiency, inventive genius, and administrative ability. Unquestionably, the application of these and other human qualities played no small part in contributing to our economic progress, but we should remember that the United States, as a result of her rich, free natural resources, has offered almost unlimited opportunities for the application of nearly all the productive human qualities.

Unquestionably, our people as a whole do have as much (if not more) intelligence, physical energy and initiative as do most other peoples. Their superior abilities have been due largely to the superior opportunities they have enjoyed; they have had a higher standard of living and opportunities for more educational training than have the people of any other country. When it is said that our people have shown the greatest inventive genius of all peoples, we should remind ourselves that

this was largely because this country offered greater opportunities for the application of mechanical inventions than did any other country. Also, it is natural that we should have more efficient business administrators than most other nations because we have more and larger business enterprises to administer. Nevertheless, we should be proud of our "American efficiency in production," and of our "American standard of living." It is upon the improvement in this efficiency in production and the preservation and advancement of this standard of living for all our people that the nation's future economic progress depends.

CHAPTER TWO

NATURE OF THE ECONOMIC CHANGES PRECEDING THE 1929 DEPRESSION

FROM 1914 to 1929 the United States experienced a phenomenal increase in production both in agriculture and in industry. The World War created an unprecedented demand for goods of all kinds and war prices stimulated a general increase in production of goods. In 1922, following the 1920 depression, another period of rapid expansion in production in the mining and manufacturing industries began, ending in 1929.

The war brought about a shortage of food supplies in Europe which caused prices of agricultural products in the United States to reach an unusually high level. The American farmer put forth every effort to take advantage of these high prices and to supply the war shortage in food products in the European countries, particularly in the countries allied against Germany. In 1914, when the war began in Europe, the United States was importing more food products than it was exporting, whereas, in 1919 our surplus exports of food products over imports amounted to $1,300,000,000.[1] While it was the extremely high war prices of agricultural commodities which induced our farmers to increase production during the war, it was the rapid mechanization of the agricultural industry which enabled them to succeed so well.

Prior to the war our farmers had become accustomed to the use of a great amount of agricultural machinery in carrying on their productive operations. They used machinery for preparing the land, for cultivating many of their crops, and for harvesting most of the staple crops. But the machinery then in use was propelled by horse power. Just before the beginning of

1 *Statistical Abstract of the United States*, 1928, p. 452.

the war the farm tractor was introduced on a few farms to take the place of horse power for propelling farm machinery. Then war prices and the shortage of farm labor brought about a widespread and rapid purchase of tractors by farmers. The general use of the tractor increased the efficiency of the farm machinery already in use, and enabled the farmers using it to purchase still larger and more efficient machines for preparing land, cultivating it, and harvesting the crops. This mechanization of the agricultural industry permitted farmers to cultivate profitably land which formerly had been considered submarginal land, or land unfit for cultivation. The direct cost of cultivation per acre was greatly decreased by the use of powerized machinery, and the productivity of the land was increased because of the more thorough preparation for cultivation made possible by the use of the tractor. Also, the displacement of the horse in the cities as a result of the development of the automobile industry, and the substitution of the tractor for the horse on the farm, made free for the production of other crops many millions of acres of farm land which had formerly been used to produce feed crops for work animals. This land was then utilized to produce food products for human beings and raw materials for manufactures.

The development and use of the farm tractor enabled the farmers at the same time to decrease the number of laborers employed in agriculture and to increase their production. The drafting of young men into the army took from American farms nearly two million young workers. Without the wide use of power farming, this decrease in the number of farm laborers would have greatly decreased our agricultural production, whereas production of agricultural commodities actually increased.

Because of the high prices received for agricultural products and the economies brought about in the use of labor through the mechanization of agriculture, the farmers' incomes increased greatly during the war period. Due to the high profits of agriculture at this time, prices of agricultural lands rose by leaps and bounds; in some communities prices of farm lands increased sixfold from 1915 to 1919. There was much speculation in buying and selling farms, and as a result of this whole

speculative movement, farm mortgages in the United States more than doubled in value during the war period.[2] If the agricultural industry had continued after the war on a profitable basis, the war increase in prices of agricultural lands and in farm mortgages would have entailed no great hardships on individual farmers and on the industry after the war. But unfortunately, as will be pointed out later, the prosperity of the agricultural industry continued only up to 1920.

The war brought intense prosperity not only to agriculture but to all industries in the United States. The European demand for munitions and for other war supplies, including ships, greatly stimulated the mining and manufacturing industries. The war demands, both domestic and foreign, resulted in a great rise in the prices of all raw materials and of all manufactured goods. These high prices and shortage of goods of all kinds furnished an unprecedented opportunity to our business enterprises engaged in fabricating products for increasing the use of automatic machinery in production. As a result of the drafting of four million young men into the army, a great shortage of labor was created. The only way to overcome this labor shortage was to substitute automatic power machinery for human labor on a greater scale than had ever been done. This movement toward greater use of automatic machinery and the development of mass production in mining and manufacturing was temporarily interfered with by the depression of 1920, but with the industrial recovery of 1922 the movement continued at a rapid rate up to 1929.

The economies in the use of labor, the high commodity prices, and the great increase in production brought about by the World War enabled practically all business enterprises in the United States to make large profits during the war period. As a result of the great increase in profits and in other incomes received by business enterprises and many of our citizens, the savings of the nation were greater during the war period than during any previous period of our history. The national savings were invested in public debts (Liberty bonds and foreign government bonds), and in private debts (particularly farm mortgages and securities held or issued by foreigners), and in new capital

2 See Table IV of Appendix A, p. 272.

for expanding business enterprises. During the war period American investors purchased from foreign investors some five billion dollars of American securities which were held abroad; they purchased from the United States government some twenty-four billion dollars of bonds and notes; and they invested many additional billions of dollars in new capital for our expanding business enterprises. Much of the new investments in business enterprises came from the corporate surpluses which were not paid out to stockholders but which were plowed back or re-invested in the businesses as new capital.

Not all the new capital funds invested during the war came from the current savings of individuals and business enterprises. A large part of the financing of the war and of the expanding business activities during the war was carried out through the expansion of bank credit. The Federal Reserve System was organized in 1915, within a few months after the beginning of the European war. If it had not been for the reserve bank credit offered by this new banking system, the Federal government would not have been able to float the great Liberty Loan issues that were sold at that time. Also, the Federal Reserve banks enabled the member banks to extend many loans to private industries, and so enable them to secure funds for expanding their production. By August, 1920, the Federal Reserve banks had extended credit to the amount of $3,390,000,000, and had outstanding Federal Reserve notes to the amount of $3,114,000,000.[3] It was the exhaustion of the reserve credit of the Federal Reserve banks which was one of the principal causes for the occurrence of the business crisis in 1920. The loans and investments of national and state banks increased nearly $20,000,000,000 from 1914 to 1920.[4]

When the depression of 1920 occurred, there was a rapid and great fall in the prices of all products; but the prices of agricultural products declined to a greater extent than did the prices of any other class of products. Our foreign trade balance declined in 1923 to less than 13 per cent of what it had been in 1920 but rose again in 1924. In 1923 the prices of minerals and manufactured goods recovered a considerable proportion of their

3 See Tables I and II of Appendix A, p. 271.
4 See Table III, Appendix A, p. 272.

1920 losses, but the foreign demand for our agricultural products continued to decline and the prices of these products remained relatively low following the 1920 depression.

Because of the high price of land, the heavy farm mortgages, and the low price of agricultural products after 1920, the farm owners, tenants, and laborers did not benefit from the high productivity of agriculture and the prosperity which was enjoyed by industry. Their incomes were reduced greatly. More extensive use of the farm tractor in the twenties resulted in greater productivity and the displacement of many farm laborers. The rural population actually decreased from 1920 to 1929. Few farmers were able to maintain their former standard of living, and pay their taxes and the interest on their indebtedness after 1920. Many of those who did retain their standard of living during this period did so by increasing their indebtedness. Most of the increase in farm mortgages and debts that occurred from 1920 to 1929 was because of losses sustained by farm operators.[5]

The improvement in industrial conditions in 1922 was the beginning of a period of the greatest peacetime increase in production and expansion of all major industries, except in agriculture and coal, that this country ever witnessed. This industrial upswing lasted until 1929 and was supported and propelled by the following powerful factors: (1) the greatest building boom of our history; (2) a strong foreign demand for our minerals and manufactured goods; (3) the development of many new industries and the expansion and reconstruction of many of the old ones; and (4) a rapid growth of instalment sales of consumers' goods. All of these factors increased the demand for the products of our forests, mines, quarries, mills, and factories.

Because of governmental restrictions placed on new private construction during the war and the feeling of prosperity caused by the war, a great shortage of homes and business buildings developed before the war closed. An after-the-war building boom had started before the occurrence of the 1920 depression, and with the coming of recovery in 1922 this boom revived and grew into the largest ever experienced by the country.

5 See Table IV, Appendix A, p. 272.

The new construction during the twenties included residences, apartments, office and business buildings, lofts, warehouses, factories and public construction of all kinds. It was a period of feverish construction of highways and new public buildings. The magnitude of the new construction of this period is indicated by Table V.[6] This table shows that construction contracts awarded in this country from 1922 to 1929 amounted to more than forty-two billion dollars. The construction not done under contract must have amounted to several billion dollars more. This fifty-billion-dollar new construction program furnished direct employment for many millions of laborers, and created a demand for enormous quantities of constructional materials of all kinds, such as cement, brick, lumber, structural steel, plumbing, and heating and electrical equipment. The industries which supplied these building materials expanded their productive capacities and employed millions of new laborers. While the building boom lasted, it was a great stimulator of general business.

As a result of the extensive purchases by American investors of foreign securities (both public and private) beginning with 1923, our favorable balance of foreign trade was kept on a high level up to 1929. From 1922 to 1929 this country's exports of goods exceeded her imports by about six billion dollars. Our excess exports consisted very largely of capital and manufactured goods. The large export demand for our goods furnished a good market for the products of our expanding manufacturing industries. Of course, American investors, through their purchase of foreign securities, furnished foreign nations the money with which to purchase our excess exports.[7]

The decade of the twenties was a period of the building of many new industries as well as one of the reconstruction and expansion of most of the old ones. The automobile industry's greatest period of development was after 1920. Since the war the radio, the rayon, and the talking-picture industries have developed. The character of the machinery and technical equipment used in practically all old industries has changed greatly

6 See Appendix A, p. 273.

7 See Table VI, Appendix A, p. 273, for foreign securities purchased by American investors during the twenties

since 1920. Practically all the major industries were extensively expanded from 1922 to 1929; the capacity of production of many of them was so increased by 1929 as to be greatly in excess of the market demand for their products. All this building of new industries and the expanding and reconstructing of old ones created a tremendous demand for new capital equipment and caused an expansion of those industries which produce such equipment. As a matter of fact, the so-called heavy goods industries which produce constructional and capital equipment were considerably overexpanded during this period. The growth of capital investments in business corporations from 1922 to 1929 is indicated by Tables VI and VII.[8] Table VI shows that thirty seven billions of dollars of new corporate securities were issued from 1922 to 1929; Table VII shows that the corporations making Federal income tax reports did not pay out as dividends seventeen billions of dollars of admitted net profits earned, but kept it as corporate surpluses. These two tables show that new corporate investments for this period were over fifty-four billions of dollars.

Production of consumers' goods for the domestic market expanded also in the twenties, and until 1928 the market demand for these goods rose almost as rapidly as did their actual production. The expanding market for consumers' goods was supported by the growth in instalment sales as well as by consumers' current money incomes. From 1922 to 1929 outstanding instalment sales notes increased about seven billions of dollars. This means that consumers purchased seven billions of dollars worth of goods in excess of their current money incomes. Also, the expenditure of paper profits made in speculating on the stock exchange during the stock market boom amounted to several billions of dollars; the expenditure of these profits had the same economic results as buying consumers' goods on credit. When the securities market crash came in 1929, the small speculators who had spent their paper profits owed banks and brokers on securities still held by them as much as, or more than, the paper profits previously spent. In this respect the stock market boom created an artificial demand for consumers' goods just as did the expansion of instalment sales.

8 See Appendix A, p. 273-74.

We might ask, Where did the funds come from with which to finance the industrial expansion boom of the twenties? During this period fifteen billions of new capital were required to finance the foreign trade and instalment sales alone. The building boom and the industrial expansion of the twenties needed the investment of about one hundred billions of dollars of new capital funds. The increase in the state and local government debt during this period demanded the investment of an additional eight billions of dollars.[9] Then, too, the stock market boom required the investment of another fifteen to twenty billions of dollars of new funds.[10] These new investment funds came from two sources: (1) the expansion of bank credit, and (2) the current savings of the nation.

During the 1920 depression, there was considerable liquidation of bank loans, but when the upturn in business came in 1922 the outstanding bank loans were much in excess of those outstanding in 1914, at the time the Federal Reserve System was organized. That the peacetime boom from 1922 to 1929 was partially financed by the extension of bank credit is shown by Table III.[11] The loans and investments of member banks increased from $34,251,000,000 in 1922 to $49,205,000,000 in 1929; this was an increase of fifteen billions of dollars of bank funds in use, but a large part of these funds went into the financing of industrial and building expansion and to the purchase of securities.

From 1922 to 1929 the profits of industrial and commercial business enterprises were larger than they had ever been in any peacetime period. Table VI shows that the corporations making income tax returns to the Federal government admit that from 1922 to 1929 they made nearly sixty two billions of dollars of net profits after all taxes were paid and after allowing more than thirty seven billions of dollars for depreciation and obsolescence. This table shows also that from year to year there was a large increase in the net profits of the reporting corporations. The part of these profits which was paid out as dividends

9 See Table VIII, Appendix A, p. 275.

10 See Table IX, Appendix A, p. 275, for information on the increase in the value of securities on the stock exchange for this period.

11 See Appendix A, p. 272.

to large income receivers was re-invested mainly in new capital. Also, in the twenties, the rental (urban and industrial), royalty, and interest incomes of large property owners increased greatly and were largely re-invested in new capital.[12] Therefore, the greater part of the new funds needed to finance the business expansion activities of the country came from the current savings of the large income receivers. Expansion of bank credit supplied only the small balance of the funds used for expansion purposes.

Notwithstanding the unprecedented national industrial developments prior to 1929, and in the face of the limitations which were placed on immigration into this country, a surplus supply of labor occurred long before the beginning of the depression. The fundamental cause of the development of the surplus labor supply was the displacement of laborers by automatic machinery in the production of goods and services. It was the greater use of powerized farm machinery which caused the migration of farm population to the cities. Greater use of automatic machinery in mines and factories reduced the number of laborers necessary to operate them. The industrial development was not great enough in the twenties to absorb all the laborers made available by the displacement process and the natural increase in the labor supply.[13]

If it had not been for the great building boom, the artificial favorable balance of trade, the building of new industries, and the expansion of old ones, and the increase in instalment sales, the industrial boom would not have been as great as it was. As long as the surplus savings of those who were receiving large incomes could be invested in new buildings, in new industries, in the expansion of old ones, in domestic and foreign securities, and in instalment notes, there was created a demand for goods about equal to the amount of the new investments. As previously pointed out, the purchase of foreign securities during the twenties enabled foreign countries to buy our goods in excess of the goods we bought from them. Also, the expansion of public debts of the states, counties, and municipalities in building new highways and new public buildings furnished a

12 See chap. iii for a discussion of the incomes of the large income receivers.

13 See chap. iii for a detailed discussion of this problem.

demand for goods somewhat commensurate with the amount of increased public indebtedness. The investment in new enterprises and in the expansion of old ones also created a demand for goods somewhat equal to the amount of the new funds invested. The investment in instalment notes made possible the sale of consumers' goods equal to the face of the notes. Also the investment in new office buildings, apartment buildings, and other buildings furnished a demand for a large quantity of constructional material. As long as large new investment funds created a demand for American goods of all kinds, industry continued to operate with an increasing production.

By 1928 it became apparent that most of our cities and industrial centers had overbuilt, and building permits declined rapidly. With the decline in construction, there was also a decline in the demand for constructional materials as well as for employment of laborers in the constructional industries. By the spring of 1929 it became evident that much of our investment in European securities during the twenties was unsound. Partly because of the shortage of new investment funds and partly because of the uncertainty in regard to the soundness of European securities, the American purchase of such securities declined rapidly. With the decline in the purchase of European securities our export trade also declined. Partly because of the letting down of activity in the building trade and the uncertain condition of the stock market, instalment sales were reduced in the spring of 1929.

As early as 1927 it became evident that many of our major industries had overexpanded and that an excess capacity of production existed in several of those industries. This was true in the automobile industry, the textile industry, the shoe industry, the steel industry, and in many others. The building of new factories and the revamping and expansion of old ones slackened in most industries by 1928. With the 1929 decline in new construction, foreign trade, and instalment sales, the market demand for our industrial products was reduced rapidly and there was a piling up of surplus goods in the market; the stock market broke, the money market became tight, and a general decline in prices and production followed. The falling off of industrial production brought more unemployment and a rapid

decline in the purchasing power of the consuming public, and further decline in both prices and production. Thus began the great depression of 1929.

CHAPTER THREE

HOW INCOME AND EMPLOYMENT WERE DISTRIBUTED PRIOR TO 1929

THE problem of the distribution of the national money income may be examined either from the standpoint of determining the degree of equality or inequality of individual or family incomes, or from the standpoint of its division among the factors of production, such as profits, rents, interest, and wages. The distribution among individuals and families is the important question from the standpoint of social welfare and national economic progress. But, because of the great unequal ownership of productive property and the concentration of business management in the hands of a small group of the income receivers, the division of the national income among the factors of production has a tremendous influence on the equality or inequality of the division of the income among individuals.

Let us consider the division of the national money income among income receivers during the twenties, for the purpose of ascertaining the facts in regard to the personal inequality in its division, and of finding the recent trend in its distribution. Did the inequalities in personal incomes become greater or less during that period? Then let us investigate the trend of the division of income among the factors of production for the same period, to throw light on the causes for the trend in the personal distribution of income.

It is generally believed that, during the past fifty years, the bulk of the nation's productive wealth has been concentrated into the hands of a small percentage of the population, and that the great mass of the people now possess only a small proportion of its productive wealth. It is generally assumed also that, while the money income of the nation has grown rapidly, a

larger and larger percentage of it has gone into the hands of a small percentage of the population. Let us now see what are the facts.

Reliable data in reference to the direct ownership of property in this country are rather meager and unsatisfactory; but the data published by the United States Treasury Department in reference to the incomes of those who make Federal income tax reports, supply valuable information as to the distribution of the national money income; these income statistics also furnish indirect information in regard to the ownership of productive property. Many studies of these individual income figures have been made by various foundations and individuals; a compilation of them, together with data gathered from other sources, has been made in Tables X and XI,[1] covering the period from 1922 to 1929.

Table X shows that those reporting tax returns to the Federal Bureau of Internal Revenue in the higher income classes received much greater increases in their incomes from 1922 to 1929 than did those in the lower income classes. This was true both for the average annual incomes received by those in each income class, as well as for the total income received by each group or class. Those reporting incomes above $50,000 in 1922 received an average income of $126,000, and in 1929 they received an average income of $181,000. The total income of those receiving $50,000 and above increased 241 per cent from 1922 to 1929. The total income of those receiving between $10,000 and $50,000 increased 79 per cent during the same period, and the income of those receiving between $5,000 and $10,000 increased 67 per cent, while the total income of those reporting less than $5,000 actually decreased. Also Table X indicates that the total income of those with incomes too low to report did not increase from 1925 to 1929.

Those in the higher income classes received the larger part of their income from dividends and other property income such as rents, interest, royalties, etc. In 1929 those receiving incomes above $50,000 received only 9.69 per cent of their total income from salaries; the other 90.31 per cent was received from dividends and property. Those with incomes between $10,000 and

1 See Appendix A, pp. 276-80.

$50,000 received 28.19 per cent of their incomes from salaries and 71.81 per cent of it from dividends and property. Those with incomes between $5,000 and $10,000 received 45.86 per cent of their incomes from salaries and 54.14 per cent from dividends and property. Those reporting incomes of less than $5,000 received 58.81 per cent of their incomes from wages and salaries and 41.19 per cent from dividends and property. Those with incomes of $50,000 and above received in the aggregate more money from dividends alone than those with incomes of less than $5,000 received altogether, though there were only 38,000 individuals having incomes of $50,000 and above and there were 3,012,000 individuals reporting incomes of below $5,000.

Table XI indicates an increase in the total national income of about 33 per cent from 1922 to 1929, and it shows also that the larger part of that increase in the national income went to the comparatively small number of those who have large incomes. The table indicates that from year to year during the twenties an increasing percentage of the national income was paid to the small number of high income receivers, and that the mass of low income receivers got a progressively smaller percentage of the national income. In 1922 those receiving $10,000 and above per annum constituted only 0.45 per cent of the total income receivers and received 10.48 per cent of the total national income; and in 1929 this group of income receivers constituted only 0.76 per cent of the total income receivers but received 17.83 per cent of the total national income. In 1922 those receiving incomes of $5,000 and above constituted 1.44 per cent of the total income receivers and got 15.59 per cent of the national income; and in 1929 this group constituted 2.34 per cent of the total income receivers, and received 24.29 per cent of the total national income. In 1925 all those making Federal income tax reports constituted 9.52 per cent of the total gainfully employed, and received 33.01 per cent of the national income; and in 1929 this group constituted 9.15 per cent of the total gainfully employed and received 36.91 per cent of the national income.

Looking at the problem from the side of the low income receivers: in 1922, 83.58 per cent of those gainfully employed

received only 58.99 per cent of the national income; in 1925, 90.48 per cent of those gainfully employed received only 66.99 per cent of the income; in 1929, 90.85 per cent of those gainfully employed received only 63.9 per cent of the income.

The table shows that in 1922, 37.66 per cent of the total population was reported as gainfully employed; in 1929, 36.30 per cent of it was so reported. From the standpoint of distribution of the national income in proportion to total population, the table shows that 6.18 per cent of the population in 1922 received 41.01 per cent of the national income; in 1925, 3.60 per cent of it received 33.01 per cent of the national income; and, in 1929, 3.32 per cent of it received 35.91 per cent of the national income. This same table shows that 0.85 per cent of the population in 1929 received 24.29 per cent of the national income, and that 0.31 per cent of it received 17.83 per cent of the income.

A close study of these two tables furnishes convincing evidence that during the twenties practically all the increase in the national money income went to those who received incomes large enough to make income tax reports to the Federal government, and the larger the size of the individual income the more rapidly did it increase from year to year.

A study of the sources of the incomes of the high income receivers given in Table X leads to the conclusion that the principal cause for the great growth in the size of these incomes during the twenties was the rapid increase in that portion of the incomes derived from profits and property. An examination of the trend of wages and profits during this same period shows that from year to year a decreasing percentage of the national income was paid out as wages and an increasing percentage of it was paid out as profits, interest, rents, royalty, and other property payments. The most reliable data in reference to the trend of wages in relation to net production relate to the manufacturing industries, which employ a very large percentage of the wage-earners of the nation.

Table XII[2] indicates that in 1929 the value of the net production (value added by manufacture) of the manufacturing industries was 73.9 per cent greater than it was in 1921, but that the

2 Appendix A, p. 281.

number of wage-earners employed in 1929 was only 27.2 per cent larger than in 1921. The value added by manufacture per laborer employed in 1929 was 36.7 per cent larger than it was in 1921, while the annual wage paid each laborer in 1929 was only 11.3 per cent more than was paid in 1921. In 1921, 44.7 per cent of the value added by manufacture was paid out as wages to laborers, whereas in 1929 the laborers received as wages only 36.4 per cent of the value added by manufacture; this was a decrease of more than 18 per cent in the part of the net production of the industry received by the laborers in 1929, as compared with the portion they received in 1921. Also, the margin between the value of finished products and the value added by manufacture became much larger from 1921 to 1929 in the manufacturing industry. In 1921 the value added by manufacture constituted 41.99 per cent of the value of the finished products, whereas in 1929 the value added by manufacture was 45.3 per cent of the value of the finished products. These figures tell the story of why the manufacturing industries were very profitable from 1921 to 1929. The margin between the cost of the raw materials used and the finished products turned out was considerably widened and the labor cost of each unit of product was drastically reduced, while the volume of production was increased greatly.

The year 1921 might be considered a depression year in business, and therefore not a suitable one in every respect to compare with 1929, but a comparison of the figures in this table for 1923 with those of 1929 will give the same general results as indicated in the foregoing paragraph. From 1923 to 1929 there was no increase in the number of laborers employed in the manufacturing industry (an increase of less than one-tenth of 1 per cent), and an increase of less than 5 per cent in the wages per laborer. But in 1929 the value added by manufacture per laborer was 22.4 per cent greater than it was in 1923 and the total value added by manufacture was 23.4 per cent greater than in 1923. The labor cost per unit of net production in 1929 was 14.1 per cent less than it was in 1923, and the margin between the value of the raw materials and the value of the finished products (per cent value added by manufacture) increased from 42.6 per

cent in 1923 to 45.7 per cent in 1929. From 1923 to 1929 the prices of manufactured goods declined less than 1 per cent.

The Bureau of Census figures for producing mines and quarries show that from 1909 to 1919 there was a decrease of 4.5 per cent in the number of wage-earners employed in these industries; for the same period there was an increase of 107.6 per cent in the total wages paid and a rise of 111.5 per cent in the value of the products.[3] From 1919 to 1929 these industries showed a decrease of 11.3 per cent in the number of laborers employed and a decrease of 8.2 per cent in the total wages paid, but an increase in the value of the products of 2.4 per cent. In each period the number of laborers employed was decreased, and the margin between the value of the goods produced and the amount of money paid as wages was widened. While the rate of wages paid laborers was a little more than doubled from 1909 to 1919, the wage rate per laborer was increased less than 4 per cent from 1919 to 1929. The horse power used by these industries increased 44.8 per cent from 1909 to 1919, and 42.2 per cent from 1919 to 1929.

The average weekly wages of all laborers in 1923 was $26.61, and in 1929 the average was $28.54; this was an increase in the average weekly wages of laborers, from 1923 to 1929, of 7.3 per cent.[4] During the same period the index of industrial production showed an increase of 18 per cent and the general price level in 1929 was a little lower than in 1923.[5] The national money income at the same time increased more than 30 per cent. It is clear from these figures that the wage-earners as a whole did not receive an increase in their purchasing power in proportion either to the increase in the national money income or the increase in the value of the goods and services produced.

All available statistics in regard to the amount and the rate of business profits during the twenties indicate that it was a period of very large profits with a rapidly increasing rate from year to year. Table VII,[6] on corporate income from 1921 to 1929, shows that the corporations compelled to make corporation

3 See Table 667, *Statistical Abstract of the United States*, 1934, p. 656.
4 See Table 341, *ibid.*, p. 309.
5 A. B. Adams, *Trend of Business*, 1922-1932, p. 16.
6 See Appendix A, p. 274.

income tax reports to the United States Treasury Department increased in number from 383,000 in 1922 to 509,000 in 1929. According to this report, their aggregate net profits (after all taxes and other deductions were made) were $5,183,000,000 in 1922, and in 1929 they were $10,677,000,000; this was an increase of more than 100 per cent in the aggregate net profits for all reporting corporations. The average net profits per reporting corporation in 1922 was $13,532, while in 1929 the average net profits per corporation were $20,976; this was an increase of 55 per cent in net profits per corporation for this period. It should be observed from this table that in 1929 the depletion and depreciation deductions before arriving at net profits were almost twice as great as were these same deductions in 1922. The rate of increase in business profits in the twenties appears to have been more than three times that of the rate of increase in physical production, and almost ten times that of the rate of increase in wages.

Notwithstanding the great building and industrial boom, which brought about a phenomenal increase in physical production from 1922 to 1929, there developed a surplus supply of labor in the United States. The occurrence of a surplus supply of labor during an industrial boom was something new for this country. But at the height of the period of prosperity in 1928 and 1929 about two million employable laborers were unemployed. This surplus of labor appeared in the face of the fact that there was little immigration into this country during this decade. It was caused by the rapid displacement of laborers by powerized automatic machinery in practically every field of production. During this period nearly every business enterprise engaged in producing goods was able to increase its production substantially and at the same time to decrease the number of laborers employed. This displacement of labor by machinery made it impossible for the productive industries to absorb the natural increase in the labor supply of the country without greatly reducing the laborers' hours of work a week. The building boom and the development of new business enterprises and expansion of old ones absorbed many of the laborers displaced by machinery in agriculture and in the mining and manufacturing plants, but laborers were displaced too rapidly for all

the natural increase in the supply of labor to be absorbed by the expanding industries.

The United States census figures show that the population of the country increased 16.1 per cent from January 1, 1920, to April 1, 1930. For this same period those enumerated as gainfully employed increased 17.3 per cent. However, the percentage of the population ten years of age or over gainfully employed decreased slightly during this period; 50.3 per cent of this portion of the population was enumerated as employed in 1920, but in 1930 only 49.5 per cent of them were counted as employed. Relatively, the employed females gained on the males: in 1920, 78.2 per cent of the males and 21.1 per cent of the females were employed; in 1930, 76.2 per cent of the males and 22.0 per cent of the females were enumerated as employed.

Table XIII[7] indicates that during the decade of the twenties both the number and percentage of workers engaged in the agricultural, the forestry, and in the fishing and the extractive industries declined: in 1920 these industries employed 28.8 per cent of all the workers, but in 1930 they gave work to only 23.4 per cent of them. There was an absolute increase in the number of laborers employed in the manufacturing and mechanical group of industries, but the percentage of the total number of laborers employed by this group of industries declined during the decade from 30.8 per cent to 28.9 per cent. As already indicated, all the increase in the absolute number of workers in this group of industries was due to the growth in the number employed in the building trades; in the manufacturing industries proper there was an actual decrease in the number of laborers employed.[8] The transportation and communication group of industries showed a slight increase in the number of laborers employed in 1930 as compared with 1920, but practically no increase (only one-half of 1 per cent) in the percentage of the total number of laborers employed by them. Contrary to popular belief, there was no great increase in the absolute number of employes in public service, and no increase at all in the percentage of the total number of workers of the country thus employed.

7 See Appendix A, p. 282.
8 See Table XII, Appendix A, p. 281, for employment from 1919 to 1929.

The greatest increases in the absolute numbers, as well as in the percentage of laborers employed during this period, occurred in trade, professional services, domestic and personal services, and clerical occupations. There was an increase of nearly 2,000,000 laborers employed in trade or commerce; in 1920 trade employed 10.2 per cent of all the laborers, and in 1930 12.5 per cent. There was an increase of more than 1,000,000 people engaged in professional services, an increase of more than 1,500,000 in domestic and personal services, and an increase of almost 1,000,000 in clerical occupations. In 1920, 13.3 per cent of all the gainfully employed were engaged in professional, domestic, and personal services; in 1930 the percentage had increased to 16.8. Clerical occupations employed 7.5 per cent of all workers in 1920, and 8.2 per cent in 1930. During this decade there was a great increase in the number of women employed in public service, professional and personal service, and in the clerical occupations.

These occupational statistics indicate that during the boom twenties, a large proportion of the laborers who were displaced by automatic machinery in the commodity-producing enterprises (agriculture, mining, and manufacturing) were absorbed by the new manufacturing industries and the building industries, but that these commodity-producing industries absorbed practically none of the natural increase in the labor supply of the country at that time. Trade and commerce and the service industries (including clerical occupations) during that period absorbed a large part of the natural increase in the labor supply of the country. But, however, the increase in employment in new industries, in the building occupations, in trade and commerce, and in the service industries did not keep pace with the displacement of laborers by machinery in the commodity-producing enterprises together with the natural increase in the supply of labor due to the growth in population. The result was the two million surplus laborers at the height of the boom.

There was a slight reduction in the weekly hours of laborers in many enterprises during the twenties. The total surplus supply of labor would have been slightly greater than it was if it had not been for this slight reduction in work hours in some industries. But it is evident that the work hours were not

reduced sufficiently to prevent the occurrence of a surplus supply of labor even under conditions of the most intense industrial prosperity.

The growing inequality in the distribution of the national money income and the displacement of laborers by automatic machinery had a tremendous influence upon the operation of our industrial system. In the next chapter the connection between the maldistribution of the national income and the industrial breakdown of 1929 will be discussed.

CHAPTER FOUR

WHY PRE-DEPRESSION CHANGES UPSET OUR ECONOMIC BALANCE

THE Brookings Institution in its volume, *America's Capacity to Produce*, states that the mining and manufacturing industries in 1929 utilized between 80 and 83 per cent of the practical plant capacity of production—in other words, from 17 to 20 per cent of the plant capacity was not used. This report further concludes, however, that the margin of unutilized plant capacity was not, in general, increasing in these industries for the thirty-year period ending in 1929.[1] To my mind, the report does not present sufficient statistical evidence of idle plant capacity in these two major industries prior to 1925 to warrant the conclusion that idle plant capacity in them was no greater in 1929 than thirty years previous, or even fifteen years previous. The evidence presented of idle plant capacity prior to the World War is meager and, in the manufacturing industries, is confined largely to industries which produce raw materials and semi-finished goods. Practically none of the earlier figures of idle plant capacity in manufacturing given in the study refers to the consumption goods industries, such as the shoe, the automobile, the radio, the clothing, and the furniture industries.

However, assuming that the actual idle plant capacity in the mining and manufacturing industries as a whole was no greater in 1929 than in 1914, it does not follow that, in proportion to the current purchasing power of American consumers, the actual excess productive capacity in these industries was not greater in 1929 than in 1914. From 1922 to 1929 there was a great build-

1 Brookings Institution, *America's Capacity to Produce* (Washington, 1934), pp. 415, 421.

ing boom and a period of great industrial expansion. Also during that time there was a large favorable balance of foreign trade financed by American loans, and a large expansion of instalment sales. All of these factors created a great demand for the products of our mines and factories. But the boom demand for the goods of our manufacturing industries was by nature temporary, and in a large measure artificial. If the idle plant capacity in the mining and manufacuring industries, notwithstanding the artificial boom demand for their products, was 20 per cent in 1929, what would it have been without the stimulation of the boom? Certainly, it would have been much greater than it was prior to the war, when there was no such boom. Also, the surplus capacity of production in manufacturing in 1929 was much more modern and effective than the surplus productive capacity of 1914, and was confined more largely to the consumption goods industries than at any previous time.

According to J. B. Say's well known so-called *law of the markets*, there cannot be a general oversupply of goods or a general shortage of market demand for goods. Say states that the general market demand for goods is always equal to the general market supply of goods *because* the creation (production) of any quantity of goods also creates an effective demand (purchasing or exchange power) equal to the value (price) of the goods produced. Therefore, he holds, there never can be a general oversupply of goods in the markets. Assuming that no fluctuating bank credit is used in paying for goods bought and that a stable price level is maintained, Say's so-called law of the markets would be true *if* all the purchasing power created by the production of all goods were distributed in such a manner that those who received this purchasing power immediately used all of it to purchase all the various classes of goods produced.

Most students of business cycles recognize the fact that extensive and fluctuating use of bank credit in business vitiates Say's law for short periods of time.[2] It will be shown in this book that, under present industrial conditions, because of the manner in which the national money income (purchasing power created by production) is distributed and used, the mass of

2 Adams, "Economics of Business Cycles," pp. 95-101.

consumers generally are unable to purchase (at prevailing prices) all the consumer's goods that are produced. It will be shown further that this shortage of consumers' purchasing power may and does result in a general market surplus (oversupply) of all classes of goods. In short, Say's conclusion that there can be no general oversupply of goods in the markets is fallacious as applied to the present operation of our industrial system.

Our industrial system was greatly out of balance in 1929. Long before the stock market crash of that year, many of the new apartment and business buildings constructed were unoccupied because tenants who could pay the rents asked could not be found. Practically none of the consumption goods manufacturing industries were operating at or near full capacity because a market for all the products they were able to produce could not be found. There was no shortage of consumers' goods of any kind, but a surplus market supply in practically every one of them. The lack of balance in our industrial system consisted primarily of an inadequacy in the market demand for the consumers' goods which our industries were capable of producing, caused by the fact that too small a percentage of the national money income was used to purchase consumers' goods, and too large a percentage of it was invested in new capital equipment for further production. When this happens over a long period of time, a surplus capacity of production in the consumers' goods industries will inevitably result.

Under conditions of stability in the outstanding bank credit and a constant price level, the total current national money income is large enough to purchase all the current net production of the industrial system; or under stable prices, the current national money income is large enough to purchase finished goods equal in value to the value of the current net production of all industry. This is true because the total national money income is derived from the net production of, or net value created by, all business enterprises; and when all the money received for the net value created is paid out by business enterprises as money income to those who furnish the factors of production, the national money income must equal the value (in dollars) of the net production of the industrial system.

When a stable price level is maintained, there can be no general shortage of current money income to purchase finished goods equal in value to the current net production of all industry. Of course, the different kinds and classes of finished goods of industry must be produced in the exact proportion that they are to be bought by the purchasers, if a market for all the goods is to be found. But if the part or portion of the national income saved and invested in new capital results ultimately in producing a quantity or supply of consumers' goods and services with a value in excess of that part of the national money income which is used for the purchase of such goods and services, there will develop a market surplus supply in them. This is precisely what happened in the United States in the twenties.

Largely because of the cumulative growth in the unequal distribution of the national money income among the income receivers of the nation, there developed a large surplus of productive capacity in the consumers' goods industries as well as a surplus of those goods in the markets in 1929. These surpluses were due to the fact that the productive capacity and actual production in the consumers' goods industries grew more rapidly than that part of the total money income used for the purchase of such goods. The enormous incomes, savings, and investments of the few very rich were responsible mainly for the great growth in the productive capacity of the consumers' goods industries. On the other hand, the relatively and actually inadequate incomes of the mass of income receivers were responsible for the inadequate market demand for consumers' goods which were or could be produced.

In the previous chapter of this book the great inequality in the distribution of the national income was pointed out.[3] The Brookings Institution, in its study, *America's Capacity to Consume,* states that on the side of the high family incomes, 0.1 per cent of the families of the nation received 12.7 per cent of the total money income received by families; and that, on the side of the low family incomes, 42 per cent of the familes received only 12.9 per cent of the total; in other words, 0.1 per cent of the families at the top of the income scales received practically the same percentage of the total national income as 42.

3 See p. 38.

per cent of the families at the bottom of the scale.[4] It is estimated that 85 per cent of the savings of the nation were made by less than 10 per cent of the population, and that 80 per cent of the population made not more than 2 per cent of the savings.[5] In the previous chapter, figures were given which indicate that during the twenties, from year to year, there was a rapid increase in the percentage of the national income which was saved and re-invested.[6] The Brookings Institution concludes also that there was a persistent increase in the percentage of the national income saved up to 1929, and that the savings for that year amounted to nearly 20 per cent of the total national income.[7]

The receivers of the largest incomes were able to spend only a small portion of their current incomes to satisfy all their wants for goods and services; the only practical thing that could be done with the bulk of these large incomes was to re-invest them in new capital for further production. On the other hand, the great mass of consumers (at least 70 per cent of them) did not have incomes large enough to enable them to satisfy all of their most urgent desires for goods and services. Moreover, a large percentage of consumers had such small incomes that they were unable to purchase enough goods and services to satisfy all of their actual needs to maintain health and physical comfort. While the comparatively small number of rich and ultra-rich were in a position not to desire any more consumers' goods and services than they were purchasing already, more than half of all consumers did not have enough money income to purchase as much as half the goods and services they actually desired; not more than 20 per cent of our people in 1929 were able to purchase all the goods and services they considered reasonably desirable. The American people would have purchased more than twice the amount of consumers' goods and services purchased in 1929 if the mass of consumers had possessed enough purchasing power to satisfy all their current economic wants. Of course, in 1929 there was neither enough productive capacity nor national money income to have enabled all of our people

4 Maurice and Laura Polk Foundation, Digest of *America's Capacity to Consume*, 1935, p. 42.
5 *Ibid.*, p. 49.
6 See pp. 40-41.
7 Digest of *America's Capacity to Consume*. p. 50.

to satisfy all their current wants for consumption goods and services. But certainly, the *surplus* productive capacity and the market surplus production of these industries was due to the inadequacy of purchasing power (income) in the hands of the mass of consumers, rather than to their lack of desire for additional goods.

There was, as previously indicated, an enormous increase in both production and productive capacity in all industries prior to 1929. This increase in industrial productive capacity, we already know, was due partly to the widespread introduction of powerized automatic machinery in production, but mainly to the rapid increase in new capital investments in industry. It has been pointed out also that the stockholders in industrial corporations received most of the benefits from the labor economies that resulted from the use of automatic machinery; we found, too, that the income from property gained much faster than the income from labor during the twenties. These were the principal reasons for the exceptional rise in the incomes of the ultra-rich at that time. Into the hands of the very wealthy flowed an increasing stream of surplus funds which were used largely as investments in new capital for industrial enterprises.

All capital investments are made either for the purpose of aiding in the production of goods or services for human consumption (consumers' goods) or for the purpose of aiding in the production of capital goods which in turn ultimately will be used to aid in the production of consumers' goods. The sole objective of all economic endeavor is to produce goods and services that will satisfy human wants. When a large part of the productive activities of industrial society is directed toward making new productive capital equipment, as it was in the twenties, a great increase in the number and size of productive enterprises of all kinds will be inevitable; a rapid and constant increase in the total production of both consumers' and capital goods will result. When all these new enterprises fulfill their one objective of producing or aiding in the production of additional finished consumers' goods, inevitably the rate of increase in the production of finished consumers' goods will exceed the rate of increase in general (net) production. Such an increase in the finished consumers' goods industries occurred in 1928 and 1929.

On the one hand, consumers' money incomes (the part of the national money income used to purchase consumers' goods) increased at a much slower rate than did the annual net production or the total national money income. On the other hand, the consumers' annual money incomes increased at an appreciably slower rate than did the annual production of finished consumers' goods. Therefore, the rate of growth of the productive capacity of the consumers' goods industries was a great deal faster than the rate of growth of consumers' money incomes.

The relative decline in the market demand for goods in general in 1929 was due primarily to the insufficiency in the market demand for existing consumers' goods. If there had been a sufficient demand for all the consumers' goods that could have been produced, and an adequate demand for all the new residences and apartments constructed, there would have been a demand for all other goods that could be produced sufficient to have kept all industries operating practically at plant capacity. The slackening in the demand for new capital goods, raw materials, and other producers' goods in 1929 resulted from the development of the excess capacity of production in the consumers' goods industries.

When there is a surplus capacity of production in the consumers' goods industries, there will be no further demand for new factories in those industries, just as there will be no additional demand for new buildings which cannot be rented. A decline in the demand for new capital goods to be used in the consumers' goods industries will cause a falling off in the demand for the commodities of the producers' goods industries, just as a decline in new construction will cause a slackening in the demand for producers' goods used in construction. A decrease in the demand for producers' goods will result in a surplus capacity of production in the industries making such goods. There will then be little or no demand for new factories in the producers' goods industries. Therefore, whenever there is a surplus productive capacity in the consumers' goods industries, or a surplus supply of such goods, the producers' and new capital goods industries will evidence a surplus capacity of

production. Thus occurred the decline in general industrial production in 1929.

In the twenties, many of the small income receivers borrowed some of the investment funds of the rich and mortgaged a part of their own small future incomes to pay the interest and principal of these loans. Many farmers increased their farm mortgages in order to secure funds with which to live; many small home-owners borrowed to buy or build their homes; a large percentage of the small income receivers bought furniture, refrigerators, radios, automobiles, and other semipermanent consumption goods on instalment credit, agreeing to pay for these goods on a weekly or monthly basis with a high rate of interest and carrying charge. This instalment paper was sold to finance companies which secured the funds for operation from investors or banks. These borrowings by small investors increased their immediate expenditures and standard of living, but lowered their future expenditures and standard of living. Their total purchases of consumers' goods were reduced by the amount which they paid as interest on borrowed funds. The borrowings by states and local governmental units prior to 1929 increased the tax burden on the low income receivers, and thus reduced their future purchases of consumers' goods. All the loans to small income receivers and to governmental units increased current production and sales, but limited future sales of consumers' goods, and therefore limited future production.

The forces which upset our industrial balance in the twenties may be summarized as follows: While on the one hand a deficiency in consumer's purchasing power developed, on the other hand a surplus of investment funds occurred. The supply of new investments funds during this period was not only large enough to make possible extensive additions to our industrial capital equipment and to finance the great building boom, but there were also sufficient funds to finance our foreign trade, state and local governmental borrowings, instalment sales, farm mortgages, and the stock market boom, and still have left large surplus investment funds. It is true that the expansion of bank credit during this period supplied a part of the new investment funds, but only a small part of them. The cash savings of individuals and corporations reposing in banks as

cash time deposits in 1929 amounted to more than half of the total expansion of bank credit from 1922 to 1929. In 1928-29 many corporations and wealthy individuals were unable to find suitable places in which to invest their surplus incomes, so they deposited them in banks or loaned them to brokers on the stock exchange; more than six billions of dollars of private funds were thus loaned in 1929. As the building boom receded and the purchase of foreign securities fell off in 1928-29, the surplus private investment funds backed up in our banks. Demand for goods of all kinds decreased and production declined; all the consequences of the depression followed.

We have seen, first, that the concentration of a large percentage of the national money income into the hands of a very small percentage of the income receivers of the nation brought about an excess of savings and investments and a deficiency in spending, and second, that this disproportion between saving and spending upset our economic balance. This small percentage of the population received a progressively larger percentage of the national income because: first, a comparatively small percentage of the people from year to year acquired ownership of and control over a larger and larger percentage of the productive property and capital of the nation and received a larger and larger share of the national income therefrom; and, second, up to 1929 the factors of production consisting of property (land and capital) and management acquired a progressively larger percentage of the national income, and labor, the other factor of production, received a correspondingly smaller percentage of it.

Many answers have been given to the question, how or why a comparatively few people acquired ownership or control of a large part of the productive property of the nation. There are those who account for the inequality of property ownership largely on the grounds of the differences between individuals as to intelligence, initiative, energy, ambition, thrift, and other qualities which may cause people to produce and save. They claim that these differences among individuals account for all, or practically all, the inequalities in the present ownership of property and the distribution of income. They point out that many people would not have enough judgment, initiative, and

thrift to retain a fortune if it were given to them. On the other hand, there are those who account for the great inequality largely on the grounds of the unequal opportunities and privileges secured by the few over the masses of people. They claim that most large individual or family fortunes were acquired either as result of fortuitous circumstances or special privileges and advantages secured by the accumulators, rather than primarily as a result of superior qualities possessed by the rich. They point to the fact that individuals who acquire or inherit great wealth possess a tremendous advantage over the masses of people who acquire or inherit little or no wealth; the rich possess such relative advantages, they point out, because, without very much effort on the part of the wealthy their great wealth and income beget more wealth.

Without question there is much truth in both these more or less conflicting views as to the causes of the great inequality in the ownership of wealth and income. Certainly, different people are unequal in their productive, acquisitive, thrift, and spending qualities and characteristics, and, because of these personal differences, equal accumulation and ownership of property would be an impossibility. If all property were arbitrarily divided equally among all the people, it would not remain so very long: some would save part of their income and acquire more property, others would sell their property and spend the money received for it. Nevertheless, few of the large fortunes were actually earned by the original accumulators solely as a result of their superior economic abilities and qualities; the majority of the large fortunes were founded largely through fortuitous circumstances or special economic advantages enjoyed by the accumulators. It is true also that the rich, in accruing future incomes and in accumulating additional property, possess powerful advantages over those who do not inherit or acquire property. In short, personal differences in individuals account for a considerable amount of the unequal ownership of property in all countries permitting private ownership of property and freedom of contract; but the concentration of the bulk of the productive wealth of the United States in the hands of a very small percentage of the people was due in large part to special economic privileges and advantages acquired or possessed by

the accumulators and possessors of the great fortunes over the non-owners of productive wealth. What kind of special advantages and privileges were acquired by most of those who became very wealthy?

Many of the large fortunes of the nation were founded as a result of the fortuitous acquisition of a large amount of urban real estate in our growing cities by the founders. Others were due to the acquiring of rich mineral lands or mineral rights. This is true of many oil men of today; it was true also of the silver and the copper fortunes of former days. Even many farmers formerly became wealthy by acquiring large areas of agricultural or grazing lands. The accumulation of large fortunes from the ownership of natural resources was made possible by the increases in site value, rentals and royalties of the resources owned; the increase in the value of the land and natural resources was due to the growth and expansion of the needs of the community, and not to any economic services performed by the owners of the property. The Astor fortune is a good example of one made from the ownership of urban real estate which increased in value because of the growth of New York City. Also, great fortunes were made from the development of the railroads in this country; among such fortunes were those of the Goulds, the Vanderbilts, the Hills, and the Harrimans. They were made partly as a result of government donations of land to the railroads, partly as a result of the economic growth of the country, and partly as a result of financial manipulation in acquiring control over the voting shares of stock of the railroads.

Most of the massive fortunes of America today, however, were accumulated as a result of the acquiring of ownership or control of a large proportion of the shares of common stock in our giant industrial, financial, and mercantile corporations by a few individuals. In a great number of instances, through holding companies, mergers, and financial reorganizations and manipulations, a comparatively few individuals, with a relatively small amount of money originally invested, acquired control over or ownership of the voting stock of a large proportion of the giant business corporations. They then used the money already invested by the bondholders, preferred stockholders,

and others, to finance the enterprises, and when the businesses became highly profitable, the few big common stockholders obtained the bulk of the large profits; though in many cases the common stock shares of our giant corporations did not represent an investment of a single dollar by the original owners. The Morgan, the Duke, the Ryan, the Doherty and many other fortunes are good examples of those originating partly from the acquisition of financial control of big corporate businesses. Also, many large fortunes have been accumulated as a result of comparatively modest original investments in business enterprises in new and growing industries. Many of the original enterprises in new industries have made enormous profits upon the actual capital invested. In some cases the high profits were due to temporary competitive advantages of the enterprises; in others they were due to monopolistic advantages gained. The Rockefeller, the Carnegie, and the Ford fortunes are good examples of those built from small original investments in new but highly profitable industrial enterprises.

Once an individual accumulates an enormous fortune, it is comparatively easy for him to increase the size of that fortune. Because of the hugeness of the income from large fortunes, the receivers are unable to spend more than a small portion of it. They have but one choice: that is, to re-invest most of their current income so that their future incomes will become still greater. The astounding rapidity at which a modest sum of money invested at a compound rate of interest over a series of years will grow into a large sum is familiar to everyone. For these reasons the large fortunes transmitted from one generation to another tends to become larger. Truly, wealth begets wealth, and the rich become richer.

The fact that for several years prior to 1929 a larger and larger share of the national income was paid out as profits and income on property interests, and a smaller and smaller share of it as wages, was a powerful special advantage gained by the rich; such a division of the national income made their fortunes and incomes grow at a more rapid rate. If all the productive property interests of the nation were equally divided among all families, the relative division of the national income between wage-earners and property-owners would have little influence

in the distribution of the national income. The total income from property then would be distributed equally among all families, most of which would have one or more wage-earners. But when the bulk of the productive property is concentrated in the hands of a small percentage of the people, and the great mass of them depend wholly upon wages and salaries for their incomes, the ratio of division of the national income between wages on the one hand and profits and property income on the other, has a decided effect on the equality or inequality of the personal distribution of the national income. An increase in the share going to profits and property causes a relative rise in the incomes of the rich (high income receivers), and a relative fall in the incomes of those who depend on wages (the low income receivers). The relative decrease in labor's share of the national income during the twenties enabled the rich to increase their incomes and wealth much faster than otherwise they could have done, and helped to prevent the mass of consumers from buying all the consumers' goods that could have been produced. It was high industrial profits and greater property incomes that hastened the breakdown in our industrial system in 1929.

Why did profits increase out of proportion to the increase in the national income prior to 1929? Why did productive property incomes (rents, royalties, interest, etc.) also receive a proportionally larger share of the national income at that time? Why did labor (wages) receive a smaller and smaller share of it?

CHAPTER FIVE

REASONS FOR LAG OF WAGES BEHIND PROFITS AND PROPERTY PAYMENTS

THE rate of industrial profits increased greatly during the twenties mainly because the prices of industrial goods were not lowered in proportion to the decline in the cost of production per unit of product; in other words, the margin between prices and cost of production was widened constantly during this period. Cost of production in practically all manufacturing establishments was lower materially because (1) of relatively lower prices of raw mineral and agricultural products; (2) of increased volume of production of each enterprise; and (3) of lower labor cost per unit of product. Prices of manufactured products were not reduced in proportion to the decline in the cost of production (1) because of the strong market demand for these products and (2) because of the growing monopolistic price control policies developed in the various industries.

Table XII[1] shows that the margin between the total value of manufactured products and the total cost of the raw materials used to make these products, constantly widened from 1919 to 1929. The prices of agricultural products used as raw materials by manufactures were much lower relatively than they were prior to the war. Because of the overdevelopment of productive capacity in the mining and mineral industries during the war, the prices of many of these products were much lower relative to the prices of manufactured goods than they were before the war. This, of course, was less true of iron and steel products where there was monopolistic control of prices, than of most of the other metals and minerals. The lower raw material cost was an important factor in lowering the cost of production in the manufacturing industry from 1920 to 1929.

1 Appendix A, p. 281.

An increase in the volume of production of a manufacturing plant which is operating below capacity of production will lower the unit cost of production in that plant. The capital and overhead costs will be raised only slightly as a result of the greater volume of production, and the direct operating expenses will not rise in proportion to the increase in output or production. Also, the building of new, larger, and more modern manufacturing plants, with automatic machinery and standardized production methods, brought about a lower factory cost of production as well as an increase in the volume of production; the modernization of old factories had the same influence on both cost of production and volume of production. The period of the twenties, as shown in chapter two, was one of a rapid increase in the volume of production in the manufacturing industry as well as one of the modernization of old factories and the building of many large new ones.

Greater use of automatic machinery in production tends to lower the labor cost of each unit of product turned out. That the labor cost per unit of product was reduced greatly in the manufacturing industry during the twenties is shown clearly by the figures in Table XII. The use of the automatic machinery in a factory reduces the number of laborers employed in proportion to the volume of production, or increases the production per laborer employed. If, under such conditions, the wages per laborer are not raised in proportion to the increase in the production per laborer, the labor cost per unit of product will decline. As pointed out in chapter three, the wage rates of employes in the manufacturing industries were not raised to correspond with the rise in production per worker.

According to the competitive price theory, the price of each reproducible commodity will tend to equal its cost of production.[2] This theory holds that whenever the cost of production of a commodity declines, the immediate profits of the producers of that commodity will increase; the higher profit margin will cause an increase in production which in turn will result in a larger market supply of the commodity; the greater market supply, with no increase in the market demand, will result in

2 Explanation and discussion of the competitive price theory is given in Appendix B, p. 289.

a lower price for the commodity; competition among producers to dispose of the greater market supply eventually will force them to lower the price to the extent to which the cost of production was lowered. The competitive price theory holds also that when there is an immediate increase in the market demand for a commodity, without a corresponding increase in the market supply, its price will rise; but the greater profit margin resulting from the higher price will stimulate production and increase the market supply of the commodity; then competition among producers in the sale of the product will bring the price down to the level of cost of production for the least efficient or marginal producer necessary to produce the quantity of the commodity demanded in the market.

In most of the manufacturing industries, during the twenties, occurred both a decrease in the cost of production of the goods resulting in a higher profit margin, and an increase in the market demand for the goods, tending to increase their prices and to raise the profit margin of the producers. The prospects of large profits resulting from these two forces caused an unprecedented increase in the capacity of production and in the volume of production in these industries. The actual increase in volume of production and in the market supply of manufactured goods, long before 1929, was greater than the increase in the market demand for them. Therefore, in compliance with the competitive price theory, the prices of manufactured goods, from 1922 to 1929, should have been lowered to an amount equal to the reduction in their cost of production. But, contrary to the theory, the price level of these goods was not lowered at all.

Of course, in accordance with the competitive price theory, the increase in the demand for manufactured goods and the decrease in the cost of production of those goods would have resulted in a rise of the immediate profits of the manufacturing enterprises. During every industrial boom the profits of industry and business rise because the margin between the cost of production and prices becomes greater, and the volume of sales increases. At such times prices generally rise and the cost of production does not rise immediately. In the twenties prices of manufactured goods did not rise, but the volume of sales in-

creased and the cost of production was lowered. This relationship gave boom profits to the manufacturers.

But the competitive price theory holds, also, that the increase in the volume of production resulting from the high profit margin would expand the market supply of goods to such an extent that competition among the producers and sellers to dispose of their products would bring the price level down to or near the new lower cost of production. In short, this price theory allows for high immmediate profits when demand for particular products increases or when the cost of their production is lowered; but it holds that future competition in the production and sale of these goods, in order to secure the high profits, will bring the prices of the products down to or near their cost of production. The theory holds that prices will decline when a market surplus of goods is produced and offered in the market. A market surplus of manufactured goods was produced prior to 1929, but the level of prices of these goods did not decline prior to that date.

Why were our manufacturing enterprises able to hold up the prices of their products in the face of an increasing market surplus of goods, a decreasing cost of production, and an increasing profit margin? There appears to be only one answer—in the main, the prices of manufactured goods at this time were not determined by competitive forces; but largely by monopolistic influences and forces. A monopoly sets the prices of its products at the level which will give it the highest net profits on its total business.[3] Monopoly prices in all cases are higher than prices set by competitive forces, and in most cases they are much higher than competitive prices.

Free and unrestrained competition was the exception rather than the rule in the production and sale of manufactured goods in this country even before the days of New Deal "codes of fair competition." The development of national markets, the standardization of goods, and the growth of large scale production prior to 1929, resulted in the reduction or elimination of competition in practically all manufacturing industries. Back in 1882, the industrial leaders began to eliminate competition in one

3 Explanation and discussion of the monopoly price theory is given in Appendix B, p. 289.

manufacturing industry after another through the formation of giant industrial combines in the form of "trusts." In the nineties they changed the form of the industrial combines to "holding companies"; about 1904 they began to organize the great industrial "consolidations" and "mergers." In those industries where the managers were not able to form giant monopolistic combines under one management, they organized themselves into associations known as "trade associations" or "open price associations" to reduce or eliminate competition in the sale of their products. The period of the World War was the heyday era of the promotion and organization of trade associations to help "win the war for democracy."

The Harding, Coolidge, and Hoover administrations encouraged and nurtured trade associations in all industries, on the grounds that through their activities both goods and production methods would be standardized, wastes eliminated, and industrial management made more efficient. Whatever may have been the desirable results of the organization and active operation of trade associations in each of the industries in reference to production, it is certain that, in reference to prices, they resulted in the lessening of competition in most industries, and in the virtual elimination of competition in many of them. The alleged chief function of most trade associations is to eliminate "unfair competition"; to the average industrialist, the most unfair competition of all is that of low price or of price-cutting. In order to eliminate price-cutting there must be some understanding in reference to "maintenance of fair prices"—that is, prices set by agreement rather than by competition. The average industrialist's idea of a "fair price" is one which will give all producers large profits.

Under the post war conditions of the concentration of control of the major manufacturing industries in the hands of a few leaders, brought about through industrial combines and trade associations, few prices in those industries were determined by active competition of producers or sellers. The development of mass production reduced the number of enterprises in most large standardized industries and made mergers and price agreements easily attainable. In the various manufacturing industries, few prices are determined by the kind of competitive conditions the

competitive price theory assumes as existing in industry. The "law" of monopoly price recently has played a far greater part in the determination of prices of goods sold by big manufacturing industries than have the "natural laws" of supply and demand.

The competitive profit theory assumes that as each industry grows and develops, profits will tend to become smaller because of the growing competition among competitive producers. But in this country profits frequently have become larger with the more complete development of each industry. Profit rates have risen because of the growth of monopolistic enterprises and organizations in the various industries. The competitive price theory assumes not only that all enterprises in each industry sell their products in a highly competitive market, but that they also borrow money, purchase supplies, and hire labor in open competitive markets. A highly monopolistic organization exercises control over the market demand for the goods and services it buys as well as control over the market supply of the goods and services it sells. It is believed that the bulk of the large industrial profits of the twenties were due more to monopolistic control over markets and to the special advantages of "bigness" than to the superior efficiency of the enterprises which received these profits.[4]

The business profits of corporations, in large part, are paid out as dividends to stockholders, while the business profits of unincorporated enterprises are paid out as owner-withdrawals. Part of the dividends of corporations may be thought of as interest on the investment in the businesses (what was paid for the shares of stock of the corporations), and part of them as surplus returns, or pure profits. Often the surplus returns in the form of dividends are referred to as compensation for risks taken by the stockholders or as compensation for efficient management. In regard to the earnings of monopolistic enterprises, such justifications of big dividends are entirely unfounded.

Often corporations attempt to conceal the rate of their profits: in many of the big business corporations a large part of prospective future profits have been "capitalized" by the is-

4 Appendix C contains a discussion of "Profits and Dividends in Theory and in Practice."

suance of shares of stock based on the anticipated profits. Some of the holding companies have exchanged bonds for the shares of stock of subsidiary companies' shares which were originally issued as a capitalization of the earning power or profits of those subsidiary companies. The fact is, that in the public utilities and in some of the holding companies in other industries, the issuance of investment securities (bonds and notes) has been so intermixed with the capitalization of earning power or prospective profits of the subsidiary companies, that it is difficult to ascertain what part of these investment securities represent actual cash loaned to, or invested in, these businesses, and what part of them represent the mere transfer of "watered" stock into bonds and notes. The bonds and notes of corporations are supposed to represent an interest charge on the cost of production before arriving at the net profits of the business enterprises, while dividends on shares of stocks are paid out of net profits. When watered stock is transformed into bonds, the interest on the bonds is charged as an item of cost of production. Of course, both the shares of stock and the bonds of corporations represent property rights, but neither necessarily represents actual investments of savings upon which interest or dlvidends should be paid.

In distributing the national money income in the twenties, property rights payments increased more than did wage payments. Interest, rent, royalty, and other property payments increased almost as much as did dividends during this period.[5] The reasons for the great rise in interest payments were (1) the rapid growth of investments in the form of loans made and bonds issued, and (2) the relatively high interest rates prevailing on these loans and investments. Rental payments rose greatly at this time because of (1) the increase in the number and size of buildings to be rented, (2) the rise in the site value of urban real estate, and (3) the high rental charges for property rented. Royalty payments rose during the period as a result of (1) the rise in the value of mineral deposits and (2) the high peacetime rate of use of those deposits. Most other property payments, such as profits from sale of securities and property,

5 This fact is brought out very clearly by the figures of Table X of Appendix A, pp. 276-77.

rose rapidly because of the rise in the sales value of the property; this was not true of agricultural and coal lands, and of obsolete urban property.

The question may be asked: If, in the twenties, the nation developed a surplus of investment funds, why did not interest rates then decline? Does not supply and demand regulate interest rates? As a matter of fact, because of the artificial uses that were made of the surplus investment funds, a market surplus of such funds did not become evident until 1929. They were used to overexpand the productive capacity of industries, to overbuild our cities, and to purchase large quantities of worthless foreign securities, as well as to inflate the prices of securities on the stock market. Nevertheless, although in 1928 and 1929 savings and time deposits did pile up in our banks, interest rates did not decline. Both the banks and the investors became uneasy as to the soundness of future loans, and interest rates actually rose.

The rate of prevailing profits in business has had more to do with setting prevailing interest rates on loans than has the supply of loanable funds. When profits are high interest rates will be high regardless of the supply of loanable funds; there will be a strong demand for new funds with which to take advantage of the high prospective profits. On the other hand, when profits are low, there will be little demand for new loanable funds. Up to 1929 profits in business were great and interest rates remained high. After the break in prices in 1930, profits declined and interest rates also declined.

As our economic society became more highly capitalized and industrialized, the value of the invested capital increased more rapidly than did the volume of production. In other words, the amount of invested capital per unit of production increases with the growth in capitalized production. If the interest rate on the capital invested remains the same, it will take a progressively larger share of the net production of industry to pay the interest on the capital invested. When the amount of investment funds exceeds the actual needs for new capital equipment, the interest rates on both old and new capital investments should decline. But the interest rate did not decline when a surplus of capital occurred. If the interest rate had been reduced in the

twenties there would not have been such a large increase in the proportion of the national income paid out as interest.

For more than one hundred and fifty years the social injustice of a great rise in economic rents and royalties on land and natural resources has been recognized by economists. As society grows, it is forced to pay the owners of urban lands and mineral resources increasing rentals for the use of such property, though the owners do nothing to deserve the larger incomes. Many undeserved fortunes have been accumulated because of a rise in the value of mineral deposits and urban real estate in the United States; many unearned large incomes were paid to such owners prior to 1929. As cities grow, the economic rents paid by the inhabitants increase per inhabitant. That was why such incomes grew at a rapid rate prior to 1929.

While profits and property payments absorbed a progressively larger share of the national income, a correspondingly smaller share of it was paid out as wages to laborers. The decrease in the percentage of the national income paid as wages was due to the fact that wages per laborer did not rise in proportion to the increase in production per laborer. As we have seen already, profits and property payments absorbed nearly all the additional national income due to increased production after the war and left to wage-earners only a small part of that additional income.

It might be argued that the greater production in industry during the twenties resulted largely from the increase in the quantity and quality of capital equipment and from more efficient business management; and that, therefore, the proceeds of the larger production should have gone to management and property as profits and other payments. There can be little doubt that the improvement in the quality of capital equipment (automatic machinery) and the increase in the quantity (amount of new capital equipment) were primarily responsible for the increase in production prior to 1929. However, the owners of the capital equipment were not responsible personally for the improvement in its quality; inventors were not responsible for its greater productivity. The efficiency in general management may have played a small part in bringing about greater production; but the efficiency of the skilled laborers and

hired technicians played a far greater part in increasing industrial production than did the productive efficiency of the owner-managers who received the greater benefits. There is no accurate method by which the productivity of any one factor of production in an enterprise might be measured. If such a method of measurement existed, the operation of the so-called natural economic laws under present industrial conditions would not give to each factor that which it produced.[6]

In the twenties, wages, or the compensation to labor as a factor of production, declined relative to profits and property payments not because labor produced, or was responsible for the creation of, a smaller share of the total production; but because of the decrease in the advantages and opportunities available to laborers in the industrial world. As a result of the economic and industrial developments during the past fifty years, the laborers of this country lost much of the wage bargaining power they formerly possessed; at the same time, the employing corporations gained greatly in their power to control the wagescales of laborers. Also, after the World War, the market supply of industrial laborers in this country increased much more than did the market demand for such labor.

The bargaining power of American laborers was also reduced greatly by the disappearance of free land and the western frontier. As long as an individual had the choice of working for an employer as a hired laborer or taking up free land, he was in a position to refuse a job unless the wages offered were high enough to compensate him for foregoing taking advantage of the opportunities offered by the western frontier. With the disappearance of the free land this alternative choice was taken from the laborer and, as a result, his bargaining power in dealing with prospective employers was weakened greatly. The decline of the western movement of population caused an increase in the supply of labor in the industrial centers.

Widespread adoption of powerized automatic machinery in all commodity-producing industries since 1914 did much to reduce the market demand for labor and to weaken the wage-

6 A discussion of economic theory having to do with the division of the national income among the factors of production is given in Appendix D, "Wages and Property Income," pp. 308.

bargaining power of laborers. Extensive use of automatic machinery was the principal force which created a surplus supply of labor in the twenties while a great industrial boom was in progress; its use reduced the market demand for labor in every enterprise where it was introduced. It was the wide use of powerized farm machinery which was the principal cause of the movement away from the farms to the cities after 1919. The movement of population to the cities and the displacement of laborers by machinery in industrial enterprises, plus the natural growth in the number of available laborers, were responsible for the available supply of labor increasing more rapidly than it could be absorbed by the new enterprises and by the building trades. Unemployed laborers were forced to bid against one another for employment. Employers were in a position to take advantage of this surplus supply of labor, and to hold wagescales down and work hours up regardless of the profits they were making from the operation of their businesses. Laborers thus lost much power in bargaining for wages.

Employers gained power in bargaining to the extent to which laborers lost such power. The development of standardized mass production under large corporations and industrial combinations resulted in strengthening the wage-bargaining power of industrial employers. Where a single corporation or combine employs hundreds or thousands of laborers, it makes little difference to it whether or not a particular laborer is employed, but it makes a great deal of difference to the particular laborer whether or not he gets a job. The employer corporation or combine is in such a position that, if it does not employ a particular laborer when it needs additional workers, it probably will be able to employ some other one just as good and at a wage rate no higher than the one it offers; on the other hand, the unemployed laborer feels that he must have an immediate job to support himself and his family. Therefore, the individual laborer, in urgent need of a job, must pit his wage-bargaining power against that of the giant employer, who is more or less indifferent to the urgent personal needs of the individual laborer.

About 10 per cent of the industrial laborers are organized into non-company trade or labor unions, for the primary purpose of strengthening their wage-bargaining power. The organ-

ized laborers, on the whole, are the highly skilled ones; the great mass, or semi-skilled and unskilled laborers, are not so organized. On the other side, the employers in most industries are organized into associations, partly for the purpose of combining their wage-bargaining power against that of the laborers; the big employers who employ a majority of the industrial laborers are so organized. As a whole, employers are much more completely and far more effectively organized to deal with laborers, than are laborers organized to deal with employers. In comparing organized labor and organized capital, unquestionably organized capital has the advantages over organized labor in having more complete and more effective organization.

The trend of industrial development up to 1929 was favorable to increasing profits and higher property incomes, and was unfavorable to increasing wages. The economic advantages and opportunities of owners and operators of business enterprises and possessors of property gained over those of workers. That was why, relatively, profits and property incomes secured a growing percentage of the national money income and wages a declining percentage of it.

CHAPTER SIX

COMPARISON OF 1929 DEPRESSION WITH PREVIOUS ONES

THE 1929 depression possessed many similarities to previous major depressions. It was preceded by an industrial boom characterized by a rapid expansion of industries and a great increase in the volume of production. During the boom security prices rose, and there was an expansion of bank credit. Just preceding the beginning of the depression, interest rates were high and there was a stringency in the money market. Before the crash occurred there was a falling off in new construction and in industrial expansion. Similar business occurrences have preceded all previous major business depressions.

As with former depressions, a decline in the volume of sales occurred prior to the fall in prices; the decline in the stock market also preceded the fall in prices. Curtailment in the volume of production followed the reduction in the volume of sales and the fall in prices; unemployment rose as a result of the curtailment of the volume of production. Our national money income decreased rapidly as a result of the fall in prices, production, profits, and employment. Because of this decline there was a further decrease in the volume of sales and in prices, which in turn caused further decreases in production and in the national money income. The vicious cycle of a downward movement in sales, prices, production, income, and employment in this depression, as in all other large ones, ran its course.

During the downward movement of the 1929 depression there was much liquidation of bank credit and many business and bank failures. All markets appeared to be glutted with goods for which there was little market demand. Pessimism and fear gripped the hearts of business men as well as the hearts of the

masses of the people. "Runs" on banks started in 1932 and financial panic resulted in 1933. Many of the newly rich lost their fortunes, and the great masses of the people suffered losses of incomes and jobs. Such happenings frequently have been characteristic of great depressions, but in the 1929 depression they were more intensified than during previous ones.

Notwithstanding the similarities between the 1929 depression and previous ones, there were many essential differences between this depression and all preceding ones. The differences lay not so much in the nature of the succession of events occurring after the depression started, but in the economic developments and happenings preceding the depression.

The characteristics of the boom of the twenties were in many respects different from those of any previous boom. During its progress the general price level did not rise as it did during the progress of previous booms; and there was little or no speculation in commodities as there usually is at such times. While bank credit expanded in the twenties there was no expansion of commercial bank loans; the bank credit expansion consisted of collaterally secured loans and of investments by banks; commercial bank credit always expanded during previous boom periods. Also, no actual shortage of bank reserves developed prior to the depression in 1929, but the reserves of the Federal Reserve banks were larger at the end of the boom than they were at its beginning. In short, the 1929 depression did not occur because there was no available bank credit to keep business going, as was the case with other depressions. Also, all previous booms were characterized by a shortage in the market supply of nearly all classes of goods, but during the boom of the twenties there was no appreciable shortage in the supply of any class of goods. On the other hand, long before the beginning of the depression, there was a surplus market supply of many classes of goods and a surplus capacity of production in most industries. Such a situation never developed in the middle of any other boom.

All other great upswings in business were accompanied by a shortage in the supply of available labor. But notwithstanding the fact that the industrial upswing of the twenties, from the standpoint of industrial expansion and increase in production, was our greatest peacetime boom, a surplus rather than a short-

age of labor developed. This was true despite the fact that there was little immigration to this country at that time, and also that there was in progress an enormous construction or building boom. It has been pointed out already that this surplus of labor was due largely to the rapid displacement of laborers by automatic machinery in production; for this reason there was little increase in the actual number of laborers employed as a result of the great increase in the volume of industrial production. Because of the surplus labor supply, there was little increase in real wages at the time of the great rise in the volume of production. Profits and savings have always increased during booms, but they rose more rapidly during the twenties than in any previous peacetime boom. While laborers as a class received less benefits from the industrial upswing of the twenties than they received from previous ones, employers and owners of productive property received more benefits from it than from any previous one. There was never a time when as large a portion of the national income was saved and invested as in the twenties; also there was never a time when current production exceeded current consumption as much as it did in this period.

The depression of 1929 was an aftermath of the great war boom of 1915 to 1920, as well as of the peacetime boom of the twenties. Only part of the inflation and industrial and economic maladjustments were liquidated during the depression of 1920; most of the consequences of the war boom were carried over into the peacetime boom of the twenties. Therefore, in the depression of 1929 it was necessary to liquidate the consequences of two booms instead of one. That was one of the principal reasons this depression was much more severe than any previous one. As already indicated, the downward movement of the vicious cycle of the 1929 depression was similar to the succession of disastrous happenings of other major depressions; the difference was that the successive downward happenings were more severe and lasted over a longer period of time than did the others.

Previously business and industry always have had what might be called a natural recovery from depressions. That is to say, prior to the 1929 depression it has never been necessary for the

government to put into operation a national recovery program in order to bring about business recovery from the various depressions which occurred from 1816 to 1920. It might be said that heretofore the government always permitted the depressions to run their natural course, or gave the so-called natural economic forces a chance to bring about recovery or prosperity. We might ask: How have previous depressions run their natural course, and how and why did recovery always follow those depressions?

Decline in sales, prices, and production during depressions has resulted always in much liquidation of debts, the squeezing out of inflated capitalization of business enterprises, as well as the deflation of outstanding bank credit and a reduction in the cost of production of goods. Also, heretofore, the surplus supply of goods on hand at the beginning of depressions has been decreased or used up as the depressions progressed in their natural course. All of such happenings during depressions resulted in the removal of much of the business and industrial debris left over from the previous booms. The cost of production must be reduced and excess debts and credits must be liquidated in order that business enterprises may produce profitably at depression prices. Then too, the surplus goods in the market must be absorbed before there will be a sustained market demand for increased production. Previously these natural occurrences during depressions have prepared the ground for future business revivals.

Ordinarily the liquidation of bank credit and the payment or adjustment of debts during depressions places the surviving business enterprises in a stronger financial position than they possessed when the depression started. The reduction in capital charges, raw material prices, overhead charges, and other operating expenses reduces the unit cost of production in all enterprises. As a result of the consumption of surplus goods in the market and the passing of the credit stringency in the depression, the prices of commodities stop declining and the volume of sales increases. A rise in the volume of sales at sustained prices causes an increase in the volume of production; improvement in production brings about more employment and a rise in the national money income. As a result of the rise in the volume of

sales and of production there is an increase in borrowings and an expansion of bank credit from the low point of the depression. Thus the beginnings of business recovery, in the past, have come about as a result of the operation of the so-called natural economic forces during depressions.

Heretofore, a slight improvement in business conditions during or following a major depression was a signal for further development of the frontier, the exploitation of unexploited resources, the establishment of new industries, and the expansion of old ones. To effectuate such undertakings required the production of great quantities of new producers' goods, as well as the financing of the new undertakings. At such times bank credit conditions were favorable for borrowings to carry out these new developments. The greater demand for new constructional goods and new capital equipment resulted in a greater volume of national production, greater employment, and a larger national money income. Such upswings in business, impelled by the new industrial expansion movement, and in turn facilitated by the use and expansion of bank credit, resulted in a rise in the general price level and an increase in production and employment in all industries.

Business revivals attended by new industrial expansion movements always have resulted in full business recoveries from previous depressions. Frequently such revivals have developed directly into intense business booms. Whether a particular industrial expansion business revival brought about conditions which were considered as "normal" or developed into another business boom, depended on the magnitude of the new movement to expand the frontier, to exploit resources, to establish new industries and to expand old ones. When the new industrial expansion movement was of great magnitude, the business revival continued on into a boom; when it was of lesser magnitude the revival resulted only in "normal" business conditions. "Normal" business conditions following revivals ended either in small depressions or booms, depending on the intensity of the new industrial developments attending and following those "normal" conditions. When the industrial expansion movement declined in intensity, a depression followed; when it increased in intensity, a boom followed.

Frequently, following the price, debt, and credit liquidation of depressions, an expansion of our export trade has played an important part in promoting business revivals. This was particularly true when the nation was largely a raw-material and agricultural producing country, and when our exports were financed by imports and interest payments on loans secured abroad. At such times large domestic crops and rising prices resulted in greater exports, which increased the national money income, which in turn caused a rise in the demand for and production of manufactured goods in this country. Under those conditions the greater part of the purchasing power received for the goods exported went into the hands of farmers and other small income receivers, who spent it for consumers' goods. Then the larger exports greatly increased the purchasing power of American consumers; and the greater consumers' purchasing power gave support to further expansion of American manufacturing industries.

When the 1929 depression occurred, there was a larger surplus of goods in the markets than at the time of the occurrence of any previous depression; the decline in the volume of production also was larger than at any previous depression. With the exception of the 1920 depression, the fall in the price level from 1929 to 1933 was greater than it was in previous depressions; also, the 1929 depression was the longest as well as the most severe ever experienced by this country. For these reasons, the depression adjustments necessary for laying a basis for natural recovery were of greater dimension. Not only was more liquidation of bank credit necessary than previously, but also it was necessary to have more adjustments of private debts and of the capitalization of business enterprises, as well as a greater reduction in the cost of production than ever before. On the other hand, business enterprises were much slower in making the necessary recovery adjustments than during previous depressions. The national propaganda that "prosperity is around the corner" was in part responsible for this slowness, and the gradual development of the depression itself was in part responsible.

Inevitably the "writing down" of capital charges, the reduction in the cost of production, and the adjustment of debts

eventually would have occurred before the end of the depression, if the depression had been permitted to run its natural course. Also, the surplus stocks of goods eventually would have been used and there would have been some increase in industrial production to supply greater current demand for goods. While the 1929 depression adjustments necessary for natural business recovery would have taken several years to run their course, eventually they would have brought about some improvements in, or recovery of, business.

On the other hand, after business started to improve as a result of such adjustments, it is doubtful whether the industrial expansion forces which heretofore have operated to bring about complete recovery, would have to any great extent come into play to bring about complete recovery from this depression. Not only has the physical frontier disappeared, but industrially this country almost has reached economic maturity. We as a nation have passed from an era of a scarcity of capital funds and productive capacity to one of a surplus of capital funds and a scarcity of markets for the products which can be produced. Let us examine the problems which at present confront the nation with reference to future industrial expansion.

It is not now possible to open up new territories in the West or to exploit vast untapped natural resources, because no suitable territories are unsettled and few natural resources are untapped. The period of the extension of railroad transportation facilities for the purpose of developing the frontier country has closed; the great western migration of population in this country is past. Little or no credit and industrial expansion in this country can be brought about in the near future as it has been in the past as a result of the western movement. Great opportunities of securing large quick profits from the exploitation and development of the West are no longer offered; therefore, there can be no concentrated market demand for capital funds and producers' goods to be used for this purpose.

Neither is it likely that the demand for new equipment or for funds with which to expand existing industrial enterprises will be large in the near future. Most of our established industries have already an adequate number of business enterprises with a surplus capacity of production, even for boom condi-

tions. Few of them will require new capital expansion in order to produce whatever quantity of goods is demanded when business starts to recover. At no other time in our national history have our established industries in the mining, transporting, manufacturing, and merchandising fields possessed such adequate capital equipment and funds and surplus productive capacity as at present. They could now expand greatly their productive operations without building new plants or borrowing or expending large capital funds. Of course, business recovery from this depression will be attended by some replacement of worn and obsolete capital equipment, but such replacements will be a normal replacement of equipment used up in past and current production and should not require new capital funds or an expansion of bank credit.

The period of the twenties was one of the greatest building booms this country has ever experienced. By 1929 practically every town and city in the United States found itself with a market surplus of store buildings,' office buildngs, and apartment houses. Also, more than 40 per cent of the home-owners found themselves loaded down with mortgages on their homes. The city real estate mortgages more than doubled in this decade and stood at about $32,000,000,000 in 1930. It has been necessary for the government to refinance a large part of these mortgages in order to relieve the home-owners and save the loan firms. Is it not unreasonable to expect that, under these conditions, a new building boom will occur to facilitate recovery of business from this depression? Why build new business buildings when many of those which exist cannot be rented to pay overhead and operating expenses? Why build new homes when existing ones can be purchased more cheaply than new ones can be built? Of course, some new business buildings and some residences will be constructed in the next few years, and many buildings of all kinds will be repaired and remodeled, but a credit inflational building boom similar to the one of the twenties is highly improbable, if not impossible. Certainly such a building boom would be unwise from the economic and business point of view, both to the individuals involved and to the nation as a whole.

Neither is there likely to be any concentrated establishment

of new industries to aid recovery from this depression. Doubtless some new industries will be established and developed in the next few years. The air-cooling industry is one now in its infancy and probably will develop rapidly. Others will appear which are now unknown. But few, if any, large basic industries will be established soon, and it is not likely that any supplementary industries comparable with the automobile, rayon, and "talkie" industries will be developed in the near future.

Unquestionably, there will be many far-reaching changes in the character of goods produced by existing industries as well as in the processes of production used, but such technological changes are not likely to involve a concentrated demand for new capital funds or a boom demand for new capital equipment. Such changes in the character of products and the methods of production surely will create a demand for replacement of obsolete capital equipment in the industries affected, but such a demand will involve little new capital expenditure. Only the new business enterprises established in the changing industries will require new capital expenditures; the technological changes in the old establishments should be made from the depreciation and replacement funds set aside for that purpose rather than from new capital funds.

There is little hope that an enormous favorable balance of foreign trade can be created to "pull us out of the depression." Under present conditions, the only method by which such a trade balance could be brought about would be for this country to make extensive foreign loans and thus enable other countries to finance the purchase of our goods. In the face of our experiences with foreign loans during the past twenty years, extensive foreign loans are not likely to be made by us in the next few years. Therefore, we must depend on our domestic market to absorb our net surplus of goods, since American investors apparently are unwilling to make foreign loans to enable foreigners to purchase our net surpluses. However, there is no valid reason why our total foreign trade (both imports and exports) should not increase greatly in the next few years.

In regard to a natural recovery from the 1929 depression we may conclude: All past business recoveries have been based on the expansion of the production goods industries as a result

of new capital investments in those industries. But because of the disappearance of the frontier and the existing excess capacity of production in most industries, it is probable that such an expansion of the production goods industries would not occur to bring about a so-called normal recovery from the present depression. In short, there does not exist sufficient prospect of profits to be derived from new capital investments in industrial expansion to justify such undertakings on a large scale. Neither is business recovery likely to be accomplished as a result of a building boom or a large expansion of export trade.

Therefore, to have permitted this depression to take its natural course as others have taken their natural courses would not have resulted in a business recovery similar to previous recoveries from depressions. This depression would run its natural course of falling prices, decline of credit, and liquidation of debts and capitalization as well as of a decrease in the cost of production and a consumption of surplus stocks of goods. Also, these depression happenings would have been succeeded by some rise in the volume of sales and production, and possibly some increase in employment and in bank credit. But revival in the capital goods and heavy goods industries would have been slight because industrial expansion would have been small. The extent of the general business revival would have depended almost entirely upon the extent of the increase in the domestic demand for consumers' goods. A rapid rise in the demand for consumers' goods probably would not have occurred because there would have been no great increase in consumers' money incomes. Heretofore, the greater part of the increase in consumers' purchasing power during recovery periods has come from the expansion of the capital goods and heavy goods industries. A natural recovery from the present depression would have resulted in only a slight rise in the physical volume of production, little decrease in unemployment, and small increase in the national money income. There would have been widespread limitation of the volume of production on the part of industries, in order to raise prices and to secure profits from a small volume of production and sales.

Such a recovery or adjustment period would have been spread out over several years, and during that time it would have been

necessary to support the great army of the unemployed with public funds. Many business failures would have occurred and there would have been much suffering. Eventually, the capital equipment representing the excess productive capacity would have deteriorated or become obsolete. Under such conditions this country would develop industrial conditions similar to those of England, with a limited productive capacity, a great army of unemployed supported by doles, and a low standard of living for all except a few industrialists.

As the 1929 depression became progressively deeper and wider, our existing national economic problems became more acute. By the spring of 1933, industrial production had declined to 50 per cent of the predepression level and employment in industry had declined more than 56 per cent. During the period 1929-33, the general price level fell more than 35 percent and bank deposits declined nearly 40 per cent. As the depression grew worse, debtors became unable to pay their debts, and it became more difficult for anyone to secure sufficient bank credit to finance legitimate business. Business confidence declined to a low ebb, and the people as a whole, because of the many bank failures, lost faith in their banks. By March, 1933, it became necessary for the President to close all the banks in the country in order to provide emergency legislation under which they might be reopened.

After the depression had continued for more than three years, and had become progressively worse, many people, including some business leaders, demanded that the government "do something" to stop it. It was believed that unless the government did something to stop it there would be a complete breakdown in our industrial system; some even feared that unless recovery could be brought about by some public policy capitalism itself might be destroyed. Many of the staid and conservative leaders lost faith in the efficacy of the "natural economic forces" to bring about a recovery and to restore prosperity to the country. There was much talk among both conservatives and progressives about the necessity of national economic planning, and many specific national plans designed to restore prosperity were put forward by individuals and groups.

In 1933 this country faced the choice of following one of three

policies or a mixture of them in reference to the depression and recovery. These optional policies were: (1) Permit the depression to take its natural course without governmental aid or interference. (2) Devise a public policy to bring about business and industrial recovery along the lines of previous recoveries. (3) Devise a public policy to reform and regulate the operation of our industrial system to restore an economic and industrial balance and to secure continuous and full operation of our industries. In this chapter we studied the probable consequences of permitting the depression to take its natural course; in the next chapter a study will be made of the economic and social consequences of the other two suggested policies.

CHAPTER SEVEN

RELATIONS OF GOVERNMENTAL POLICIES TO BUSINESS RECOVERY

REGARDLESS of what kind of national industrial and business recovery policy is or should be followed, it was necessary for the national government to have some kind of policy of giving financial relief to those who suffer most from depression conditions. The millions of unemployed and their families were without funds and without means of securing an income by their own efforts, and for these reasons they could not be left to shift for themselves. Private charity was insufficient to care for them. Failure to provide public aid for them in the form of "doles" or otherwise would have meant starvation of many men, women, and children, which might have resulted in political and industrial revolution. As long as millions of workers are unemployed because jobs cannot be had, the nation must provide some kind of public relief for the unemployed.

Also, it was necessary to adopt some kind of public policy of giving temporary or permanent relief to distressed debtors during the depression. Because of low incomes, many farm-owners were unable to make payments on their farm mortgages and were faced with impending mortgage foreclosures whereby they would lose their farms. For the same reasons many urban home-owners faced impending foreclosures on their homes. Such occurrences not only would have left many substantial citizens homeless, but would have engendered a mob spirit against "heartless" creditors. Also, it was necessary to facilitate adjustment of the debts of many worthy business enterprises in order to preserve them. Again, the great agricultural population as a whole was without adequate income for support because of the

relatively low prices of agricultural products, and it was necessary for some public policy to give the farmers immediate relief from these relatively low prices.

It is generally agreed that the various relief measures adopted should be designed with the primary purpose of giving immediate and effective relief to those who have been or are being crushed by the prevailing economic and industrial conditions. Insofar as possible and practicable, these relief policies should give permanent as well as temporary relief to the sufferers. The depression relief measures which are adopted might be designed as "purely relief measures" with little or no direct connection with the national recovery policies used; or relief and recovery measures might be co-ordinated into a relief-recovery policy. Should the laissez-faire recovery policy of allowing economic and business adjustments to take their natural course in bringing about recovery be followed, there could be little or no direct connection between the relief and the recovery policies of the government. On the other hand, if a *publicly controlled* recovery policy of directing the economic and business adjustments in such a manner as to bring about recovery is followed, relief policies may be closely correlated with the recovery policies.

As indicated in the preceding chapter, the nation might adopt either one of two distinct and somewhat opposing publicly controlled recovery policies. The first may be designated as the *business and industrial stimulation recovery policy;* the second, as the *business and industrial reform recovery policy.* A discussion of each of these policies as applied to the operation of our industrial system under prevailing economic conditions is given below:

The business stimulation recovery policy is based on the general assumption that little or nothing is fundamentally wrong with present operation of our industrial system. Our industrial breakdown in 1929, so the advocates of this policy believe, was due primarily to fortuitous world and domestic economic conditions over which man had little or no control; and because of the continuation of unfavorable economic conditions during the depression, business was unable to recover quickly through the operation of natural economic forces. Con-

sequently, so the argument runs, a large body of business leaders lost confidence in the business outlook and refused to exercise business initiative to bring back prosperity. Business, so the advocates of this policy say, got on a "dead center," and the "business pump" ran dry. In 1933 they claimed that all that was needed to restore prosperity to the country was for the government to prime the business pump and to supply a "kick-off" stimulation to set the wheels of industry in motion again. They claimed that once industry is pushed off the dead center and its pump is primed, the operation of the natural economic forces would restore prosperity to the country, and our industrial system would serve the public more effectively than ever before.

Restoration of predepression business and industrial conditions seems to be the desired goal of the advocates of the business stimulation recovery policy. Their desire apparently is to restore not only the predepression volume of trade and production, but also the predepression price level, credit expansion, and profit margins. They would bring about business recovery along the traditional lines of creating business opportunities to make desirable profits from industrial expansion; they would make an artificial market demand for the products of the heavy goods (capital and construction goods) industries in order to induce full operation of industry. They assume that full operation of industry not only would eliminate unemployment and increase the national money income, but would restore a natural balance between production and consumption. Most of the advocates of the stimulation recovery policy are looking backward industrially and hoping to restore economic and industrial conditions which prevailed prior to the depression in 1929.

There is not entire agreement among the supporters of the stiumulation recovery policy as to the specific measures that should be used to restore prosperity. In general, however, they advocate the adoption of the following kinds of governmental policies:

1. Permit business enterprises in each industry to make private agreements in reference to control over volume of production and prices to be charged for their goods. Through such agreements business profits would be restored by raising

prices and limiting production to current market demand for products. It is claimed that this policy eventually would cause an increase in production and in employment.

2. Artificially raise the general price level, either by inflating bank credit or the currency or by reducing the value of the standard dollar. As a result of inflated prices a speculative buying of goods on a rising market would be created which would increase the volume of production. The higher prices and the greater volume of sales and production would restore profits to business and raise the national money income.

3. Encourage a revival of the building trades by inducing people to build new homes, and revive the capital goods industries by encouraging the building of new industries. This private industrial expansion is to be brought about through low interest rates, government loans, and the arousal of public interest and enthusiasm in such construction. Greater volume of production and an enlarged national money income would thus result from the revival of the building trades and capital goods industries.

4. Launch a large public building program to stimulate demand for constructional goods and increase the national money income by furnishing jobs directly and indirectly to the unemployed. Through this increased consumers' money income it is hoped to bring about recovery.

These business stimulation measures, it is claimed by many, would pull the country out of the depression; they claim that once the back of the depression is broken, sound recovery and prosperity would follow. Doubtless the application of such policies would cause at least a temporary revival of business. Unquestionably immediate profits would increase, and so would production, sales, and employment, as a result of a simultaneous application of all these policies. But it does not follow necessarily that a business revival thus brought about would be sound, lasting, or beneficial to the country. On the other hand, there are very good reasons for believing that a revival brought about through such policies would be of short duration and would be followed immediately by another disastrous depression.

Let us examine the economic consequences of each of the suggested recovery measures. Self-regulation of prices and production by organized industry certainly would result in raising prices in relation to the cost of production so as to insure "reasonable" profits to industry. Such self-regulation also would involve a definite limitation on current production in relation to current market demand for the products. The limiting of production in relation to current market demand would discourage both full utilization of existing productive capacity and further industrial expansion. Also, this policy would increase definitely the percentage of the proceeds of net production which goes to profits and property and decrease the percentage of it which goes to wages. It would increase the prices of consumers' products faster than it increased the money income of the mass of consumers. This policy would result immediately in an actual decrease in the volume of industrial production; the relatively higher prices and profits would cause a relatively lower purchasing power on the part of consumers, and industrial production would remain on a low level instead of rising.

Artificial inflation of the general price level creates a temporary increase in the volume of sales. Possessors of "dollars" will desire to exchange their declining dollars for goods. Such a speculative movement will create a semblance of a trade revival, but the revival will not be attended by a greater business demand for producers' goods, or an increased purchasing power of consumers; such a revival is based on a desire on the part of the public to transfer declining dollars into values (goods) which are not declining. Because of the artificial increase in prices and in the volume of sales there will be some improvement in the volume of production, but this temporary improvement will result in little or no industrial expansion of the capital goods industries. Artificially higher prices, production, and profits brought about by inflation will cause a decrease in the purchasing power of consumers in proportion to the rise in the market value of the goods currently produced. This is true because wage payments do not rise as rapidly as prices and production in the up-trend in business. Therefore, a shortage of consumers' purchasing power will soon develop, and both trade and production again will decline. For these reasons no price inflational

movement can increase the physical volume of trade and production for any great length of time. The relapse following such a movement probably will leave business in a worse state than it was before the inflational movement started.

Assuming that a private building and construction boom could be started and that the capital goods industries could be revived through a government policy, such a revival of those industries under present national economic conditions, in my opinion, wolud not and could not contribute to permanent business recovery. While it lasted, the revival would contribute to an increase in both the general physical volume of production and the national money income, as well as result in an expansion of bank credit and higher prices. But such an industrial expansion would add to the existing surplus capacity of production or deficiency in consumers' purchasing power. Profits would increase because of the revival in the building and the capital goods industries, but consumers' purchasing power, in proportion to the current net production of the nation, would decline; wages and employment would not increase in proportion to the increase in the current net national production. It is likely, therefore, that a new depression would follow on the heels of such an artificial building and industrial expansion movement.

While it is probable that a large public works program, financed from public borrowings, will produce a temporary business and industrial revival, it is probable also that such a revival would last only so long as the public works program is in actual progress. Such a program increases consumers' purchasing power directly by giving employment to workers; it directly increases the demand for constructional goods used in the public projects; and, it indirectly causes a general increase in both production and employment. Also, as a result of the public building program, prices will rise and profits will increase. Inevitably business and industry will become adjusted to the artificial supplement to the current national money income furnished by the government from public credit in carrying out the program. This artificial supplement to the national income, in part, will contribute to a larger consumers' purchasing power; and, in part it will contribute to larger profits and property incomes. But when the public building program ends, the

artificial supplement to the national income supplied by government credit will end also. Those employed on the projects will be thrown out of jobs, and the demand for constructional goods will decline; prices, volume of production, and private employment then will decline, and the nation again will be faced with greater unemployment, a smaller volume of production and other depression problems.

Each of the four measures of the stimulation recovery policy would bring about a more unequal division of the national money income than existed before or during the 1929 depression. Prices would rise faster than wage scales; the volume of production would increase faster than private employment; and the rate of profits would increase faster than either prices or the volume of production. Under the operation of the so-called natural economic laws, wages never rise as rapidly as prices, and, under modern industrial conditions, employment lags far behind an increasing volume of production. Profits always rise rapidly as a result of a rise in both prices and the volume of production. Consequently the stimulation recovery policy would result in a larger percentage of the proceeds of current production being paid to property interests and big income receivers, and a smaller percentage of it being paid to wage earners and little income receivers. Therefore, a large share of the national money income would be saved and invested, and a smaller percentage of it would be used to purchase consumers' goods and services.

In a previous chapter it was pointed out that the fundamental cause which produced the 1929 depression was a relative surplus of savings and a relative deficit of consumers' purchasing power. The existence of the great surplus productive capacity and the large deficiency in consumers' purchasing power were the principal reasons why the 1929 depression was the most severe ever experienced by this country. The stimulation recovery policy, rather than curing this unbalanced industrial situation, would make it more unbalanced because each of the four artificial stimulation measures suggested by the advocates of this policy would result in greater inequality in the distribution of the national money income and a greater deficiency in consumers' purchasing power in proportion to the

physical volume of production. Such artificial stimulants to business, therefore, would tend to produce another depression more disastrous than the one the remedies were designed to cure.

Also, as a result of the application of the recovery stimulants, the nation would find itself with an unbearably large national indebtedness, and probably a badly disorganized monetary and credit system. Just what would happen in a depression under such conditions would be hazardous for anyone to predict. Certainly, it would be necessary for the national government to bring about drastic changes in the operation of our industrial system to prevent starvation and possible destruction of the private property and profits system.

As has been previously pointed out, our industrial system as it is now organized and as it now operates is fairly strong in its productive power; but it is extremely weak in ability to use its productive power to anything like full capacity; it is still weaker in ability to use to best advantage its great productive power to promote the general welfare. The industrial system's greatest defect, under the laissez-faire policy, is that it does not divide the proceeds of production (or national income) in such a manner as to enable the people to secure anything like the full economic benefits that its productive capacity and efficiency are capable of producing. The inequality in the distribution of the national money income is too great to permit full operation of our industrial system. Another glaring defect in the operation of the system is that it does not furnish jobs for all the employable laborers. Again, the individual rewards which the system now gives are too frequently out of proportion to the actual productive contributions which the receivers make.

Our industrial system was developed under conditions in which the laissez-fair policy had free rein; that is, up to 1933 there was practically no government regulation of activities of private business enterprises other than in the field of the public utilities. Whatever defects developed in our industrial organization were due to the operation of the so-called natural economic forces and laws. The only force which can be substituted for the operation of the so-called natural economic laws in the co-ordination of our industrial system is that of

government regulation. It is my opinion that if we are to correct the defects in the operation of our industrial system it must be done by government regulation of certain kinds of private business activities. We must through government regulation and control force our industrial system to serve the public to its fullest capacity; it has been demonstrated that this can not be done under the laissez-faire policy. This is the fundamental defense of a reform recovery policy.

There is no quick, easy and agreeable way out of our present national industrial and business difficulties. To my way of thinking, the only method by which this nation can secure a sound and lasting industrial and business recovery is by solving the basic problem of the deficiency in consumers' money income or relative surplus savings and investments. We must restore a workable balance between productive capacity and consumptive power (purchasing power). Continuous operation of industry at full capacity is possible only if consumers have enough purchasing power to buy for their use the finished goods and services produced by industry. This adjustment is possible only when a larger percentage of the national money income (derived from the net production of the nation) is spent for consumers' goods and a smaller percentage of it is saved and invested than was done during the twenties. The only way to bring about this adjustment in the division of the national money income is for the government to decrease the relative number and amount of the large individual incomes and to increase the relative number and amount of the small individual incomes; to accomplish this fundamental reform, opportunities to work must be created for all those who are willing and able to work, and each must be given a fair compensation for his real services in contributing to the production of industrial society.

Through what specific public policies can the necessary changes in the operation of our industrial system be brought about? It is my belief that these reform policies must be along the following lines:

1. Adjust the weekly work hours of laborers from time to time so that all employable laborers at all times would have jobs in private industry regardless of the physical volume of

production at any particular time. As the total volume of industrial production declines the weekly work hours should be reduced, and as the volume of production rises the weekly hours of laborers should be increased. Why "lay off" part of the laborers when production declines; why not divide the work among them? This, of course, will not be done voluntarily in each enterprise or even in each industry, but I see no insurmountable difficulty in the Federal government doing it for our industrial system as a whole.

2. Increase the percentage of the proceeds of the current net production of industry which goes to the industrial laborers by increasing the real wage rate per hour for each laborer. Adjust the total wage scales in industry from time to time, in accordance with changes in profits and in the volume of production.

3. Eliminate monopolistic control over prices and volume of production in private industry and prohibit private agreements in reference to both prices and the volume of production.

4. Provide for Federal incorporation of all business enterprises doing an interstate business and prohibit the organization of holding companies among them. Through Federal control of corporations, prohibit issuance of stock bonuses, stock dividends, watered stock and inside manipulation and reorganizations of corporations by the few who control them for their personal profits and to the detriment of both the other stockholders and the public.

5. Increase the real incomes of farmers (1) by adjusting production of the agricultural industry to the current market demand for agricultural products, so as to raise the prices of farm products in relation to the prices of industrial products, and (2) by adjusting the debts of farmers to where they will be in line with their current incomes and the current value of their farms.

6. Reduce the total interest payments of debtors by decreasing the prevailing rate of interest on loans; and refinance farm loans, home loans, public bonds, and railroad bonds on a lower interest rate. All debts should be adjusted to correspond with the actual market value of the property on which they are

based. This will reduce the debt payments by many small income receivers and increase their current purchasing power as consumers; it will reduce also the excess incomes of the large income receivers.

7. Make the high income receivers bear the brunt of the burden of supporting the government by imposing steeply progressive personal income taxes upon high incomes and by imposing excess profits taxes upon corporations and other business enterprises.

8. Greatly reduce or break up the huge family fortunes by imposing sufficiently high progressive inheritance, gift, and succession taxes as to take as taxes all of the huge estates above a reasonable sum to each heir or recipient upon the death of the possessors of large fortunes.

The nation must reach a stage of economic adjustment where further industrial expansion, as well as further increase in the volume of production, is based largely upon an expanding market demand for consumers' goods and services. An actual market demand for the products of new factories should be the principal reason for an expansion of the capital goods industries, rather than expand them merely because of the existence of surplus investment funds or because of the availability of bank credit. Industry should not be expanded for the primary purpose of giving employment to the unemployed, but it should be expanded for the fundamental purpose of producing more goods and services for the masses of the people. The only way by which such a market demand for the finished products of industry can be created is through a more equal distribution of the national money income; by no other method can consumers' purchasing power be increased in proportion to current production; only thus can a lasting industrial balance be restored.

Many objections might be advanced against such a reform industrial recovery policy as outlined above. It might be said that its application would result in political domination of industry through bureaucratic control, or that the policy would bring about industrial regimentation by the government. Some would argue that such a policy would destroy rugged individualism and discourage private initiative in industry. It might even be claimed that such a policy would retard, if not prevent,

business recovery. Still another assertion might be that the whole policy is designed to take property and income from certain individuals and groups and to give it to others.. Doubtless there is an element of truth in each of these criticisms of the industrial reform recovery policy. In later chapters we shall analyze the strength and the weakness of these various criticisms.

At this point it might be admitted frankly that the industrial reform recovery policy is designed in part to take part of the income from certain groups of individuals and to give more income to other groups who now have little or none. Also, it might be admitted that the policy is designed to limit individual initiative in pursuing action which would be detrimental to others or to society. It is a social control policy and, therefore, is in direct conflict with the laissez-faire policy of permitting business and industrial affairs to take their "natural" course. Again, it should be admitted that the adoption of such a public policy probably would not result in immediate and rapid industrial recovery. I do not believe, however, that under present industrial conditions, it would be possible, with any kind of recovery policy, to secure a rapid recovery of business which would be sound or permanent. Unquestionably, the national economic adjustments which would result from an application of the reform recovery measures would lay a basis for a sound industrial and business recovery; an unsound recovery eventually would be a national injury.

The Roosevelt Administration New Deal relief and recovery policies contain some of the elements of the three kinds of recovery policies discussed in this and the preceding chapter. A large part of most of the remaining chapters of this book is devoted to a study of the various Roosevelt New Deal economic policies. Suggestions will be made in these chapters as to why and how various ones of the Roosevelt policies should be changed so that a co-ordinated national economic policy will be developed that will achieve lasting national economic security.

CHAPTER EIGHT

NEW DEAL PROGRAM AND CONFLICTING GROUP INTERESTS

FOLLOWING the cumulative downward movement of business during the depression, the following national problems became so acute that they received widespread public attention and discussion: (1) relief for the sixteen to twenty million unemployed; (2) provision of adequate bank credit for legitimate business; (3) relief for debtors who were being forced into bankruptcy because of inability to pay on debts; (4) relief for farmers who had been suffering for several years from overproduction and low prices; (5) the necessity for an increase in the money income of consumers to revive retail trade; (6) stimulation of industrial production to furnish more jobs; (7) the necessity of a decrease in hours of labor to furnish more jobs; and (8) elimination of "sharp practices" in financing business enterprises and in the sale of their securities. In addition to these major problems many special problems developed, such as how to save the railroads from bankruptcy, and what kind of aid should be given the insurance companies, and other financial institutions to help them weather their current financial difficulties.

All during the Hoover administration the atititude of the government toward the depression was, with but few exceptions, one of laissez-faire, or allowing conditions to take their natural course. For more than three years Mr. Hoover took the position that the depression was of minor consequence, that business was fundamentally sound and would recover naturally within a short time. Finally, he did agree to the organization of the Reconstruction Finance Corporation (a government-owned corporation) for the purpose of making large loans to the big

banks and big business enterprises in order to permit them to renew loans and expand business. But on the whole the Republican administration maintained the attitude that the depression was largely financial, brought about by financial disturbances in foreign countries, and that the country would recover from the depression, as it had recovered many times in the past, as a result of the operation of natural recovery forces.

If the depression had been permitted to take its natural course, without any government aid or interference, one of two things inevitably would have happened: Either there would have been substantial recovery of business from the low point of the depression, or there would have been a complete breakdown in our industrial system. Assuming that there would have been some kind of recovery rather than a complete breakdown, the recovery certainly would have been very slow and would have been characterized by great business failures, large property losses and much human suffering. If the general price level had not continued to decline, it certainly would not have risen; it would have been necessary for business enterprises to reduce the cost of production drastically in order to be able to produce at the low price level. Such a reduction in costs would have entailed the scaling down of debts and of capital values, as well as further reduction of wages.

Assuming that our people and our business enterprises could and would have withstood a natural business recovery in 1933 (without any aid or interference from the government), such a recovery would not have eradicated many of the undesirable features of our industrial system which were responsible for the occurrence of the depression. Through bankruptcy, adjustments, and repudiations there would have been some reduction in debts. But, it is probable that wealth and income in the nation would have been more highly concentrated in the hands of a few after such a recovery than it was in 1929 when the depression occurred. It is probable, also, that with such a recovery there would have been further curtailment of national production as a result of trade association agreements. Certainly, wages would have been reduced drastically and the amount of unemployment remaining after such a recovery would have been appalling, if not unendurable. Also, consumers' money income

would not have been increased comparably with our productive capacity. Such a recovery would have been a mere re-establishment of the profit margin in business, with little or no increase in the volume of production or in the welfare of the people as a whole.

By the spring of 1932 there was a widespread public demand that the government do something to stop the depression and bring about improvements in industry and in business. The Republican party, which was in power, failed to heed this demand, and as a result that party was voted out of power in the general election of November, 1932. The Democratic party, which made vague promises of giving a "New Deal," was given control of the government. The promise of the New Deal at least was an assurance that something would be done by the government concerning the depression.

The New Deal program developed by the Roosevelt Administration has three general objectives: first, relief of suffering; second, recovery of business; and third, reform in our industrial system. The *relief measures* consist of (*a*) direct aid to the unemployed, and "made work" under the CWA, FERA, and the CCC, (*b*) unemployment insurance and pensions for the unemployed, and government-owned industries, (*c*) relief for debtors through the refinancing of debts and government loans made by the RFC, the Federal Land Banks, the Home Owners' Loan Corporation, and other agencies. The *recovery measures* consist of (*a*) direct stimulation of production, employment and income through the public works (building) programs; (*b*) the agricultural adjustment program, (*c*) the money, currency and banking policies; and (*d*) the NRA codes of fair competition to increase profits. The *reform measures* thus far have consisted of the Securities Act, the Stock Exchange Act, the Public Utility Act, the Banking Acts, and the wages, hours, and labor provisions of the National Industrial Recovery Act.

There is considerable overlapping and much contradiction among these three classes of measures of the New Deal program. For example, the debt relief measures may be looked upon as reform measures as well as relief measures insofar as they permanently reduce the debt burdens of the debtors. The Agricultural Adjustment Act is as much a temporary relief measure

as it is a recovery measure. The banking acts, insofar as they help to re-establish public confidence in the banks, are recovery measures as well as reform measures. The public works program gives immediate relief to the unemployed as well as stimulates temporary recovery by increasing consumers' incomes and the demand for constructional goods. The direct relief program, insofar as it results in government-owned industries and in unemployment insurance, may be looked upon as a reform measure, the NIRA might have been used either as a reform measure or as a recovery measure.

There has been marked improvement in business since March, 1933, when the first of the New Deal program was enacted. There has been much public discussion of just what each of the New Deal acts has contributed to the recovery which the country has enjoyed since. Necessarily there are many contradictions between the provisions of the various measures in a national program of such comprehensive dimensions and organized in such a short period, as was the Roosevelt program. The conflicting interests of different economic groups are responsible for many of the contradictory policies and provisions of the various measures. What kind of conflicts in policies do we find in these New Deal acts?

At first, one of the proclaimed objectives of the Roosevelt Administration was to balance the government's budget; but the public expenditures involved in the various relief and recovery measures made it impossible to raise enough current revenues to meet the current expenditures of the government. As will be pointed out in chapters to follow, some of the recovery measures tend to perpetuate the fundamentally bad features in our industrial system and thus make permanent recovery improbable, if not impossible. Also, some of both the relief and recovery measures, because of the fear they engender in many business men, tend to retard recovery. This fear is aroused principally because of the uncertainty of the future value of the dollar caused by the monetary policy and the mounting public debts resulting from the relief measures. In the course of our detailed examination of the various New Deal acts, other conflicts in the policies of this legislation will be discussed.

In the framing of the various acts of the Roosevelt program, different economic groups in the country exerted powerful conflicting pressure upon both the President and Congress to place in those acts the provisions they wanted. The agricultural group wanted legislation which would give special advantages and privileges to the farmers. The organized labor group wanted legislation which would award special privileges to organized labor. Organized industry and trade sought legislation which would stimulate trade and protect and promote their profit interests. The organized financial and big banking groups were perfectly willing to have legislation which would enable them to borrow money directly from the government or from the Federal Reserve banks, but they bitterly opposed all measures designed to curb the special privileges they already possessed. Cutting across these special interest groups was a fairly well defined group of students of public questions who advocated provisions in the various measures designed to improve the operation of our industrial system, and thus ultimately to benefit all groups. Several individuals in this group were closely associated with the Roosevelt Administration; some of them had formerly been college professors, and they were dubbed "brain trusters"; they were supposed to have great influence with the President in helping him to make up his mind as to the exact provisions which should be included in each New Deal act.

Notwithstanding the alleged dominating influence of the so-called brain trusters (the majority of whom are popularly supposed to be intellectual radicals, highly theoretical and impractical) the Congress and the President accepted and placed in the New Deal acts many specific suggestions of the special interest groups. As a result of their efforts to placate or please each special interest group by accepting suggested provisions each wanted included in the new legislation, the President and the Congress have been accused of attempting to ride simultaneously various horses going in different directions. Notwithstanding the President's compromising attitude in the formulation of the New Deal legislation, in carrying out his program during the first three years of his Administration, he has much displeased some people and only a minority have given his

whole program unreserved approval. However, it is believed that the vast majority of the people approve certain parts of his program and disapprove certain other parts—but different individuals do not approve or disapprove the same provisions of the program. At the time of the formulation of the program the President admitted that much of it was experimental and intended to be temporary only.

Public opinion in reference to the kind of national economic policies which should be adopted to deal with the present industrial situation is by no means uniform. In the main, public opinion on this question is divided into two opposing camps. On the one side we have the *right camp:* the Reactioneers, the Stand-patters, the Conservatives, the Laissez-Fairists and the Constitutionists. On the other side we have the *left camp:* the Liberals, the Progressives, the Radicals, and possibly some Socialists. Those on the right hope to convert the public, the President, and the Congress to their way of thinking so that the New Deal program will be revised in such a manner that the laissez-faire policy and the operation of the industrial system will be preserved as they were before the depression in 1929. The right-hand camp emphasizes property rights and individual rights as defined by the wording of the Constitution. On the other hand, the left-camp hopes to influence the public, the President, and the Congress in such a manner that the New Deal program will be revised along lines that will result in constructive reforms in the operation of our industrial system. They emphasize human rights and opportunities as opposed to property rights in the operation of industry.

Of course, there is no complete unanimity of opinion in the camp on the right. It is made up of conservative Democrats, Stand-pat Republicans, and capitalists and industrialists (who are generally non-partisan but who are always stand-patters in the protection of property rights and special privileges). Some are in this camp because they would lose money, property income, power, and prestige should there be a change in our industrial system which would eliminate special privileges and give a more equitable distribution of the national income. Others are in this group because they fear any kind of changes; others because they fear the growing power of government over

the activities of its citizens, bureaucracy, as they put it; others are there because they worship the words of the Constitution as they were written by the founders of our government; while others are there because they fear that even slight changes in our industrial system and in our Constitution would result ultimately in the adoption of state socialism; and some may be there for purely political reasons. All profess to believe in the efficacy of the laissez-faire policy, and are opposed to government regulation, or "regimentation" as they are pleased to call it. All profess to believe in a literal interpretation of, and compliance with, the exact wording of the Constitution as it was written 150 years ago. The Constitution was written at the time individual freedom and the laissez-faire policy were being glorified both in Europe and in America, and it embraces that philosophy in its wording. It is because of the fact that the Constitution embraces the laissez-faire philosophy that many in the camp on the right are such devout believers in the wording of the Constitution as the basic guide for our future national economic policies.

It is probable that there is less unanimity of opinion among those in the camp on the left than is found among the members of the camp on the right. It is made up of liberal Democrats, Progressive Republicans, intellectual radicals, and many laborers, farmers, professional men, and middle class business men who either are not satisfied with their present economic status or who desire to see some fundamental changes brought about in our industrial system which would give them broader opportunities to make a better living. Most of them are in favor of such things as government regulation of security issues, of stock exchange transactions, and of transactions of banks in order to protect the interests of honest investors. Some of them are in favor of government regulation of hours of labor and of wage-scales in order to eliminate unemployment and increase the purchasing power of consumers. Some are in favor of scaling down debts or of reducing interest rates on outstanding contracts to relieve oppressed debtors; all want to eliminate monopoly advantages and profits resulting therefrom. Some would reduce the size of large estates through high rate inheritance or succession taxes, while all would have those with high personal

incomes bear a larger share of the burden of supporting the government.

Though the members of the camp on the left may not be as unanimous in their opinions as to the best course of action to improve the national economic situation as those in the camp on the right are in their opposition to any kind of reform action, they are unanimous in their opinions as to the goal to be reached. Practically all members of the camp on the left desire to eliminate all special privileges and to revamp our industrial system in such a manner that it will operate continuously and serve the best interest of the whole people. To them the Constitution was made for the purpose of serving the best interest of the whole people at all times and must be interpreted so that it will do so. They think, therefore, that the Constitution should be interpreted liberally rather than literally so that it may be made to fit changed conditions and new problems. Many of them do not hesitate to advocate changes in the Constitution if necessary to do so to pursue legislative policies that will improve the operation of our industrial system.

The business leaders of the country have been more outspoken in their criticism of the Roosevelt policies and have made more definite suggestions as to the kind of economic policies they think the nation should follow than any other group. The United States Chamber of Commerce, the American Manufacturers Association, and other groups of business leaders issued several statements in 1934 and 1935 in reference to New Deal policies. These statements indicate that the leaders of these organizations of business men are opposed to the New Deal policies in the following particulars:

1. They fear the experimental monetary and currency policy of the Administration, and desire that the government return to a definite monetary policy based on a definite gold standard. They express fear that rank currency inflation may result from the growing national indebtedness and the experimental monetary policy. It is claimed also that these two policies of the Administration hold back recovery of business.

2. They are opposed to strict government control over the Federal Reserve System and over the operation of member banks. They fear that the banking business in the future may

be operated in the interest of government financing and other policies of the government, rather than in the interests of commerce and trade. They are opposed to the government entering the banking business and making loans directly to farmers and to business enterprises.

3. They are apprehensive of the mounting national indebtedness caused by the large relief and recovery expenditures of the Roosevelt Administration. They demand that the extraordinary expenditures be decreased and that the budget be balanced as nearly as possible.

4. They are not in favor of a large public works program to stimulate recovery and to give employment to the unemployed. They think that Federal expenditures for the support of the unemployed should be reduced; that unemployment relief given should be direct in the form of "doles" and should be based on actual needs rather than on rights of the unemployed.

5. They are not in sympathy with the President's social security program providing for unemployment insurance and old age pensions. It is claimed that the security plan will burden industry and stifle the initiative and energy of laborers.

6. They are opposed to the Tennessee Valley Authority as well as to all other government activities in competing with private industry in the operation of business.

7. They are in favor of self-regulation of industry (by the leaders in each industry) and liberalized anti-trust laws. They favor "codes of fair competition" made and enforced by the leaders of industry. They are definitely opposed to government regulation of business, and particularly opposed to the government regulating hours and wages of laborers. They desire to see all of Section 7, the labor provisions of the National Industrial Recovery Act, abolished.

8. They are not in sympathy with the Administration's agricultural program under the Agricultural Adjustment Act. They are particularly opposed to the processing taxes on agricultural products, and express some opposition to any kind of restrictions on agricultural production.

9. They think that most provisions of the Securities and the Stock Exchange acts are too drastic in regulating the issuance

of new securities and in controlling the trade in securities on exchanges. They are opposed to all the provisions of the Holding Company Act.

10. They are against high corporation, income, and inheritance taxes. They decry any effort on the part of the government to use the taxing power to equalize personal incomes or to redistribute wealth and income.

11. They want a national economic adjustment on the basis of the operation of the "natural economic laws of supply and demand"—with the business leaders manipulating both through self-regulation of industry.

The legislative program of the American Federation of Labor of 1935 appears to have been in favor of the following measures:

1. An extension of the NRA with its guarantee of bargaining rights for labor.

2. Passage of a thirty-hour week bill.

3. Support of the President's social security program providing for unemployment insurance and old age pensions.

4. Support of the Wagner Labor bill providing for the outlawing of company unions and the enforcement of collective bargaining.

5. A large program of public works to furnish jobs for the unemployed.

The majority of the American farmers, insofar as they have expressed themselves, appear to be in favor of a continuation of the Administration's agricultural program of control over farm production through the provisions of the Agricultural Adjustment Act and the Bankhead Cotton Production Control Act. A poll of farmers in October, 1935, registered a decisive majority in favor of continuance of these acts.

A host of nationally known writers and speakers have made specific criticisms of various parts of the Roosevelt program. Many of these criticisms will be noted in later chapters, with detailed analysis of various parts of the Roosevelt program. On September 30, 1934, President Roosevelt addressed the American people on the state of the union and on the Administration's attitude toward its program. The following are extracts from this speech:

"Nevertheless the gains of trade and industry, as a whole, have been substantial. In these gains and in the policies of the administration there are assurances that hearten all forward-looking men and women with the confidence that we are definitely rebuilding our political and economic system on the lines laid down by the new deal—lines which as I have so often made clear, are in complete accord with the underlying principles of orderly popular government which Americans have demanded since the white man first came to these shores.

"We count, in the future as in the past, on the driving power of individual initiative and the incentive of fair private profit, strengthened with the acceptance of those obligations to the public interest which rest upon us all. We have the right to expect that this driving power will be given patriotically and whole-heartedly to our nation."

. . . . . .

"Nearly all Americans are sensible and calm people. We do not get greatly excited, nor is our peace of mind disturbed, whether we be business men or workers or farmers, by awesome pronouncements concerning the unconstitutionality of some of our measures of recovery and relief and reform. We are not frightened by reactionary lawyers or political editors. All of these cries have been heard before. More than twenty years ago, when Theodore Roosevelt and Woodrown Wilson were attempting to correct abuses in our national life, the great Chief Justice White said:

> 'There is great danger it seems to me to arise from the constant habit which prevails where anything is opposed or objected to, of referring without rhyme or reason to the constitution as a means of preventing its accomplishment, thus creating the general impression that the constitution is but a barrier to progress instead of being the broad highway through which alone true progress may be enjoyed.'

"In our efforts for recovery we have avoided on the one hand the theory that business should and must be taken over into an all-embracing government. We have avoided on the other hand the equally untenable theory that it is an interference

with liberty to offer reasonable help when private enterprise is in need of help.

"The course we have followed fits the American practice of government—a practice of taking action step by step, of regulating only to meet concrete needs—a pratice of courageous recognition of change. I believe with Abraham Lincoln, that 'the legitimate object of government is to do for a community of people whatever they need to have done but cannot do at all, or cannot do so well for themselves in their separate and individual capacities.'

"I am not for a return to that definition of liberty under which for many years a free people were being gradually regimented into the service of the privileged few. I prefer and I am sure you prefer that broader definition of liberty under which we are moving forward to greater freedom, to greater security for the average man than he has ever known before in the history of America."

CHAPTER NINE

CONSEQUENCES OF THE ROOSEVELT MONETARY POLICIES

IN ORDER to understand the Roosevelt monetary policies it is necessary, first, to know what he expected to accomplish through them, and, second, to understand the monetary theory upon which they are based. According to his own statement the President hoped to raise prices to the level "where debtors could pay their debts with dollars of the same value as the dollars they borrowed." Why raise prices to such a level? What is the theory of how best to accomplish the feat?

There is an irrefutable ethical defense for the argument that it is unjust and unfair to expect debtors *to pay* their debts with dollars having a much greater value (purchasing power) than the dollars they borrowed. Moreover, it is evident to any student of business affairs that it is impossible for most debtors to discharge debt obligations, contracted when prices and incomes were high, under conditions of low prices and incomes. Paying ability as well as social justice requires that debtors receive incomes large enough to pay their debts, if their debts are paid. The defenders of the President's reflation monetary policy argue that the raising of prices to the predepression level would so stimulate trade, employment, and production that debtors again would receive predepression incomes. Therefore, it is thought that higher prices not only would relieve debtors of the unbearable burdens of their debts but would result in general business recovery. The most ardent advocates of reflation claim that business was depressed because prices were low, and that prices were low because there was a shortage of money. To them the evident remedy for the depression was to raise prices and increase the volume of production by increasing the volume of money (purchasing power).

The Roosevelt monetary policy is based on the theory that not only is it possible to raise the general price level by increasing the supply of purchasing power, but that it is also possible to stabilize the price level at any desired point by controlling the volume of purchasing power in circulation. This theory is often referred to as the stable price level or controlled currency theory. It is stated by Professor Irving Fisher in the form of an equation as follows: $MV+M'V'=PT$. M is the specie and currency in circulation; V is the velocity of circulation of M; M′ is the volume of demand bank deposits; V′ is the velocity of circulation of the bank deposits; P is the general price level; and T is the physical quantity of trade. An increase in either money and currency or in bank credit will necessitate an increase in the quantity of trade or in the price level to balance the increase in the quantity of purchasing power. A decrease in the quantity of money or in bank credit would cause a decrease in the price level if the volume of trade remained the same.

Those who hold to this theory claim that in the past all major fluctuations in the price level have been due to fluctuations either in the quantity of specie and currency or in the quantity of bank credit. Those theorists assume further that the government could exercise control over the quantity of money and the volume of bank credit in circulation and thereby control the general price level at will. In short, they hold that all fluctuations in the general price level are due to changes in the quantity of purchasing power in circulation not warranted by changes in the physical volume of business, and that such price fluctuations can be prevented by government control over the volume of purchasing power in circulation.

These theorists would control the prevailing price level (1) by regulating the amount of money (specie and currency) in circulation, and (2) by regulating the quantity of outstanding bank credit. In extreme cases they would decrease the gold content of the standard dollar and increase the number of gold dollars or certificates in circulation to make prices rise, or increase the gold content of the standard dollar to force prices to fall. They would increase the amount of outstanding currency (Treasury notes, silver and silver certificates and bank notes) to force

prices to rise, or decrease it to force prices to fall. Again, they would increase the amount of outstanding bank credit to cause prices to rise, or contract it to force prices to fall. Through the exercise of these three policies, they claim that the government should be able to control the general price level at its pleasure, or to maintain a stable price level forever if it desired to do so.

In short, the controlled price level theorists base both their theory and their policies upon the following assumptions: First, that the general price level can be stabilized by the government's regulating the general market demand for goods in relation to the prevailing general market supply of goods. Second, that the general market demand for goods can be regulated by the government through controlling the quantity of purchasing power (money and bank credit) in circulation. Third, the government can control the quantity of purchasing power in circulation by applying the three methods enumerated in the paragraph above.

Unquestionably, the Federal government has the constitutional power to control the quantity of money (standard dollars, subsidiary coins and currency) in circulation if the Congress grants such powers. The Roosevelt monetary policy is based on the theory that the Federal government may and should exercise control over the quantity of money in circulation in such a manner as to bring about an increase in prices to the predepression level and then stabilize them at that point. Also, the Roosevelt banking policy, as we shall see in the next chapter, is, in part, based on the theory that the government may control the operation of banks in such a manner as to regulate the quantity of outstanding bank credit. During the first two and one-half years of his administration, President Roosevelt's monetary policy was as follows:

By 1932, as a result of the declining price level and the inability of debtors to meet their obligations, there was a growing demand on the part of many groups that the government do something to raise prices and improve business. Only a few were openly in favor of inflation of prices. The most influential advocates of higher prices were in favor of reflating prices to the predepression level or to the 1926 level. The National Democratic platform of 1932 declared that the party was in

favor of a "safe adequate currency system." As a result of the continued decline in the price level up to March, 1933, the inflationists and the reflationists gained strength in Congress.

Because of this growing sentiment for inflation the so-called Thomas amendment was attached to the Agricultural Adjustment Act (approved May 12, 1933), giving the President discretionary power to reflate or inflate the price level by the use of one or more of four devices. The optional monetary and currency control devices stated in the Thomas Amendment (Inflation Act) which might be exercised by the President are: (1) Power to order the Federal Reserve banks to purchase United States securities up to the amount of three billion dollars in excess of such securities held by the Reserve banks on the date of the passage of the Act; (2) power to cause to be issued Treasury notes (government paper money) up to the amount of three billion dollars for the purpose of purchasing outstanding interest-bearing obligations of the government; (3) power to reduce the gold content of the dollar not more than 50 per cent of its former weight; and (4) power to fix the weight of the silver dollar and to provide for an unlimited coinage of both gold and silver at the ratio so fixed.

Before the passage of the Inflation Act, the President announced that it would be his policy to raise the price level to the point at which debtors would be able to pay their debts with dollars of the same value as those they borrowed, and then stabilize the price level at that point. While he did not state exactly how much he desired to raise the price level or at what particular level he desired to stabilize, it was generally supposed that he desired to reflate prices to the 1926 level and stabilize at that point.

In pursuance of this monetary policy, on April 19, 1933, the President declared the United States off the gold standard and put into operation the device of reducing the gold content of the dollar. By establishing a government market for gold in terms of dollars the President was able to raise the price of gold to $35 an ounce and to depreciate the value of the dollar a little more than 40 per cent in terms of gold. By a proclamation on January 31, 1934, and in pursuance of the Gold Reserve Act approved the day before, the President fixed the content

of the dollar at 13.71 grains of fine gold, or 59 per cent of its former weight or gold content. As a result of the gold devaluing process, the government increased the number of gold dollars (or gold certificates) in the country to the amount of $2,800,000,000 and made a paper profit of an equal amount. According to the Gold Reserve Act, the President may from time to time temporarily fix the gold content of the dollar anywhere within a range of from 50 to 60 per cent of its former weight of 23.22 grains of fine gold. While by his proclamation of January 31 the content of the standard dollar was fixed temporarily at 13.71 grains of fine gold, he may reduce it later to one-half of 23.22, or to 11.61 grains, if he decides such a reduction is advisable.

Many bond contracts in this country contain a "gold clause" providing that the principal and interest of the bonds shall be payable in gold dollars of 23.22 grains of fine gold. After the President took the country off the gold standard in the spring of 1933 the Congress passed a joint resolution nullifying the gold clause in all debt contracts by providing that all debt contracts shall be settled through the payment of standard dollars prevailing at the time the payments are made on those contracts, instead of through payment of so much gold or money equal in value to so much gold. In the early spring of 1935 the Supreme Court sustained the constitutionality of the action of the Congress in nullifying the gold clause in existing private contracts.

Following the passage of the Inflation Act (the Thomas Amendment) the Federal Reserve banks made heavy purchases of government securities; from the date of the passage of the Act to September 1, 1934, these banks increased their holdings of such securities almost two billion dollars. Such purchases by the Reserve banks resulted in increasing the cash reserves of the commercial banks, which, as will be seen in the next chapter, were expected to cause an expansion of private bank loans. An increase in commercial bank loans, it was assumed, would be attended by an increase in buying and in prices. While cash piled up in the commercial banks as a result of the purchase of government securities by the Federal Reserve banks, there was very little increase in bank loans or expansion of commercial

bank credit up to June, 1935. This problem will be discussed further in chapter ten.

Other than providing for the purchase by the United States mints of newly mined silver at an increased bullion price, for more than a year the President did not put into operation the silver provision of the Inflation Act. Then the Congress passed the Silver Purchase Act, which was approved on June 19, 1934. This act declared it to be the policy of the United States government to increase the monetary stock of silver in proportion to gold with the ultimate objective of having and maintaining one-fourth of the monetary value of such stock (gold and silver) in silver. The President is authorized through executive order to require delivered to the United States mints any or all silver by whomever owned and to pay a fair market price for the same. The silver purchased is to be coined into standard silver dollars or is to be used as a basis for the issuance of silver certificates based on standard silver dollars.

In pursuance of the Silver Purchase Act of 1934, the President issued a proclamation and an executive order on August 9, 1934, nationalizing silver and providing for its purchase by the government at 50 cents an ounce. The President also ordered the Treasury Department to issue silver certificates at the ratio of $1.29 per ounce for all the silver it possesses or acquires at 50 cents an ounce for silver; this action meant a money inflation of 79 cents on each ounce of silver possessed or purchased, or 60 cents on each one-dollar silver certificate issued. In short, a one-dollar silver certificate is backed by 40 cents of silver bullion at a market price of 50 cents per ounce, plus the fiat of the government. At the time of the executive order (August 9, 1934) the Treasury possessed 62,000,000 ounces of silver which at 50 cents per ounce is worth $31,000,000, but for which it had actually paid $46,900,000. The Treasury was directed to issue $80,000,000 silver certificates (paper money), secured by this silver bullion costing $46,900,000; this transaction increased the circulating currency $80,000,000 and gave the government a paper profit of more than $33,000,000.

As a result of the President's silver nationalization proclamation and executive order of August 9, 1934, from that date up to May 10, 1935, the United States government acquired 112,-

733,192 ounces of silver at 50 cents an ounce, or at a cost of $56,366,596; upon a basis of this amount of silver the Treasury is authorized to issue $145,225,757 of silver certificates (at the ratio of $1.29 of silver certificates for each ounce of silver); this transaction gives a paper profit of over $88,000,000 to the government, or an actual currency inflation of that amount.

On December 21, 1933, the President issued a proclamation authorizing the Treasury Department to purchase silver newly mined in the United States and to pay a fair price for it. The prices actually paid have ranged from 50 cents an ounce to 77.57 cents (April 24, 1935). From the date of this proclamation up to May 10, 1935, the United States Treasury purchased 35,480,000 ounces of newly mined silver. As a result of the Roosevelt silver policy the amount of silver certificates in circulation (outside the United States Treasury and the Federal Reserve banks) increased from $387,000,000 in October, 1933, to $623,000,000 in March, 1935.

In order to carry out the objective stated in the Silver Purchase Act of 1934, of having silver bullion constitute one-fourth of the monetary stock of the nation, it would be necessary for the government to acquire 1,300,000,000 ounces of silver above that which it owned on August 9, 1934. From that date to April, 1935, the government acquired less than 150,000,000 ounces of silver; at the latter date the government still was short more than 1,000,000,000 ounces of silver in having one-fourth of the value of its monetary stock in silver. Should the President decide to acquire this huge quantity of silver in the world's market, the amount of monetary inflation that would result from the Silver Purchase Act would be tremendous. It would require more than $500,000,000 with which to purchase this silver at 50 cents per ounce; as a result of its purchase there would be issued more than $1,300,000,000 additional silver certificates. Should such a policy be followed the nation could have, as a result of the Silver Purchase Act, more than $1,700,000,000 new silver certificates, and an inflation of the currency (and a paper profit to the government) of about $1,000,000,000.

Up to the summer of 1935 the President's silver policy had resulted in very little actual inflation of the currency—less than $250,000,000 in new silver certificates. But the policy caused

a good deal of uneasiness on the part of the sound money advocates and stimulated public fear of impending inflation. The policy also greatly increased the domestic and the world price of silver. The domestic price was raised from about 35 cents an ounce to over 77 cents. There exists a strong silver bloc of senators in the United States Senate who insist that the government "do something for silver" and the silver-producing states whom they represent. Because of the increase in the world price of silver, the foreign trade of China has been injured greatly (China was on a silver standard) and the internal trade of that country was disorganized considerably as a result of falling domestic prices, forcing that nation on November 4, 1935, to abandon the silver standard for a managed currency and a program somewhat similar to that of the United States.

I am unable to see any national or international advantages in this silver policy; apparently it works to the advantage only of a few silver producers. Certainly, if currency inflation is desired it could be secured more effectively by the issuance of Treasury notes (paper money) than by the purchase of silver at artificially high prices in order to issue silver certificates.

The President did not see fit to issue any of the $3,000,000,000 Treasury notes authorized by the Inflation Act. Many of the inflationists in the Congress were greatly disappointed at his failure to use this means of increasing the currency in circulation. In May, 1935, the Congress passed the Soldiers' Bonus bill providing for the payment of $2,200,000,000 to the soldiers as adjusted compensation, payments of which were to be made by the issuance of that amount of Treasury notes. On May 22, 1935, the President vetoed that bill and in his veto message to the Congress made the following statement in reference to the proposed issuance of the $2,200,000,000 Treasury notes:

"To meet a claim of one group by this deceptively easy method of payment will raise similar demands for the payment of claims of other groups. It is easy to see the ultimate result of meeting recurring demands by the issuance of Treasury notes. It invites an ultimate reckoning in uncontrollable prices and in the destruction of the value of savings, that will strike most cruelly those like the veterans who seem to be temporarily benefited. The first person injured by skyrocketing prices

is the man on a fixed income. Every disabled veteran on pension or allowance is on fixed income. This bill favors the able-bodied veteran at the expense of the disabled veteran.

"Wealth is not created, nor is it more equitably distributed by this method. A government, like an individual, must ultimately meet legitimate obligations out of the production of wealth by the labor of human beings applied to the resources of nature. Every country that has attempted the form of meeting its obligations which is here provided has suffered disastrous consequences.

"In the majority of cases printing press money has not been retired through taxation. Because of increased costs, caused by inflated prices, new issue has followed new issue, ending in the ultimate wiping out of the currency of the afflicted country. In a few cases, like our own in the period of the Civil war, the printing of Treasury notes to cover an emergency has fortunately not resulted in actual disaster and collapse but has nevertheless caused this nation untold troubles, economic and political, for a whole generation."

It is not possible for anyone to state precisely the immediate and ultimate business and industrial consequences of the adoption of the Roosevelt monetary and currency policies. At the time of the adoption of these monetary policies several other New Deal measures were undertaken for the purpose of aiding business recovery. Among these other measures were relief for the unemployed, the public works program, the agricultural program, and the NRA.

There was much improvement in business for the first four months of the Roosevelt Administration. Production increased from 59 per cent of the 1926 level to 100 from March to July, 1933. At the same time the factory employment index increased from 59 per cent to 73 per cent of the 1926 level. Wholesale prices increased from 60 per cent of the 1926 level in March, 1933, to 69 per cent in July of that year. Unquestionably, much of the improvement in business up to July, 1933, was due to inflation of prices caused by going off the gold standard and by the public talk of currency inflation. During this period manufacturers were stimulated to increase their volume of production in order to take advantage of the low cost of production

before the application of the labor provisions of the NRA raised their costs.

Following July, 1933, industrial production declined. From July, 1933, to July, 1934, industrial production declined from 100 per cent to 76 per cent of the 1926 level. In July, 1933, the price index stood at 68.9 and a year later it was 74.8. However, employment during that time increased from 73 per cent to 79 per cent. The index for payrolls from July, 1933, to July, 1934, increased from 50 to 60 per cent of the 1926 level. Unquestionably, most of the increase in employment and in payrolls from July, 1933, to July, 1934, was due more to the operation of the NRA than to the rise in production and in price level; production actually decreased during this period.

After the first four months the price inflation policy did not keep industrial production on a high level. It is believed that the small increase in the price level from July, 1933, to June, 1935, was partly due to the large sums of money paid out by the government to consumers, partly to the operation of the NRA and the AAA, and was due only slightly to the inflation policy of the Administration. It might be said that the inflation policy was not successful in raising prices and stimulating production from July, 1933, to June, 1935. The silver action of August, 1934, probably had a small influence in raising prices after that date.

On the other hand, the Administration's monetary and currency policy engendered a great deal of uncertainty and fear in the minds of business men and bankers. They became uncertain as to the future value of the dollar; they feared price inflation and its consequences. This fear and uncertainty tended to retard industrial expansion; it was one of the principal reasons for the only slight expansion of commercial bank credit during the first two and one-half years of the Roosevelt Administration. Because of the uncertainty and fear created by it, the President's monetary and currency policy largely defeated its own purpose of raising prices and stimulating production.

To my way of thinking, the price control theory upon which the President based the monetary and currency policies is unsound. Also, it may have been unwise to have attempted to raise

prices artificially to the predepression level. The reasons for these conclusions follow:

If it is granted that the government will be able to control or regulate the gold exchange value and the quantity of the purchasing power in circulation, it is unsound to conclude from this assumption, as the stable price level theorists do, that the government will be able to control the general price level at will. In other words, the price level is not determined entirely by the quantity or the gold exchange value of the money in circulation. An increase or a decrease in the total purchasing power of "the money in circulation" does not always increase or decrease the market demand for goods. Under modern economic conditions, the market demand for goods depends as much upon the extent of the distribution of the money in circulation as upon its quantity and quality. In short, the stable price theory completely ignores the fact that the degree of the distribution of the money in circulation has anything to do with the intensity of the market demand for goods, or with the general price level.

Regardless of how much increase might be made in the number of dollars in circulation, unless, at the same time, there is an increase in the number of dollars in the hands of consumers there will be no increase in the market demand for consumers' goods. Should the volume of money in circulation become more and more concentrated in the hands of a few savers and investors and less and less distributed among the mass of consumers, there will be a decrease in the market demand for consumers' goods and a fall in their prices, even though there is no decrease in the quantity of money in circulation. Unless there is a corresponding increase in the real incomes of consumers, a rise in the volume of money in circulation and a temporary rise in the volume of production and in prices will result inevitably in an oversupply of consumers' goods and a fall in the general price level.

A mere reduction of the gold content of the dollar in itself does not increase the purchasing power of consumers, or give them more dollars; such action, therefore, will not and can not permanently raise prices or keep them up in the face of a shortage in consumers' purchasing power. Ultimately the prices of

producers' goods must depend on the prices of consumers' goods, just as the market demand for and production of producers' goods must depend on the market demand for and production of consumers' goods. Because of the fact that in an upswing, business wages and fixed incomes do not rise as rapidly as prices and production, a temporary rise in prices and in production resulting from devaluing the dollar will decrease rather than increase the purchasing power of consumers in relation to the volume of production; then a subsequent decline in prices and in production will be inevitable.

Stable prices cannot be maintained unless the national money income is divided or distributed in such a manner that consumers are able to purchase, at prevailing prices, the consumers' goods produced and offered in the markets. If too much of the national money income goes to investors and too little of it to consumers, eventually there will be an oversupply of consumers' goods and a fall in the general price level. A shortage of consumers' purchasing power cannot be cured by raising prices through decreasing the gold content of the dollar; a speculative rise in prices resulting from such action causes an inevitable shortage in consumers' incomes; consumers' incomes do not rise as rapidly as production and prices.

The assumption of the controlled price level theory that the government can control the value and quantity of money (including bank credit) actually in current use in business is false. It is true that the government can determine the gold value, and thereby the number, of the standard dollars (gold certificates) in the country; it can determine the amount of paper currency which it issues; it can regulate the operation of banks, and under certain conditions can exercise much control over the use of bank credit. But a reduction of the gold content of the standard dollar and an increase in the number of gold certificates does not in itself put more gold certificates in actual circulation; it merely increases the number of gold certificates in the hands of the government and leaves the same number in actual circulation. The issuance of new silver certificates or Treasury notes increases the United States Treasury "cash reserve" or "balance," but it does not in itself put this new currency in actual circulation. In order for the new currency

to get into actual circulation the new currency must be paid out by the government as a gift or as payments for goods or services. The placing of the new currency in circulation must be in pursuance of some *non-monetary* policy of the government; too frequently it is paid out to cover a fiscal deficit in the budget.

Theoretically, new currency issued by the government might be used to increase the quantity of purchasing power in circulation by despositing it in the Federal Reserve banks as a "balance." This government balance would increase the "cash reserves" of the Federal Reserve banks and give them greater loaning power. The controlled price level theory assumes that larger cash reserves in the Federal Reserve banks will cause member banks to borrow more money from the Reserve banks and extend more loans to their customers for business purposes.

It will be shown in the next chapter that business men and business enterprises do not borrow money merely because their bankers are willing to make loans to them; they borrow only when they see a prospect of making profits from the use of the loans. Also it will be shown that member banks do not borrow from Federal Reserve banks to make loans to customers merely because the Reserve banks have large cash reserves. Such transactions on the part of member banks are limited to making loans to customers which are applied for and which they consider sound; they borrow from Reserve banks only when they need to do so to replenish their own cash reserves. The government will be able to bring about little increase in the purchasing power (bank credit) in actual circulation either by attempting to force business firms to apply for bank lonans they do not want, or by attempting to force banks to make loans they consider unsafe.

When there is a business depression, and the prospects of profits are not bright, the government cannot bring about an increase in the amount of bank credit in use as it may desire. Therefore, it cannot control the quantity of money (bank credit) in circulation sufficiently to control the price level at such a time. Normally, 85 per cent of the purchasing power (money) in circulation consists of bank credit. Also, it is doubtful if any government would, if it could, control the expansion of bank

credit during a boom movement so as to prevent the rise in prices.

While I am convinced that there are no purely monetary and banking methods or policies through which the government, at will, can regulate completely the general price level or maintain a stable one, I am cognizant that the government could easily bring about a temporary artificial inflation of prices. Through devaluing the standard dollar, the issuance of great quantities of paper currency, and the distribution of this currency through doles, bonuses, public works, and other donations and expenditures the price level could be increased greatly by the government. Prices could be made to "skyrocket" to the extent to which the people were made to lose faith in the soundness of their money and to the extent to which artificial purchasing power is paid out by the government to the public. Such an inflational movement at present would bring about a temporary improvement in business, but in the end it would be detrimental if not disastrous for the country. Rank inflation is one of the dangerous possibilities of the New Deal monetary and banking policies, as they may be affected by its public expenditure and public finance policies.

Granting that an improvement in business immediately follows any artificial inflation of the price level, it is my opinion that such a business recovery could not in its very nature be a permanent one. Recovery brought about by such methods would prevent the necessary readjustments in our industrial system which normally occur during periods of depression. Booms preceding depressions cause an overexpansion of bank credit, an accumulation of surplus stocks of goods, an overcapitalization of business, unsafe investments, and much inefficiency in the operation of business enterprises. Ordinarily, these defects in the operations of our industrial enterprises are temporarily cured by the severity of the depressions. To bring about recovery of business through artificial prices would tend to perpetuate these bad consequences of the boom of the twenties and carry them over into a new boom of the thirties.

At the beginning of the 1929 depression it was generally recognized that there was a great shortage of consumers' money income, and that one of the chief ways to bring about recovery

was to increase this income. It has been shown that artificial inflation of the price level tends to decrease consumers' actual purchasing power in proportion to goods produced, rather than to increase it. A recovery brought about by an artificial inflation of the price level, therefore, tends to intensify as well as to perpetuate the causes which produced the depression; such a recovery surely would result in another depression.

Again a rise in the price level due to artificial inflation has only a temporary effect in stimulating production. In order to keep production going through such tactics it is necessary to continue to inflate the price level. The ultimate results of such a policy are inevitable: if the process is continued indefinitely the money becomes worthless and it becomes necessary to establish a new monetary and currency system under conditions of great business and industrial disorganization and depression. On the other hand, if the process is stopped, an immediate depression will follow.

In view of the above conclusions, it is my opinion that it would have been far better in 1933 for the Administration to have recognized the fact that "production costs" should have been adjusted to a lower price level than that of 1926. Such a policy would have necessitated scaling down debts, writing off inflated capital charges, some monetary reduction in wages, and developing greater efficiency in business administration. It is true that such a policy would have required greater reorganization of business and financial institutions than we have yet experienced. But business recovery on such a basis would have been possible, and it is certain that whatever recovery was made under it would have been based on a solid foundation rather than on the quicksand of inflation.

It is true that such a recovery policy would not have brought about a quick business recovery, or have relieved the debtors by enabling them to discharge their debt obligations. But a sound and lasting business recovery is far more important to the country than a rapid but temporary one. There are other methods by which recovery can be stimulated; these other methods will be discussed in later chapters. There are other means also of relieving debtors of the unbearable burdens of their debts, and these will be discussed in later chapters.

CHAPTER TEN

BANKING AND BANK CREDIT POLICIES OF THE NEW DEAL PROGRAM

THE Roosevelt banking policies appear to have been directed principally toward the accomplishment of the following objectives: (1) Restoring public confidence in the safety and soundness of our banking institutions; (2) eliminating unsound banking practices which developed prior to 1929; (2) making bank credit facilities adequate in all communities for all businesses and industries; (4) lowering the rate of interest charged on all new loans; (5) controlling the expansion and contraction of bank credit; and (6) forcing the Federal Reserve and member banks to absorb a large part of the new government loans. The methods of accomplishing these objectives are: First, stricter laws regulating banking practices; second, government financial aid to privately owned banks, and the creation of governmental loaning institutions; and, third, extensive government control over the operation of the Federal Reserve banks, and detailed control by the Federal Reserve Board over the operation of member banks.

The Emergency Banking Act (March, 1933) was designed primarily to restore public confidence in our banking institutions. The National Banking Act of 1933 was drawn primarily to eliminate the admittedly bad banking practices, and secondarily to increase the banking facilities of the country. The Thomas Amendment clause, providing for the purchase of government securities by the Federal Reserve banks, was intended to increase the cash reserves and the loaning power of member banks. A great number of governmental loaning agencies were organized or developed to furnish adequate credit facilities to businesses that were not being served adequately

by privately owned banks. All of these measures were intended to lower the interest rates on loans. The proposed Banking bill of 1935 was designed to give the government through the Federal Reserve Board more complete control over the operation of the Federal Reserve banks, and more complete regulatory power over the operation of member banks. Apparently, this proposed act was intended also to make complete the government's power to control the expansion and contraction of bank credit and to give it unlimited power to force the banks to absorb new government loans.

It is generally conceded that the misuse of bank credit during the twenties was one of the causes for the severity of the depression which occurred in 1929. Many unsound banking practices developed during and following the World War. During the war our banking facilities developed far beyond the peacetime needs of the country; following the war and up to 1929 our commercial banks, finding it impossible to employ their funds in legitimate commercial loans, diverted a large part of their assets to investments and to speculative loans. Many of the banks acquired ownership in and control of investment companies and other affiliate organizations to which they made large loans. When the depression of 1929 occurred, a large number of the banks found that only a small part of their assets were liquid or convertible into cash; too much of their funds were tied up in securities, collateral loans, and other loans of an investment or speculative character. More than six thousand bank failures resulted.

In a previous chapter it was pointed out that when Franklin D. Roosevelt became President in March, 1933, more than half the banks in the country already were closed. In order to deal with the crisis in the banking field the President, on March 5, issued a proclamation closing all the national banks and called the Congress into an extraordinary session to pass emergency banking legislation. Within a few days the Emergency Banking Act was passed providing for the immediate reopening of all banks in a sound condition and for a gradual reopening or liquidation of those found to be not in a sound condition. The Emergency Banking Act authorized the Federal Reserve banks to issue temporarily Reserve notes backed by com-

mercial paper only, and permitted the member banks and other commercial banks to borrow from the Reserve banks upon their own notes or upon certain collateral not previously acceptable by the Reserve banks as security for loans.

From the standpoint of the later development of the New Deal banking and credit policies, the most important provision of the Emergency Banking Act was the one concerning the reorganization and rehabilitation of weak banks. It provided that whenever the comptroller of the currency found a national bank in an unsafe or non-liquid condition, he was directed to appoint a "conservator" for that bank. After taking over such bank the conservator was given the power either to liquidate or to reorganize it according to his discretion and the demands of the community. In case a conservator decided to reorganize a bank, the Reconstruction Finance Corporation was authorized to purchase the preferred shares of stock of the recapitalized bank. Largely as a result of this provision, the Reconstruction Finance Corporation, up to March 31, 1935, had invested more than $882,000,000 in the shares, notes and debentures of the capital of banks, and the government had become the owner of stocks in more than three thousand banks. This large ownership of stock in banks gives the government a voice in their management. In addition to this large ownership of bank stock, the Reconstruction Finance Corporation had outstanding on March 31, 1935, more than $531,000,000 loans to banks and trust companies.

As a result of the reopening of the banks under the Emergency Banking Act the bank crisis soon ended. There were no more runs on banks, and the people redeposited their hoarded funds. The reopening and reorganization of the weak and unsound banks under the supervision of conservators proceeded in an orderly manner.

The Banking Act of 1933 was approved by the President in June, 1933. It was written largely by Senator Carter Glass and was passed for the purpose of correcting the admitted abuses which had developed in banking practices prior to 1929. The law states that it is "an act to provide for the safe and more effective use of the assets of banks, to regulate inter-

bank control, to prevent the undue diversion of funds into speculative operations and for other purposes."

The Banking Act of 1933 places restrictions upon the use of bank credit for speculative purposes by giving the Federal Reserve Board power to control the discounts, advances, and accommodations of Reserve banks to individual member banks. Whenever it becomes evident that a particular member bank is using its funds for speculative purposes the Board has the power to prevent it from securing additional accommodations from the Reserve banks. Member banks are prohibited from acting as agents for individuals or firms making loans to brokers on securities as collateral. Also, member banks are to be limited in dealing in securities for their own account by such regulations as may be prescribed by the comptroller of the currency. Then, there are provisions further limiting the amount of loans to one corporation and its subsidiaries, as well as limiting the amount of bank funds which might be invested in real estate.

Also, bank affiliate and group bank activities are curtailed by the Act, and such affiliates are subjected to examination by bank examiners. An affiliate is a state-organized company owned either by the trust company of a national bank or by the stockholders of the bank. An affiliate may be a banking organization or it may be an organization to deal in securities; group banking, as well as speculation in securities with bank funds, is carried on under the affiliate type of organization. The Act provides that after three years member banks must divorce themselves from any connection with affiliate or group banks organized to deal in securities. Examiners for all affiliate banks may be appointed by the Federal Reserve Board; loans to any one affiliate bank by a member bank are limited to 10 per cent of the bank's capital and surplus, and it may not loan more than 20 per cent of its capital and surplus to all affiliates combined. Also, such loans must be secured by the kind of collateral specified by the Act.

The Act sets up the Federal Liquidating Corporation to take over failed banks and liquidate their assets. This corporation is provided for the purpose of facilitating the winding up of the affairs of failed banks and paying off the depositors, and organ-

izing new banks to take the place of failed banks where such banks are needed. The Act also gives the Federal Reserve Board complete control over the relations and transactions of all Federal Reserve banks with foreign banks. In many respects the provisions of the Act further centralize the control of our banking facilities in the hands of the Federal Reserve Board.

The 1933 Banking Act also created the Federal Bank Deposit Insurance Corporation and provided for a deposit insurance fund. This fund was made up of $150,000,000 appropriated by the Federal government, plus stock subscriptions by the banks. This section of the Act provides a guarantee for all individual deposits up to $2,500 from January 1, 1934, to June 30, 1934; it provides that after July 1, 1934, the Corporation, under a permanent insurance fund, shall insure fully all the deposits of all member banks under $10,000 and partly insure those above that amount. Deposits in non-member state banks are insured until July 1, 1936, and after that date the insurance is limited to members of the Federal Reserve System. In June, 1934, the Bank Deposit Insurance Act was passed extending the temporary bank deposit insurance plan until July 1, 1935, and increasing the amount of the guaranteed deposit from $2,500 to $5,000. This act also postponed the termination of insurance of non-member bank deposits under the permanent insurance fund until July, 1937.

Practically all conservative bankers and students of banking problems are agreed that the banking reforms provided for in the Banking Act of 1933 were desirable, if not absolutely necessary in order to place banking in this country on a sound basis. There were some objections on the part of bankers to certain provisions of this Act, such as the separation of banks from affiliates and the guarantee of deposits. But that opposition was not strong, and died out soon after the passage of the Act.

As a result of the creation of the Reconstruction Finance Corporation by an act of the Congress approved in January, 1932, the Hoover Administration initiated the policy of the government extending direct financial aid to debtors and those in need of new loans. This act has been amended, expanded and modified many times since its original passage. The Reconstruction Fianance Corporation was created originally for the

purpose of making loans to distressed banks and railroads. As a result of various amendments, the functions of the Corporation were expanded so that it is now authorized: (1) To provide intermediate credit for financial institutions and for railroads; (2) to purchase preferred stock in banks and to supply capital funds for various government-owned financial corporations, such as the Federal Home Loan Banks, the Home Owners' Loan Corporation, and for the Land Bank Commissioner; (3) to provide intermediate credit for agriculture and loans to finance the storage and sale of surplus agricultural products; (4) to provide loans for public and regulated private construction projects; and (5) to direct capital loans to small business enterprises.

The Roosevelt Administration expanded the powers of all existing governmental financial agencies for making loans and created several new ones. The various loaning agencies and loaning institutions of the government, other than the Federal Reserve banks and the Reconstruction Finance Corporation, may be divided roughly into three classes: (1) Those which provide funds for refinancing old funded and unfunded debts; (2) those which make new loans; and (3) those which guarantee outstanding debt obligations, such as bonds, mortgages, and deposits. Many of the government financial agencies could not be placed exclusively in any one of these classes because they perform two or more of the three functions. Such would be true

THE THREE CLASSES OF GOVERNMENT FINANCING AGENCIES

For Refinancing Old Debts	For Making New Loans	For Guaranteeing Debt Obligations
Farm Credit Administration	Farm Credit Administration	The United States Treasury
Federal Farm Mortgage Corporation	Commodity Credit Corporation	Federal Deposit Insurance
Federal Land Banks	Production Credit Corporation	Federal Savings and Loan Insurance Corporation
Home Owners' Loan Corporation	Intermediate Credit Banks	Home Credit Insurance Corporation
Federal Home Loan Banks	Export-Import Banks	
Land Bank Commissioner	Federal Savings & Loan Associations	
	Banks for Co-operatives	
	Federal Land Banks	
	Federal Home Loan Banks	

of the Federal Farm Mortgage Corporation, the Farm Credit Administration, and the Home Owners' Loan Corporation. The chart here given divides the various governmental financing institutions into three classes, according to their chief functions in reference to loaning and guaranteeing loans.

The assets and liabilities of all the governmental corporations and credit agencies, as of February 28, 1935, will be found in Table XIV of Appendix A. Table XV[1] gives detailed statistical information in reference to the loaning activities of the Reconstruction Finance Corporation. Chapter twelve is devoted to a study of the refinancing of debts and other debt relief measures, and the debt refinancing functions of the governmental financial agencies will be discussed in that chapter. The present chapter is concerned only with the activities of these agencies in making new loans.

All of these governmental financial agencies were created for the purpose of relieving an emergency financial situation in some phase of our economic life. Most of them were organized at the time our banks were having serious financial difficulties and many of them had failed. As already pointed out, the Reconstruction Finance Corporation was created to give relief to the large debtors. The Intermediate Credit Banks were organized to provide loans to farmers who were unable to borrow from their local banks. Insofar as these agencies fulfilled a real financial need that could not be served by the privately owned and operated banks, their creation was justified. Unquestionably, some of these agencies have furnished needed and deserved financial assistance to many business concerns and farmers which could not have been secured from local banks. Business enterprises have been kept operating that otherwise would have closed down; thus the credit banks have, in many cases, aided production and employment.

The banking policy of the Roosevelt Administration from the first has been to do everything possible to encourage the expansion of bank loans. As already indicated, the Administration proceeded upon the assumption that a forced expansion of bank credit would result in an increased volume of production and trade and in a rise in prices. It was pointed out in

1 Pp. 285-86.

chapter nine that prices did rise as a result of going off the gold standard and that production increased temporarily, but commercial bank loans did not expand. In order to increase the loanable funds of the banks in the early part of the Roosevelt Administration, the Reconstruction Finance Corporation loaned large sums of money and purchased many hundreds of millions of dollars of these banks' shares of stock. Also, as already indicated, the Federal Reserve banks purchased large quantities of government securities from the member banks in order to increase their cash reserves. Then, too, by the winter of 1933-34 a large part of the huge funds paid out by the government for relief and for public works flowed into the banks to swell their reserves; but the banks did not expand their loans to customers.

In the spring of 1934, some of the officials of the Roosevelt Administration accused bankers of not co-operating with the government in its recovery program, and said that many of them had refused to make needed industrial and business loans to deserving business enterprises. The bankers replied that few sound business firms had made applications for new loans; they claimed that requests for additional loans came mostly from financially weak business concerns who desired to refinance their old debts rather than to expand their businesses. Some of the bankers asserted that solvent and safe business firms did not desire to expand their businesses because of the uncertainty of the business outlook, and that, therefore, such concerns did not desire additional bank loans. A few of the bankers admitted that they did not desire to make a great many new loans because they feared the possibilities of wild inflation; some claimed that they were cautious about making new loans because of their sad experiences with old loans from 1929 to 1933, and because of the uncertainty of the future business situation. Also, it was stated by several bankers that the government at that time was absorbing the best loans through its own loaning agencies.

To encourage new capital loans to business enteprises, Congress passed an act in June, 1934, which permitted the Federal Reserve banks and the Reconstruction Finance Corporation, under stipulated safeguards, to make direct capital loans of from one to five years to small business concerns. The Federal

Reserve banks are authorized to make such loans to an aggregate not to exceed $280,000,000. Also, the Federal Reserve banks are directed to co-operate with member banks in making capital loans of from one to five years to small business enterprises in need of operating capital.

There seems to have been little opposition on the part of bankers to the government's refinancing of home and farm mortgages, but as already indicated, there has been much opposition to the government financial institutions' making new loans to individuals or to corporations. Is the government unduly competing with private banks and private financial institutions for new commercial loans? The questions here involved are: Is it necessary for the government to remain in the banking business to supply adequate loanable funds to deserving and responsible borrowing individuals and business concerns? Should the government attempt to expand bank credit and bring about a rise in the price level by going into the banking business? The first question does not admit a ready answer, since one does not know whether solvent banks now refuse to make loans requested by solvent firms to be used for legitimate business purposes. But, in reference to the second question, I feel certain that it is unwise and unsafe for the government to go into the banking business for the purpose of expanding credit and raising the price level. Government engagement in the banking business seems to me justified only if and when private bankers fail to supply needed banking services.

In the early days of the 1935 session of the Congress, the Roosevelt Administration submitted a proposed banking act of 1935 for the consideration of the Congress. The bill aroused much public discussion and was the object of extensive hearings by the banking committees of the two houses of the Congress. Many business men and bankers condemned title II of the proposed act, and many of the supporters of the Administration defended the provisions contained in it. On April 21, 1935, Senator Duncan U. Fletcher, Chairman of the Senate Committee on Banking and Currency, issued a public statement on the proposed banking act of 1935, in which he explained its provisions and briefly defended them.[2]

2 See Appendix E, p. 318.

It was claimed by the opponents of this Banking bill that an enactment of its provisions would subject both the Federal Reserve banks and the member banks to great dangers of political domination of their policies and operations. They opposed the suggested provision that the Governor of the Federal Reserve Board be permitted to hold office only during the pleasure of the President; they also objected to the proposal that the governor of each Federal Reserve bank must be approved annually by the Federal Reserve Board. They also opposed limiting to six years the services of directors of the Reserve banks who represent commerce and industry; they protested against the proposed changes in the eligibility qualifications of the appointive members of the Federal Reserve Board. It was claimed that the suggested provision that the Reserve Board members be qualified "to participate in the formulation of national economic and monetary policies," and the proposal that the Board use such powers as it possesses to mitigate "unstabilizing fluctuations in the general level of production, trade, prices and employment," introduced the national planning idea into the policies of the Federal Reserve System. The opponents of the bill asserted that such a new policy would not be in harmony with sound banking principles and practices.

Many of the big business leaders and bankers objected to practically all of the provisions of the suggested act in reference to changing the banking practices of the Reserve banks and member banks. A special committee of the Chamber of Commerce of the United States in May, 1934, registered the following objections to these proposed changes:

> "It should not be provided that the open market policies of the System shall be determined by the Federal Reserve Board or by a committee composed of the Governor and two members of the Board and two governors of reserve banks, or that either such group shall possess broad powers to dominate the purchases and sales of government securities and bankers' acceptances by the Reserve banks, to pass upon their discount policies, or, as was later suggested, to modify from time to time the reserves required of member banks.

"It should not be provided that obligations guaranteed by the government shall be eligible for purchase and sale by the reserve banks, without limits as to volume or maturity.

"It should not be provided that the only specific cover to be required for Federal Reserve notes shall be a minimum of 40 per cent in gold certificates.

"It should not be provided that the eligibility requirements for the rediscount of commercial and other paper and for advances to member banks shall be left to the discretion of the Federal Reserve Board.

"It should not be provided that the reserves to be required of member banks from time to time shall be left to the discretion of the Federal Reserve Board, or, as was later suggested to the proposed open market committee.

"It should not be provided that the powers of the member banks to make loans upon the security of real estate shall be changed in the manner originally proposed in the bill or, as was later suggested, be left to the discretion of the Federal Reserve Board."

It is probable that there are no really valid reasons for objecting to the provisions of the bill which would give the government more complete control over the Federal Reserve System. In my opinion, the governor and manager of each Federal Reserve bank should be a representative of the Federal Reserve Board, and the Board should be able to control the detailed operating policies and current practices of each of these banks. Therefore, the Federal Reserve Board should have sufficient power over the board of directors of each Federal Reserve bank to enforce its own general policies in the operation of those regional banks. But, I am not in accord with the proposal that the Federal Reserve Board may formulate national economic and monetary policies. The Federal Reserve Board's powers should be limited to the management of the nation's bank credit policies, in conformance with sound banking principles stated in the banking laws. But both the national monetary policies and the national economic policies should be determined only by legislative action of Congress.

The proposal that the Federal Reserve Board use all the powers it possesses to mitigate "unstabilizing fluctuations in the general level of production, trade, prices and employment" is entirely too broad a grant of power, and, in my opinion, embraces a false economic and monetary theory. This proposed grant of power is in part, based on the fallacy of the stable price level theory, which holds that all fluctuations in our industrial system can be controlled through management of our monetary and bank credit policies. In chapter nine the fundamental fallacies of this theory were exposed. Certainly, nothing short of comprehensive government control over the distribution of the national money income, as well as government control over monetary and credit policies, could eliminate business depressions. One of the basic causes of business depressions in modern times is a relative shortage of consumers' purchasing power, which, in turn, is caused by unequal distribution of the national income. Whenever a business depression occurs, trade, production, employment, and prices will fall regardless of the government control over the national monetary and bank credit policies.

On the other hand, undue expansion of bank credit, and unwise uses of it during business boom conditions, is the principal reason booms become intense and inflational in their nature. Intense inflational booms usually are followed by drastic deflational business depressions. Therefore, the Federal Reserve Board should have specific power to prevent undue expansion and unwise uses of bank credit during periods of upswings in business. The proposed banking law should be changed to read that "the Federal Reserve Board is directed to use all the powers it possesses to prevent undue expansion and unwise uses of bank credit," instead of that it may use its powers to mitigate "unstabilizing fluctuations in the general level of production, trade, prices, and employment." Control over expansion of bank credit is a power which, at times, could and should be exercised by the Board. But, the broader powers proposed in the bill could not be exercised effectively by the Board during periods of downswings in business; an attempt to do so likely would do harm to the nation. On the other hand, prevention of undue expansion of bank credit during periods of upswings in

business would mitigate extreme fluctuations in the general price level; such control would tend to reduce the intensity of both inflational booms and deflational depressions.

Most of the bill's proposed changes in our banking law in reference to the regulation of banking practices are, in my opinion, unwise. The provision which would give to the Federal Reserve Board the power to control the "open market operations" of the Federal Reserve banks, I think, is sound in principle. On the other hand, I believe the proposal that all obligations guaranteed by the government should be eligible for purchase and sale by the Reserve banks without limits as to volume or maturity, is unsound, if not positively dangerous. Under these two combined provisions the government might force the Federal Reserve banks to use all their available assets to maintain both the credit of the government and a market for its securities. But should the government in the future continue to increase its debt obligations and force the Reserve banks to purchase them, the primary purpose of the Reserve banks (to furnish adequate business and commercial credit facilities to the country) would be destroyed.

Also, I think the proposal to eliminate the present legal requirement—that the Reserve banks hypothecate with the Board specific eligible commercial paper and government bonds as security behind all Federal Reserve note issues—is unwise. Bank assets in the aggregate (which might be unliquid) and a 40 per cent gold certificate reserve behind Federal Reserve notes might prove to be inadequate security for them; such would be the case if the Reserve banks should tie up the principal part of their assets in government obligations. This proposal, together with the one in reference to the purchase and sale of government securities, appears to be designed primarily for the purpose of making the Reserve banks absorb any quantity of new government securities. Certainly neither of the proposed provisions was designed to strengthen the commercial banking facilities of the Reserve banks or of our banking system.

What sound reason, if any, is there for leaving to the Federal Reserve Board the power to determine, at its discretion, the eligibility requirements for paper to be rediscounted for mem-

ber banks by the Federal Reserve banks? Banking practices are, or should be, sufficiently standardized to permit the requirements of eligibility of paper to be rediscounted by the Reserve banks to be stated in the banking law rather than to have the requirements subject to change from day to day by an administrative body. Under such a policy no banker would know today what part of his notes and securities would be accepted for rediscount at the Reserve banks tomorrow. The adoption of this proposal would inject into our banking policies and practices an unnecessary uncertainty which would tend to encourage undesirable fluctuations in the use of bank credit.

The proposal that the amount of "reserves" to be required of member banks be left to the discretion of the Federal Reserve Board, to my mind, is even worse than the one that the Board shall determine the eligibility of paper to be rediscounted by the Reserve banks. Under such a provision, a member bank might be encouraged to increase its loans today and thus reduce its "reserves," and tomorrow that same bank might be told it must reduce its loans in order to increase its "reserves." Why inject the possibilities of such sudden changes and uncertainties into the current operation of member banks? Have we not learned from experience the minimum amount of "legal reserves" commercial banks should possess at all times? If the object of this proposal is to give the Federal Reserve Board the power to limit the amount and character of credit which member banks may extend to customers, the law should define that power directly; it should not be given indirectly through the power to change reserve requirements.

It is unwise also, as proposed in the bill, to increase the amount of real estate loans which member banks are permitted to make. The experiences of our banks prior to 1929 with loans secured by real estate should convince anyone that our commercial banks should make *less* rather than *more* real estate loans in the future. We should separate commercial banking from investment banking more completely than we have yet done. Real estate loans belong largely to the field of investment banking; member banks should be commercial banks primarily and should make fewer real estate loans.

The Banking Act of 1935, signed by the President on August 23, 1935, differs materially from the original Banking bill discussed above. The final Act, in the main, follows the substitute Banking bill written by Senator Glass and passed by the Senate. Title I of the Act (the Federal Deposit Insurance division) contains about the same provisions as did the original bill providing for insurance of deposits. Title II (amendments to the Federal Reserve Act) has provisions which differ materially from those of the original proposed Banking Act of 1935. The Act which was passed has the following principal provisions:

The President of each Federal Reserve bank shall be the chief executive officer of that bank. In each case he shall be appointed by the board of directors, with the approval of the Board of Governors of the Federal Reserve System (the new name for the Federal Reserve Board), for a term of five years, and all other executive officers and employes of the bank shall be responsible to him; the First Vice President shall be appointed in the same manner as the President.

The name of the Federal Reserve Board is changed to "Board of Governors of the Federal Reserve System" and its membership is increased from six to seven. All members are to be appointed by the President of the United States, for a term of fourteen years, and the Secretary of the Treasury and the Comptroller of the Currency are eliminated from membership on the Board. The President is to designate one of the members to serve as chairman and another to serve as vice chairman, each for a term of four years. There are no limitations as to the qualifications of the members of the Board (political, personal, or professional) other than that the President shall have due regard for a fair representation of the financial, agricultural, industrial, and commercial interests, and geographical divisions of the country in making the appointments.

There is created an Open Market Committee, consisting of the Board of Governors of the Federal Reserve System and five representatives of the Federal Reserve Banks. The Committee is to make regulations relating to the open market transactions of the Reserve banks and is to direct the open market operations of each of the Reserve banks.

The purchase of government securities by the Federal Reserve Banks is limited to open market operations. In other words, no government securities may be purchased by the Reserve banks directly from the Federal government.

Power to raise or to lower the "reserve" requirements of member banks is given to the Board of Governors, provided they shall not be lowered below the present legal minimum requirements or raised above double those legal minimum requirements. This provision is inserted to enable the Board to prevent injurious credit contraction or expansion.

Every fourteen days the directors of each Reserve bank are to set the discount rate of their respective banks; and these rates must be approved by the Board of Governors of the Federal Reserve System.

Reserve banks are permitted to make advances (or loans) to member banks upon time or demand notes having maturities of not more than four months. Such notes must be secured to the satisfaction of the Reserve banks making the loans. Loans by Reserve banks upon the basis of self-liquidating commercial paper are given a hard blow, if not destroyed, by this provision.

The authority of national banks to make real estate loans is increased, but the Act does not permit them to participate in the business of underwriting securities.

CHAPTER ELEVEN

COSTS AND FINANCIAL CONSEQUENCES OF THE NEW DEAL POLICIES

IN 1929 the national debt stood at about $16,000,000,000, whereas in March, 1933, when the Roosevelt Administration took charge of the government, the national debt had risen to about $21,000,000,000, an increase of about $5,000,000,000 in four years. On June 30, 1935, the outstanding national debt was $28,701,000,000, or an increase of nearly $8,000,000,000 during the first twenty-eight months of the Roosevelt Administration. Also, since 1930 the Federal government has created several finance corporations either wholly or partly owned by the government, whose obligations the government guarantees either as to principal or interest, or both. These financing agencies on June 30, 1935, had outstanding about $4,000,000,000 of obligations guaranteed by the government. On the other hand, on that date the government held promises to pay, from individuals and corporations to which it had loaned money, to the amount of $4,307,000,000 which when paid will reduce the national debt to that amount.

The authorized New Deal emergency expenditures for the fiscal year ending June 30, 1936, are a little more than $4,880,000,000. Unless there are increases in taxes, the President estimates that the deficit in the budget for this fiscal year will amount to about $3,892,000,000. The current government receipts from taxes have been barely sufficient to meet the ordinary governmental expenditures; consequently, most of the emergency expenditures had to be met either from the Treasury surplus or from the sale of new government obligations.

The deficit in the Federal budget each fiscal year following 1931 was as follows: 1932, $2,741,000,000; 1933, $2,607,000,000;

1934, $3,606,000,000; 1935, $3,575,000,000; and 1936 (estimated) $3,892,000,000. As the Roosevelt Administration did not take office until March, 1933, the deficits for the fiscal years ending on June 30 of 1932 and of 1933 are chargeable largely to the Hoover Administration.

In a public statement in August, 1934, Henry Morganthau, Jr., Secretary of the Treasury, estimated that from March 4, 1933, to June 30, 1934, the Roosevelt New Deal program had not cost the $6,000,000,000 represented by the increase in the national debt during that period; but that actually it had cost less than $500,000,000 as shown by a balance between the new assets and liabilities of the government on June 30. He summarized his conclusions on this point:

> "The gross increase in the national debt between March 4, 1933, and June 30, 1934, amounted in round numbers to $6,000,000,000. Against this gross increase we can offset, either now or ultimately, the following assets:
>
> "(1) An increase in the Treasury's cash balance of $1,600,000,000; (2) the 'profit' of $2,800,000,000 resulting from the reduction in the gold content of the dollar; (3) the increase in the net assets of the agencies wholly owned and financed by the government, amounting on June 30, 1934, to $1,095,000,000. This is wholly aside from the increase in the capital investment of the government in agencies which are partially financed by funds raised outside of the Treasury."

From the standpoint of the amount of money which the government in the future must raise through taxation to pay the six-billion-dollar increase in the public debt up to that time, this statement possibly is correct. However, the soundness of the statement on this point will depend largely upon the earning power and ultimate value of the government's investments in the government-owned financial agencies.

Though the budgetary deficit for the fiscal year ending June 30, 1935, was $3,575,000,000, the net increase in the public debt during that year was only $1,648,000,000. The $1,927,000,000 difference was accounted for as follows: First, the Treasury used up $741,000,000 of its cash account during this

period, leaving only $1,841,000,000 in that account. Second, the $573,000,000 required to be set aside by the government to help retire its debts was used for that purpose. Third, the other $613,000,000 was accounted for by the increase in the trust funds over the expenditures—these trust funds include funds to meet the soldiers' bonus, pay pensions to retiring government employes and to buy books for the Library of Congress.

The United States government's income for the fiscal year ending June 30, 1934, was $3,116,000,000; the expenditures (including the "ordinary" and the "emergency") were $6,722,000,000, and the deficit was $3,606,000,000. The sources of the income for that year were: Income taxes, $818,000,000; internal revenue taxes, $1,470,000,000; customs duties, $313,000,000; miscellaneous receipts, $160,000,000; and processing taxes (AAA) $353,000,000. The expenditures were: Ordinary expenditures (including cost of departments, army and navy, benefits to veterans, sinking fund and interest payments, and benefit payments to farmers under the AAA) $3,101,000,000; emergency or extraordinary expenditures (including FERA, CWA, PWA, CCC, loans of RFC and miscellaneous), $3,621,000,000.[1]

For the fiscal year ending June 30, 1935, the total receipts of the government were $3,800,000,000, which was nearly $700,000,000 more than in 1934. Total expenditures for this year were $7,376,000,000 , which was $654,000,000 more than in 1934. The deficit of $3,575,000,000 for this year was $31,000,000 less than the deficit in 1934. All classes of revenues in 1935 increased over the receipts in 1934, but the greatest increase in revenues was from income and processing taxes. Both ordinary and emergency expenditures in 1935 increased over those of 1934.

The receipts from the processing taxes and the payments made therefrom to the farmers by the Agricultural Adjustment Administration are classed as "ordinary" revenues and expenditures. These expenditures are classed as "ordinary" only because the payments are made out of revenues collected

1 A detailed discussion of the various Federal emergency expenditures will be found in later chapters.

through the special taxes levied on the processing of agricultural products. In reality the taxes are "emergency" taxes and the expenditures should be classed as "emergency" expenditures; the payments are made to farmers because of overproduction in agriculture and the low prices of farm products. It is estimated that government payments to farmers who produce staple crops, during the year 1933, constituted from one-fourth to one-third of their total money incomes. These payments are made under an "emergency" law passed by Congress to aid farmers, and both the revenues and expenditures should be classed as "emergency."

Where did the nearly $8,000,000,000 borrowed by the government from March, 1933, to June 30, 1935, come from? A large part of it, unquestionably, came from the Federal Reserve banks and the member banks. From January 1, 1933, to March 4, 1935, government obligations owned by the Federal Reserve and member banks increased nearly $4,000,000,000. This increase in Reserve banks' and member banks' holdings of government securities indicates that more than half of the $7,700,000,000 new obligations of the government were absorbed either directly or indirectly by them. Other banks and financial institutions, together with individual investors, purchased the remaining new government securities. In other words, less than half of the new securities issued by the Federal government from January 1, 1933, to March 4, 1935, have been paid for out of current savings of individuals; more than one-half of them have been paid out of bank credit or bank funds accumulated in the past. How long will the government be able to continue to sell the bulk of its new notes and bonds to banks? What influence will such transactions have upon the future financing of private business?

Unquestionably, up to 1935, banks purchased these government securities with bank funds and not with current savings deposited by the public. This is shown by the fact that there was no increase in time deposits and only a slight increase in demand deposits of the banks from 1932 to 1935. Because of the great decrease in private demand for bank funds (as evidenced by their decrease in loans and discounts from 1929 to 1935), the banks had large surplus funds and used some of them by making

heavy purchases of government securities; they deposited most of the remaining "surplus funds" in the Federal Reserve banks. The excess deposits (that is, in excess of legal requirements) of member banks in the Federal Reserve banks in March, 1935, amounted to $2,065,000,000, which was more than four times as much as their excess deposits in December, 1932. These excess deposits of member banks increased the ability of the Federal Reserve banks to purchase new government securities. As long as the Federal Reserve banks hold large surplus reserve deposits of member banks, they will be able to purchase additional large issues of new government obligations.

Until the pecuniary volume of the nation's business increases appreciably, a large part of the funds paid by the banks to the government for the new securities will flow back to the banks as cash deposits or temporary savings of the public, when they are paid out by the government in its expenditure program. The enterprises and business men who ultimately receive these funds as they are spent by the government will use them either: (1) To retire part of their remaining obligations at the banks, and thus further reduce their outstanding bank loans; (2) or to deposit them in the banks for future business uses or investment; (3) or directly to expand their business activities. If the receivers of the funds use them to pay their bank loans, the *reserves* of the banks will be increased by the amount of the repayments of the loans, and the banks' power to purchase new government obligations will be increased by the amount of the loans repaid. If the funds are redeposited and kept in the banks as temporary savings, the *surplus reserves* of the banks will be increased to the extent of about nine-tenths (assuming a 10 per cent reserve) of the new deposits. But, if the funds are used directly to expand the volume of private business, they will not result in increasing bank reserves, but on the other hand, will cause an increase in bank loans and a decrease in bank reserves.

Should the government's spending program result in stimulating private business to such an extent that business enterprises demand and secure large new loans from banks in order to get the necessary funds to carry on their businesses, the *surplus reserves* of the commercial banks would diminish rapidly. Then,

the member banks would not only withdraw their surplus deposits in the Federal Reserve banks, but eventually they would be compelled to call upon the Federal Reserve banks for additional funds so as to be able to accommodate their borrowing customers. If such a contingency should occur—and the Administration undoubtedly hopes that it will occur—the power of the Federal Reserve banks, as well as that of the member banks, to purchase additional government securities would be curtailed greatly, if not eliminated entirely. Indeed it is conceivable that the demand for commercial loans and private investment funds might increase so much that it would become necessary for the member banks to sell part of the government obligations they hold in order to supply the necessary funds for private business expansion.

However, unless the banks greatly increase their holdings of government obligations in the near future, and unless at the same time there is a rapid revival in the pecuniary volume of private business, there is not likely to be a shortage of bank funds to accommodate private business. The United States Treasury, on June 30, 1935, had a net balance in the general fund of the Treasury of $1,841,000,000, which may be used to pay excess government expenditures and avoid heavy borrowing.

Many people are fearful of what might happen to our banks should the price of government bonds decline. It has been predicted by some students of our present banking situation that should the price of government bonds decline appreciably, more than 80 per cent of our banks would fail. Under the present circumstances failure of many banks would be inevitable as a result of such occurrence, because such a great part of their assets is invested in government securities. However, the fear that the price of Federal government securities will decline in the near future is unfounded. The banks are now in the position where they must support the market for these securities. If it were not necessary for them to do so, the government would not have been able to reduce the interest rate on its new loans, as it has since 1933, and sell them to the banks at parity.

Of course, there is a point beyond which it would not be safe

for the government to expand its credit. Undue expansion of government debts will cause the public and investors to lose faith in the soundness of the government's obligations. Should that point of safety be exceeded, with the banks holding a large percentage of government bonds, there would be many bank failures and a financial panic. Just how much more the Federal government could increase its indebtedness without positive and serious injury to its credit no one knows. It is believed by many that under present conditions it would not be safe for the government debt to go many billions beyond thirty—possibly thirty-six billions would be the maximum.

With the direct and indirect aid of governmental financial institutions, together with the aid of the Federal Reserve banks and member banks, the government would be able "to make a market" for its new notes and bonds until the people lose faith in the soundness of its credit. If it is necessary to do so, pressure can be brought to bear upon the banks to induce them to purchase and to hold several billions of dollars of new government securities. There are many indications that a large number of the nation's bankers are out of sympathy with the Administration's spending program, but they are not in a strong position to do anything about it. The government's control over the Federal Reserve banks, as well as over the government-owned or controlled financial institutions, gives the Administration power to induce banks to purchase and to hold large quantities of government securities which pay an unusually low interest rate. For this reason the government is not likely to find itself without a market for its new securities. Should any serious difficulties be encountered, the President has the power to issue $3,000,000,000 of new paper money (Treasury notes).

The most important question in reference to future government financing is, when will the Administration be able to balance its budget? That is, when will the government be able to reduce its expenditures or to raise enough revenues to meet them? It is easy to say that the government should discontinue all so-called emergency expenditures and balance its budget, but, under present conditions, it is questionable whether it would be wise for the government to eliminate all its emergency

expenditures. Unless there is a rapid improvement in private employment by 1937, it is not likely that the government will leave the great army of unemployed without government aid when the present Public Works program ends.[2]

The Federal budget can be balanced only by: (1) reducing expenditures to equal present revenues; (2) increasing revenues to equal present expenditures; or (3) reducing expenditures and increasing revenues until the two are equal. Unquestionably, the third method will be the one which will be used when and if the budget is balanced. There is a strong demand on the part of many conservative business men that all emergency expenditures be eliminated and the budget be thus balanced. But, as already indicated, no Federal Administration will be able to discontinue giving aid to unemployed, employable workers as long as there is great number of such individuals. The only way by which such Federal expenditures could be eliminated is for private industry to give jobs to the employable unemployed. It is likely that private industry will not voluntarily do this in the near future.

From the beginning of the depression in 1929 to 1935, the only increase in tax rates or new taxes levied by the Federal government was in levying new internal revenue taxes on alcoholic beverages, gasoline, bank checks, theater and other amusement tickets, etc., and in imposing taxes on the processing of agricultural commodities. All of these taxes (except bank checks) bear most heavily upon people of small incomes. The rates on inheritances, incomes, and corporations were not raised to meet the emergency expenditures. Taxes on business and incomes were not increased because it was argued that to do so would discourage business recovery. Therefore, in order to give business a chance to recover, practically all the government's relief and recovery expenditures were financed through borrowings. From the first, however, it was understood that taxes on business and incomes eventually would be increased to pay for the emergency expenditures.

On June 19, 1935, President Roosevelt delivered to the Congress a message on revamping our Federal system of taxation.

2 In other chapters the question of the value of "recovery" or business stimulation expenditures by the government will be discussed.

Several newspapers referred to this message as the President's "soak the rich" proposals. This message contained the following specific recommendations in reference to taxing large estates, large incomes and the incomes of big corporations:

1. That, in addition to the present estate taxes, there should be levied an inheritance, succession, and legacy tax in respect to all very large amounts received by any one legatee or beneficiary; and that to prevent evasion of this tax, gift taxes suited to this end should be imposed.

2. That a definite increase be made in the taxes now levied upon very great individual net incomes; and that graduation of the rate be extended to apply to annual incomes in excess of $1,000,000.

3. That a corporation tax, graduated according to the size of corporation income, be imposed in the place of the present uniform corporation tax of 13.5 per cent. That the rate for smaller corporations might well be reduced to 10.5 per cent, and the rate graduated upward to a rate of 16.5 per cent of the net income of the largest corporations.

In this message the President made it clear that he considered the enactment of these three tax proposals more important from the standpoint of social and economic reforms than from the standpoint of raising additional revenues or of balancing the budget. In regard to the necessity of breaking up large personal fortunes the President said:

> "The transmission from generation to generation of vast fortunes by will, inheritance, or gift is not consistent with the ideals and sentiments of the American people.
>
> "The desire to provide security for one's self and one's family is natural and wholesome, but it is adequately served by a reasonable inheritance. Great accumulations of wealth cannot be justified on the basis of personal and family security. In the last analysis such accumulations amount to the perpetuation of great and undesirable concentration of control in a relatively few individuals over the employment and welfare of many, many others.
>
> "Such inherited economic power is as inconsistent with the ideals of this generation as inherited political power was

inconsistent with the ideals of the generation which established our government.

"Creative enterprise is not stimulated by vast inheritances. They bless neither those who bequeath nor those who receive."

In regard to the desirability of imposing heavy taxes on large individual incomes he said:

"Social unrest and deepening sense of unfairness are dangers to our national life which we must minimize by rigorous methods. People know that vast personal incomes come not only through the effort or ability or luck of those who receive them, but also because of the opportunities for advantage which government itself contributes. Therefore, the duty rests upon the government to restrict such incomes by very high taxes."

The social and economic justification for a progressive rate of taxation of incomes of corporations according to their size was stated by the President as follows:

"The advantages and the protections conferred upon corporations by government increase in value as the size of the corporation increases. Some of these advantages are granted by the state which conferred a charter upon the corporation, others are granted by other states which, as matter of grace, allow the corporation to do local business within their borders. But perhaps the most important advantages, such as the carrying on of business between two or more states, are derived through the Federal government—great corporations are protected in a considerable measure from the taxing power and the regulatory power of the states by virtue of the interstate character of their businesses. As the profit to such a corporation increases, so the value of its advantages and protections increases."

The conservative newspapers, the organizations representing big business, such as the United States Chamber of Commerce,

and several wealthy individuals, voiced strong opposition to the social and economic reform aims of the President's tax proposals. Also, they interposed objections against such a method of raising additional revenues. It was claimed by them that an enactment of the proposals would be class legislation of the most vicious kind. They argued that such a tax program would prevent business recovery, and would dry up the sources of new capital for further economic expansion of the country. A heavy taxation of incomes of large corporations, they said, would impose a heavy burden on a great number of small stockholders. They argued that Federal taxes should not be increased at all, but that expenditures should be reduced to equal current revenues.

Few, if any, of the arguments of the opponents of the "soak the rich" tax proposals (as the President's proposals were called) are sound. Always reform measures are called class legislation, and in the sense that they are designed to curb special privileges of the few they are directed against a certain class. Certainly such a tax program would not prevent a sound business recovery, but would promote it. We need not fear that the nation will have a shortage of necessary investment funds needed for new capital expansion in the future; one of our difficulties up to 1929 was that there was a surplus of capital funds and a deficiency of consumers' purchasing power. All measures designed to tax monopolistic profits of corporations generally are condemned on the ground that they would impose heavy burdens on small stockholders and widows. If small stockholders receive excess earnings on such securities owned by them, they should pay heavy taxes on those earnings. It has been pointed out that the Federal budget cannot now be balanced by eliminating all emergency expenditures. Therefore, taxes must be raised in order to balance the budget and prevent too much increase in the public debt. From what source should these taxes come?

The public should be in hearty accord with the President's proposed tax measures. Their application, as he suggests, eventually would result in desirable social and economic reforms. High inheritance, succession, and gift taxes eventually would pay the national debt as well as help break up the con-

centration of control in business and industry. Heavy income taxes on large incomes would place a tax burden on those most able to bear it, and would produce additional revenue; the amount of new revenues produced by such a change in the income tax law would depend on the rate structure of the tax on various income classes. The proposed progressive corporation tax plan would tend to equalize the advantages between the small and large corporations, and could be made to produce considerable new revenue.

In compliance with the "soak the rich" recommendations of the President, Congress passed a tax measure, the leading provisions of which were summarized by the *New York Times* on August 21, 1935:

"*Estate Taxes*—An increase in the rates of the present estate taxes, beginning the impost at 2 per cent on net estates of more than $40,000, and ranging upward to a maximum of 70 per cent on that part of the estate above $50,000,000.

"*Gift Taxes*—Revision of the present gift taxes to make them approximate three-fourth of the new estate tax schedule.

"*Individual Taxes*—Increases in individual surtaxes beginning in income brackets above $50,000, and graduating upward to a maximum of 75 per cent on income in excess of $5,000,000.

"*Graduated Corporation Tax*—A new graduated corporation tax, to substitute for the present flat rate of 13.75 per cent, to be levied as follows: 12.5 per cent on net corporation income up to $2,000; 13 per cent, $2,000 to $15,000; 14 per cent, $15,000 to $40,000; and 15 per cent in excess of $40,000.

"*Capital Stock Tax*—An increase in the capital stock tax, now levied at the rate of $1 per $1,000 on the declared value of corporation stock, to $1.40 per $1,000.

"*Excess Profits Tax*—A graduated tax on excess corporation profits: 6 per cent on profits exceeding 10 per cent and not over 15 per cent and 12 per cent on profits exceeding 15 per cent of the declared value of corporation stock.

"*Intercorporate Dividends*—A partial limitation on the exemptions heretofore given dividends paid from one corpora-

tion to another, making 10 per cent of such dividends taxable at the new graduated corporation rate.

"*Personal Holding Company Tax*—An increase in the rates of tax on undivided profits of personal holding companies to make them conform to the higher surtaxes."

Possibly the greatest hazard resulting from our increasing public debts is the danger of uncontrolled inflation. Should the government's credit be weakened because of excessive debts and the budget remain unbalanced, it is almost inevitable that the deficit would be met by the issuance of government paper money. Therefore, it is incumbent upon the Administration to balance the budget before many more billions of Federal debts are incurred.

It was pointed out in chapter nine that there is now considerable sentiment in this country in favor of the issuance of government paper money. Many who are strongly in favor of a much higher price level than we now have believe that such an objective could be accomplished most effectively and expeditiously by issuing large quantities of Treasury notes. Some go so far as to advocate the retirement of the total interest-bearing national debt by paying the obligations with non-interest-bearing legal tender Treasury notes. They argue that by doing so two desirable objectives would be accomplished: First, that the burden of taxation would be decreased; and second, that the price level would be raised sufficiently to relieve debtors of the crushing burden of their debts. The inflationists argue that the Administration's price policies of reducing the gold content of the dollar and of stimulating the expansion of bank credit have failed in their objective of raising prices to the desired levels, and that consequently it is now time to use the more effective policy of issuing paper money. Unless the budget is balanced soon, the inflationists may increase rapidly in numbers.

Newspapers, authors, and even officials of the Administration, frequently refer to the increase in the public debt since March, 1933, as "the cost of the New Deal program." An inference might be drawn from such a statement that the emergency legislation passed by the Roosevelt Administration

was responsible entirely for the increase in the public debt since March, 1933. The public debt increased $5,000,000,000 during the Hoover Administration, and there was no New Deal program. The ravages of the depression were responsible for the debt increase during that time. The depression was worse, and the increase in the budget deficit was greater at the end of Hoover's Administration than it had ever before been in peacetime in this country. If Hoover's Administration had continued for one or two years longer, the public debt certainly would have continued to increase and the depression might have become still more disastrous. Certainly not all the increase in the public debt since Roosevelt became president has been due to "the cost of the New Deal program"; a considerable portion of it must be charged to "the cost of the depression."

If all New Deal legislation should be repealed, it would be necessary to continue to support the great army of unemployed from public funds, or it is likely we would have mob violence, and possibly worse. If human suffering is to be avoided and peace and order are to be preserved, the unemployment problem must be faced as an industrial and political problem and dealt with by government assistance of some kind. The question is not, should we have a New Deal program? We must have a constructive government program to deal with the new industrial situation. The question should be, what kind of New Deal program should we have? Or, what revisions should we make in the New Deal program we now have? The remaining chapters of this book are devoted to a discussion of the last two questions.

CHAPTER TWELVE

RELIEF FOR DEBTORS AND FOR THE AGRICULTURAL INDUSTRY

OTHER than the government and its subdivisions, there are three classes of debtors in the country whose funded debts are large and who, after 1929, were debt-ridden: They are the farmers, the home-owners, and the railroads. However, heavy debt burdens have not been confined to these alone during the depression; many financial, industrial, and commercial enterprises have been unable to meet the interest on their debts or to reduce the principal since 1930. As a matter of fact, during the depression the debt problem played a larger part in our national life than ever before. As previously pointed out, there are two main reasons for the great importance of the debts question during the past few years: First, since the beginning of the World War, debts have increased tremendously in the United States; and, second, the depression so drastically reduced the income of many debtors that since 1929 they have been uanble to meet their obligations.

There were two principal reasons for the great increase in the debts of all classes during the period prior to 1929, (1) the existence of large surplus investment funds and (2) overoptimism on the part of the borrowers. Never was there a time in our national history when such large surplus investment funds existed as from 1915 to 1929. Much of the war profits and the profits from the boom of the twenties were invested in bonds and loaned to borrowers on real estate. It was necessary for the receivers of large funds to invest or loan them. The speculative mania which swept the country during the war and during the twenties made prospective borrowers con-

fident that they would make or receive enough money from their ventures or labors to be able to pay back the loans.

The speculative rise in the value of farm lands during the war induced many farmers to assume crushing debts in order to secure sufficient funds with which to purchase farms at inflated prices. The great building boom in the cities in the twenties induced prospective home-owners to borrow money and to build more expensive homes than their incomes would justify. Considering the instability of their incomes, the slogan "Why pay rent when you can own your own home," made too strong an appeal to too many city dwellers. Also, the public demanded more public improvements than the taxpayers were able to pay for currently, and governments borrowed money on the theory that "future generations should pay for permanent public improvements." Many farmers, during the twenties, increased their farm mortgages for the purpose of securing funds with which to maintain their standard of living—their current incomes were not sufficient to enable them to do so. The railroads borrowed heavily several decades ago on the ground that railroad traffic would continue to increase with the economic development of the country. The managers of these roads did not foresee the development of the automobile industry and the building of great highway systems as coming competitors of the railroads.

Even before the depression set in in 1929 many individuals, governmental units, and some businesses were paying entirely too large a proportion of their incomes as interest on borrowed funds. When the depression cut the income of most individuals in half, many found that it was impossible to meet their debt payments. This was particularly true of many farmers and home-owners, and of some government units. Few of the debt-oppressed individuals were in a position to secure additional loans with which to pay the interest on their old loans, but many of the government units were able to secure such loans for that purpose. With the drastic decline in prices and volume of business, property values behind the farm and home loans declined from 40 to 50 per cent— to where in many cases the face of the loans greatly exceeded the sales value of the property securing them.

However, not all farmers are mortgage ridden. Only about 45 per cent of all farms are mortgaged, and on the average, the face of the mortgages amounts to about 40 per cent of the supposed value of the land and improvements at the time the mortgages were made. Of course, in many cases, the present value of some of these farms is less than the face of the mortgages against them. It is the owners of such farms who are debt ridden, and there are many of them. And, by no means are all the urban home-owners and other owners of urban real estate overburdened with mortgages and other debts on their property.

Many home-owners have homes entirely free of encumbrances, and many of the apartment, office, and other business buildings are either free of mortgages or are only lightly encumbered. On the other hand, many of the small home-owners own only a little equity in the original cost of their homes; they are under contract to pay off mortgages on their homes on the instalment plan. Because of the great decrease in their incomes and in the value of real estate since 1929, the majority of these people have been unable or unwilling to continue the payments on their homes. During the boom twenties there was an overbuilding of apartment, office, and business buildings in the majority of our cities. Many of these structures were built by enthusiastic promoters who borrowed through real estate bonds to finance construction. Since the depression, the income from many of these buildings has been insufficient to pay the interest charges on the bonded indebtedness.

Because of the inability of many debtors to meet their current obligations, by 1932 there were many foreclosures of mortgages and many bankruptcy proceedings. Several state legislatures took action to forestall mortgage foreclosures by enacting mortgage or debt moratorium laws. Some of these acts made it unlawful to foreclose on mortgages for two years from the date of the acts; others specified longer periods of time. Such legislation did not relieve the debtors of any part of their debts, but on the theory that business conditions soon would improve and that debtors would then be more able to pay, the acts simply postponed the date of payments on debts. They were emergency acts only, passed to prevent possible rioting on

the part of oppressed debtors who were about to lose their property.

One of the last acts approved during the Hoover Administration was the Amended Bankruptcy Act of 1933. This act provided for direct composition or extension of debts by agreement between the debtor and his creditors, under the supervision of a Court. Or, in case such a voluntary agreement cannot be secured between a debtor and his creditors, the act provides that the court, upon application of the debtor and after a legal hearing, may issue an order of composition or extension of the debts. The act provides also for the adjustment of debts of corporations, somewhat in the same manner as it does for the adjustment of debts of individuals. In June, 1934, a new corporate bankruptcy act was passed by the Congress which provided for corporate reorganization with the consent of the majority of the creditors and allowed financial compromises when a majority of the creditors might agree. In May, 1934, a congressional act provided that, during an emergency period of two years, cities and local tax units might petition Federal courts for approval of plans for re-adjustment of their debts, if the petitions are endorsed by holders of 51 per cent of their outstanding obligations.

Also, in June, 1934, the Federal Farm Bankruptcy Act was approved. This law grants extension of time to distressed farmers for payment of their existing debts and mortgages and permits them to retain possession of their property, under the control of the court, during the period of adjustment. In case a farmer fails to secure a voluntary adjustment of his debts he may apply to the court to be adjudged a bankrupt and have his property appraised; the farmer then may, with the consent of the lien holder, purchase his property at the appraised price or value by making payments over a period of six years as provided in the act; in case the consent of the lien holder is not secured, the farmer may continue to possess his farm for six years by paying a reasonable rental specified by the court. He then, at any time within the six years, may repurchase his farm by paying the court the appraised price of the property. This act was declared unconstitutional by the United States Supreme Court in May, 1935.

The fundamental object of each of these bankruptcy laws was to enable hard pressed debtors to secure an adjustment or a scaling down of their debts so that they might continue to hold their property or operate their businesses without being closed out by bankruptcy or foreclosure proceedings. In short, these acts were passed for the purpose of providing a fair and equitable method of scaling down debts which had proved to be entirely too heavy; and for the purpose of permitting debtors to discharge their debt obligations according to their respective abilities to pay.

As a result of the passage of the amendments to the National Bankruptcy Act, many business enterprises (particularly in the retail trade) were able to secure sufficient adjustments in their excess debts to continue operating their business, whereas, otherwise, they would have been compelled to close up shop under voluntary or involuntary bankruptcy proceedings. If the Federal Farm Bankruptcy Act had not been declared unconstitutional, under it many debt-ridden farmers would have been able to secure a scaling down of their short-term debts as well as their mortgage debts. It is hardly necessary to point out that the numerous bank failures during the depression were due in part to the fact that many borrowers from banks were unable to pay their maturing notes, and that the bank failures resulted in the drastic scaling down of many short-term debts owed the banks by borrowers. Of course, many banks which did not fail still hold some "frozen" notes, which may or may not become liquid in the future.

As a substitute for the Federal Farm Bankruptcy Act, Congress passed the Farm Mortgage Moratorium Act, which was signed by the President on August 29, 1935. Under the provisions of this act, a three-year moratorium of farm mortgages may be granted by the court on a showing of such necessity by the farmer. During this period the farmer may retain possession of the property by paying a "reasonable rental" fixed by the court. After taxes and insurance are paid any surplus from this rental will go to the creditor or creditors.

At any time during the moratorium period the farmer may acquire his property by paying the appraised value. If the creditors are dissatisfied with the appraised value, they may

demand that the property be re-appraised or sold at auction; for ninety days thereafter the debtor has the right to redeem the property by paying the sales price.

The next class of legislation designed to help debtors was the passage by the Congress of various acts to enable debtors to refinance their debts on an equitable basis at a lower interest rate. These various acts expanded the activities of the existing governmental financial agencies and created several new ones. An analysis of these various laws and their operation follows:

The Farm Mortgage Act of May, 1933, authorized the existing Federal Land banks to refinance farm mortgages at 4.5 per cent interest through the issuance of not more than $2,000,000,000 in bonds. Also, the act authorized the Land Bank Commissioner to refinance some of the outstanding short-term loans of farmers. Under this act the Federal Land banks may buy the outstanding defaulted farm mortgaged from the owners at whatever price is agreed upon (considering the value of the land and the financial status of the farmer) and may take a new mortgage on the mortgaged land for the amount paid for the old mortgage.

Largely because of the lack of a good market for the new Federal Land bank bonds, the Farm Mortgage Refinancing Act of 1934 was passed. This new act created the Federal Farm Mortgage Corporation, with a capital of $200,000,000, to aid in refinancing farm debts. It authorized the corporation to issue an aggregate of $2,000,000,000 worth of bonds guaranteed both as to interest and principal by the government. It granted the corporation permission to exchange its bonds for the bonds of the Federal Land banks; gave the corporation power to invest its funds directly in mortgage loans under the Farm Mortgage Act of 1933. The act also granted authority to the Land Bank Commissioner to make supplementary loans to farmers in refinancing their old loans up to $600,000,000 on behalf of the Federal Farm Mortgage Corporation.

As a result of these two farm mortgage acts, the government has refinanced the debts of a great number of farmers. In carrying out this refinancing of debts the farmers in all cases have been able to reduce the interest charges on their outstanding obligations, and in many cases to reduce the principal of their

debts. Donald Richberg, in his report to the President in August 1934, estimated that at that time the government agencies held at least one-half the agricultural debt obligations outstanding.

During the depression, many holders of delinquent farm mortgages have been unwilling to sell the mortgages at a substantial discount or to exchange them for the low-interest-bearing bonds of the Federal Land banks. The bonds of the Federal Farm Mortgage Corporation, which are guaranteed both as to principal and interest, should be more acceptable in exchange for farm mortgages than were the bonds of the Federal Land banks. Many holders of delinquent farm mortgages have been unwilling to sell them at a substantial discount, even though the face of the mortgages amounts to more than the present value of the land, and in spite of the fact that the farmers are not now able to pay current interest charges on the mortgages. They desire to hold the mortgages because they believe that the agricultural industry will again become prosperous as a result of the Agricultural Adjustment policy of the government. In short, the agricultural relief policy has somewhat retarded government refinancing of farm mortgages. But the provisions of the Farm Moratorium Act should encourage or induce most private holders of delinquent farm mortgages to sell them to the Federal Land banks at a fair present value. If debt-ridden farmers are permitted to take full advantage of the Farm Moratorium Act, the Federal Land banks and the Federal Farm Mortgage Corporation doubtless will soon own the vast majority of the farm mortgages in this country.

Congress also took action to aid distressed home-owners in the cities. In June, 1933, the Home Owners' Refinancing Act was approved. This act provided for the creation of the Home Owners' Loan Corporation, with a capital of $200,000,000 contributed by the Reconstruction Finance Corporation. The corporation was authorized to issue $2,000,000,000 in bonds to exchange for real estate mortgages. In 1934 Congress amended this act by providing a United States government guarantee for the bonds of the Home Owners' Loan Corporation, both as to principal and interest. The 1935 Congress further amended that act to permit the Home Owners' Loan Corpora-

tion to issue bonds up to a maximum of $4,750,000,000, of which $300,000,000 may be used to finance new real estate loans through private loaning agencies. Through its suboffices in the various states this corporation has refinanced mortgages on homes up to February 28, 1935, to the extent of $2,544,000,000; and had issued its own bonds and notes to the amount of $2,255,000,000. Many of these mortgages were purchased from the owners at considerable discount and were refinanced for home-owners by the corporation at a 5 per cent rate of interest. The old mortgages were purchased from building and loan associations, insurance companies, and others who held them.

The Home Owners' Refinancing Act also provided for the organization of twelve Federal Home Loan banks. These banks were organized for the purpose of making loans to building and loan associations, insurance companies, co-operative loan associations, and other firms that deal in mortgages on urban real estate. Bonds issued by the Federal Home Loan banks, according to an amendment to the act, may be purchased by the Home Owners' Loan Corporation up to $50,000,000. The Federal Home Loan banks were organized both to aid in refinancing old loans and to provide for new real estate loans. On February 28, 1935, the Federal Home Loan banks had made loans to the amount of $77,000,000 from the capital funds furnished by the Federal government; at that date these banks had issued none of the bonds authorized.

As a result of the Home Owners' Refinancing Act, interest rates on urban mortgages have been lowered and, in many cases, the principal of many old loans has been reduced to correspond with the decrease in the value of urban property. In June, 1935, much of the refinancing of home mortgages was yet to be completed.

In June, 1933, the Emergency Railroad Transportation Act was approved. This act provided for the appointment of a Federal Co-ordinator of railroads, whose duties were to eliminate wastes, effect economies, and in other ways to improve the operating finances of the railroads. Under him greater co-operation and consolidation were brought about among the various existing railroad systems. Since its organization the Reconstruction Finance Corporation has extended vast loans

to the railroads. On March 31, 1935, the outstanding loans of the RFC to the railroads were $380,000,000. In June, 1935, the Congress passed a joint resolution extending the life of the Emergency Transportation Act until the spring of 1936.

Most students of the financial problems of the railroads believe that a complete financial reorganization of most of the railway companies will be necessary before the industry can be placed on a sound financial basis. Considering the probable volume of railway traffic in the future—as well as its present volume—and the relative cost of carrying traffic by rail and by truck and bus, the railway revenues in the future probably will not secure a reasonable return on their present capitalization. Practically all of them are overcapitalized; their bonded indebtedness is entirely too large. Inevitably there must be a redistribution of ownership interest among the holders of railway securities. No such comprehensive reorganization plan has been devised as yet. Refinancing the debts of the railroads is a problem for the near future.

Another policy of the Roosevelt Administration to aid debtors was that of attempting to raise the money income of the debtors. The plan of inflating the general price level was undertaken, first, for the purpose of stimulating business and, second, for the purpose of lightening the debt burden of the debtors. Unquestionably, an increase in the current money income of the debtor will lighten the burden of his debts. If payments on a debtor's debts amount to 20 per cent of his net income, and his income is doubled, his debt payments will amount to only 10 per cent of his new income.

However, general price inflation does little or nothing to lighten the burden of mortgage debts on many city home-owners. Most of the small home-owners in the cities are wage and salary receivers, and it is a well known fact that wages and salaries do not rise as rapidly as prices during an inflation period. For this reason, general inflation of prices may increase the debt burden of many city dwellers. But price inflation increases the net income of most business enterprises. Therefore, as a result of the upswing in prices, most business enterprises are better able to make payments on their old debts. Insofar as the net incomes of individual or corporate debtors are increased

as a result of a rise in the price level, their debt burdens are lightened at least temporarily.

A rise in the general price level will cause a slight increase in the net income of some farmers and would tend to lighten their individual debt burdens. But, under conditions which existed in the agricultural industry up to the spring of 1933, a rise in the general price level would not have produced a corresponding rise in the prices of agricultural products; therefore, the net incomes of some farmers are reduced rather than increased as a result of a rise in the general price level. Consequently, the Agricultural Adjustment Act, approved in May, 1933, was passed for the specific purpose of increasing the prices of agricultural products in relation to the general level of prices and thus raising the net income of farmers. This act declares it to be the policy of the Congress to establish and maintain such balance between production and consumption of agricultural commodities as will re-establish prices to farmers at a level that will give agricultural commodities a purchasing power, with respect to articles that farmers buy, equivalent to the purchasing power of agricultural commodities in the period from August, 1909, to July, 1914. To carry out this policy the Agricultural Adjustment Administration was created by the Act and given power to reduce the acreage of production of staple crops. The government was to accomplish this by renting the necessary number of acres of land devoted to the cultivation of the staple crops and reducing production sufficiently to eliminate surplus production. Power was given to the Secretary of Agriculture to levy such processing taxes on agricultural commodities processed by manufacturers, as would produce sufficient funds to pay rentals to the farmers for the land taken out of cultivation by the government.

As a result of the application of the Agricultural Adjustment Act, and the destruction of agricultural crops by the drouth of 1934, the large surplus supply of agricultural commodities which existed at the time the act was passed has been greatly reduced. Relative to the general price level, the prices of agricultural commodities have risen and the net incomes of farmers (including the rentals paid to them by the government) have

been increased materially. Therefore, as a result of this act farmers are now in a better position to pay debts.

A dangerous political principle is involved in taxing consumers of agricultural products in order to pay farmers for reducing their production so that the prices of farm products may be raised. Why tax consumers to raise funds so that farmers may be induced to do something which manifestly is to their own interest to do anyway? When farm production is reduced and the prices of farm products are raised, the increased prices penalize the consumer for the farmer's benefit. Certainly the farmers should have fair prices for their products, and consumers should pay fair prices for them. But, except as a temporary measure, the consumer should not be compelled to pay for inducing the farmer to raise his prices to the consumer. The principle of the Bankhead Cotton Control Act—that of penalizing the farmer for overproducing—is much sounder than taxing the consumer in order to pay the farmer not to overproduce. If land temporarily must be taken out of cultivation, why not allow acreage and production of each crop to each state, county, township, and individual farmer, and compel each farmer to pay a heavy tax for any and all overproduction?

To strengthen its constitutionality the Congress amended the Agricultural Adjustment Act and it was signed by the President on August 24, 1935. The Agricultural Adjustment Administration shortly thereafter issued a summary of the changes made by the amendment. Changes made in the act in order to strengthen, clarify, and correct the farm program may be grouped under nine headings:

1. The parity price or fair exchange value of farm products is modified somewhat by adding mortgage interest rates and tax rates as factors in computing this price.

2. In connection with basic commodities, payments are authorized for other purposes than rental or benefit payments, namely for:

a. Removal of surpluses.
b. Expanding domestic or foreign markets.
c. Production under a domestic allotment.

3. Tax rates and tax procedure are spelled out in greater detail, with three objects:

a. Insuring flexibility so that rates may be adjusted to fit market conditions.
b. Smoother operation.
c. Specifying the procedure for refund and recovery of taxes.

4. The Ever-Normal Granary plan for storage of certain crops on the farm, as insurance against shortages and violent price swings, is incorporated in the farm program.

5. Provision is made for control of competing imports when they jeopardize the success of a program.

6. The procedure for marketing agreements is spelled out in great detail, to clarify and strengthen this method. Notable under this head are:

a. Change from "licenses" to "orders" as the means for enforcing marketing agreements among handlers.
b. Provision for putting orders into effect without consent of a majority of handlers under certain carefully defined circumstances.
c. Legal safeguards for handlers in the form of petition and court review.
d. Authority to examine books and records of handlers under certain circumstances.

7. Changes are made in certain provisions for specific commodities:

a. Cotton—Amendments to the Bankhead Act and to provisions of the Agricultural Adjustment Act dealing with cotton option contracts and the cotton pool.
b. Tobacco—Amendments to Kerr-Smith Act.
c. Barley—Tax rate specified.
d. Sugar beets and sugar cane—Adjustments in taxes and payments.

8. In the provisions for protection of the consumers' interest, it is specified that nothing in the act shall be interpreted as authorizing maintenance of prices above parity levels.

9. Miscellaneous provisions in the amendments cover the following points:

a. Encouragement of producer co-operatives.
b. Appropriation of funds for elimination of diseased cattle.
c. Organization of the hog cholera serum industry under a marketing agreement.
d. Appropriation of funds to carry out existing options for purchase of submarginal lands.
e. Appropriation of 30 per cent of the annual receipts from customs duties, to stimulate agricultural experts and domestic consumption and to finance production adjustments.

On January 6, 1936, the Supreme Court of the United States, by a majority decision of six to three, declared the Agricultural Adjustment Act to be unconstitutional. The grounds upon which the Act was declared unconstitutional were: (1) The Act is a statutory plan to regulate and control agricultural production, a matter beyond the powers delegated to the Federal Government. It therefore invades the reserved rights of the states. (2) The Congress has no power to enforce its commands on the farmers to the ends sought by the Agricultural Adjustment Act. It may not indirectly accomplish those ends by taxing and spending to purchase compliance. Therefore, the processing tax is not a proper exercise of the Federal taxing power; neither is this tax within the general welfare clause of the Constitution.

In holding that the regulation of production by the Federal Government is unconstitutional the court by implication says that production is not a part of commerce and does not directly affect commerce, and that the regulation of production is not authorized by the interstate commerce clause of the Constitution. In declaring the processing tax unconstitutional, it holds that since the object to be accomplished by the proceeds of the

tax (regulating production) is not constitutional, the tax itself is not constitutional. In accordance with this reasoning, the Bankhead Act regulating cotton production would be delcared unconstitutional.

The Agricultural Adjustment Act was passed admittedly as a temporary expedient to give immediate relief to distressed farmers. Its application would not permanently cure the problem of overproduction in agriculture. As a result of the government's renting land, some land is taken temporarily out of cultivation; but the plan does not take any land out of cultivation permanently. To cure the agricultural problem of overproduction, enough land must be taken out of cultivation permanently to reduce the supply of agricultural products so there will be no annual surplus crops in the future. This can be accomplished only by the government's buying up many million acres of land now devoted to cultivation. Making such a land policy effective would require several years, unless billions of dollars of public money are spent at one time to make it effective.

In order to take land out of cultivation the Federal government has a program for purchasing submarginal agricultural land. In 1933 President Roosevelt allotted the Agricultural Adjustment Administration $25,000,000 to be used for that purpose, and in May, 1934, an additional $50,000,000 was set aside out of the $525,000,000 drouth relief appropriation, to be used for the purpose of purchasing submarginal agricultural lands. Those funds are administered jointly by the Federal Emergency Relief Administration and the Agricultural Adjustment Administration.

In May, 1935, it was announced that, from this fund, seven million acres of agricultural land had been purchased by the government and that $20,000,000 of the fund remained unexpended. In October, 1934, it was stated that the average price paid for lands purchased up to that time was about $5.00 an acre, and that it was anticipated that additional lands to be purchased would cost more than an average of $5.00 an acre, but that none were to be purchased at more than $10.00 an acre. It was announced that most of the land purchase projects were on the western edge of the Great Plains, the southern

Great Lakes section, and the Lower Piedmont Plateau of the Southeast.

Some of the land purchased is to be used for reforestation, some of it for grassland, some for national park purposes, and a small part for the establishment of subsistence homesteads. With the $75,000,000 the government should be able to purchase at least ten million acres of submarginal land. In my opinion, this land purchase policy is a sound one, and was suggested in the author's *Our Economic Revolution.* The lands thus acquired will be taken out of cultivation permanently, and will be used in a manner to preserve the natural fertility of the soil, control the flow of streams, and restore some of the beauty of nature which we, as a people, have destroyed in our exploitation of the natural resources of the country. The agricultural adjustment problem can be solved permanently only by pursuing such a policy.

One of the principal divisions set up in the President's $4,800,000,000 new public works program is called the Rural Resettlement Administration, of which Rexford G. Tugwell is the head. The President's executive order establishing the Resettlement Administration stated that it would be assigned the following tasks:

"a) To administer approved projects involving resettlement of destitute or low-income families from rural and urban areas, including the establishment, maintenance, and operation in such connection, of communities in rural and suburban areas.

"b) To initiate and administer a program of approved projects with respect to soil erosion, stream pollution, seacoast erosion, reforestation, forestation, and flood control.

"c) To make loans as authorized under the Emergency Relief Appropriation Act of 1935 to finance, in whole or in part, the purchase of farm lands and necessary equipment by farmers, farm tenants, croppers, or farm laborers."

Under the act as much as $850,000,000 of the total appropriation may be spent for the above enumerated tasks. Just how much additional submarginal land will be acquired by Dr. Tugwell is not now known. One of the principal functions of the Resettlement Administration is to rehabilitate the one million farmers who were on the public relief rolls in the spring

of 1935; this problem will be discussed in a later chapter. Another function of the division will be to conserve the natural fertility of land and prevent soil erosion; still another function will be to furnish jobs to the unemployed. However, in carrying out the resettlement projects much marginal land must be purchased and taken out of cultivation by the government.

As pointed out in earlier chapters of this book, one of the factors which upset our industrial balance was the fact that too large a proportion of our national money income was diverted to the payment of interest on debts. These large interest payments reduced the percentage of the national income available for the purchase of consumers' goods, and caused an increase in our surplus investment funds. One of the ways to correct this evil is to reduce drastically the interest rates on both old and new loans. This the Roosevelt Administration, in a large measure, is accomplishing through the debt refinancing plans and through control over the making of new loans. If we secure an elimination of excess profits in business, and a reduction of interest rates on loans, excess investment funds such as existed in the twenties, probably will not again contribute to upsetting our industrial balance.

CHAPTER THIRTEEN

UNEMPLOYMENT RELIEF AND BUSINESS STIMULATION POLICIES

UNEMPLOYMENT as a more or less permanent national problem is new to the United States. As late as 1914 there were many students who argued that for many years in the future it would be necessary for the United States to secure a million or more immigrant workers each year to obtain a sufficient supply of laborers to keep her industries operating at full capacity. But, since the World War the Congress has passed stringent immigration laws to prevent the influx of a host of foreign laborers, and by 1928, when business was enjoying great prosperity, more than two million employable American citizens were without jobs. Then by 1933, as a result of the business depression, we had about sixteen million unemployed laborers.

When the depression occurred in 1929 the unemployed were living off their savings, or were being taken care of by their families, or were receiving aid from local private charities. With the increasing severity of the depression, the number of unemployed increased rapidly. The personal savings of most of those without work were soon exhausted, and their growing numbers became a heavy charge upon private charity. By 1931 many of the municipalities, counties, and states began to provide public funds to aid the unemployed and to supplement dwindling private charity funds. Because of the virtual cessation of private charity and the increased burden of caring for the growing number of the unemployed, state and local governments soon found themselves unable to cope with the situation of supporting the unemployed. State and local revenues as well as private incomes had been curtailed greatly as a result of the

depression. Then the national government was called upon to provide funds to aid those without jobs and without funds.

After some opposition to granting Federal funds for unemployment relief purposes, President Hoover approved an act of the Congress authorizing the Reconstruction Finance Corporation to make loans to states up to the amount of $300,000,000, the proceeds of which were to be used to relieve the unemployed. By the time the Roosevelt Administration came into office many of the states had exceeded their borrowing capacity and unemployment had become so great that it was impossible for state and local governments to carry the financial load of providing relief. Mr. Roosevelt, as a presidential candidate, promised Federal relief for the unemployed; as President, in May, 1933, he approved a bill providing an appropriation of $500,000,000 to be used for that purpose and providing for the setting up of a Federal Emergency Relief Administration (FERA) to administer the expenditure of this fund and to organize a Federal relief program for a two-year period, or less if the emergency passed sooner.

The act provided that the head of the FERA was to be appointed by the President, and, under rules and regulations to be laid down by him, the administrator was given broad powers to allot and to administer the expenditure of this fund. The Federal Administrator appointed state administrators and these in turn organized local branches. Of the original grant of $500,000,000 the Administrator allotted one half ($250,000,000) to the various states on the basis of their relief expenditures during the previous three months; the other half was allotted to states on the basis of need. In some states it was necessary for the Federal government to furnish more than 90 per cent of the relief funds; in others it furnished less than 10 per cent. The Federal relief expenditures from this fund during 1933 varied from 60 to 80 million dollars each month. In the nine months ending Feberuary 1, 1934, the FERA had spent $374,000,000 for direct and work relief.

During the summer and autumn of 1933 the FERA organized "work relief" projects, which were a continuation of the locally supported "made-work" projects. The first work projects developed by the FERA were: transient camps and service

centers where itinerants received food and lodging and opportunities for work; the emergency educational program for unemployed teachers; the women's division sewing rooms; and road and street projects. When winter came on in 1933 the Civil Works Administration (CWA) was organized in order to create emergency employment. The CWA was organized under the Federal Emergency Administrator; it was allotted $83,000,000 of the funds of the FERA and $400,000,000 of the funds of the Public Works Administration. The CWA was organized because, with the coming of winter in 1933, unemployment was on the increase, and the Public Works Administration was slow in getting its projects under way.

After the origination of the CWA, all the FERA specific work projects were converted into CWA projects. Also, many new work projects were started at once. About the only limitation set on new work projects was that any proposed project must have a social value and be of such a nature that it could be completed in two months. In most cases the local authorities furnished the necessary materials for the projects, and CWA paid the wages, which were from 40 to 50 cents an hour for unskilled labor, and $1.00 to $1.20 an hour for skilled labor. In February, 1934, the Congress granted the FERA a new appropriation of $950,000,000, of which the Administrator allotted $450,000,000 to the CWA to wind up the projects already undertaken; in order to make the money last for the CWA work, all workers from households where other members were otherwise employed were dropped from the rolls, and the hours of work for all were cut from thirty to twenty-four a week. In May, 1934, the CWA was discontinued and the Local Works Division (LWD) of the FERA was created to take over the unfinished projects of the CWA. Projects of the FERA under the LWD were continued throughout the summer of 1934.

Whatever may have been the waste, inefficiency, and graft connected with the CWA (and doubtless all three were present), the scheme at least furnished jobs for about four million unemployed workers during part of the winter months. Whether such jobs, under the atmosphere which surrounded them, were better for the unemployed than straight doles is a debatable question.

The FERA sponsored the organization of the Federal Surplus

Relief Corporation (FSRC) which was incorporated under the laws of Delaware. Its purpose was to purchase and to receive surplus commodities and to distribute them among the needy. Each state matched the funds spent by the Federal government for supplies distributed within its borders. Up to February, 1934, the FSRC had spent $25,000,000 for supplies consisting largely of necessities such as dairy products, meat, flour, cloth, shoes, etc. In June, 1934, the Congress appropriated $525,000,000 for drouth relief. The distribution of this fund was made jointly by the FERA and the Department of Agriculture. Also, the Congress appropriated $119,500,000 to be used for road construction over a period of three years, with the heaviest expenditures in 1935.

From the time of the organization of the FERA until the spring of 1935 the number of people on the Federal relief rolls continued to increase. Table XVI[1] shows that from August, 1933, to November, 1934, the number of persons on the FERA rolls increased from 15,282,000 to 18,900,000. The second part of that table shows that less than half of the "cases" were on "work relief" and a little more than half of them were on "direct relief" in November 1934, but that from month to month prior to that time the percentage of work relief cases increased over the direct relief cases. Table XVII[2] shows the cost of relief given by the FERA from January 1933 to December 1, 1934. Federal relief expenditures for the twenty-three months was $1,418,171,000. According to preliminary reports, the FERA expenditures for relief during the first six months of 1935 were about $500,000,000; this makes a grand total of about $2,000,000,000 paid for unemployment relief by the FERA up to July 1, 1935.

In March, 1933, the Emergency Conservation and Reforestation Law was enacted which provided for the creation of the Civilian Conservation Corps (CCC). The law was passed primarily to relieve unemployment among young men and secondarily to help restore the country's natural reserves. The original act provided for the enlistment of 250,000 whose families were on the relief rolls, 25,000 World War veterans, and

1 Appendix A, p. 287.
2 Appendix A, p. 288.

a necessary number of experienced woodsmen and other specialists. The enlisted men were to be paid $1.00 a day and board and lodging and other necessary care. Those with dependents have as much as $25.00 a month subtracted from their pay to be sent home. The Emergency Conservation Work was placed under a Director, who has the co-operation of the Departments of Agriculture, Labor, Interior, and War. Up to July, 1934, about two thousand CCC camps had been established, with some in every state in the Union; at that time the full strength of all these camps was 303,000 men.

When organized, it was intended that the CCC camps would be continued for six months only, but recovery was delayed and the camps proved to be so popular that they were continued. The men enlist for six months; those who desire may enlist for an additional three months, then for another three months; no one is allowed to re-enlist after completing one full year in the camps. The work of the CCC is confined largely to national parks and forests. The work consist of planting trees, thinning forests, stopping erosion, building and repairing roads, and keeping them cleared in the parks. The men may be employed on private forests where the work is clearly of public benefit. It is generally conceded that the CCC Administration has done valuable public work in our national parks and forests and that the young men who have enlisted in these camps have received great benefits both physically and morally. The CCC Administration may find a permanent place in our national policy.

Title II of the National Industrial Recovery Act (approved June, 1933) created a Federal Emergency Administration of Public Works and made an appropriation of $3,300,000,000 for carrying out public works and construction projects. The act provided that the funds may be used for the erection, extension, and improvement of public or semi-public buildings, and for highway construction and improvement; for flood control, soil erosion, or irrigation; for the development of harbors and for the transmission of power facilities; for naval construction and for construction of facilities for the army; for the construction of self-liquidating works such as water works and other municipal utilities; for loans to the railroads and elimination of grade

crossings; and for the elimination of city slums and the construction of low cost housing. A National Public Works Board was provided to administer the provisions of this Law. The President appointed the Secretary of the Interior as chairman of the National Public Works Board and as head of the Public Works Administration which was set up to administer the act.

It was thought that the public building program resulting from the act would be much larger than the $3,300,000,000 appropriated by it; the law provided that the National Public Works Board may contribute 30 per cent of the cost of approved local public works projects and may, if necessary, loan the local governmental unit or public board that undertakes the project a part or all the balance of the cost of the approved project. The borrowing local agency, under the law, is required to give the Public Works Administration adequate security for the money borrowed and is to pay an interest of 4 per cent on the loan. The Board allotted about half of the vast funds provided by the act to Federal government projects, $450,000,000 to the CWA, a considerable sum to slum clearance and homestead projects, and most of the balance to state and local projects. In carrying out these public works projects the Public Works Administration up to March 31, 1935, had extended loans to the amount of $276,000,000. In short, the act did not induce state and local governments and other public bodies to undertake a great number of new public construction projects by issuing securities to be sold either to the PWA or to the public.

The Public Works program was undertaken for the dual purpose of furnishing employment to the jobless and stimulating private business. When these projects were undertaken, it was estimated that they would furnish direct employment for two million or more laborers and indirect employment for at least an equal number. It was thought that carrying out the projects would increase greatly the market demand for construction materials of all kinds, and thus stimulate production by the enterprises furnishing those materials. The theory of the plan was that private production and employment would be stimulated both indirectly and directly; the money income of consumers would be increased thereby, and general business would be stimulated by a larger retail volume of sales. Unques-

tionably, all these things did happen to some degree as a result of this large public works program, but it did not greatly reduce unemployment or pull business out of the doldrums.

In the first place, the Public Works program did not get under way as quickly as the proponents of the program assumed that it would. The Administrator and the Public Works Board were very cautious in accepting non-Federal projects; and most of those which were accepted could not be executed immediately because of the safeguards thrown around the expenditure of the Federal money. Because of the slowness in putting the PWA program into operation, the FERA organized the CWA program of work projects for the winter of 1933-34. However, the Public Works Administration had its program in full operation during the winter of 1934-35, but at the same time the number of unemployed on the FERA rolls increased rather than decreased. As a matter of fact, there was never a great number of laborers employed directly on PWA projects: In January, 1935, only 344,000 were employed; in February, 272,000; and in March, 282,000.

Also, the Public Works program resulted in much less indirect employment than was at first anticipated by its proponents. Because of the great decline in private building and construction during the depression, most of the producers of constructional materials were left with large stocks of those goods on hand. In cases where they did not have such surplus stocks, when the PWA was organized in 1933, they anticipated the extent of the demand for their products to carry out the Public Works projects, and produced them in anticipation of the demand. Consequently there was little stimulation of the constructional goods industries during the winter of 1934-35 as a result of the PWA program. The Public Works projects did give indirect employment to many of the unemployed, and there was some direct stimulation to private business. Without these projects there would have been a greater number of unemployed to be taken care of than otherwise, and without the Public Works program, consumers' money income and the volume of trade and production of the country would have been less than it was during the winter of 1934-35.

However, the most enthusiastic advocates of public works as

a means of eliminating unemployment and restoring prosperity now admit that the carrying out of the $3,300,000,000 Federal Public Works program neither eliminated unemployment nor produced business recovery. But many of them claim that these objectives would have been accomplished by the program if it had been a much larger and more rapid one. Certainly a larger program would have had a greater stimulating effect on both employment and business than a smaller one—while it lasted.

The original law providing the $3,300,000,000 Public Works and Construction Projects allocated $25,000,000 to be used for aiding the redistribution of the overbalance of population in the industrial centers or for "subsistence homesteads." Then part of the CWA funds were used for this purpose, and the President set aside additional funds from the 1934-35 emergency funds for the construction of subsistence homesteads. The subsistence homestead projects consist of rural village homes for workmen with a plot of land for gardens or for small farms allotted to each home in each project constructed. The object of these projects is to enable workers to produce a part of the food they consume and to make them less dependent on employment in mills and factories for a living. The government intends to sell the homesteads to workers on a long-time payment plan, or in some cases to rent or to lease the homes to settlers. The settlers are to be drawn from both industrial centers and rural districts and are to consist in large part of unemployed or only partly employed people. The money collected as rentals or payments on the homes is to constitute a revolving fund to be administered as directed by the President.

In various public statements the President indicated that he believes that both a redistribution of population and a decentralization of industry is necessary in this country. He has also indicated that he believes that much progress may be made toward both the decentralization of industry and a redistribution of population through the establishment of subsistence homesteads. Many of these homesteads are purely agricultural, with large tracts of land (as much as 40 acres in some cases) for each settler, while others are industrial, with small plots of ground for gardens. Up to May, 1935, the PWA and the FERA had built or had under construction sixty-three different sub-

sistence homestead projects. As already indicated, the Resettlement Administration created in May, 1935, takes over and operates all these homestead projects and will create new ones in both rural and suburban areas. These projects are to be developed for the resettlement of destitute or low-income families from rural and urban areas. Several state and local corporations have been organized to co-operate with the Federal government in constructing such homestead projects for their people.

Theoretically, industrial subsistence homesteads (with a few acres of land for each homesteader) would be an ideal life for industrial workers who are employed twenty-five or thirty hours a week in industrial plants. But such an arrangement necessitates the establishment of adequate industries at or near the homestead projects, or the location of the homestead projects near established industrial plants desiring such laborers. Few of the established industrial plants at present want to employ such additional laborers. However, if the hours of employment for all laborers were reduced sufficiently by government action, the old established industrial plants would require additional laborers to keep them operating.

Doubtless, if a great number of successful rural industrial subsistence homestead projects could be constructed and put in operation in rural communities, they would have a permanent influence on reducing the number of unemployed in our industrial centers; they would tend also to decentralize industry as to location, size of factories, and labor policies. Were the unemployed put to work constructing these projects, the net cost of them (over and above that which would otherwise be paid the workers as direct relief) should not be very great. If the problem of locating successful industrial plants at or near these projects can be solved without imposing an undue public expense, it would be advisable for the government to build several rural industrial projects. But, if industrial plants cannot be secured specifically for each of the projects, those which are established should be located near industrial centers where the settlers might be able to secure at least part-time industrial employment.

It is almost certain to be unwise for the government to

establish industrial subsistence homestead projects without definite assurance that industrial jobs will be available for the settlers in those homesteads. It might be wise to pay a reasonable government subsidy, or to give a reasonable guarantee of return on private investment, to secure the establishment of such industrial plants near these homestead projects. But, it probably would be unwise for the government to build the necessary industrial plants at these homesteads either to be operated by the government or to be leased to private operators.

Upon the recommendation of the President, the Congress passed the Emergency Relief Appropriation Act of 1935 (approved April 8) to provide bigger and better Federal work relief and public works program than the previous ones. This act (joint resolution) made available a fund of $4,880,000,000 for the new work relief program by making a new appropriation of $4,000,000,000 and making available an additional $880,000,000 of unexpended money in emergency funds previously appropriated. The expenditure of this vast sum is to be made at the discretion and under the direction of the President, subject to the broad limitations contained in the act.

The funds may be spent for the following purposes: (1) Continuing relief as authorized under the Emergency Relief Act of 1933 as the President may deem necessary; (2) highways, roads, streets, and grade-crossing elimination, $800,000,000; (3) rural rehabilitation and relief in stricken agricultural areas, and water conservation and irrigation and reclamation, $500,000,000; (4) rural electrification, $100,000,000; (5) housing, $450,000,000; (6) assistance for educational, professional, and clerical persons, $300,000,000; (7) Civilian Conservation Corps, $600,000,000; (8) loans or grants, or both, for projects of states and possessions including subdivisions and agencies thereof, municipalities and self-liquidating projects of public bodies thereof, $900,000,000; (9) sanitation, prevention of soil erosion and stream pollution, reforestation, forestation, flood control, rivers and harbors, and misecellaneous projects, $350,000,000. Thus, $4,000,000,000 of the appropriation is earmarked by the act, but it provides that not to exceed 20 per cent of the total amount appropriated may be used by the President to increase

any one or more of the above limitations if he finds it necessary to do so in order to effectuate the purpose of the act.

This act extends the life of the Federal Emergency Relief Act until June 30, 1936, and the life of title II of the National Industrial Recovery Act (the Public Works Administration) until June 30, 1937. The President is given the power to make loans from the funds made available by the act to finance the purchase of farm lands and necessary equipment by farmers, tenants, or farm laborers. Other powers given to the President by the act are as follows:

"In carrying out the provisions of this joint resolution the President is authorized to established and prescribe the duties and functions of necessary agencies within the government.

In carrying out the provisions of this joint resolution the President is authorized (within the limits of the appropriation made in section 1) to acquire, by purchase or by the power of eminent domain, any real property or any interest therein, and improve, develop, grant, sell, lease (with or without the privilege of purchasing), or otherwise dispose of any such property or interest therein.

"The President is authorized to prescribe such rules and regulations as may be necessary to carry out this joint resolution, and any willful violation of any such rule or regulation shall be punishable by fine of not to exceed $1,000.

"The President shall require to be paid such rates of pay for all persons engaged upon any project financed in whole or in part, through loans or otherwise, by funds appropriated by this joint resolution, as will in the discretion of the President accomplish the purposes of this joint resolution, and not affect adversely or otherwise tend to decrease the going rates of wages paid for work of a similar nature.

"The President may fix different rates of wages for various types of work on any project, which rates need not be uniform throughout the United States."

In order to carry out the provisions of the Act and to get the new public works program under way as expeditiously as possible, the President set up the following administrative Divisions: First, the Division of Applications and Information,

which gives preliminary consideration to all requests for work relief projects and forwards the applications and plans to the Works Allotment Division; second, the Works Allotment Division, which studies the proposed works projects and makes recommendations to the President for final action on each—approval or disapproval; third, the Works Progress Division, which checks up on approved projects to see that they get started and that the purchase of materials and the employment of labor is co-ordinated with other projects and that the work is kept up to schedule. In addition to these main administrative divisions, several special administrative divisions were created for the purpose of promoting, supervising or administering the projects in the different classes of work, such as the Resettlement Administration, the Rural Electrification Division and the Division of Grade Crossing Elimination. The various national and local agencies of the PWA and the FERA are co-ordinated in the administration of this Act. They work through and in co-operation with the state, county, and municipal governmental bodies in the origination, approval, and effectuation of the works projects.

The approved projects fall into the following classes or subdivisions: (1) Those undertaken and carried out by the Federal government itself through direct employment of labor and purchase of materials under such agencies as the Resettlement Administration or the Rural Electrification Division. (2) Those undertaken and paid for by the Federal government for the construction of which contracts are let. (3) Those undertaken and carried out directly by state and local governmental subdivisions for which the Federal government contributes part or all of the funds. The Federal government urges the local governments to contribute enough toward these projects to purchase the materials used so that the Federal contributions will be limited to payment for the labor used, as was the case in carrying out most of the CWA local projects. (4) State or local public projects constructed under contracts for which the Federal government contributes 45 per cent of the cost and the state or local government contributes 55 per cent. The contribution by the state or local government to a project may

be borrowed from the Federal government upon acceptable security. Regardless of the class to which a project belongs, and regardless of whether it is constructed directly or under contract, the labor employed on it must be taken from the FERA rolls. In cases where projects are constructed directly by the governmental units (not under contract) the laborers will receive the "security" wage rates established by the President for public works projects. But where projects are constructed under contract the laborers will receive the wage rates which prevail in private industry for corresponding classes of labor.

In asking the Congress to pass the Emergency Relief Appropriation Act of 1935, the President stated that its enactment would enable the government to end the "dole" or FERA direct relief payments. It was his belief that the works program directly and indirectly would furnish jobs for all the employable people on the Federal relief rolls, and that the Economic Security Act[3] and the state and local governments would take care of all the unemployables in need of public relief. He stated that the program would furnish jobs directly for 3,500,000 of the unemployed. Therefore, it is assumed that when the works program is put in full operation FERA direct relief will be discontinued. December 1, 1935 was the date set for discontinuing Federal direct relief. It is probable that political pressure will be brought to bear on the Administration to continue direct relief for the unemployables.

The Administration hopes that this new public works program will stimulate private industry to such an extent that the country will have full business recovery. Like the $3,300,000,000 public works program, the $4,880,000,000 program is a scheme "to prime the business pump" and bring about business recovery. The President has expressed a belief that business will receive such a stimulation from the program that all the workmen employed on the public projects will be absorbed in private industry when the projects are completed. Of course, it is expected by the Administration that some of the works projects, such as the resettlement and homesteads, will make definite

3 See chapter seventeen.

contributions toward a permanent solution of our industrial problems. Then, too, all the projects are expected to have a permanent value in their usefulness.

It is my opinion that the new public works program will make no contribution toward bringing about permanent recovery of business. To be sure, it will give much temporary relief to the unemployed and will result in a temporary stimulation of private business. This second program probably will have a greater temporary effect on both unemployment and business than did the first one. But, neither a small nor a large public works program can bring about the necessary adjustments in our industrial system to enable it to have continuous operation. In fact, it is my opinion that this big public works program will tend to retard rather than to promote sound and lasting business recovery.

In carrying out such a program the government will pay out large public funds secured through the expansion of bank credit as well as through the expansion of government credit. These government payments will induce private business enterprises to adjust their prices and policies to a national money income received in part from the expansion of credit. Normally, all the national money income is derived from current production of saleable goods and services produced by private business enterprises. To the extent to which the national income is augmented by credit expansion its purchasing power will exceed the stabilized value of the goods and services currently produced. Prices will rise because consumers' purchasing power has increased faster than current production and for that reason business will become more profitable. Profitable business will continue so long as the government pays out the large funds derived from the expansion of credit. But the public works program must be completed eventually, and the government payments to the public of artificial money income derived from credit, rather than from the production of saleable goods, must stop also. Then consumers' money incomes will consist only of money derived from the productivity of private industry, and it will not be in excess of the value of the goods and services produced by private business. When that time comes to adjust

business to a smaller volume of sales, not only will employment and money income decline but prices and production must decline also.

In an earlier chapter it was pointed out that if the nation is to achieve permanent prosperity, prices and production in private industry must be adjusted so that the goods and services produced can be purchased with the money incomes paid out by private industry to those who contributed to its net production. It will be impossible to secure such an adjustment as long as part of the current money income of consumers is derived from artificial purchasing power created by the government through the expansion of credit. When this government policy stops (and it must stop sooner or later) private business must adjust its production and prices to a national money income which is created entirely by the productivity of private industry.

The payments made by the AAA to farmers have been derived from taxes levied on the current income of the nation, but all of the past emergency government expenditures for the support of the unemployed under the Emergency Relief Administration, the CCC, and the Public Works Administration have been derived from borrowings secured through expanding bank credit. All these emergency expenditures have had the same effect in perpetuating an unsound situation in our industrial system as will the payments made on account of the new public works program. The past government payments for support of the unemployed doubtless were justifiable as a temporary humane expedient; they may be justified as a measure to preserve the Union; but they cannot be justified on the ground that they helped to bring about permanent recovery of business. All emergency expenditures of the Federal Government which have been and are to be made with funds derived from government credit, rather than from the current national money income, tend to perpetuate an undesirable situation in our industrial life.

After this big public works program is completed, unless something is done in the meantime to reduce the hours of workers in private industry, there will be many millions of un-

employed laborers in this country. In such an eventuality we may be just starting with the dole system instead of ending it. Hungry millions cannot be left to starve; they will not starve in peace.

CHAPTER FOURTEEN

THE NRA, LABOR ADJUSTMENTS AND OUR INDUSTRIAL BALANCE

WHEN the depression became extremely severe early in 1933 there was a widespread public demand that the government take action to restore industrial prosperity and to bring about an equilibrium in our industrial system. There was much talk of a "planned industrial society" or a "plan for industry." The industrial leaders were as vociferous for some kind of action along this line as were other economic classes. The passage of the National Industrial Recovery Act (June, 1933) was the Administration's immediate answer to this demand.

Title I of the National Industrial Recovery Act contains the industrial control sections of the law. The act authorized the President to set up administrative machinery to put this division of the law into operation. The administrative machinery which was organized to carry out this part of the law was known as the National Recovery Administration, or better known as the NRA. The act declared it to be the policy of the Congress to remove obstructions to the free flow of interstate and foreign commerce and to provide for the general welfare by (1) promoting the organization of industry for the purpose of co-operative action among trade groups; (2) eliminating unfair competitive practices; (3) promoting the fullest possible utilization of the present productive capacity of industry and avoiding undue restrictions of production; (4) inducing and maintaining united action of labor and management under adequate governmental sanction and supervision; (5) increasing the consumption of industrial and agricultural products through

increasing purchasing power; (6) reducing and relieving unemployment; and (7) improving standards of labor.

According to the act, all of these stated methods of aiding commerce and promoting the general welfare were to be put into operation through the formulation and adoption of "codes of fair competition" for the various industries. The first three objectives enumerated above were intended to be of specific benefit to business enterprises affected; the fourth was expected to result in industrial peace; the last three were intended to be of special benefits to laborers, and of general benefit to consumers. After the passage of this act, the NRA, in conjunction with trade associations and the leaders of various industries, promulgated and put into operation more than four hundred separate codes of fair competition. These codes, after having been approved by the President, were to have force of law.

The various provisions of the National Industrial Recovery Act (Industrial Control Law) represented a compromise between the desires of industrial leaders for industrial recovery legislation and those of the labor leaders and of the "brain trust" for reform legislation. The industrial leaders desired to have the antitrust laws repealed, at least temporarily, and to secure legislation which would permit enterprises in the different industries to make agreements as to limitation of output, as to the setting of prices, and as to the regulation of trade practices. The labor leaders desired to secure legislation providing for the shortening of the hours of laborers in industry (as was evidenced by the Black thirty-hour-week bill which had already passed the Senate). Also, the labor leaders desired legislation which would give a legal status to independent labor unions and at the same time recognize the personal rights of laborers to be members of such unions. Some of the students of our national economic problems desired legislation to bring about an increase in wage rates as well as shorter hours for laborers; they wanted legislation which would bring about an increase in the purchasing power of consumers. The act embraced all these ideas, conflicting though they were, and provided that all of them be included in the codes of fair competition.

As a result of the President's declaring the country off the

gold standard on April 19, 1933, and of the passage of the Inflation Act (approved May 12, 1933), there was a considerable rise in the general price level by June 15. Then, as a result of the passage of the National Industrial Recovery Act (approved June 16), both the general price level and the volume of production increased rapidly from June 15 to July 15 of that year. Notwithstanding, there was little or no increase in the rate of wages and only a very slight increase in the number of workers employed. Industrial enterprises increased their volume of production in anticipation of the higher cost of production which was expected to be entailed by the adoption of codes of fair competition under the NRA. They increased their volume of production also because of the anticipation of a rise in the general price level resulting from inflation. Moreover, in the interim, practically none of the industrial leaders presented codes of fair competition for acceptance by the NRA, but postponed presenting such codes as long as possible. Up to August 1, 1933, only the textile industry was operating under an NRA permanent code.

In July the President became concerned because of the lagging of employment and wages behind the increasing cost of living. On July 27, 1933, he decided to ask all employers to sign a temporary re-employment agreement with the NRA which would later be superseded by permanent codes adopted by the respective industries. The President's Re-employment Agreement was generally accepted by American business enterprises and a "Blue Eagle" emblem was awarded to each employer who accepted this agreement. The emblem was to be exhibited as public evidence that the employer had accepted the President's Re-employment Agreement. The contents of the agreement referred almost entirely to hours of labor, rates of wages, and employment conditions.

In this agreement the employers agreed not to employ any person under sixteen years of age, except that persons between fourteen and sixteen might be employed for not more than three hours a day. They agreed not to work any clerical employe or salesman in any store, office, or establishment for more than forty hours a week, and not to employ any factory or mechanical worker more than an average of thirty-five hours

a week from August 1 to December 31,1933 (but with the right to employ such workers a maximum of forty hours a week for any six weeks within that period). They agreed not to pay any salesman or clerical employe less than $15.00 a week in any city of over 500,000 population, not less than $14.50 in any city between 250,000 and 500,000, nor less than $14.00 a week in any city between 2,500 and 250,000 population, and in towns of less than 2,500 population to increase all wages not less than 20 per cent, provided this increase would not require wages in excess of $12.00 a week. They agreed not to pay any factory or mechanical employe less than forty cents an hour unless the hourly rate for the same class of work on July 15, 1929, was less than forty cents an hour, and in which case not to pay less than the hourly rate of July 15, 1929, and in no event less than thirty cents an hour. They agreed also not to reduce the compensation for employes then receiving wages in excess of the minimum wages stipulated in the agreement and to increase the pay for such employes by an equitable readjustment of all pay schedules. They agreed further not to increase the price of any goods and merchandise over the price of July 1, 1933, by more than was necessary as a result of the increase in the cost of production or replacement, and to refrain from taking profiteering advantages of the consuming public.

As a result of the President's Agreement more than one million unemployed laborers were reemployed. Also, there was a substantial increase in the wages of the lowest paid laborers in the country. Compliance with the President's Agreement by small employers in the retail trades and in the service industries, in many cases, entailed considerable sacrifices and hardships on their part, because many of them were not benefited by any increase in volume of business. But, on the whole, the larger industrial enterprises were in a position to accept this agreement without sacrifices, because they had been able to get much higher prices for a larger volume of sales of their products as a result of the inflational movement.

Beginning September, 1933, partly as a result of the President's Re-employment Agreement and partly as a result of inducements and pressure from the NRA, several of the major industries presented codes of fair competition for acceptance

and approval of the President. The proposed permanent codes were written by the leaders of the respective industries, and they naturally contained what these leaders wanted to get for themselves and for their industries from the NRA. The codes submitted for the major industries generally contained no more labor provisions than those the act required should be inserted in all approved codes. The larger part of each of the codes for the major industries was devoted to provisions in reference to control of output, to elimination of price competition, or to policies in reference to prices, and to the regulation of specific trade practices.

After holding public hearings upon proposed codes, the NRA sometimes revised them to conform to its ideas, and then recommended them to the President for approval. At these hearings the public was supposed to be represented by the Consumers' Advisory Board of the NRA, and labor was supposed to be represented by the Labor Advisory Board of the NRA. There was widespread complaint that these two boards were not given an adequate opportunity to represent the respective interests, and that the Administrators paid little or no attention to the opinions of the members of these boards in the formulation and adoption of the various codes. Most of the immediate assistants of the Administrator, as well as the members of the Industrial Advisory Board, were business men drafted into the services of the NRA. The traditional private business point of view appears to have prevailed in the formulation and adoption of the permanent codes by the NRA; at least no more labor safeguards were placed in them than the act required.

In chapter fifteen will be found a discussion of the provisions of the NRA codes which had to do with limitation of production, price control, and so-called trade practices. The discussion of codes in the remaining part of this chapter will be confined largely to their labor provisions. The labor provisions of the law were given in Section 7, which reads:

> "SEC. 7 (*a*) Every code of fair competition, agreement, and license approved, prescribed, or issued under this title shall contain the following conditions: (1) That employes shall have the right to organize and bargain collective-

ly through representatives of their own choosing, and shall be free from the interference, restraint, or coercion of employers of labor or their agents, in the designation of such representatives or in self-organization or in other concerted activities for the purpose of collective bargaining or other mutual aid or protection; (2) that no employe and no one seeking employment shall be required as a condition of employment to join any company union or to refrain from joining, organizing, or assisting a labor organization of his own choosing; and (3) that employers shall comply with the maximum hours of labor, minimum rates of pay, and other conditions of employment, approved or prescribed by the President.

"(*b*) The President shall, so far as practicable, afford every opportunity to employers and employes in any trade or industry or subdivision thereof with respect to which the conditions referred to in clauses (1) and (2) of subsection (*a*) prevail, to establish by mutual agreement, the standards as to the maximum hours of labor, minimum rates of pay, and such other conditions of employment as may be necessary in such trade or industry or subdivision thereof to effectuate the policy of this title; and the standards established in such agreements, when approved by the President, shall have the same effect as a code of fair competition, approved by the President under subsection (*a*) of section 3.

"(*c*) Where no such mutual agreement has been approved by the President he may investigate the labor practices, policies, wages, hours of labor, and conditions of employment in such trade or industry or subdivision thereof; and upon the basis of such investigations, and after such hearings as the President finds advisable, he is authorized to prescribe a limited code of fair competition fixing such maximum hours of labor, minimum rates of pay, and other conditions of employment in the trade or industry or subdivision thereof investigated as he finds to be necessary to effectuate the policy of this title, which shall have the same effect as a code of fair competition approved by the President under subsection (*a*) of section 3. The President may differentiate according to experience and skill of the employes affected and

according to the locality of employment; but no attempt shall be made to introduce any classification according to the nature of the work involved which might tend to set a maximum as well as a minimum wage."

There was more public discussion of paragraph (*a*) of Section 7 than of any other part of the National Industrial Recovery Act. The sentence giving employes the right to organize and bargain collectively through representatives of their own choosing, and the one stating that no employe shall be required as a condition of employment to join any company union or refrain from joining or organizing a labor union of his own choosing, were the center of much discussion and of many labor controversies during the life of the act. The act states that all codes of fair competition approved by the President shall recognize these rights of employes as well as contain prescriptions as to maximum hours of labor and minimum rates of pay for all employes of the enterprises to be affected by the respective codes. Paragraph (*c*) gave the President the power to prescribe maximum hours of labor and the minimum rates of pay for *all industries* regardless of whether or not they submitted codes of fair competition.

The guarantee of the rights of employes to organize and bargain collectively and their right to organize or join a labor union of their choice was inserted in most of the codes simply by quoting the exact wording of Section 7 (*a*). None of the important permanent codes provided for fewer hours of labor than those specified in the President's Re-employment Agreement, and several of them contained provisions permitting employers to employ laborers a greater number of hours than was permitted by the temporary agreement with the President. Neither did the wage provisions of many of the permanent codes raise the minimum pay of laborers above the minimum already agreed to in the emergency agreement with the President.

In short, the masses of laborers gained nothing in the way of shorter hours or higher wages as a result of the adoption of the permanent codes, over and above what they had already gained as a result of the employers' acceptance of the President's Re-employment Agreement of July 27, 1933. At the

time of the adoption of the permanent codes, it was argued by business leaders that they were then unable to raise wages or to shorten hours beyond the provisions of the President's Agreement; several of them stated that they would shorten hours and raise wages as soon as business became more profitable and their industries were better able to bear the extra financial burden.

By March, 1934, such a large number of major industries were operating under permanent codes it was estimated that 85 per cent of all industrial workers were employed in enterprises subject to some one of these codes. As a result of the decline in the stimulating effects of the inflation "shot" administered to business in the spring of 1933 by the President and as a result of the industrial "let-down" in production after the major industries became subject to permanent codes, there was practically no increase in private employment during the winter of 1933-34. The President and the NRA became concerned over the lagging of private employment and called a conference of all code authorities and business leaders to meet in Washington in March, 1934. The object of this conference was to induce the various industries to amend their codes by providing for decreased hours of labor a week for employes without correspondingly decreasing the weekly wage payments to each. The President addressed the conference and asked that industry immediately adopt this labor policy.

On the whole this conference was a failure. Practically none of the industries were willing to accept the President's recommendation in reference to shorter hours without reducing the weekly pay. The industrial leaders argued that private industry could not then stand such an increased cost burden. Many of them admitted that, on the whole, profits had increased since March, 1933, but they claimed that the increase in profits had not been sufficient to enable industry to accept such a labor policy. It was generally understood at this conference that the various industries separately, from time to time, would accept this labor policy, but only when, and if, their respective profits would permit them to do so. But such a time never did occur.

It was the opinion of many of the industrial leaders present at the March NRA conference that the government should do

something further to stimulate the building and construction, and the heavy goods industries. These leaders claimed that industry, as a whole, could not recover until the building trades and the heavy goods industries recovered. They pointed to the fact that construction throughout the country in 1933 was only 25 per cent of what it was in 1926, and that in 1926 the construction and heavy goods industries employed some four or six million workers more than they did in 1933. Their conclusion was that if these industries could be revived (to the 1926 level) a long step would be made toward solving the unemployment problem without reducing the hours of work of laborers. Committees were appointed to study these problems. As a result of the work of one of the committees, the National Housing Act was passed for the purpose of stimulating a revival in the building trades. As a matter of fact, as previously pointed out, neither the construction nor the capital goods industries should be revived to the 1926 relative level; such a revival would not produce a recovery, it would cause a destructive boom which would produce a greater disequilibrium in our industrial system than we now have.

It is evident from the nature of the permanent codes and from the results of the March NRA conference of business leaders, that too many of our business leaders were still thinking in terms of 1926 business conditions and of the 1926 level of profits. Notwithstanding the backward attitude of these individuals, if it were possible to make such a return, business should not be permitted to return to 1926 conditions of excess profits, overinvestments, overexpansion and inadequacy of consumers' money income. Also, our experiences with the permanent codes and with the conference, should show that an industrial equilibrium will not be established through industrial control exercised by the business leaders. They are prone to think too much in terms of immediate profits; they will not accept voluntarily wages and hours of labor policies which are necessary for the elimination of unemployment and the establishment of an industrial equilibrium. As we shall see in the next chapter, the trade policies, as well as the labor policies, they adopted under a self-regulation plan were designed too much for "self-benefit" and too little for the benefit of employes and

of consumers. If our national labor policies are to be successful and beneficial to labor and to the public they cannot be designed and administered by industrialists. Practically all the benefits which laborers received as a result of the NRA were awarded as a result of the President's Re-employment Agreement, and by the action of government labor boards.

When the permanent codes were adopted a code authority was created as an enforcement agent for each. The code authorities were made up largely of representatives of the industries for which the respective codes were adopted. On each code authority was a representative of the NRA; and there could have been a representative of labor on each code authority, but labor appointed a representative on few of the code authorities.

It was soon found that the code authorities were not effective agencies for enforcing the labor provisions of the several codes. The NRA then appointed State Compliance Boards to each of which were attached a labor compliance officer and a trade compliance officer. It was the duty of these state compliance officers to see that the provisions of the various codes were enforced locally. Many of the state labor compliance officers did valuable work in inducing or forcing employers to comply with the wage and hour provisions of the codes. Such officers were of special value in protecting the interests of the unorganized employes and forcing employers to pay the code minimum wages. Practically none of the United States district attorneys attempted to assume original jurisdiction in seeing that code provisions were enforced, though the act stated that the several district courts of the United States were invested with jurisdiction to prevent and restrain violation of any approved code of fair competition.

As a result of the insertion of Section 7 (*a*) in the Recovery Act guaranteeing laborers the right to bargain collectively, through representatives freely chosen without hindrance from employers, there was an immediate movement on the part of both the American Federation of Labor and the employing corporations to organize laborers into unions. The American Federation of Labor and the trade and industrial unions affiliated with it took action to organize non-union workers

into unions to be affiliated with the Federation. The large industrial companies took action to organize their employes into "company unions" over which they would have a large measure of control. The American Federation of Labor reported an increase in its membership for the first three months of the NRA's existence of 1,300,000, making a total membership of over 4,000,000. It is estimated that there were more than 5,000,000 members of independent or outside labor unions on September 1, 1933. During the period of code-making the large industrial concerns were active in forming company unions. It was estimated that in May, 1934, about 46 per cent of the employes in the code industries were organized in company unions, or that the employers were dealing with them through such unions; at the same time only 10 per cent of the employes were being dealt with through outside or independent unions; the other 44 per cent of the employes were being dealt with as individual or non-union laborers.

Also, as a result of the National Industrial Recovery Act there was a great increase in the number of labor strikes. During July, August, and September, 1933, there were 212,000 strikes, which was nearly four times as many a month as had occurred during the preceding three years. Ordinarily, strikes are more numerous during recovery periods. Many of the strikes since September, 1933, have been large ones, such as the strike of the textiles workers in the autumn of 1934. Several of the strikes have been called to enforce code wages, and some have been called to improve the code wage minima. Some strikes have been called to force employers to recognize or deal with the independent unions. In addition to the many strikes, there have been many more threatened strikes and controversies between employes and companies over code provisions and over the application of Section 7(*a*).

Because the various NRA code authorities appeared unable to cope with the increasing number of labor difficulties, the President created the National Labor Board to compose all conflicts threatening the industrial peace of the nation, with power to use conciliation, mediation, or arbitration in settling the controversies. The Board was originally composed of three representatives of employers, three of laborers' and Senator

Wagner as chairman; the Board's membership was later increased to eleven members. The larger part of the work of the Board was confined to employer-labor disputes over interpretation and application of code provisions. The work of the Board was so heavy that it organized Regional Labor Boards to handle the local disputes, and confined its work to the larger cases. Up to February, 1934, the National Labor Board, together with its regional boards, had handled eighteen hundred labor disputes involving more than nine hundred thousand laborers; out of the eighteen hundred cases over eleven hundred settlements were secured. Of the 132 strikes handled by the Board, 107 were settled satisfactorily. Between February and June, 1934, the Board handled an additional nineteen hundred cases, most of which were settled by conciliation agreements.

In March, 1934, Senator Wagner introduced a bill in the Congress to make permanent the National Labor Board and to broaden its powers in settling labor disputes. The bill would have outlawed company unions and forced employers to deal with the freely chosen representatives of the laborers. The Wagner bill met much opposition in the Congress, and at the close of the session in June a joint resolution was substituted for it. The joint resolution gave the President power to establish a board or boards of labor relations to investigate and act as mediator in labor disputes, to hold elections of employes' representatives, and in other ways to give effect to the bargaining provisions of the National Industrial Recovery Act. The National Labor Relations Board, created as a result of this joint resolution, was effective in adjusting numerous labor controversies. However, several serious strikes occurred after the National Labor Relations Board was created, of which the general strike of San Francisco and the textile strikes in the East and the South were the most serious. The powers of this Board were destroyed by the United States Supreme Court's decision in May, 1935, in declaring title I of the National Industrial Recovery Act (the NRA) unconstitutional.

The NRA fell short of the objective of re-establishing an industrial balance. In relation to the value of the net production of industry, the NRA did not increase the purchasing power of consumers. There was considerable decrease in unemploy-

ment as a result of the acceptance of the President's Re-employment Agreement of September 1, 1933. Also, that agreement resulted in some improvements in the standards of labor because of the reduction in hours of labor per week and of the increase in the wages of the low-wage receivers. But as a result of the adoption of the permanent codes of fair competition no additional progress was made in shortening hours or raising wages. Section 7(*a*) of the act enabled organized labor to increase its strength, but resulted also in a rapid growth of company unions and in many strikes.

Lack of success of the NRA labor policy was not due to inadequacy of the labor provisions; it was due to the ineffective administration of the provisions of the Act. The President was given adequate power to regulate hours of labor and minimum rates of wages in all industries. He did not see fit to exercise this power except with the consent and co-operation of the industrial leaders. In general the industrialists refused to consent to improvements in the standards of labor beyond those accepted in the President's voluntary Re-employment Agreement. They placed in the codes submitted for approval labor standards no higher than those of the Re-employment Agreement; the President accepted those standards in accepting the codes; the employers in the March, 1934, conference refused to consent to higher labor standards, and the Administration did not use its powers under the act to force them to do so.

But unemployment cannot be eliminated in this country without a further reduction of the work hours of laborers in industry. An industrial equilibrium cannot be established until laborers and other small income receivers get a larger percentage of the national money income. In accomplishing this balance laborers must receive higher wages (in relation to the net value produced by industry) than they received before the depression. A final estimate of the value of the NRA as a national plan to effectuate an equilibrium in our industrial system cannot be arrived at until a study has been made of production, price, and trade practice provisions of the codes of fair competition.

At this point it might be well to summarize the fundamental

reforms which must be brought about in our industrial system in order to secure an industrial equilibrium.

To place our industrial system in a condition of balance or equilibrium it would be necessary to re-adjust both the flow of the national money income and the *relative* productivity of the different industries. It would be necessary to place a larger percentage of the national income in the hands of the mass of consumers, and smaller percentage of it in the hands of investors than was done during the predepression days. We must have *relatively* less saving on the part of the few, and *relatively* more spending on the part of the masses. With such a change in the flow of the national money income there would be less new construction and expansion of industries in proportion to total production than we had in the twenties. Therefore, there would be relatively less demand for constructional materials and for commodities of the heavy goods industries than before the depression. On the other hand, there would be relatively more demand for consumption goods than during the twenties. In other words, the establishment of an industrial equilibrium would boost the consumption goods industries and cause them to expand, but it would not revive immediately the capital goods industries. Should we secure an industrial equilibrium, it would be a long time before the demand for new constructional and capital goods would equal that of 1927.

With an industrial equilibrium there would be no surplus investment funds or production of idle capital equipment. There would be a productive use for all savings, and a current demand for all goods produced. The different classes of goods would be produced in proportion to the relative demand for each. Industry as now constituted would readjust itself to the new *relative* demand for the different classes of goods. A smaller proportion of the total capital and labor of the country would be engaged in producing new capital goods, and a larger percentage of both capital and labor employed in producing consumption goods than formerly.

CHAPTER FIFTEEN

THE NRA, SELF VERSUS GOVERNMENT REGULATION OF BUSINESS

AFTER the business depression of 1929 became severe there were many requests from business leaders that the anti-trust laws be repealed or at least temporarily suspended to permit enterprises in the various industries to co-operate in bringing about business recovery. Some leaders argued that if the government would repeal or suspend the antitrust laws and permit competitive business enterprises to co-operate through trade associations, private business could develop a plan of self-government of industry which would result in speedy business recovery. They claimed that industrial recovery from the depression could not be brought about as long as great over-production in the various industries and grossly unfair trade practices were prevalent. It was said that many unfair trade practices had sprung up during the depression, and that they could be eliminated only through co-operative action of competitors. They claimed that a balanced production and a national trade free of unfair practices could be attained only through a plan of self-government of industry.

The passage of the National Industrial Recovery Act was a partial answer to the appeal for self-government in industry. This act, through its codes of fair competition, gave various industries an opportunity to set up a self-governing plan of regulation. It gave them an opportunity to place limits on production, and in some cases to set prices and allot production among the different enterprises in the respective industries. The National Industrial Recovery Act did not abolish the anti-trust laws, but on the contrary stated that the codes adopted under the act should not permit monopoly and monopolistic

practices. The act did state, however, that no business enterprises would be subject to prosecution for violation of any of the provisions of the antitrust laws because of action taken in compliance with the provisions of a code of fair competition which had been approved by the President; however, the act stated that the President was not to approve codes of fair competition the provisions of which were in violation of the antitrust laws. Therefore, presumably none of the provisions of the codes approved by the President were in conflict with the provisions of the antitrust acts.

Consequently, when the President approved codes permitting price agreements among business enterprises, those price code provisions presumably were in harmony with the provisions of the antitrust acts; at least no business enterprise could be prosecuted for violation of the restraint of trade provisions of the antitrust acts because of compliance with such provisions of the approved codes. Practically all of the codes for the major industries contained provisions which permitted the industries to exercise restraints upon the volume of production; more than half of the major codes permitted either direct or indirect price control through the code authorities. Most of the price agreement provisions of the codes were effectuated through what are known as open price agreements. The open price plan provided that each enterprise must file with the code authority its future intention to lower prices, and must wait at least two weeks before putting into effect the proposed price changes. By bringing pressure to bear upon the enterprises proposing to make price cuts, this scheme gave the code authority of the industry an opportunity to prevent the lowering of prices.

It was claimed by most of the industrial leaders that it was necessary to insert price control provisions in the NRA codes because of the increased cost of operation as a result of the hour and wage provisions of the codes. They took the position that since business enterprises, through the codes, agreed to shorten hours of laborers and raise minimum wages, the business enterprises should be given the privilege of regulating the prices of their products so that the increased cost of operation would be offset by increased prices. Many of the industrialists went so far as to maintain that regulation of hours of

labor and wage rates by the Government necessitated the regulation of prices by private industry. In other words, they claimed that it was not possible to shorten hours and raise wages of employes without at the same time, *by concerted action of the employers,* raising the prices of the products of the industries which employ the laborers.

All the NRA codes had provisions in regard to specific trade practices in the respectives industries. Practically all of them prohibited commercial bribery by members, and had regulatory provisions in regard to the terms of sale of goods. But, in the opinion of the majority of industrialists, the most pernicious unfair trade practice is that of price-cutting. Of course, price-cutting may or may not be an unfair practice: If the lower prices offered by a competitor are below the cost of production, and if at the same time the lower prices are offered temporarily by the competitor for the purpose of injuring or driving others out of business, the practice is unfair. But, merely offering to sell at lower prices because of superior efficiency over competitors is not an unfair trade practice, though it may be called price-cutting. Such price-cutting should not have been prohibited by codes of fair competition; such competition should be encouraged rather than suppressed.

From the standpoint of the consuming public, the adoption of the permanent codes resulted in the imposition of limitations on the volume of production as well as in an arbitrary raising of prices of industrial products. Also, from the public welfare point of view, many of the NRA codes resulted in holding back industrial progress, and in withholding from the public the benefits of maximum industrial efficiency: Some of the codes prohibited further introduction of labor-saving devices. The price control measures discouraged efficiency in business by guaranteeing a profit return to business enterprises regardless of productive efficiency.

It is hardly necessary to state that industrial recovery did not result from the adoption and application of the NRA codes of fair competition in the various industries. It is now evident that self-regulation of industry, through the NRA codes, did not bring about general business recovery. However, because it boosted prices through the price- and production-control

provisions of the codes, the NRA resulted in a considerable increase in the profits of most industries. Owing to the fact that prices were increased more rapidly than the general level of wages, the codes did not result in a relative increase in the purchasing power of wage earners or of consumers in general; on the contrary, because of the arbitrary increase in prices, the application of the codes as a whole resulted in *reducing*, rather than increasing the actual purchasing power of consumers in proportion to current production.

If the government had not paid out billions of dollars to aid the unemployed and to carry on public works during the life of the NRA, there would have been a decrease in the volume of production as a result of the adoption of the NRA codes, which tended to limit physical production in industry to correspond to the market demand for those products at higher prices. The market demand for finished industrial products would have been reduced eventually as a result of the higher prices, and production then would have been adjusted to fit the limited market demand for consumers' goods. The artificial money incomes paid to consumers as a result of the government's aid program bolstered up the decreased purchasing power of consumers resulting from the adoption of codes and kept the volume of sales from declining following the advent of the NRA.

The NRA codes, by enabling business enterprises to increase immediate profits, prevented them from adjusting their businesses to a lower price level and profit margin. The codes enabled business enterprises to avoid making desirable reductions in their capitalization and administrative expenses so they might operate on a lower price level. Also, because of the higher prices established as a result of the codes, business executives were dissuaded from applying the available methods of increasing efficiency in production, which under a lower price level they would have applied in order to decrease their cost of production per unit of product. In a large measure, the codes caused business executives to stress high profits per unit of products sold, and encouraged them to put a limit upon their production so they might raise that unit profit margin. To secure a sound business recovery, however, emphasis must be placed upon the sale

of a large volume of goods at a small margin of profit per unit of goods sold. General and lasting prosperity, depends upon the sale of a large volume of goods at a small margin of profit per unit of sales.

The argument that government regulation of hours of labor and wage levels made it necessary to permit competing enterprises to agree on the volume of production and prices is unsound. Competitive business enterprises do not need mutual agreements concerning prices for finished goods so that they may adjust their businesses to any given labor cost level which might be set by the government. The application of a uniform scale for hours of labor and for rates of wages in competitive enterprises in an industry should not, and does not, prevent those enterprises from competing with one another in efficiency of production and in quality of products as well as in prices. A uniform labor cost policy would place competitive enterprises on an equal and fair basis of competition in both production and sale of their products. A uniform labor cost should in no way prevent competitive enterprises from competing in prices.

I do not maintain that higher wages in some industries in the autumn of 1933 did not necessitate an immediate increase in the prices of their products. But, because of a general increase in the labor cost of production, price increases in each industry could have been, and should have been, made on a competitive basis. Government control of hours of labor and wage scales would have eliminated the unfair competitive practice of having some employers paying lower wages than their competitors. Uniform wage rates for competing employers should place competition among them on a fairer and higher level, rather than make competition impossible.

The policy of voluntary price agreements results in the preservation of a great number of inefficient business concerns which are able to exist only because of the high prices prevailing in their respective industries. Such a national policy stifles improvements in methods of production and the application of the most efficient methods of production and of business administration. It creates an artificial scarcity of goods and an artificial limitation on standards of living. The only defense which can be given for this policy is that it gives immediate

profits to the operating business enterprises and enables them to perpetuate inflated capital charges and high administrative expenses.

One of the greatest mistakes in applying code provisions to American business was in attempting to apply them to all sizes and all kinds of industries (including the service industries). Not even the wages and hours provisions of the President's Re-employment Agreement should have been applied to the small, individually owned business enterprises. Certainly none of the provisions of the permanent codes should have been applied to small enterprises in the retail and service industries. The NRA itself, in June, 1934, admitted that it was a mistake to have price-control provisions in the codes for the service industries.

As pointed out in an early chapter of this book, one of the main causes of the depression was the fact that prices of industrial products during the twenties were not reduced in proportion to the decreases in the cost of production. One of the principal reasons why prices remained high under conditions of a decreasing cost of production was the controlling influence exercised by the monopolistic corporations and the trade associations in the various industries. As a result of the price policies carried out through trade associations, many of the industries were able to keep the prices of their products from falling even though there was a considerable decrease in the cost of producing as well as an increase in the volume of production. Many of the NRA codes of the major industries legalized this price-control activity of the trade associations, and made it more effective and more destructive of necessary adjustments between cost and prices. Yet the legalization of the price control activity of trade associations was for the alleged purpose of bringing about business recovery; recovery from a depression which in part was produced by industries controlling prices through monopolistic agencies.

Public protest was so general against the "high code prices" in the service industries that in June, 1934, the NRA decided to drop price-fixing regulations from the codes of the service industries, such as the cleaning and dyeing, beauty shops, automobile laundries, etc. Also, on June 7, 1934, the NRA announced

a change in policy in respect to price regulation provisions of all codes. This announcement stated that status quo would be maintained in price provisions of existing codes until such time as new provisions could be worked out, but laid down principles to be effective immediately for any new codes. These principles were: That the fixing of minimum prices would be allowed only in the event of an extreme emergency arising from destructive competition; that the minimum price in such case is to be fixed to match the lowest minimum cost in the industry, as such cost is determined by the NRA; that open price agreements would be permitted in an industry only when prices are posted with a neutral agency to go into effect immediately without any waiting period. This announcement was a belated admission by the NRA that previously it had gone too far in approving price regulatory provisions in the various codes. There is no evidence that the NRA ever put this new policy in reference to price-fixing in operation by changing the adopted codes.

Public criticism of price regulation and production control through code provisions was general and persistent. President Roosevelt in a speech September 30, 1934, took cognizance of this public criticism and admitted its possible justification in these words:

> "Let me call your attention to the fact that the National Industrial Recovery Act gave business men the opportunity they had sought for years to improve business conditions through what has been called self-government in industry. If the codes which have been written have been too complicated, if they have gone too far in such matters as price fixing and limitation of production, let it be remembered that so far as possible, consistent with the immediate public interest of this past year and the vital necessity of improving labor conditions, the representatives of trade and industry were permitted to write their ideas into the codes. . . . . There may be a serious question as to the wisdom of many of those devices to control production, or to prevent destructive price cutting which many business organizations have insisted were necessary, or whether their effect may have been

to prevent that volume of production which would make possible lower prices and increased employment."

On May 27, 1935, in handing down a unanimous decision in the Schechter case, the Supreme Court declared unconstitutional the major portions of title I of the National Industrial Recovery Act. The Court held that the act's delegation of power to the President, to approve codes of fair competition which would have the force of law, was an unwarranted delegation of legislative power under the Constitution. It held further that the attempt of the Federal government under the National Industrial Recovery Act to fix hours and wages of employes in purely intrastate businesses was not a valid exercise of the Federal power granted by the interstate commerce clause of the Constitution. Also, the Court held that the existence of a national emergency was not sufficient grounds to warrant the Federal government in exercising powers not specifically granted to it by the Constitution. On this point the Court said:

"Undoubtedly, the conditions to which power is addressed are always to be considered when the exercise of power is challenged. Extraordinary conditions may call for extraordinary remedies. But the argument necessarily stops short of an attempt to justify action which lies outside the sphere of constitutional authority. Extraordinary conditions do not create or enlarge constitutional power.

"The Constitution established a national government with powers deemed to be adequate, as they have proved to be both in war and peace, but these powers of the national government are limited by the constitutional grants. Those who act under these grants are not at liberty to transcend the imposed limits because they believe that more or different power is necessary.

"Such assertions of extra-constitutional authority were anticipated and precluded by the explicit terms of the Tenth Amendment,—'The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people'."

As a result of this decision all approved NRA codes of fair competition lost their legal status and became non-enforceable; the antitrust laws are re-instated in full force regardless of code provisions. The labor provisions of Section 7 of the National Industrial Recovery Act are not declared to be unconstitutional except as applied to intrastate businesses. However, the labor provisions of the act are enforceable only through prescribed or approved codes of fair competition; the approval of compulsory codes of fair competition is declared to be an unwarranted delegation of legislative power to the executive. Therefore, the labor provisions cannot be enforced, since the act provides for enforcement only through approved codes.

Because of the fact that the National Industrial Recovery Act was to expire on June 16, 1935, and because of the Supreme Court's decision invalidating most of the provisions of the act, Congress passed a joint resolution (approved June 14) extending the valid provisions of the act until April 1, 1936. This brief joint resolution reads:

> "*Resolved by the Senate and House of Representatives of the United States of America in Congress assembled,* That section 2 (*c*) of title I of the National Industrial Recovery Act is amended by striking out 'at the expiration of two years after the date of enactment of this Act' and inserting in lieu thereof 'on April 1, 1936.'
>
> "SEC. 2. All the provisions of title I of such Act delegating power to the President to approve or prescribe codes of fair competition and providing for the enforcement of such codes are hereby repealed: *Provided,* that the exemption[1] provided in section 5 of such title shall extend only to agreements and action thereunder (1) putting into effect the requirements of section 7 (*a*), including minimum wages, maximum hours, and prohibition of child labor; and (2) prohibiting unfair competitive practices which offend against existing law, including the antitrust laws, or which constitute unfair methods of competition under the Federal Trade Commission Act, as amended."

1 Exemptions from provisions of the antitrust laws in complying with provisions of approved codes.

Just what effect this joint resolution will have is not quite clear. It repeals all the invalidated provisions of the NIRA which gave the President power to approve or prescribe codes of fair competition. On the other hand, it apparently legalizes private agreements in industry by exempting from the anti-trust laws agreements in reference to (*a*) rights of laborers to organize and to belong to unions of their choosing; (*b*) minimum wages; (*c*) maximum hours; (*d*) child labor; and (*e*) prohibiting unfair competitive practices which offend against existing law or which constitute unfair methods of competition under the Federal Trade Commission Act. No authority is given for specific government approval of any of these private agreements. What government agency is to supervise these private agreements to determine whether the competitive practices prohibited by them are offenses against existing laws, or constitute unfair methods of competition under the Federal Trade Commission Act? Evidently that would be left to the Federal Trade Commission and to the courts.

The President set up a much abbreviated National Industrial Recovery Administration to take the place of the one whose powers were destroyed by the Supreme Court's decision. Apparently, the chief functions of this "Little NRA" are to observe and report on the industrial and economic consequences of the abolition of the compulsory codes of fair competition. Particular attention is to be paid by this administrative body to the trend of changes in hours of labor and wage scales following the abolition of the compulsory codes. There have been conferences between the "little NRA" and the Federal Trade Commission in reference to the approval by the Commission of voluntary codes of fair competition, and a plan for voluntary codes may be worked out as a result of these conferences.

Newspaper dispatches quote one of the members of the Federal Trade Commission as having said that "open price agreements" would be a possibility under voluntary codes which might be approved by the Commission. He evidently feels that the Commission might decide that price-cutting constitutes an unfair method of competition under the Federal Trade Commission Act. Such a decision would be a great victory for monopolistic trade associations.

As a result of the nation's experiences with NRA codes, it is safe to conclude that self-regulation of industry with government co-operation and supervision did not succeed. The experience also indicates that self-regulation of industry could not succeed under any plan. The soundness of the policy of government regulation of prices may be seriously questioned, and regulation of prices and production by leaders of industry in all probability would never result in benefit to the public. There should be public regulation of the general business policies of the large enterprises in our major industries. While business leaders should make suggestions to the government as to the kind of regulatory policies to be adopted, the function of regulation should be exercised directly by the government, and not by representatives of the industries.

The government needs a new business policy of government regulation rather than self-regulation of industry. This new national industrial regulation policy should recognize the fact that our industrial system is made up of an aggregate of private business enterprises operated for profits. The private profit motive should be fully recognized by this new policy; it should not discourage reasonable profits from the operation of efficient competitive businesses which produce desirable goods or services. The new industrial control policy should recognize private initiative in business as the most valuable force in our economic system; and, therefore, it should encourage and protect constructive private initiative in business.

However, the new business policy should prohibit private initiative from making money at the expense of, or to the detriment of, the public. The prohibition of the exploitation of labor would prevent employers from making money by paying starvation wages. The exploitation of consumers by sellers charging monopoly prices also should be prohibited under the new government regulation policy. Under it there should be no restraint on legitimate price competition due to superior productive efficiency. It must be the aim of the new business policy of the government to curb private initiative in making profits out of all kinds of exploitation, and to encourage it in making reasonable profits from the performance of useful productive services to society.

Therefore, the new industrial regulatory policy should not permit the elimination of legitimate competition of any kind; it should be designed to raise competition to a higher level of constructive usefulness to society. It should not be used to stifle socially useful initiative in business, but to give such business initiative a chance to serve society as well as private business interests. Sound business training and constructive business leadership should be more valuable under such a public industrial control policy than they were under the old laissez-faire order, or under the now defunct NRA codes. Under the new policy each business effort should have a chance to be rewarded in proportion to its real value to society. Under it real constructive efficiency in business should be at a higher premium than it was under the laissez-faire policy, or under the NRA codes. Only ingenuity in exploiting the public should be discouraged by the new public regulation plan. The standard of competition set by it should be above the level of exploitation, but on the level of highest efficiency.

Regulating prices and production should not be a part of the new national business policy. However, there are a few industries in which, for a short period of time, it would be desirable to have some strict governmental limitations on production. It is my opinion, however, that the number of such industries is very small, and that the policy of limiting production in those industries should not be continued as a permanent one. Government control of production might be applied temporarily to the soft coal and petroleum industries.

If there is any place in our economic system for codes of fair competition in the various industries, those codes should be limited in application to trade practices as such; they should not include any kind of provisions in reference to the volume of production or to prices. They should include only such things as the regulation of specific unfair trade practices, such as the misrepresentation of competitors and competitors' goods, commercial bribery, local price-cutting, the use of "leaders" and of "fighting brands" in trade, terms and conditions of sales, terms of extension of credit to customers, and other activities which are related to trade practices.

This new national policy of government regulation of business should be enacted into law in three separate acts. The first and second acts should deal with the questions of labor relations and the regulation of hours of work and wages of laborers. A discussion of the Labor Relations Act and the proposed Labor Adjustment measure will be reserved for the next chapter.

The third act to replace the NRA should make effective a new national industrial regulation policy. This act should deal with the question of competition in business and with unfair trade practices separate and distinct from all labor questions. *The act should abolish the present temporary policy of self-regulation of industry and provide one of government regulation of competition.* The act might be called the Federal Trade Adjustment Act. The Federal Trade Commission should administer this act as well as enforce the anti-trust laws.

The proposed Federal Trade Adjustment Act should exempt no one from the provisions of the Federal antitrust acts. It should specifically prohibit trade associations from pursuing policies which directly or indirectly result in the limitation of production or the regulation of prices. It should permit the Federal Trade Commission to adopt "codes of fair trade practices" for interstate trade in all industries. Those codes should contain no labor provisions; the regulation of hours and wages should be a government function to be exercised by a Federal Labor Adjustment Board. Neither should the codes contain any provisions in reference to price or production control, except that local price-cutting for purposes of injuring competitors should be prohibited in all the codes. The provisions of all codes should be confined entirely to trade practices unrelated to open competition in prices and in production.

This law should provide that any industry for which a code of fair competition is adopted might set up a committee to advise with the Federal Trade Commission in reference to the enforcement of provisions of the code in the elimination of unfair trade practices in the industry. The act should give the Commission power to secure from each enterprise doing an interstate business in each coded industry all pertinent information in regard to its current operations: such as volume of production, prices

received, stocks of goods on hand, laborers employed, wages paid, balance sheets, profit and loss statements, etc. This act should apply only to the business enterprises in each of the industries which do an interstate business.

CHAPTER SIXTEEN

PERSONAL ECONOMIC SECURITY, SELF-HELP AND THE CONSTITUTION

THE individual may be given assurance of greater economic security through opportunity to work and earn a living for himself and his family and to save for contingencies, or through a government guarantee to him of at least a subsistence income in the form of doles, pensions, and social insurance when he is incapacitated or unable to secure work. It is hardly necessary to remark that economic security obtained through self-help is far more desirable and beneficial both for the individual and for society than economic security obtained through doles, pensions and social insurance. Therefore, one of the supreme aims of the government should be to regulate or to control our industrial system in such a manner as to afford each individual an opportunity at all times to work and earn an income in proportion to his ability to contribute to the nation's real income. These two methods of accomplishing economic security for the individual are not in direct opposition, but may be used simultaneously as complementary methods. However, each represents a different school of political and economic thought.

The concept that the government should guarantee economic security to its citizens through government doles and social insurance may be called the professional social workers' view of how to give economic security to all citizens. Such a program of economic security is based on the assumption that many individuals inevitably will find themselves without private incomes or other means of support either because of their own faults (inefficiency and thriftlessness) or because of economic forces over which they have no control. Consequently, by this

reasoning, the only way an individual can be given security against such unfortunate but unavoidable happenings is to provide doles and insurance payments for those who become victims. In other words, the advocates of the social insurance personal security program proceed on the assumption that inevitably the nation will have a large number of individuals and families with little or no savings whose suffering, as a result of unavoidable unemployment, sickness, old age, and death, can be prevented only by providing public doles and social insurance payments for them when these hazards occur.

The proponents of doles and social insurance as the best means of giving economic security to the individual may accept the glaring defects in the operation of our industrial system as natural and beyond the control of men or governments. They may accept the laissez-faire governmental policy toward business and industry, and oppose any effort on the part of the government to redistribute economic opportunities, employment, wealth, and income. They may not be averse to preserving special privileges, present unemployment, and the concentration of wealth and incomes in the hands of the few; they may accept the theory that these characteristics of our industrial system are natural and inevitable. In short, the advocates of social insurance as the sole means of giving economic security to the individual may be apologists for the defects in our industrial system as it now operates.

On the other hand, those who believe that a great amount of economic security for the individual can and should be attained by the government's taking action to create greater economic opportunities for the ordinary citizen through controlling and regulating the operation of our industrial system deny that low incomes, dire poverty, and unemployment are unavoidable. They claim that should our industrial system be made to operate continuously at full capacity with jobs for all, and with a fair and equitable distribution of the proceeds of production, all unemployment of employables, and most of the lowest incomes, would be eliminated. It is believed by them that constant occupations at fair compensation for all employable people is the best economic security a government can give the mass of its citizens against the unavoidable hazards of

sickness, old age, and death. They hold that if resonable economic opportunities are accorded to all citizens, only a small portion of them would fail to make adequate provisions against the unavoidable personal hazards. Moreover, they believe that it is not only possible for the government to regulate and direct the operation of the industrial system in a manner to produce greater individual economic security, but that it is the supreme duty of the government to put such a policy into operation.

The advocates of greater individual economic security through economic and industrial reforms do not oppose all government doles and social insurance plans. Most of them insist that it is the duty of the government to furnish all individuals and families an income if it does not afford them an opportunity to work and earn incomes for themselves. It is believed that because of the great inequality of the division of the national income during the past few decades, and because of the widespread unemployment during the past fifteen years, many individuals and families have been and are unable to provide against unemployment, sickness, old age, and death; for these reasons they believe the government should furnish such unfortunates funds for sustenance. But they consider such an economic security policy as a temporary and somewhat degrading substitute for a permanent, sound, and uplifting security policy based on opportunities, self-help and self-reliance. After adequate economic opportunities are given to all citizens, they would apply the dole and compulsory social insurance plans only to the small number of unfortunate or inefficient and thriftless individuals who could not, or would not, take advantage of the existing opportunities to earn and save.

Before discussing the various policies which the Federal government should adopt for the purpose of creating greater economic opportunities for the nation's wage-earners, let us recall the various economic opportunities which have been taken from them as a result of industrial development during the last fifty years:

The disappearance of the western frontier in this country took from our laborers the choice between remaining as hired hands or taking up homesteads in the West. The growth of corporations as large employers of laborers, and the association

of corporations into employers' organizations, weakened the individual bargaining power of laborers in dealing with employers. Today it makes little difference to a large corporation which employs thousands of laborers whether it employs any one individual laborer, but it makes a great deal of difference to the individual laborer whether or not he gets a job. The laborers in each of the large industries are placed in the position of competing with one another to get jobs from the same employer or from a few large employers acting in unison. The development of integration and centralized control in industry rendered the individual laborer almost helpless in bargaining with an employer in work contracts.

The growth of mass production and the use of automatic machinery in industry resulted in an increased production per laborer employed, but at the same time resulted in a decrease in the number of available jobs. Because of technological progress, a large surplus of labor was created under conditions of greater industrial productivity. But the mass of laborers received a smaller and smaller share of the fruits of this industrial progress because their bargaining power in dealing with employers became weaker and weaker. In order to retain an industrial balance, while this technological progress was taking place, laborers' real wages by the hour should have been increased in proportion to industry's increase in production per laborer; also, while these changes were occurring in industry, the hours of work a week for laborers should have been decreased sufficiently to create new jobs for all those displaced by the technological improvements in methods of production. But, because of the surplus of laborers created as a result of their displacement, and their weaker bargaining power in dealing with employers, they were unable to secure an improvement in their working conditions during the period of great industrial progress.

If all workers in each industry were to combine their bargaining power and deal with their employers through well organized independent labor unions, they doubtless would be able to force their employers to give them higher wages and shorter work hours. But, if all laborers were so organized in unions, they might demand shorter hours and higher wage rates

than would be justifiable. Such a contingency, however, is not likely to occur because of the fact that the great mass of industrial laborers are yet unorganized; they, as a whole, have never shown any marked disposition or ability to organize or to join independent unions. Only about 10 per cent of all laborers now belong to independent labor unions, the other 90 per cent are either unorganized or belong to company unions. We need not have fears or hopes that all wage-earners in this country will soon deal with their employers through effective independent labor unions. There seems little or no probability that the bulk of our unskilled workers will in the future organize themselves into effective independent labor unions.

There are only two methods by which the mass of American laborers may regain the economic advantages and opportunities taken from them as a result of recent economic changes. First, they might so strengthen their bargaining power through unionization that they would wrest these advantages from their powerful employers. Second, the government might, through effective regulation of hours, wages and work conditions in our large industries, restore these advantages to them. The growth of labor unions could not benefit the bulk of laborers within a reasonable period of time, though a large number of the skilled laborers would receive benefits from the growth of unionization. Restoration of the economic advantages lost by the mass of laborers must be accomplished largely through government regulation of hours, wages, and working conditions in the large industries.

In the past, one of the principal reasons American laborers did not, to a greater extent, organize themselves into unions independent of employers was the effective opposition of organized employers. No one now questions the legal and economic rights of laborers to organize and to belong to such unions. However, employers oppose them because they strengthen the bargaining power of laborers and correspondingly weaken the power of employers to dictate wage contracts. Employers make effective their opposition to such labor organizations principally by (1) refusing to employ laborers who have membership in labor unions, (2) discharging employes who join unions, or (3) refusing to deal with their employes through the

officers of such unions. Such opposition on the part of large employers has prevented many laborers from becoming members of independent labor organizations.

Section 7(*a*) was inserted in the National Industrial Recovery Act for the purpose of curbing the activities of employers in opposing the unionization of laborers. As previously stated, this section provided that every code of fair competition must contain a stipulation that employes shall have the right to organize and bargain collectively through representatives of their own choosing, and shall be free from interference, restraint, or coercion from employers in pursuing such policies. It provided further that the codes must stipulate that no employe and no one seeking employment should be required, as a condition of employment, to join any company union, or to refrain from joining, organizing, or assisting a labor organization of his own chooosing.

It has been pointed out already that section 7 (*a*) had the effect of stimulating growth of labor organization independent of employers, but also, at the same time, had the effect of stimulating employers to organize additional company unions. Following the passage of this act the growth of company unions was much greater than the growth of independent unions. In 1933-35 many of the labor controversies were over the question of whether the company unions or the independent unions of the employes in various industrial plants had the right to represent or speak for all the employes of those plants. It was largely for the purpose of settling controversies over this question that the President, in 1933, appointed the National Labor Board. This question continued to be the center of many labor controversies up to May, 1935, when the Superme Court nullified all provisions of codes of fair competition. Following the Court's decision, Congress passed the National Labor Relations Act (Wagner bill) which was approved by the President on July 5, 1935.

The National Labor Relations Act makes the principal provisions of section 7(*a*) of the National Industrial Recovery Act a part of the substantive law of the nation, and creates a National Labor Relations Board to administer its provisions. This act states, "Employes shall have the right to self-organiza-

tion, to form, join or assist labor organizations, to bargain collectively through representatives of their own choosing, and to engage in concerted activities, for the purpose of collective bargaining or other mutual aid or protection." It states that it shall be an unfair labor practice for an employer (1) to interfere with, restrain, or coerce employes in the exercise of their rights of self-organization; (2) to dominate or interfere with the formation or administration of any labor organization or contribute financial or other support to it; (3) to discriminate in regard to hire or tenure of employment because of membership in any labor organization; and (4) to refuse to bargain collectively with the representatives of his employes chosen by the majority of such employes. The provisions of the act are to apply only to labor relations in industrial plants belonging to employers who do an interstate business.

Unquestionably the Supreme Court will be called upon to pass upon the constitutionality of this act. Doubtless it will be alleged by the opponents of the act that its provisions interfere with the freedom of contract of employers, and that its regulatory provisions do not apply to interstate commerce as such.

In the meantime, what will be the results on the growth of labor organizations? Doubtless, the passage of the act will result in further growth of independent unionization. Certainly, if its constitutionality is upheld by the Court it will result eventually in the death of company unions. However, the act could not result in solving the problem of excessive hours and low wages for the mass of unskilled laborers. Certainly, it will not result in solving the great problem of unemployment. Neither will it solve the problem of a shortage of consumers' purchasing power. Even though the influence of the operation of the Labor Relations Act will be in the direction of improving the economic status of a substantial portion of our laborers, its operation will not result in labor organizations growing fast enough and becoming strong enough to solve our basic labor problems.

The problem of excessive hours of labor and inadequate wages can be dealt with adequately only through direct intervention of the government. This fact was recognized by the Congress in the passage of the National Industrial Recovery Act which, through the codes, gave the President power to

determine the hours of work and minimum wages of laborers in all industries. Other than the submission of the voluntary re-employment agreement in 1933, the President did not see fit to make effective use of this power. Largely because he did not make use of this power, the NRA had little influence in reducing unemployment and bringing about a balance between production and consumption.

Since the NRA is now dead, Congress should pass a new act giving the government power to regulate hours and wages of laborers in all plants or firms doing an interstate business. As indicated in the previous chapter, the problem of regulating competition in industry should be separated completely from the problem of regulating hours, wages, and other labor relations. The act providing for the regulation of hours and wages should be known as the National Labor Adjustment act. Operation of the proposed National Labor Adjustment act should result in the elimination of unemployment through adjustment of the hours of work of laborers in the major industries; its operation should result in an increase in consumers' purchasing power through adjustment of wage rates of workers in the major industries. The act should create a Labor Adjustment Board to administer its provisions.

This act should declare it to be an unfair labor practice for any employer who does an interstate business to employ any laborer more than 30 hours a week unless specifically permitted to do so by the Labor Adjustment Board. The Labor Adjustment Board should be given power to determine from time to time the maximum weekly hours of work for laborers in each industry; the adjustment of hours to be made in accordance with the number of unemployed laborers at the time the hours are fixed. Weekly hours of laborers in all the major industries should be so adjusted as to keep unemployment at a minimum at all times, and at the same time to prevent the development of a shortage of labor in industry. Through adjustment of hours by the Board, the supply of labor and the demand for labor should be equalized.

The Board should have power at its discretion to increase or decrease the weekly wage rates without changing the number of work hours; and it should also have the power to increase

or decrease the hours per week without interfering with the rate of wages by the hour or piece. A decrease in the weekly hours without a corresponding increase in the rate of pay per hour would result in a decrease in the weekly wages of the laborers affected, and an increase in the weekly hours without a corresponding decrease in the rate of pay per hour would result in an increase in the weekly wages of those laborers. The wage rates in the different industries should be adjusted according to the prosperity of each industry, but the hours per week should be adjusted according to the supply of labor. Adjustments in hours should not be made, necessarily, at the same time that adjustments in wage rates are made.

A reduction in the hours of workers sufficient to eliminate unemployment would automatically bring about some increases in the general wage scales of laborers. The disappearance of the surplus supply of labor would strengthen the bargaining power of laborers and thereby increase their opportunities to secure higher wages. Whenever the Board found that hours should be reduced in an industry and issued an order to that effect, it should at the same time specify the minimum weekly wages the employers in the industry must pay. In other words, an immediate reduction in weekly hours for all employes in an industry may entail some reductions in the weekly wages, but the Board should not permit the weekly wages of the lowest paid laborers to be reduced below a certain minimum.

All official action of the National Labor Adjustment Board in reference to adjusting hours or wages should be in the nature of formal orders covering all the interstate enterprises in an industry. Each order should be based on a thorough investigation of the labor and business conditions surrounding the industry, such as the amount of unemployment, the volume of production, prices, and profits. Also, before an order is issued a public hearing on the questions of labor and economic conditions surrounding the industry should be held and the laborers and employers should be given a chance to present their views on these questions. The Board should be given the power to enforce its orders through the Federal courts, and employers and employes should have the right to appeal to those courts for modification or annulment of the Board's orders, just as

appeals to the courts may be made in reference to orders of the Federal Trade Commission.

To establish more definitely the power of the Board to regulate hours and wages in all industries which are engaged in interstate commerce, a system of requiring a Federal license for each such enterprise should be required by the act. Such a licence should be issuable to a firm only on the condition that it agreed to abide by all orders of the Labor Adjustment Board that are uncontested or sustained by the Courts; the license should be revocable in case of violation of any of the Board's orders. Again, to prevent large manufacturing and other producing concerns from carrying on their interstate business through subsidiary trading companies, the use of subsidiary or allied companies for that purpose should be prohibited by the act. The most effective method of controlling the activities of subsidiary and holding companies would be to require Federal incorporation for all firms which engage in interstate or foreign commerce. Under Federal incorporation all intercompany relations could be controlled by the Federal government. In chapter eighteen the question of the desirability of Federal incorporation of firms doing an interstate business will be discussed.

The Tenth Amendment of the United States Constitution limits the powers of the Federal government in the following words: "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." However, it was anticipated by the framers of the Constitution that changed economic and social conditions would bring about the necessity for the people to grant additional powers to the Federal government, and methods of amending the Constitution were provided in Article V. The framers of the Constitution provided that it might be amended by means of Congress proposing an amendment which would receive a favorable vote of three-fourths of the state legislatures, or a favorable vote of state conventions of three-fourths of the states.

There is no provision in the Constitution designating how and by whom the constitutionality of acts of Congress are to be determined. Under Chief Justice Marshall the Supreme Court took unto itself that authority, and, up to the present

time, the exercise of this power by the Court has not been officially challenged either by the President or by Congress. Therefore, whenever the Supreme Court decides that Congress in any of its acts has exceeded the authority granted to the Federal government by the Constitution the prohibited powers are not exercised unless or until the Constitution is amended to permit the use of those powers. In the past the Constitution has been changed, as will be pointed out later.

The unconstitutionality of the National Industrial Recovery Act was decided by the Supreme Court mainly on the grounds that the act delegated unwarranted legislative power to the President, in giving him power to accept codes of fair competition which have the force of legislative acts. However, the constitutionality of much of the New Deal legislation will depend largely on the Court's interpretation of the interstate commerce clause of the Constitution as applied to the regulatory provisions of the new laws. By a strict interpretation of the commerce clause of the Constitution, and by a narrow definition of commerce and interstate commerce, the Supreme Court might find grounds for declaring various provisions of several of those acts in conflict with the Constitution. A basis for an adverse decision on many of these regulatory measures would be laid should the Court continue to hold to the position it took in the NRA case, that extraordinary conditions (or changed economic conditions) do not enlarge Constitutional power, that "the Constitution established a national government with powers deemed to be adequate, as they have proved to be both in war and peace." Notwithstanding such an interpretation of the Constitution, and in spite of a narrow interpretation or definition of the interstate commerce clause, the Supreme Court might hold most, if not all, of the regulatory provisions of New Deal legislation to be constitutional. That would depend on the Court's interpretation of "commerce," or "interstate commerce," and of "what affects commerce."

In its Child's Labor law decision (*Hammer* vs. *Dagenhart*) in 1918, the majority of the Supreme Court of the United States defined commerce as follows: "Commerce consists of intercourse and traffic. . . . and includes the transportation of persons and property as well as the purchase, sale and exchange

of commodities. The making of goods and the mining of coal are not commerce, nor does the fact that these things are to be afterwards shipped or used in interstate commerce make their production a part thereof." In this decision the Court went back to the majority decision in the E. C. Knight case, in which it drew a sharp distinction between commerce and manufacture and held that manufacturing was not a part of commerce. Interstate commerce, of course, is commerce among the several states and with foreign nations.

Even under such a narrow definition of commerce as that given above, the Court might find that hours and wages in producing industries, which make goods for interstate commerce sufficiently *affect* interstate commerce as to subject wages and hours to Federal regulation under the interstate commerce clause of the Constitution. The Court has said that the powers of the Congress extend not only to the regulation of interstate commerce transactions as such, but also, to the protection of that commerce from injury. It has declared that the Congress has the power to protect interstate commerce from injury even though the injury is because of conduct of those engaged in intrastate operations.

In the NRA case the Court in effect said that the Congress had the power to regulate transactions which *directly affect* interstate commerce, but not the power to regulate transactions which affect interstate commerce only indirectly. But the precise line between direct and indirect effect on commerce can be drawn only as individual cases arise, said the Court. Also, in this case, the Court stated that "the distinction between *direct* and *indirect* affect [effect] of intrastate transactions upon interstate commerce must be recognized as a fundamental one, essential to the maintenance of our constitutional system. Otherwise, as we have said, there would be virtually no limit to the Federal power and for all practical purposes we should have a completely centralized government."

The Supreme Court's interpretation of the nature, scope, and permanent adequacy of the Constitution as given in the NRA case, is a narrow one. Its statement that "the Constitution established a national government with powers deemed to be adequate" is doubtless true as applied to the conditions and

beliefs at the time of its adoption. But the additional statement by the Court that the constitutional powers granted the Federal government "have proved to be" adequate "both in war and peace" is not a fact but a bit of judicial dictum. Before making any such statement the members of the Court should have recalled the Dred Scott case, the Civil War, and the twenty-one amendments which already have been made to the Constitution. They should have recalled also the proposed Child Labor amendment which resulted from an adverse decision of that Court on the Child Labor Act passed by the Congress. *If the Constitution as adoped was adequate for our needs why have we already amended it twenty-one times?* However, the process of amending the Constitution is so difficult that, under modern conditions of rapid economic changes, a strict interpretation of its provisions by the Court tends to make our regulatory laws antiquated at the time they are passed.

The Court's statement, that changed or extraordinary conditions do not create or enlarge constitutional grants of power, is true in a very narrow sense; but in a broader and more practical sense changed economic and social conditions call for the exercise of those constitutional grants of power in new ways and by new methods. In order to make the Constitution best serve the welfare of the nation it should be interpreted broadly, and in the light of changed conditions and present problems; otherwise the nation's welfare is sacrificed to the words of the Constitution, and a gross violation of its fundamental purposes is committed. The preamble of the Constitution states its purposes:

> "WE THE PEOPLE of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this CONSTITUTION for the United States of America."

As already pointed out, the only power delegated to the Federal government by the Constitution under which hours

and wages in producing enterprises might be regulated, is the power to regulate interstate and foreign commerce. Unless the Court conceives commerce to consist of producing and processing as well as transporting and buying and selling, the regulation of hours and wages would not be an exercise of the *direct* power to regulate interstate commerce. By what process of careful reasoning could any court separate the producing activities from the trading activities of large modern industrial corporations?

The Court might decide that the Federal government may exercise regulatory powers over wages and hours in enterprises which do an interstate business because labor conditions surrounding production of goods which enter interstate commerce *directly affect* interstate commerce. Every student of our present national economic and industrial problems should know that the labor and other economic problems connected with our great industrial plants are tremendous forces affecting the volume and character of interstate trade. To claim that low wages, high profits, and unemployment in industry do not directly affect trade among the states seems to me to be a fantastic assumption unrelated to facts. Therefore, Congress should pass legislation providing for Federal regulation of hours and minimum wages of laborers working in our large industries upon the theory that production is as necessary to modern commerce as is buying and selling, and upon the further fact that wages and hours in large industrial plants are subject to regulation because they directly affect interstate commerce.

The Supreme Court appears reluctant to concede that the Federal government should have the power under the Constitution to control transactions which indirectly affect interstate commerce because, says the Court, if such power is granted "there would be virtually no limit to the Federal power and for all practical purposes we should have a completely centralized government." In view of that statement, one may well wonder if the learned justices realize the tremendous amount of centralized control in both industry and commerce which has taken place in this country during the past fifty years. Most of the vexing economic problems connected with modern industry and commerce are truly national in their scope, and

can be dealt with adequately only by the national government.

That the national government should not be granted adequate powers to deal with pressing national economic problems because to do so would infringe on "states' rights" and interfere with local self-government, is an argument made largely by the economically privileged classes who desire to retain their special privileges. It is assumed by many that the Civil War settled the question of "states' rights" when they come in conflict with national rights. Today it is a well recognized fact that, largely because of the great concentration of control in our major industries, state governments have been unable to deal adequately with the great national economic problems caused by the development of modern industry. The industrialists are aware of this fact, and that is the reason they use the "states' rights" argument against Federal control of industry; local control means practically no effective government control over their business activities. What they want is freedom from governmental interference so they may take full advantages of their special privileges gained through industrial control.

The alleged and real fear that Federal control over our national economic problems would destroy the functions of local government is unfounded in fact. In the field of economic activities, the local governmental units would be left the regulation of purely local businesses such as the retail and service industries, as well as the professions. In the field of general activities, the local governments could still perform the same police functions of protection of life, property, and health that they now perform. Rights and duties of persons in relation to others, and a large part of the property relations, would still be subject to control by local governments. Supplying educational, eleemosynary, and charitable services would still be functions for local governments to perform. In fact, Federal regulatory policies dealing with our national industrial and economic problems would take from state and local governments practically no functions that they now perform in the interest of the public. On the other hand, the national government would perform new regulatory functions which are greatly

needed because of the acuteness of the problems and the inadequacy of state and local governments to deal with them.

Should the Supreme Court see fit to declare unconstitutional such Federal regulatory functions as are provided for in Congressional acts, the people, through their representatives, should proceed to amend the Constitution in such a manner as to make certain that the Federal government shall have adequate powers to perform these functions. This action must be taken in order to promote the general welfare and secure the blessings of political and economic liberty for the people as a whole. Otherwise, the objects of the Constitution itself are violated.

CHAPTER SEVENTEEN

SOCIAL SECURITY THROUGH DOLES, PUBLIC WORKS, AND SOCIAL INSURANCE

WHEN the Roosevelt Administration acquired control of the Federal government it immediately adopted a plan of giving Federal aid by means of direct aid (doles) to the unemployed (both employable and unemployable) through the Federal Emergency Relief Administration set up for that purpose; and it also gave jobs to the unemployed on public works projects, undertaken by the Public Works Administration and the Federal Emergency Relief Administration. The number of people on Federal emergency relief rolls continued to increase until in the winter of 1934-35 the number reached more than twenty million. It was difficult, if not impossible, to keep Federal relief rolls from constantly increasing, and there seemed little prospect that they would decrease in the near future. In face of this situation the Administration adopted a new policy.

When the 1935 session of the Congress convened in January, the President asked it to pass a bill providing for a new four-billion-dollar public works program to enable him to end the dole (direct relief) system of aiding the unemployed. Also, at that time the President stated that the proposed Social Security bill, providing old age pensions and unemployment compensation, was a part of his new plan for dealing with the unemployment problem. The principal features of the Administration's new plan for dealing with the unemployment problem are:

First, the new public works program is expected to provide employment (directly and indirectly) for all employable individuals on the Federal relief roles. Second, old age pensions, paid

by the Federal and state governments jointly under the provisions of the Social Security Act, are expected to provide for the aged unemployable persons who are or would be on the Federal rolls. Third, the balance of the unemployables on the relief rolls are expected to be taken care of in part by other provisions of the Social Security Act and state and local governments, and in part by relatives and local charity. Whatever objections may be interposed against this new policy of dealing with the immediate unemployment problem, it has one commendable objective: Through it the Administration expects to be able to discontinue giving direct relief (doles) to the unemployed now on the Federal rolls.

It was observed on all sides that many people who were placed on Federal relief rolls for direct relief rapidly became pauperized. Some of them lost all desire for self-supporting jobs; they lost much of their former independence, self-reliance, and self-respect. In many cases the acceptance of charity from the government did not bring to their cheeks a blush of humiliation, because they came to feel (under the circumstances with some justification) that it was the duty of the government or the public to support them. It is not yet known to what extent the millions of people who became dependent on government doles were made unfit for future usefulness. At present it is not known how many of such people will be employable when real jobs are found for them.

Not only is direct Federal relief likely to be demoralizing to the individuals who receive it, but the unscientific method inaugurated by the FERA of placing all needy persons on the Federal relief rolls, regardless of previous records or employability, tended to corrupt public morals and was a very dangerous policy from the political point of view. It encouraged the use of political pressure on the part of individuals to get on the relief rolls and subjected members of Congress and the Administration to such pressure. It encouraged politicians to use the relief rolls for political advantages.

Certainly under any kind of national unemployment relief policy, the unemployed employable individuals should be separated from the unemployable ones. At first, no such definite distinction was made by the FERA between these two classes.

To furnish jobs or to provide an income for the employable individuals who lost their jobs through no fault of theirs is distinctly a responsibility which the Federal government should assume. Ordinarily, in large measure, if not entirely, state and local governments and the families and communities should assume responsibilities of caring for unemployable individuals, insofar as they are able. Unquestionably, if our industrial system is made to operate so that each employable individual is given an opportunity to provide for himself and his dependents, the care for unemployables should not be an obligation of the Federal government. It becomes an obligation of the Federal government only when industry is disorganized and demoralized so that no other means of support of the unemployable can be found. When all the employable people secure jobs in private industry, or are otherwise provided for, the families, communities, and state and local governments should care for the unemployables, except that the Federal government might be justified in contributing to the support of the aged.

In his new policy of dealing with the unemployment problem the President was correct in insisting that the Federal government assume full responsibility in seeing that employable individuals are given jobs. There are only two ways by which they can be re-employed: First, they may be given employment by having private industry absorb them; and, second, the government may temporarily employ them on public works. As between these two methods of re-employment, the first, of course, is a better solution of the problem. Some of the objections to public works projects as a means of stimulating business and giving employment to the unemployed have been mentioned already. The various economic and fiscal objections to such a policy may be summarized as follows:

A large public works program perpetuates, and even facilitates, an unbalanced industrial situation, when such a program is paid for by public borrowings and an expansion of governmental or bank credit. It creates an artificial current purchasing power for goods which is not derived from current production of goods and services. This artificial income paid out by the government is used to supplement the national income derived from production in the purchase of goods in the

market; this artificial purchasing power stimulates prices, production, private employment and profits, and is thus industrially beneficial while it lasts. But such an expansion of public and bank credit cannot last indefinitely; therefore, a public works program thus supported must come to an end. When it does end not only will those employed directly on the projects be without jobs, but private industry will slump because of the removal of the stimulating effects of the artificial purchasing power injected into industry by the public works expenditures.

A public works program financed with funds received from taxes under a condition of a balanced budget would not facilitate an unbalanced industrial situation, and neither would it stimulate private industry. If a public works program were financed from current revenues, it might be continued indefinitely without upsetting our industrial balance or destroying the credit of the government. Such a policy, however, would be a rather expensive method of furnishing an income to those who are unable to secure employment in private industry. On the average, only about 35 or 40 per cent of the money paid for public projects is paid to laborers as wages; the balance is spent for materials and supervision and administration. Most of those who advocate doles, in preference to public works, as a means of supporting the unemployed do so on the grounds that doles are a much cheaper method of supporting a given number of unemployed people.

After all, it may as well be recognized that those who are employed on public works or on any public job are dependents on the public treasury. In so far as the work done by any public employe is considered as highly desirable and a necessary public service or function, the employment and the compensation received therefor is defensible on the grounds of public payment for necessary public services rendered. On the other hand, if public employment is given for the primary purpose of furnishing jobs to deserving individuals, and not for the purpose of getting a necessary public service rendered, such public employment is not defensible on the grounds of payment for needed public service. Public works programs are, and should be, defensible mainly on the grounds that they furnish jobs for

people who should be employed and who otherwise could not secure employment; of course, a secondary defense for such programs is that the completed public projects render a real service to the public. In short, a program of extensive public works is not a profitable method for society to employ in order to give incomes to a large proportion of its population for a long period of time.

Few, if any, would deny that employment on public works projects is less demoralizing to the individual than is the receipt of doles. On the other hand, most people would agree that, in general, private employment will have a better moral influence on the individual than employment on public projects. This is true particularly if public employment is undertaken primarily for the purpose of furnishing jobs for the unemployed. Certainly, "made work" is positively demoralizing to the workers. To the degree to which employment on public works projects is placed on the same basis as private employment, will it prove less demoralizing to the workers. If the pay in public employment is higher than the pay for the same kind of work in private industry, the effect will not be good on either the workers or private industry. But if the wages paid for public employment are on a mere subsistence level and the employment is made a substitute for doles, the effect on the worker will be discouraging and somewhat degrading.

Because of the great number of people on the relief rolls in the winter of 1934-35, and because private industry was making little or no progress in absorbing the unemployed, there was much defense for the adoption of the second public works program at that time. At least, it should enable the President to clear the relief rolls of the unemployables, and should give jobs instead of straight doles to most of the employable unemployed. However, it must be realized by the Administration and by the people that this public works program is only a temporary plan of dealing with the unemployment problem. It will not solve it. What will the Administration do when the works program ends?

Unless private industry absorbs practically all the employable unemployed while the public works program is in progress, and continues to keep them at work after it ends, the nation

again will be faced with the problem of what to do for the great army of unemployed. It has been pointed out that the theory that public works programs and other recovery measures will result in permanent recovery of business, and in the absorption of the unemployed workers in private industry, is false. Even if the Administration could secure complete recovery of business through its recovery measures, private industry, on its own initiative, would not absorb all the unemployed; it did not do so at the height of the boom in the twenties. To solve this problem the Administration must put into operation a plan which will result in re-employment of the unemployed in private industry; therefore, the adoption of a policy similar to the one embraced in the suggested National Labor Adjustment act is necessary. Unless a policy of reducing work hours and forcing private industry to absorb the unemployed is adopted by the government before the end of the present public works program, it is almost certain that the Administration again will be confronted with a big unemployment problem.

Should the unemployment problem again become acute when the public works program ends, the government will then be faced with three alternatives: First, it may expand the unemployment provisions of the Social Security Act[1] so as to give doles to the unemployed; second, it may provide for still another public works program; and, third, it may provide for a reduction in the hours of workers and force private industry to absorb the unemployed. To accept the first alternative would be a return to doles and an acceptance of the British system of caring for the unemployed. If the second alternative is accepted it would be necessary to pay for the new public works program from current revenues or by the issuance of paper money rather than by additional borrowings. There is extreme danger in further increasing the public debt after the present public works program is finished. Should the third alternative be adopted, it would then be necessary to reduce hours in private industry under business conditions more depressed than they are at present. If hours of laborers in private industry are to be reduced for the purpose of giving jobs to the unemployed,

1 See p. 236.

they should be reduced while the present public works program is in progress.

It is fairly evident that should Congress enact laws along the lines suggested in the proposed Federal Labor Adjustment act, unemployment would not be eliminated within a few weeks or a few months as a result of the act's application. The adjustment of hours should proceed in an orderly manner, starting first with the very largest industries. Probably it would take more than twelve months, and possibly as long as two years, to reduce the hours of laborers in private industry sufficiently to absorb all the jobless workers. In the interim the Federal government should be able to take care of the unemployed by employing them on the public works projects of the present program.

It is generally conceded that economic society must support those who are unable to support themselves. If laborers are not given an opportunity to work and support themselves and families, these families must be supported by public funds. Under a just system of taxation the funds for support of the unemployed must sooner or later come from industry and from those who have large incomes. Since industry in the long run must support the unemployed, would it not be wiser and cheaper for industry to give these people employment, where they could produce goods and services in return for their incomes?

In August, 1935, the President approved the Social Security Act passed by the Congress. This law provides for a Federal-state old age pension system, as well as a plan for the payment of Federal old age insurance annuities. It also makes grants to states for aid to dependent children, as well as grants for maternal and child welfare, and public health work. It creates a national system for Federal-state unemployment compensation payments and provides grants to states for unemployment compensation administration. It is not necessary here to give a detailed description or explanation of the various provisions of this law. Only the old age and unemployment compensation payments provided and their economic consequences are of major importance in providing *economic* security for the individual worker.

The act provides that old age assistance shall be given under

both a Federal-state old age pension plan and a Federal old age insurance compensation plan. In order for states to secure Federal aid in the payment of old age pensions, their pension laws must conform to the standards set down for them in the Social Security Act. State old age pension laws must provide: (1) that the plan will be statewide; (2) that there be financial participation by the state; (3) that a single state agency be set up to administer the plan; (4) that a fair hearing be given individuals whose claims for old age pensions have been denied; (5) that methods of administration satisfactory to the Social Security Board be used; and (6) that the state agency will make such reports as the Board requires. Federal aid will not be given if a state plan imposes, as a condition of eligibility for old age assistance (1) an age requirement of more than sixty-five years after January 1, 1940; (2) any residence requirement which excludes those who have resided in the state five years preceding the application for assistance; and (3) any citizenship requirement which excludes any citizen of the United States.

One-half of the old age pension payments under any state-approved plan will be paid by the Federal government, provided the payments to any eligible individual do not exceed $30 a month. The Federal government will pay an additional 5 per cent of the total pension payments to be used for administration of the state plan. In any state which does not have an approved old age pension law, from July 1, 1935, to July 1, 1937, the Federal government will pay $15 a month to each individual sixty-five years of age or more who is declared by any authorized agency to be entitled to receive the same. This provision was included to give the various states time and opportunity to pass approved old age pension laws.

The Federal old age insurance compensation provision sets up an "Old Age Reserve Account" to provide for the payment of monthly stipends to the eligible aged who on or after January 1, 1942, reach the age of sixty-five. This old age insurance plan is to apply to all employes except agricultural laborers, domestic servants in private homes, casual laborers and Federal, state, and local government employes. Every qualified individual shall be entitled to receive an old age benefit (payable in monthly instalments) of not less than $15 and not more than $85 a

month, depending on the total amount of wages earned by him from December 31, 1936, to the time he reached the age of sixty-five. If any individual dies before he reaches the age of sixty-five, there will be paid to his estate an amount equal to 3.5 per cent of the total wages determined by the Board to have been paid to him with respect to employment after December 31, 1936. No part of the wage received by an individual in excess of three thousand of dollars per annum shall be counted by the Board in computing the total wage. Each individual not qualified to receive monthly payments under this plan after reaching the age of sixty-five, is entitled to receive a lump sum payment of 3.5 per cent of the total wages received by him, as determined by the Board, with respect to employment after December 31, 1936.

In order to secure the funds necessary for enabling the United States Treasury to accumulate the required reserves in the Old Age Reserve Account to pay the stipends of those who reach the age of sixty-five after 1942, both employes and employers are required to pay a Federal tax on wages received and paid. There is levied on every individual a tax equal to the following percentage of the wages (as defined by the act) received by him after December 31, 1936, with respect to employment (as defined by the act): (1) During the calendar years 1937, 1938, and 1939 the rate shall be 1 per cent of the total annual wages; (2) during the years 1940, 1941, and 1942 the rate shall be 1.5 per cent; (3) during the years 1943, 1944, and 1945 the rate shall be 2 per cent; (4) during the years 1946, 1947, and 1948 the rate shall be 2.5 per cent; and (5) after December 31, 1948, the rate shall be 3 per cent. This tax is to be collected by the employer by deducting same from the wages when paid.

Also every employer shall pay a tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined by the act) paid by him after December 31, 1936: (1) During the calendar years 1937, 1938, and 1939 the rate shall be 1 per cent of wages paid; (2) during the years 1940, 1941, and 1942 the rate shall be 1.5 per cent; (3) during the years 1943, 1944, and 1945 the rate shall be 2 per cent; (4) during the years 1946, 1947, and 1948 the rate shall be 2.5

per cent; and (5) after December 31, 1948, the rate shall be 3 per cent. It is estimated that by 1949 the payroll taxes paid by the employes and the employers on account of the old age insurance payment plan will amount to about two billion dollars (6 per cent of the total wages paid).

As the Federal old age insurance payment plan becomes more fully effective, the importance of the Federal-state old age pension plan will decline in size and importance. In other words, the greater the number of aged persons taken care of under the annuity insurance plan the fewer will be the number necessary to care for under the old age pension plan. The psychological and social affects upon the receivers of the payments under the annuity insurance plan will be much better than under the old age pension plan. Half the cost of the annuities will have been paid for by the aged receivers out of their previous earnings; these payments by them will give them the feeling that they are to receive the old age payments from the government as a result of their own efforts. The old age pensions are in reality paid by the government to those who have accumulated nothing and are unable to support themselves; necessarily they have a humiliating influence upon many of the receivers.

The Social Security Act provides a system for Federal-state unemployment payments to the unemployed. For the purpose of assisting the states in the administration of their unemployment compensation laws, the act makes an annual appropriation of forty-nine million dollars to be distributed to states which have approved unemployment compensation laws. In order to be approved by the Social Security Board, the state laws must comply with certain standards such as: (1) the methods of administration must be calculated to insure full payment of unemployment compensation when due; (2) payment of unemployment compensation must be made through public unemployment offices in the state; (3) the law must provide opportunity for fair hearing for individuals whose claims for unemployment compensation are denied; (4) payment of all money received in the unemployment fund of such state must be deposited with the Secretary of the Treasury to the credit of the Unemployment Trust Fund; (5) all money

requisitioned by the state agency from the Unemployment Trust Fund must be spent immediately in payment of unemployment compensation; and (6) the making of such reports as called for by the Board is required. Whenever the state administrative agency fails to comply with the state law the Board may stop payments.

The act further stipulates that no unemployment compensation shall be payable to any individual for time unemployed prior to two years after the first contributions are made to the state unemployment fund. The act also specifies that state unemployment compensation laws shall not deny any otherwise eligible individual compensation for refusing to accept new work (1) which would make him a "strike-breaker"; (2) when the hours and wages are substantially less favorable than those prevailing for similar work in the locality; and (3) when he would be required to join a company union, or refrain from joining or resign from an independent labor organization.

To raise the funds necessary to pay adequate unemployment compensation to the unemployed in the United States, the Social Security Act imposes upon employers a tax on the wages (defined by the act) paid by all employers (of four or more employes) as follows: (1) During the calendar year 1936, the rate is 1 per cent of all wages paid by each employer; (2) during 1937 the rate shall be raised to 2 per cent; and (3) after December 31, 1937, the rate shall be raised to 3 per cent. Employers who pay taxes into a state unemployment fund under a state law, may credit the amount of such state tax against this Federal tax for the same year, provided the total credit allowed an employer on a state unemployment tax does not exceed 90 per cent of the Federal unemployment tax assessed against him. Deduction credit will be allowed taxpayers only for contributions made under state unemployment compensation laws approved by the Social Security Board for the taxable year. It is estimated that this tax will raise about one billion dollars in 1938.

The Social Security Act places no limitations on state governments as to the kind of taxes they may exact to raise revenues for their unemployment funds; however, it is likely that most of them will raise such funds by placing a tax on payrolls

similar to the Federal tax. States which have approved unemployment compensation laws must deposit all unemployment taxes collected by them with the United States Treasury in the Unemployment Trust Fund. The Secretary of the Treasury is directed to pay out of the fund to any authorized state agency such amount as it may duly requisition, not exceeding the amount standing to the account of such state agency at the time of such payment. Should any state fail to pass an unemployment compensation act which imposes state taxes for funds to pay unemployment compensation, that state would have no funds with which to pay unemployment benefits to its unemployed. The Federal government, however, would receive all the unemployment taxes imposed upon employers of that state with respect to unemployment, and presumably would use these funds to relieve an unemployment situation which might arise in that state.

There is no specification laid down in the Social Security Act as to what the Federal government may or may not do with the funds it collects from employers with respect to unemployment. Presumably it may use these funds when collected to pay unemployment benefits *where, when,* and *as* it pleases. Other than specifying that under state unemployment compensation acts, no compensation shall be allowed for unemployment which occurs prior to two years following the collection of the first taxes under such laws, the act places no limits on state unemployment compensation laws with reference to the conditions under which unemployment compensation shall be paid to an individual or the amount of such payments. All such details are left to the state legislatures in framing the respective state laws.

Should unemployment in this country become great, when the present public works program ends in 1937, the unemployment funds collected under the Social Security Act will not be adequate to take care of the unemployed. At that time there will not be large reserves in the Unemployment Trust Fund and in the United States Treasury accumulated as a result of collections from Federal and state unemployment taxes. It is doubtful if large enough reserve funds to provide for the unemployed could be built up in this country to take care of great

and persistent unemployment. Certainly unemployment reserves are not a solution of the unemployment problem; the elimination of unemployment is the only solution.

It seems a sound principle, economically and politically, to tax employers directly to secure funds for taking care of those whose jobs in private industry have been taken from them through no faults of their own. If private business enterprises do not furnish jobs to the jobless, then private industry should support them in idleness. The Federal payroll tax with respect to unemployment is based on this principle. This tax should arouse in our business leaders a definite incentive to decrease unemployment and to solve the unemployment problem in this country. When unemployment is eliminated, the unemployment tax will be unnecessary.

Every American citizen has the right to an opportunity to attain economic security. But the kind of economic security which is most vital is that security which comes from opportunities to earn a good living and provide for family and for old age.

Unfortunately, the possibility of attainment of this kind of economic security by every citizen, under present industrial conditions, does not exist. On the one hand we have permitted the development of special economic privileges and the concentration of a large part of the wealth and income of the nation in the hands of a few. On the other hand we have permitted a large number of our people to be left without jobs and without private incomes. As a result, we have idle factories and reduced national production because the masses of people do not have enough money to buy the goods which our industrial system is capable of producing. The fundamental economic difficulties which stand in the way of national progress and greater economic security are *unemployment* and the *unequal distribution of income in the nation.* We can remove these difficulties only by further reduction in the hours of labor and by increasing the percentage of the national income which goes to the great mass of people and correspondingly decreasing the percentage of it which goes to the few very wealthy.

Old age pensions and unemployment compensation cannot cure these fundamental economic evils. They merely soften the

harsh results of those evils. If we redistributed opportunities to work, created conditions of fair pay for economic services performed by each individual, and eliminated special privileges, within a decade we would have little need for old age pensions, though we might need old age insurance annuities. Necessary economic reforms cannot be brought about immediately. For this reason we must accept old age pensions and unemployment compensation as temporary expedients for giving a more or less humiliating type of economic security to our unfortunate citizens.

The American people want economic security; they demand it. However, most of them demand the kind of economic security which comes from an opportunity to work and to receive full compensation for their part in the production of the national income; they desire to provide for themselves and their families. They will accept the kind of security which comes from doles and pensions only in cases of necessity. The mass of people want economic independence which comes from their own efforts; they believe that the greatest security which can be given them is the opportunity to earn a good living for themselves. We must preserve rugged individualism by doing away with special privileges and distributing economic opportunities among our people; there is no other means through which self-reliance and rugged individualism can be preserved for each. There is no other method by which widespread pauperism can be avoided.

CHAPTER EIGHTEEN

PUBLIC REGULATION OF CORPORATE ACTIVITIES AND RELATIONS

IF IT had not been for the development of the corporate form of business organization our present industrial system would be vastly different from what it actually is today. To a considerable extent the development of our mammoth factory system was made possible by the corporate form of business organization; without such form of business organization, the rapid growth of our giant industrial enterprises would have been an impossibility. It is doubtful that it would have been possible, under any other type of business organization, to bring together the necessary capital funds to develop our industrial system's large plants and giant business enterprises. Modern business enterprises and corporate organization are almost synonymous.

From the beginning, business corporations have been the creatures of state governments rather than of the Federal government. With few exceptions, up to about 1840 each corporation was created by a special legislative act of some one of the state legislatures. About that time the various state legislatures began to enact general corporation laws under which corporate charters might be issued to any group of incorporators who, in making application for the same, complied with the provisions of the general corporation law of the particular state. When the first general corporation laws of the various states were passed their provisions were rather strict in regard to the purposes, capitalization, organization, and operation of the corporations organized under them. At that time few of the corporations were large and most of them

confined their business operations to the states in which they were incorporated.

The expansion of railroad transportation and the development of means of rapid communication, together with the growth of large-scale production, resulted in the development of the immense industrial and other business corporations which transact business in many or all the states of the Union. Notwithstanding the fact that the business of most large industrial enterprises became interstate or even international in scope, the corporation as a legal entity remained a creature of the state in which it was incorporated. As the business of corporations grew in volume and scope, there was a strong demand on the part of big business men for "liberalization" of the state corporation laws.

In compliance with this demand, the corporation laws of the various states were revised so as to give more privileges and liberties to incorporators in reference to the purposes for which corporations might be organized, the character of their capital structure, operation, and control, as well as to their inter-relationships. It was the desire of many state governments to induce large corporations to take out charters under their laws in order to get the incorporation and annual fees which would be paid the states as a result of such incorporations. Consequently, competition between certain state legislatures in liberalizing their respective corporation laws was destructive of practically all serious effort on the part of the various state governments to regulate or control the organization, capitalization, financial and business operations of the corporations they created. Under the "liberalized" state corporation laws, promoters, organizers, and operators of corporations were left with practically a free hand to create, capitalize, and operate their corporations as they saw fit.

The giant business and industrial corporations of today do a very small part of their total business in the states in which they are incorporated. Many of them are incorporated in the states of Maine, Delaware, and New Jersey, two of which are very small states. Evidently it makes little difference to the people of these states how the large corporations created under their state governments are organized, capitalized, or operated.

ized by those already heavily financially interested in the corporation securities affected by the pooling operations.

The growth of mammoth unregulated industrial combines was the principal cause for the development of extensive monopolistic restraints of trade in this country. Without the development of the corporate form of organization, vast industrial enterprises would have been impossible; without the creation of the holding company, the giant industrial combines could not have been brought about. The increase in the size of industrial enterprises in our major industries decreased the number of competitors in each industry, and made it easy to arrive at agreements on restraints of trade. Through the large holding companies and mergers the principal competitors in each of several industries were combined into large monopolistic "trusts." These holding companies and trusts remained as creatures of the states which gave them legal life, though their business and financial operations are national and international in scope. The heart of the "trust" problem is the acquisition of shares of stock of corporations by other corporations.

In 1890 the Congress passed the Sherman Antitrust Act to prohibit monopolies and monopolistic activities, and to make unlawful activities in restraint of interstate commerce. This act was not effective in accomplishing its objectives because both monopolistic combines and restraints of trade have increased greatly since its passage. Its failure has been due in part to the fact that the Federal government has attempted to enforce the provisions of the act without having control over the principal instrument—the corporation—through which are brought about monopolies and a large part of the restraints of trade.

In brief, the development of giant unregulated industrial and business corporations produced *three* serious national economic problems; First, the manipulation of the finances and securities of corporations by promoters and "insiders" to their personal interest; second, the development of "sharp" practices in the security exchanges where corporate securities are bought and sold, practices which result in injurious speculation and undue use of bank credit; and third, the growth of monopolies and restraints of trade through large corporations, holding com-

panies, and mergers. All three of these evils have facilitated the rapid concentration of a large part of the wealth and income of the nation in the hands of a few people. The Roosevelt Administration enacted legislation to deal with two of these problems by the passage of the Securities Act of 1933 and the Securities Exchange Act of 1934. Other than the Public Utility Act of 1935, no legislation has been enacted to deal with the problem of monopoly and restraint of trade through holding companies.

In order to provide full and fair disclosure of the character of the new securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in their sale, the Securities Act of 1933 was passed. This act provides that no security shall be offered for sale by an issuer (except those specifically exempted by the act) until a registration statement in reference to the security has been approved by the Securities and Exchange Commission. The act states that any security may be registered with the Commission under the terms and conditions provided by the act by filing a registration statement in triplicate, properly signed and authenticated. The required registration statement (when relating to a security other than one issued by a foreign government) shall contain the detailed information and be accompanied by the various documents specified by the act in Schedule A.

The law provides that the prospectus of a corporation security shall contain the same statements as those made in the registration statement filed with the Commission, except that it need not contain the documents required as a part of the registration statement. Under the law, if it appears to the Commission that a registration statement is on its face incomplete or inaccurate in any material respect, the Commission may, after due notice, issue an order refusing to permit such registration to become effective until it has been amended in accordance with such order. Or, the Commission may issue a stop order against a registration statement previously approved if it later discovers misrepresentation of facts in such registration statement. All orders of the Commission are subject to review by the Federal courts.

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Penalties are provided for those who wilfully make misstatement of facts in registration statements, by making them liable to those who may lose as a result of such misrepresentation. The act also provides for the registration with the Commission of foreign government securities to be sold in this country.

The object of the Securities Act is to force corporate officials and other individuals who issue new securities and offer them for sale to the public to give detailed and accurate information concerning the financial status and business of the issues and the rights and equities which the security, will give the purchasers. The act does not give the Commission the power to prevent the issuance of a proposed security on the grounds that it would be a bad investment for a purchaser, or that the issuer is acting unwisely in issuing it. The purpose of the act merely is to protect prospective purchasers of new securities against perpetrated fraud and misrepresentation of facts by the issuers. The Commission may prevent the issuance of a new security only when the issuer fails or refuses to disclose the facts which the act requires them to give to the Commission and to the public in order to get approval for sale.

The provisions of the Securities Act do not prohibit inside manipulation of corporate securities by the issuance of stock dividends, stock bonuses and the exchange of one type of corporate security for another between a corporation and its stockholders or between corporations. The act is not designed to prevent overcapitalization of corporations, such as the issuance of securities for services and for good-will, or the payment of stock dividends and stock bonuses, or the swapping of bonds for shares of stock; it is not designed to prevent holding companies from acquiring the shares of stocks of other corporations. In no material way does the act give the Commission control over the organization, reorganization, or capitalization of corporations. Insofar as this act is concerned, corporations are left as creatures of the several states subject only to the loose provisions of the state corporation laws in reference to their organization and operations, except that they must disclose the facts in reference to new securities they offer for sale to the public.

The Securities Exchange Act of 1934 was passed to provide

for Federal regulation of securities exchanges and to prevent inequitable and unfair practices on such exchanges. The necessity for such regulation has been indicated already. This act makes it unlawful for any broker, dealer, or exchange to use the mails or any means of interstate commerce to effect any transaction in a security, or to report any such transaction, unless such exchange is registered as a national securities exchange under the act, or is exempted from such registration by the Securities and Exchange Commission. Any exchange may be registered with the Commission by filing a registration statement in such form as the Commission may prescribe, containing the agreements and setting forth the information and accompanied by the documents specified by the act as required for registration.

Also, all securities dealt in on the exchanges must be registered with the Commission. In order to obtain registration for a security, the issuer of the same must file an application with the Commission containing detailed information in reference to the financial and business record of the issuer, how, why, and under what conditions the security was issued and other information required by the act and the rules of the Commission.

The act contains detailed provisions designed to prevent manipulation of security prices on the exchange and to regulate the use of manipulative and deceptive devices. It is declared unlawful for any person or any member of a national securities exchange to create a false or misleading appearance of active trading in or market for a security by (1) effecting transactions in it which involve no change in the ownership thereof, and (2) entering orders for the purchase or sale of the security with knowledge that orders of substantially the same size and price for the sale or purchase of same have been or will be entered. Those dealing in a security are prohibited from the circulation of information or reports that the security will or is likely to rise or fall because of market operations of one or more persons in the security. It is declared to be unlawful for dealers or brokers or other persons to make false or misleading statements in reference to any security for the purpose of inducing people to buy or sell the same. The act contains detailed regulatory provisions in reference to transactions which are designated

as "puts," "calls," "straddles," "options," and "privileges." Short sales and stop-loss orders also are made subject to regulation by the Commission.

Any person who wilfully participates in any act in violation of the provisions of the law regulating transactions on the securities exchanges shall be liable to any person who shall purchase or sell any security at a price which was affected by such act. The person so injured may sue in law or in equity, in any court of competent jurisdiction, to recover the damages sustained as a result of such act. Also, issuers of securities are made liable to those who may lose as a result of false or misleading statements made in the applications for registration of securities.

For the purpose of preventing excessive use of bank credit in the purchase or carrying of securities, the act provides that the Federal Reserve Board shall prescribe rules and regulations with respect to the amount of credit that may be extended on any security registered on a national securities exchange. All banks lending on stock exchange securities must file with the Federal Reserve Board an agreement to comply with its rulings in reference to such loans, and all members of such exchanges and all brokers and dealers who transact business through the exchanges are permitted to borrow only from the banks which have filed such agreements with the Board.

The Commission has the power to examine all books and records of brokers and dealers and to require them to make reports to the Commission in reference to their transactions. Also, every issuer of a security registered on a national securities exchange must file with the exchange and with the Commission current reports as required by the rules of the Commission. All large stockholders, directors, and officers of corporations having registered securities on any exchange must file with the exchange and with the Commission information in reference to their current transactions in buying and selling the securities of those corporations.

The provisions of the Securities Exchange Act are sufficiently rigid and definite to prevent manipulation of, and undue speculation in, securities listed on the exchanges. The effectiveness

of the act will depend largely upon its administration by the Securities and Exchange Commission.

The Public Utility Act of 1935 is generally referred to as the Utility Holding Company Act. Title I of this act provides for the elimination of useless holding companies and for minute regulation of those which are not eliminated in the electrical and gas industries. The major provisions in reference to the regulation, reorganization, and dissolution of holding companies are as follows:

1. All public utilities holding companies and subsidiaries must be "registered" with the Securities and Exchange Commission.

2. The Securities and Exchange Commission is directed to take such action as is necessary to limit the operation of holding companies to a single integrated utility system, with certain exceptions. For example, a registered holding company may continue control of additional systems which cannot be operated economically as independent systems; or holding companies may be permitted to control additional systems which are situated in one state or adjoining states if deemed advisable by the Commission.

3. Holding companies that are permitted to remain in existence are not to be allowed to make profits from the operating companies. Service companies set up to provide engineering and other services may be formed but they are not to be permitted to make profits from the operating companies by charging them exorbitant prices for such services.

The act also requires all gas and electric holding companies and subsidiaries to furnish to the Securities and Exchange Commission detailed information in reference to their desire to issue new securities or to purchase or deal in any securities. This information is in the form of a "declaration" which must be approved by the Commission before the securities are issued, exchanged, or purchased. Detailed regulatory provisions are contained in the act as to requirements the new securities must meet and the purposes for which they may be issued. The acquisition of new property or interest in other companies by either holding companies or their subsidiaries is subject to strict regulation by provisions of the act; the acquisition of both

securities and capital assets by them is subject to approval by the Commission.

Title II of the act deals with the sale and transmission of gas and electricity by operating companies with particular reference to co-ordinating the services of the private utilities with the Tennessee Valley Authority service.

According to the act, public utility holding companies are affected with a national public interest because (1) the securities of such holding companies are widely marketed and distributed by use of the mails and instrumentalities of interstate commerce. (2) Their service, sales, construction, and other contracts and arrangements are likewise performed. (3) Their subsidiary public utility companies sell and transport gas and electric energy in interstate commerce. (4) Their practices in respect of, and control over subsidiary companies materially affect the interstate commerce in which those companies engage. (5) Their activities extending over many states are not susceptible of effective control by any state and make difficult, if not impossible, effective state regulation of public utility companies.

In the report of the Senate Committee on Interstate Commerce recommending the Public Utility Bill for passage, the conditions which necessitate Federal control over public utility holding companies are given as follows:

> "(1) The securities of such public utility holding companies, subsidiary companies, and affiliates are sold to a large number of investors in different states; (2) such investors cannot obtain the information necessary to appraise the financial position or earning power of such issuers because of the absence of uniform standard accounts; (3) such securities are frequently issued without the approval or consent of the states having jurisdiction over subsidiary public utility companies; (4) such securities are often issued upon the basis of fictitious asset values and of paper profits from intercompany transactions and do not accurately reflect the sums invested in underlying public utility properties; (5) such securities are often issued in anticipation of excessive revenues from subsidiaries which if realized would burden consumers,

and the failure to realize such revenues, because of state regulation of subsidiary public utility companies, results in loss to investors who have been led to believe that such revenues are a legitimate part of the issuer's income; (6) such securities, when improvidently, issued, subject subsidiary public utility companies to the burden of supporting an overcapitalized superstructure to the detriment of investors and consumers and tend to prevent voluntary ra e reductions, which over a period of time might promote a greater and more economic use of gas and electric energy and thereby srengthen subsidiary public utility companies; (7) subsidiary public utility companies are often subjected to excessive charges for services, construction work equipment, and materials, to the detriment of investors and consumers; (8) subsidiary public utility companies often enter into transactions with affiliates in which the absence of arm's-length bargaining operates to the detriment of investors and consumers; (9) control of subsidiary public utility companies throughout the United States has often been used to secure to holding companies, their affiliates, and subsidiary construction companies construction work for public utility companies in restraint of free and independent competition in that field; (10) service, management, construction, and other contracts involve the allocation of charges among subsidiary public utility companies in different states and present problems of regulation which cannot be dealt with effectively by the states without the assistance of the Federal government; (11) control of subsidiary public utility companies materially affects the accounting practices and rate, dividend, and other policies of such companies, thereby in many instances complicating and obstructing state regulation of such subsidiary companies; (12) the growth and extension of holding companies in some cases have borne no relation to the economies of management and operation or to the integration and co-ordination of related properties but have been influenced by a desire for economic power and security profits and have tended toward the concentration and monopolization in a few holding company systems of control of gas and electric utility companies to the detriment of inves-

tors, consumers, and the general public; (13) the abuses above enumerated are so commonly associated with the activities of many public utility holding companies, have been so persistent and so widespread that they necessitate legislation to control the holding company and eliminate it as an artificial corporate device inherently injurious to investors, consumers, and the general public, except where it is useful and necessary for the operations of a geographically and economically public utility system."

All that may be said as to why public utility holding companies are affected with a national public interest will apply with equal or greater force to industrial holding companies and to all large industrial corporations and their allied and affiliated companies. Also, practically every reason given by the Public Utility Act why public control over the activities of utility holding companies is necessary, could, with equal justification, be given as reasons public control over industrial holding companies, mergers, and their affiliates is needed to protect the interest of investors and the public. The tycoons of the public utility combines merely copied the tactics of the promoters and operators of large industrial combines in manipulating the securities and the finances of those combines and in securing monopolistic control in the major industries. Surely monopolistic control, through holding companies and mergers in the industrial field, more vitally affects public welfare than does monopolistic control in the public utilities. The gas and electric utilities absorb not more than 10 per cent of the national money income; the mining and manufacturing industries absorb more than five times as much of it. Theoretically, rates of utilities are regulated by state regulatory bodies.

It might be argued that industrial combines are already regulated or controlled by the Federal government through the Securities Act and the antitrust acts. But actually neither the Securities Act nor the antitrust acts have been or will be effective in getting at the heart of our national problems in reference to the financial and business activities of large industrial combines. It is generally conceded that the antitrust acts did not stop the growth of large monopolistic industrial com-

binations or prevent increasing restraints of trade in interstate commerce. Insofar as the antitrust acts have been applied as remedies, they were applied after the monopolistic combines were perfected rather than before or at the time of their organization. The Securities Act was not designed to prevent those in control of corporations from issuing watered stock, stock bonuses, or any other kind of securities permitted under the state corporation laws; neither was it designed to prohibit corporations from acquiring the stock or property of others or effecting any kind of corporate relationships. It was intended merely to force issuers of securities to tell the public the truth and the whole truth about those securities.

We need Federal legislation which will break up many of the large industrial combines and prevent the formation of any such combines in the future. This legislation should be designed also to prevent the manipulation of the finances and securities of corporations by insiders. Watered stock, stock bonuses, and stock dividends should be prohibited. Through Federal incorporation of all business enterprises doing business in interstate commerce, all these desirable objectives could be accomplished with a reasonable degree of effectiveness. Therefore, a federal corporation law should be enacted, which should contain the following chief provisions:

No Federal corporation should be allowed to own stock in any other corporation, or an interest in a local unincorporated enterprise, unless it can be shown conclusively that such ownership is for the public welfare. All corporations that are federalized should be compelled to comply with this provision within a reasonable period of time. No corporation should be allowed to acquire any of the capital assets of any other corporation or of any business enterprise without the specific consent of the Commission, consent to be given when it is shown that such ownership is in the interest of public welfare. The act should prohibit the holding or ownership of any of the voting shares of stock of a federal corporation by any holding company or security trust created under state laws. In this Federal system of corporations there should be no place for either Federal or state security holding companies which merely hold the securities of operating companies.

The federal corporation act should provide that all shares of stock issued by corporations shall have a stated par value for each share, and that no corporation shall be permitted to issue more than two classes of stock. No corporation should be permitted to issue non-voting shares of stock and bonds of a total par value greater than the total par value of the voting shares issued. No corporation should be permitted to issue any security or obligation for personal or professional services; neither should any security be issued in payment for intangible property (good-will, trade-marks, brands, lists of customers, etc.) which cannot be proven to have a true value at least equal to the true value of the securities exchanged for such intangible property. The same rule in regard to true value should apply to the exchange of securities for tangible property. No stock dividends or stock bonuses should be permitted. No corporation should be permitted to issue any new security without the specific consent of the Commission, which before it gives consent must satisfy itself that the equitable interest of all security holders will be protected adequately as a result of the issuance of the security.

In my opinion, only through Federal incorporation of corporations, or through a strict Federal corporation license system, can be stopped the growth of monopolistic combines in industry, and the overcapitalization and inside financial manipulations of corporate securities. To argue that such legislation would be an infringement on "states' rights" by the Federal government, is little short of ridiculous. The business of the large corporation is interstate, and the enterprises which carry on this interstate business should be creatures of the Federal government. The Federal government unquestionably has the power under the interstate commerce clause of the Constitution to regulate the form and the character of the business enterprise which engages in interstate commerce. It is clear to all students of corporation problems that the various state governments have failed to control, in the interest of the public, the giant corporations which they created.

CHAPTER NINETEEN

GOVERNMENTAL POLICIES AND OUR ECONOMIC FUTURE

THE nation should stop looking for a return of the predepression prosperity or the predepression price level. Even if it were possible for business to return temporarily to the boom conditions of 1928, such conditions would not be beneficial and could last only for a short period. The price level of 1928 was a product of the business situation of that time, and there is no sound economic reason why we should attempt to return to that price level under the greatly changed business conditions of today. Business conditions prior to the depression of 1929 were highly undesirable and they should not be looked upon as a normal state which industry and business should aspire to regain.

The government, business leaders, and the public should accept the business situation and the business conditions of today as a starting point for initiating changes in our industrial system which will lay a basis for permanent security and prosperity for all in the future. Such a policy would be much sounder than trying to bring about a lopsided boom condition of prosperity which would soon end in a crash. Under conditions which prevail today, it would be less difficult to initiate the necessary changes in the operation of our industrial system and bring about an economic equilibrium than it would be under conditions similar to those which prevailed in 1926-28. As a matter of fact, the business situation today (in terms of the history of business for the past one hundred years) is nearer a *normal* (the average) than was the situation in 1928. But the people do not desire *normal* business conditions in terms of those which have prevailed in the past, because such "normal"

conditions have not been most desirable or beneficial for the masses of the people; they want a lasting industrial prosperity in which all will share; an industrial equilibrium in which all who contribute to production will share in the fruits of continuous and full productive activity.

Under modern conditions of mass production with automatic machinery, the so-called natural economic laws do not operate to maintain an industrial balance. Ordinarily, and particularly during boom periods, the so-called natural economic laws permit too large a proportion of the national money income (derived from net production) to go to money-lenders and profit seekers, and too small a proportion to small income receivers, farmers, and laborers. As a result of this lopsided division, two conditions develop: a shortage of consumers' purchasing power, and a relative surplus of productive capacity (capital investment) in industry. Because of this maldistribution of the national money income among those who furnish the factors of production, the country too frequently suffers from destructive depressions, as it has suffered since 1929. Displacement of laborers, resulting from standardized productive methods by automatic machinery, developed technological unemployment in the midst of the 1922-29 boom. Because of their weak bargaining power, compared with the strong bargaining power of the employing corporations, laborers were not able to secure a reduction in their work hours as a result of the increase in production per laborer. Under the present methods of production and the present methods of distributing the national money income, the operation of the so-called natural economic laws cannot be depended upon either to eliminate unemployment or to give to the mass of consumers adequate purchasing power with which to buy the goods industry can produce.

Therefore, to remedy the fundamentally bad features of the operation of our industrial system, the Federal government must exercise more regulation and control than heretofore over the distribution of the national money income (or the division of the proceeds of production) and over the weekly hours of laborers. This control should prevent the overcapitalizing of business enterprises and should influence interest, profit, and wage rates in such a manner as to give laborers and other

small income receivers a relatively larger percentage of the national income; this control should break up the largest estates and radically reduce the very large personal incomes.

Theoretically, unemployment might be eliminated either by increasing the amount of work (or industrial activity) to absorb the available labor supply at the prevailing hours of work per week for laborers, or by reducing the weekly hours of laborers so as to absorb the unemployed regardless of an increase in the amount of work (or of industrial activity). It is my opinion that, at least for the present, we shall not be able to absorb all or a large part of the unemployed by artificially increasing industrial activity. We shall be able to make more immediate progress in solving this problem in the near future by reducing the hours of work per week for all industrial laborers.

Because of the 1929 business depression, industrial activity is still at a low ebb. Business and industry are slowly recovering from the depression, though the recovery is not on an entirely sound basis. The volume of production of the industries producing consumption goods should be increased to full capacity and then there should be further expansion of those industries. The capital goods industries should be expanded, but only as their products are needed by the expanding consumption goods industries. Such a business recovery can come about only as consumers' purchasing power is increased enough to enable them to buy the goods of the expanding consumers' goods industries. To the extent to which many of the present recovery measures of the Federal Administration actually stimulate business activity, they do not stimulate it in a manner to bring about permanent recovery. In my opinion, the Administration should stop trying to force business recovery either by artificially raising the price level, or by carrying out a large public works program, or by permitting industry to agree on prices and on limitation of production. None of these methods could possibly bring about a sound recovery of business. The stimulating effects of such recovery measures can be temporary only; each of them tends to amplify the undesirable features of operation in our industrial system.

As a consequence of these analyses of our present national economic difficulties and of this study of the so-called New

Deal legislation, it is my opinion that the New Deal program should be revamped somewhat as follows:

1. Discontinue all governmental efforts to raise the general price level. Accept the prevailing price level as a basis for recovery and reconstruction of business and industry. Do not decrease further the gold content of the dollar or expand the silver purchase policy. Above all, do not issue Treasury notes or other paper money. Discontinue the policy of trying artificially to force an expansion of bank credit, but offer reasonable credit facilities through the banks and the government's financial agencies.

2. Continue to encourage the readjustment or refinancing of old debts of farmers, home-owners, railroads, local governments, and of distressed business enterprises. The principal of these debts in many cases should be reduced greatly and the interest rates on them should be cut drastically, so as to reduce materially the annual debt charges on these debtors. Through the regulation of banks and the control over the government's financial agencies the Administration should keep the current rate of interest for new loans at a low level.

3. At the end of the present public works program, the policy of trying to revive business through a large public works program must be discontinued; also the policy of attempting to apply artificial stimulation to private construction and to the heavy goods industries should be stopped. A public works program increases the public debt rapidly and furnishes to business only a temporary artificial stimulation which cannot contribute to permanent recovery. Also, artificial stimulation of private construction will further lower the value of existing buildings; such stimulation likely would result in overbuilding many communities, and might result in considerable financial losses to the government through the guarantee of the mortgages. The heavy goods industries should be permitted to revive only as there is an actual demand for their goods on the part of solvent expanding business enterprises. It should be remembered that relative to the national money income and to the volume of trade of the consumption goods industries, the so-called heavy goods industries were greatly overexpanded from 1915 to 1929.

4. Amend the Agricultural Adjustment Act, with its provi-

sions for processing taxes and non-production payments, by giving the government the power to allot to each farmer the maximum quantity of each major agricultural product he may be permitted to produce and sell each year; the act should provide heavy penalties for those who exceed their production allotment. Also, continue and enlarge the Administration's program of purchasing submarginal agricultural lands and taking them out of cultivation. The farmers should reduce production in their own interest; in the future they should not be paid to do it, but penalized if they refuse. The submarginal farms should be taken out of cultivation because they are an injury to the agricultural industry as well as a detriment to those who cultivate them.[1]

5. Prohibit any agreements by industries through trade associations or otherwise in reference to prices or volume of production. Enforce the antitrust acts against monopolistic activities and restraints of trade. In addition to the National Labor Relations Act, the Congress should enact two additional laws to take the place of the National Industrial Recovery Act as follows:

(*a*) A Federal trade adjustment act should be enacted to provide for a limited amount of self-regulation of *trade practices* through codes of fair trade practices. All industries should be prohibited from exercising any control whatever over price competition and production through these codes. The provisions which these codes may contain should be stated specifically in the act, which should also provide for the Federal Trade Commission to administer its provisions and to supervise the making and enforcement of voluntary trade practice codes. There should be adequate provision in the law for preventing all kinds of restraints of trade and monopolistic practices, and it should state the code provisions shall not be in violation of any portion of the antitrust laws, which shall be rigidly enforced.

(*b*) A Federal labor adjustment act should be passed to regulate hours and wages of laborers employed in industries engaged in interstate commerce. A Federal Labor Adjustment

1 Much of the land in the Middle West is being ruined for future generations through cultivation when it should never have been plowed. For a brilliant discussion of this vital aspect of the land problem, see *Deserts on the March* by Paul B. Sears (University of Oklahoma Press, 1935).

Board should enforce all its provisions. The act should prohibit employment of laborers in such industries for more than thirty hours per week without specific permission from the Labor Adjustment Board. It should prohibit the employment of laborers in these industries at wage rates which are found by the Board to be unfairly and unjustly low. All orders of the Labor Adjustment Board should be subject to review by the Federal courts, and should be enforceable through the courts when found in accord with the provisions of the act and the facts in each case. Through the administration of the provisions of this act, private industry should be forced to absorb all employable unemployed laborers.

6. The unscientific system of giving direct Federal relief to the unemployed through the FERA should be abolished. Whatever Financial unemployment relief is given should be on a scientific basis. Except through pension systems, no Federal aid should be given to unemployable persons. In so far as practicable, Federal aid to employable jobless persons should be given by furnishing employment; it is much more desirable that this employment be in private industry than in public works projects. When the jobless cannot be given jobs of any kind they should receive adequate unemployment compensation paid for by taxes on industry. Such unemployment taxes on business enterprises should encourage employers voluntarily to reduce hours of laborers enough to absorb the unemployed. The provisions for old age annuities and unemployment compensation contained in the Social Security Act are defensible, though it is to be hoped that unemployment compensation payments in the near future will become unnecessary because of the disappearance of unemployment in this country. Through the employment offices in the various states, giving aid to the unemployed and re-employing the jobless in private industry should be tied together. Hours should be shortened and jobs in private industry should be found for those on public works and unemployment compensation rolls.

7. The Securities Act, the Securities Exchange Act, and the Public Utility Act should be supplemented by the passage of a law providing for Federal incorporation of all corporations doing an interstate business. This act should eliminate all

sions for processing taxes and non-production payments, by giving the government the power to allot to each farmer the maximum quantity of each major agricultural product he may be permitted to produce and sell each year; the act should provide heavy penalties for those who exceed their production allotment. Also, continue and enlarge the Administration's program of purchasing submarginal agricultural lands and taking them out of cultivation. The farmers should reduce production in their own interest; in the future they should not be paid to do it, but penalized if they refuse. The submarginal farms should be taken out of cultivation because they are an injury to the agricultural industry as well as a detriment to those who cultivate them.[1]

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able time will result in a permanent business recovery. Such a recovery would develop slowly but it would be on a sound basis. There would be a gradual revival of the so-called heavy goods industries as their products are needed by the expanding consumption goods and service industries. As the consumption goods industries expanded they would demand more raw material and more capital equipment. The heavy goods industries would be called upon to supply these raw materials and capital equipment. As the heavy goods industries revived, along with the capital equipment industries, there would be an expansion of bank credit to take care of the increasing volume of business and production. The building trades would then expand naturally as a result of the actual demand for more business and industrial construction. With an increase in the real income of small income receivers, resulting from this kind of business revival, there would be a great increase in the market demand for better homes.

The Federal government should exercise whatever regulatory powers necessary to bring about an equilibrium in the operation of our industrial system. Such regulatory measures would involve regulation of hours and wages of laborers in the major industries; control over the financial and business activities of large corporations; control over agricultural, oil, and coal production; and a taxation system which would eventually break up the great estates and personal incomes. We are told by the defenders of the special interests that such regulatory measures are unconstitutional. It is believed, however, that by a reasonably liberal interpretation of the provisions of the Constitution they may be declared to be constitutional. Anyway, they should be passed by the Congress, and if the Supreme Court declares them unconstitutional, the Constitution should be amended so that such regulatory measures will be constitutional.

Standpatters and conservatives tell us that to permit the Federal government to exercise extensive regulatory power over big business, would infringe upon individual rights and liberties and would tend to break down individual initiative and rugged individualism. They neglect to tell us that the individual initiative and rugged individualism of a large part of our people

in business and in industry have been crushed already by the few who dominate our big industries. The primary object of the proposed government regulatory measures is to restore to all an opportunity to exercise individual initiative. They tell us also that "property rights" would be taken away by such a governmental regulatory policy. How would our personal and property rights and our liberties be affected by such regulatory measures?

We all agree that the Federal government was created to safeguard our individual rights and liberties. It is generally agreed also that liberty unrestrained by law is mere license for the economically powerful. Each must be forced by the government to respect the economic rights and liberties of others. Few do not recognize the fact that ownership of great wealth and control of industry by a small percentage of people under a laissez-faire economic policy gives those people great power over the lives and destinies of the majority of our citizens. The question is: Shall we permit the economically powerful to exercise those powers under the guise of individual rights and liberty, freedom of contract, and property rights? When the use of the economic power by those who control industry is unrestrained, the economic rights and liberties of the average citizen are crushed. It is the supreme duty of the government to prevent any individual or any class of individuals from destroying the rights and liberties of others.

There is much discussion of the question of "property rights" *versus* "human rights." There is no such thing as property rights separate and apart from human or individual rights. The right to own, hold, and use property is a right which is accorded to the individual, and is one of the important human rights. The use of property by individuals or groups of individuals should be free and unrestrained in freedom of contract so long as the use thereof does not restrain or injure the personal rights of others. On the other hand, when property is used by individuals to injure others or to limit their personal rights, such uses should be prohibited by the Government. Attributing artificial personality to inanimate property and then assigning "rights" to it as an artificial being are ridiculous. Such a concept originated as a result of corpo-

ration laws attributing artificial personality to the corporation with certain "rights" and "obligations" as a legal entity, separate and distinct from the personal rights and obligations of the individual owners or stock-holders. The "rights" given the corporation were derived from the "rights" of the stock-holders acting in unison, but in no case should the corporation rights be as great as the personal rights of the stockholders who own it. There should be no conflict between property rights and human rights, for in reality there are no property rights apart from the human rights of the owner to use his property within the law.

The staunch conservatives love to tell us that the Constitution, as it now stands, is the Ark of Covenant of our liberties, and that to change it and give the Federal government more power of regulation or control over industry would destroy our individual liberties. They argue that as the government acquires more power, individuals' liberties are curtailed. May we ask: What recognized individual liberty would be curtailed by the exercise of power by the government to regulate big business? It is true that the individual and group power and license of a small minority to interfere with and impose upon the economic rights and liberties of others would be curtailed by the exercise of such governmental power. But the exercise of such power by the government would not reduce individual liberty; by destroying special privileges and licenses it would increase individual liberty.

Should our Constitution be changed so as to grant the Federal government unlimited power to regulate industry, does anyone assume that such power would be exercised against the interest or in opposition to the will of the majority of the people? We elect a House of Representatives every two years, one-third of the Senate every two years, and a President every four years. Suppose the Federal government should attempt to exercise control over industry and business contrary to the wishes of the majority of the people, how long would such an administration stay in power? Why should we be afraid to give our government desirable and adequate powers to protect our economic liberties? Do we not control our government? Why should we fear that which we control?

APPENDICES

APPENDIX A

TABLE I

RESERVE BANK CREDIT OUTSTANDING
1918-1933
AVERAGE OF DAILY FIGURES
(In millions of dollars)

YEAR	BILLS DISCOUNTED	BILLS BOUGHT	UNITED STATES GOVERNMENT SECURITIES	OTHER RESERVE CREDIT[1]	TOTAL
1918	1,134	287	134	168	1,723
1919	1,906	324	254	141	2,625
1920	2,523	385	324	158	3,390
1921	1,797	91	264	46	2,198
1922	571	159	455	41	1,226
1923	736	227	186	56	1,205
1924	372	172	402	50	996
1925	481	287	359	68	1,195
1926	568	281	350	59	1,258
1927	442	263	417	53	1,175
1928	840	328	297	40	1,505
1929	951	241	208	59	1,459
1930	272	213	564	38	1,087
1931	326	245	669	34	1,274
1932	521	71	1,461	24	2,077
1933	283	83	2,052	11	2,429

[1] Includes government overdrafts in 1918, 1919 and 1920.

Source: *Annual Report of the Federal Reserve Board* for the year 1933, Table I, p. 71.

TABLE II

DEPOSITS, RESERVES, NOTE CIRCULATION AND REVENUE PERCENTAGES OF FEDERAL RESERVE BANKS
Average of daily figures for month of June each year
(In millions of dollars)

YEAR	TOTAL DEPOSITS	FEDERAL RESERVE NOTES	CASH RESERVE		RESERVE PERCENTAGE
			Total	Excess	
1917	1,108	492	1,133	549	70.8
1918	1,792	1,661	1,983	691	57.4
1919	1,941	2,501	2,248	569	50.6
1920	1,975	3,114	2,103	166	41.3
1921	1,723	2,683	2,606	930	59.1
1922	1,883	2,138	3,136	1,619	77.8
1923	1,931	2,247	3,204	1,630	76.7
1924	2,065	1,871	3,247	1,776	82.5
1925	2,209	1,660	2,953	1,516	76.3
1926	2,241	1,703	2,976	1,510	75.4
1927	2,355	1,718	3,170	1,658	77.8
1928	2,395	1,618	2,728	1,243	68.0
1929	2,374	1,667	3,011	1,513	74.5
1930	2,458	1,441	3,213	1,776	82.4
1931	2,483	1,656	3,490	1,959	84.3
1932	2,166	2,630	2,799	989	58.4
1933	2,457	3,128	3,814	....	68.3
1934	4,131	3,072	5,008	....	69.5

Source: *Annual Reports of the Federal Reserve Board* for 1928, Table II, p. 50; and 1932, Table VIII, p. 52, and *Federal Reserve Bulletin*, July, 1934, p. 493.

TABLE III

LOANS AND INVESTMENTS OF COMMERCIAL BANKS
Classified as to Member and Non-Member Banks
On or about June 30, each year, 1913 to 1934
(In millions of dollars)

YEAR	ALL BANKS	MEMBER BANKS	NON-MEMBER BANKS
1913	16,063	.....	.....
1914	16,902	.....	.....
1915	17,559	8,764	8,795
1916	20,478	10,315	10,163
1917	24,119	12,453	11,666
1918	27,725	18,507	9,218
1919	32,251	22,240	10,011
1920	36,845	25,559	11,286
1921	34,356	24,121	10,235
1922	34,251	24,182	10,069
1923	37,374	26 507	10,767
1924	38,549	27,167	11,382
1925	41,598	29,518	12,080
1926	43,836	31,184	12,652
1927	45,981	32,756	13,225
1928	49,102	35,061	14,041
1929	49,205	35,711	13,494
1930	48,686	35,656	13,030
1931	44,744	33,923	10,821
1932	35 978	28,001	7,977
1933	30,274	24,786	5,488
1934	32,860	27,175	5,785

Compiled from *Reports of Comptroller of the Currency* and *Annual Reports of Federal Reserve Board.*

TABLE IV

FARM MORTGAGE DEBT IN THE UNITED STATES
(In billion dollars)

YEAR	FARM MORTGAGE DEBT
1910	3,320
1920	7,858
1925	9,361
1928	9,469
1930	9,241

Source: Bureau of Agricultural Economics.

TABLE V

Construction Contracts Awarded

Year	In 27 states		In 37 states[1]	
	Number of projects (thousands)	Value (millions of dollars)	Number of projects (thousands)	Value (millions of dollars)
1920	58	$2,533	.....	.....
1921	78	2,360	.....	.....
1922	108	3,353	.....	.....
1923	105	3,494	.....	.....
1924	109	3,880	.....	.....
1925	132	5,043	174	$6,006
1926	132	5,422	171	6,381
1927	144	5,473	185	6,303
1928	.....	5,836	200	6,628
1929	.....	4,999	172	5,751

[1] Information on thirty-seven states not available for years prior to 1925. Includes small towns and rural districts, as well as large cities.

Source: *Statistical Abstract of the United States.*

TABLE VI

Capital Issues

(In millions of dollars)

Year	Corporate issues			Corporate and government		
	Total	New	Refunding	Total	Refunding	Foreign Gov't
1919	$2,740	$2,303	$ 436	$4,286	$ 698	$533
1920	2,966	3,070	256	4,010	375	344
1921	2,391	1,822	593	4,204	627	455
1922	3,073	2,336	738	5,236	932	632
1923	3,233	2,702	530	4,990	685	293
1924	3,839	3,323	516	6,353	759	927
1925	4,738	4,100	637	7,126	906	791
1926	5,300	4,357	942	7,430	1,086	624
1927	7,319	5,392	1,928	9,934	2,143	912
1928	7,818	6,079	1,739	9,992	1,878	689
1929	10,026	8,640	1,387	11,592	1,409	130

Source: All except new and refunding corporate issues from *Statistical Abstract of the United States*, 1934, p. 277.

New and refunding corporate issues from *Standard Statistics Base Book.*

TABLE VII

Corporation Incomes

(Values in millions of dollars)

Year	Number of returns (thousands)	Depreciation and depletion	Other tax (not income)	Compiled[1] net profit	Income tax	Income[4] after taxes	Dividends paid	
							Cash	Stock
1921	356	2,573	1,473	1,156	702[3]	454	....[5].....	.....[5].....
1922	383	2,889	1,518	5,967	784[3]	5,183	3,437	3,348
1923	399	3,116	1,635	7,634	937	6,697	4,169	891
1924	417	3,187	1,670	6,795	882	5,913	4,339	511
1925	430	3,330	.....[2].....	9,316	1,170	8,146	5,189	544
1926	455	3,841	1,878	9,510	1,230	8,280	5,945	758
1927	475	3,848	2,014	8,669	1,131	7,538	6,423	703
1928	496	4,112	2,203	10,737	1,184	9,553	7,074	550
1929	509	4,430	2,222	11,870	1,193	10,677	8,356	1,289

[1] Compiled receipts less statutory deductions.
[2] Not shown separately; included in miscellaneous deductions not appearing in this table.
[3] Includes war and excess-profits tax.
[4] Compiled net profit less income tax.
[5] Not available.

Source: *Statistical Abstract of the United States; Corporation Income Tax Returns*, 1934, p. 180.

TABLE VIII

GOVERNMENT DEBT

(In millions of dollars)

YEAR	STATE AND LOCAL[1]	STATE
1912	3,822	423
1919		694
1922	8,690	1,163
1924		1,593
1925		1,746
1926		1,858
1927		1,995
1928		2,144
1929		2,300
1930		2,444
1931		2,666
1932	17,590	2,896

[1] Gross debt less sinking fund assets of states, counties, cities, towns and all other civil divisions.
Source: *Statistical Abstract of the United States*, 1934, pp. 207 and 210

TABLE IX

STOCKS AND BONDS ON NEW YORK STOCK EXCHANGE

(As of January 1 each year)

1925-1929

YEAR	STOCKS			BONDS		
	Number of Shares (millions)	Market Value (millions)	Average Market Price (dollars)	Face Value (millions)	Market Value (millions)	Average Market Price (dollars)
1925	433	$27,072	$62.45	$35,458	$33,612	$94.79
1926	492	34,489	70.15	36,995	35,509	95.98
1927	586	38,376	65.53	37,900	37,168	98.06
1928	655	49,736	75.93	36,881	36,875	99.98
1929	757	67,478	89.10	48 589	47,379	97.51

Source: *New York Stock Exchange Yearbook.*

Note—Average market price of stocks listed increased 42.6 per cent from 1925 to 1929. Average market price of bonds increased 2.8 per cent in the same period.

TABLE X

Individual Money Incomes as Shown by Federal Income Tax Returns

1922-1932

Year	Groups in Thousands of Dollars	Number of Returns	Income			Wages & Salaries		Dividends		All Other Property		Group Classification	
			Total Income Returns[2] (000)	Average Income	Per Cent of 1922	Income from Wages and Salaries (000)	Per Cent of Total Income Returned	Income from Dividends (000)	Per Cent of Total Income Returned	Income from all Other Property (000)	Per Cent of Total Income Returned	Per Cent of Number of Returns	Per Cent of Total Income Returned
1922	All Groups	6,787,481	24,871,908	3,664	100.0	13,693,993	55.06	$2,664,219	10 71	$8,513,696	34.23	100.00	100.00
	Below 5	6,193,270	15,553,016	2,511	100.0	10,760,539	69.19	490,684	3.15	4,301,603	27.66	91.25	62.53
	5 - 10	391,373	3,127,162	7,990	100.0	1,375,159	43.97	356,317	11.39	1,395,686	44.63	5.77	12.57
	10 - 50	186,807	4,128,270	22,100	100.0	1,280,898	31.03	1,142,680	27.68	1,704,882	41.30	2.75	16.60
	50 & Above	16,031	2,063,460	128,710	100.0	277,397	13.44	674,538	32.69	1,111,525	53.87	.23	8.30
1923	All Groups	7,698,331	29,318,928	3,808	117.9	14,230,209	48.54	3,126,503	10.66	11,962,216	40.80	100.00	100.00
	Below 5	7,072,424	19,312,014	2,731	124.2	11,069,242	57.32	683,869	3.91	7,558,903	39.14	91.87	65.87
	5 - 10	397,630	3,183,408	8,001	101.8	1,410,310	44.30	346,049	10.87	1,427,049	44.30	5.17	10.86
	10 - 50	211,633	3,052,099	14,422	73.9	1,453,381	47.62	1,183,997	38.76	415,721	13.62	2.74	10.41
	50 & Above	16,634	3,771,407	226,730	182.8	297,276	7.88	913,588	24.27	2,560,543	67.90	.22	12.86
1924	All Groups	7,369,788	29,578,997	4,013	118.9	13,617,663	46.04	3,250,914	10.99	12,710,420	42.97	100.00	100.00
	Below 5	6,672,650	18,168,236	2,723	116.8	10,126,749	55.74	634,043	3.44	7,407,444	40.77	90.54	61.42
	5 - 10	437,330	3,500,580	8,004	111.9	1,521,771	43.47	292,105	8.34	1,686,704	48.19	5.93	11.83
	10 - 50	238,277	5,205,055	21,845	126.1	1,644,714	31.60	1,209,731	23.24	2,350,610	45.66	3.23	17.60
	50 & Above	21,531	2,705,121	125,640	131.1	324,429	11.99	1,115,035	41.22	1,265,662	46.79	.30	9.15
1925	All Groups	4,171,051	25,272,035	6,059	101.6	9,742,160	38.55	3,464,625	13.71	12,065,249	47.74	100.00	100.00
	Below 5[1]	3,340,381	10,449,908	3,128	67.2	5,708,249	54.63	419,257	4.01	4,322,302	41.36	80.08	41.34
	5 - 10	503,362	4,044,267	8,035	129.3	1,697,230	41.97	321,290	7.94	2,025,747	50.09	12.07	16.00
	10 - 50	296,500	6,539,213	18,682	158.4	1,844,326	28.21	1,186,177	18.14	3,508,710	53.65	7.11	25.88
	50 & Above	30,518	4,243,647	139,050	205.7	492,255	11.60	1,537,901	36.24	2,213,491	52.16	.74	16.78
1926	All Groups	4,138,092	25,447,436	6,150	102.3	9,994,365	39.27	4,012,598	15.77	11,440,473	44.96	100.00	100.00
	Below 5[1]	3,243,224	10,079,477	3,108	64.8	5,630,970	55.87	430,228	4.27	4,018,279	39.92	78.37	39.61
	5 - 10	560,549	4,491,074	8,012	143.6	1,884,976	41.97	435,309	9.69	2,170,789	48.34	13.55	17.65
	10 - 50	304,217	6,545,674	21,516	158.6	2,055,135	31.40	1,482,060	22.64	3,007,479	45.96	7.35	25.72
	50 & Above	30,102	4,331,211	143,884	209.9	423,284	9.77	1,664,001	38.42	2,243,926	51.81	.73	17.02

(*Continued on next page*)

TABLE X (*Continued*)

1927	All Groups	4,101,547	26,208,560	6,390	105.4	10,218,450	39 00	4,254,829	16.28	11,735,281	44.77	100.00	100.00
	Below 5[1]	3,187,950	9,948,576	3,121	63.9	5,694,174	57.24	492,919	4.95	3,761,483	37.81	77.73	37.96
	5 - 10	567,700	4,517,770	7,958	144.5	1,952,271	43.21	430,621	9.53	2,134,878	47.26	13.84	17.24
	10 - 50	312,202	6,735,228	21,573	163.1	2,005,314	29.77	1,514,473	22.49	3,215,441	47.74	7.61	25.70
	50 & Above	33,695	5,006,986	148,597	242.7	566,691	11.31	1,816,816	36.29	2,623,479	52.40	.82	19.10
1928	All Groups	4,070,851	28,987,634	7,121	116.5	10,862,331	37.47	4,350,979	15.01	13,774,324	47.52	100.00	100.00
	Below 5[1]	3,059,964	9,564,418	3,126	61.5	5,854,045	61.21	341,064	3.57	3,369,309	45.23	75.17	32.99
	5 - 10	628,766	4,950,698	7,874	158.3	2,230,255	45.05	438,373	8.85	2,282,070	46.10	15.45	17.08
	10 - 50	338,937	7,351,052	21,689	178.1	2,106,462	28.66	1,529,492	20.81	3,715,098	50.53	8.33	25.36
	50 & Above	43,184	7,121,466	164,910	345.1	671,569	9.43	2,042,050	28.67	4,407,847	61.90	1.05	24.57
1929	All Groups	4,044,327	29,946,952	7,405	120.4	11,198,979	37.40	4,786,028	15.98	13,961,945	46.62	100.00	100.00
	Below 5	3,012,256	10,236,784	3,398	65.8	6,019,938	58.81	538,997	5.27	3,677,849	35.92	74.48	34.18
	5 - 10	658,039	5,243,756	7,969	167.7	2,404,992	45.86	506,118	9.65	2,332,646	44.49	16.27	17.10
	10 - 50	335,143	7,416,900	22,131	179.6	2,090,797	28.19	1,666,781	22.47	3,659,322	49.34	8.29	24.77
	50 & Above	38,889	7,049,512	181,273	341.6	683,252	9.69	2,074,132	29.42	4,292,128	60.89	.96	23.54
1930	All Groups	3,707,509	22,412,446	6,045	90.1	9,921,952	44.27	4,197,304	18.73	8,293,190	37.00	100.00	100.00
	Below 5[1]	2,897,078	9,205,629	3,178	59.2	5,514,346	59.90	488,648	5.31	3,202,635	34.79	78.14	41.07
	5 - 10	550,977	4,513,555	8,192	144.3	2,233,256	49.48	573,156	12.70	1,707,143	37.82	14.86	20.14
	10 - 50	239,607	5,487,832	22,903	132.9	1,768,163	32.33	1,582,081	28.83	2,137,588	38.95	6.46	24.49
	50 & Above	19,847	3,205,430	161,507	155.3	406,187	12.67	1,553,419	48.46	1,245,824	38.87	.54	14.30
1931	All Groups	3,225,924	17,268,451	5,353	69.4	8,325,162	48.21	3,113,861	18.03	5,829,428	33.76	100.00	100.00
	Below 5[1]	2,635,193	8,256,869	3,133	53.1	5,005,134	60.62	530,187	6.42	2,721,548	32.96	81.69	47.81
	5 - 10	417,655	3,502,761	8,387	112.0	1,810,439	51.69	485,755	13.87	1,206,567	34.44	12.95	20.28
	10 - 50	162,062	3,745,932	23,114	90.7	1,265,713	33.79	1,128,915	30.14	1,351,304	36.07	5.02	21.69
	50 & Above	11,014	1,762,889	160,059	85.4	243,876	13.83	969,004	54.97	550,009	31.20	.34	10.21
1932	All Groups	3,877,430	14,392,080	3,712	57.9	8,136,717	56.54	1,972,133	13.70	4,283,230	29 76	100.00	100.00
	Below 5[1]	3,520,988	9,022,434	2,562	58.0	6,079,462	67.38	431,508	4.78	2,511,464	27.84	90.81	62.69
	5 - 10	251,014	2,144,370	8,542	68.6	1,136,926	53.02	318,765	14.87	688,680	32.11	6.47	14.90
	10 - 50	97,690	2,235,056	22,879	54.1	759,754	33.99	659,577	29.51	819,831	36.50	2.52	15.53
	50 & Above	7,738	990,220	127,968	47.9	160,575	16.63	562,283	56.78	263,255	26.59	.20	6.88

[1] Based upon samples.
[2] Total income before deductions.

Source: Statistics of Income (1922-1932), United States Treasury Department.

TABLE XI

Division of National Money Income Among Groups of Income Receivers

1922-1932

Year	Groups[1]	Income of those gainfully employed[2] (000,000)	Per cent of national income received by each group	Cumulative[3] per cent of national income received	Average income received by each group per person	Number gainfully employed in each group[2] (000)	Per cent gainfully employed in each group	Cumulative per cent gainfully employed[3]	Per cent of number employed in each group to total population	Cumulative[3] per cent of number employed to total population
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1922	No. 1	$36,315	59.35	100.00	$1,054	34,543	83.58	100.00	31.39	37.58
	No. 2	15,553	25.42	41.01	2,511	6,193	14.98	16.42	5.64	6.18
	No. 3	3,127	5.11	15.59	7,997	391	.95	1.44	.35	.54
	No. 4	4,128	6.75	10.48	22,075	187	.45	.49	.17	.19
	No. 5	2,063	3.37	3.37	129,938	16	.04	.04	.03	.02
	Total	61,187	100.00	.....	1,480	41,330	100.00	.....	37.58	.....
1923	No. 1	39,976	57 69	100.00	1,160	34,458	81.74	100 00	31.06	38.01
	No. 2	19,312	27.88	42.30	2,731	7,072	16.78	18.26	6.37	6.94
	No. 3	3,813	4.59	14.43	7,997	398	.94	1.48	.36	.57
	No. 4	3,052	4.40	9.84	14,396	212	.50	.54	.19	.21
	No. 5	3,771	5.44	5.44	221,824	17	.04	.04	.03	.02
	Total	69,295	100.00	.....	1,644	42,157	100.00	.....	38.01	.....
1924	No. 1	42,326	58.86	100.00	1,184	35,753	82.91	100.00	31.83	38.89
	No. 2	18,168	25.27	41.14	2,723	6,673	15 47	17.09	5.94	6.56
	No. 3	3,501	4.87	15.87	8,011	437	1.01	1.67	.39	.62
	No. 4	5,205	7.24	11.00	21,870	238	.55	.60	.21	.23
	No. 5	2,705	3.76	3.76	122,955	22	.05	.05	.02	.02
	Total	71,905	100.00	.....	1,167	43,123	100.00	.....	38.39	.....

(*Continued on next page*)

TABLE XI (*Continued*)

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1925	No. 1	51,289	66.99	100.00	1,293	39,673	90.49	100.00	34.34	37.94
	No. 2	10,450	13.65	33.01	3,129	3,340	7.62	9.52	2.88	3 60
	No. 3	4.044	5.28	19.36	8.040	503	1.15	1.90	.43	.72
	No. 4	6,539	8.54	14.08	22,017	297	.68	.75	.26	.29
	No. 5	4,244	5.54	5.54	136,903	31	.07	.07	.03	.03
	Total	76,561	100.00	.....	1,746	43,844	100.00	.....	37.94	.....
1926	No. 1	54,837	68.30	100.00	1,357	40,422	90.71	100.00	34.39	37.92
	No. 2	10,079	12.57	31.70	3,108	3,243	7.28	9.29	2.76	3.53
	No. 3	4,491	5.59	19.13	8,005	561	1.26	2.01	.48	.77
	No. 4	6,546	8.15	13.54	21,533	304	.68	.75	.26	.29
	No. 5	4,331	5.39	5.39	144,367	30	.07	.07	.03	.03
	Total	80,284	100.00	.....	1,802	44,560	100.00	.....	37.92	.....
1927	No. 1	56,712	68.39	100.00	1,374	41,271	90.96	100.00	34.72	38.17
	No. 2	9,947	12.00	31.61	3,121	3,188	7.03	9.05	2.68	3.45
	No. 3	4,518	5.45	19.61	7,954	568	1.25	2.02	.48	.77
	No. 4	6,735	8.12	14.16	21,587	312	.69	.77	.26	.29
	No. 5	5,007	6.04	6 04	147,265	34	.08	.08	.03	.03
	Total	82,921	100.00	.....	1,328	45,373	100.00	.....	38.17	.....
1928	No. 1	55,131	65.54	100.00	1,281	43,029	91.36	100.00	35.73	39.11
	No. 2	9,564	11.36	34.46	3,125	3,060	6.49	8.65	2.54	3.38
	No. 3	4,951	5.89	23.10	7,871	629	1.34	2.15	.52	.84
	No. 4	7,351	8.74	17.21	21,684	339	.72	.81	.28	.32
	No. 5	7,121	8.47	8.47	165,605	43	09	.09	.04	.04
	Total	84,119	100.00	.....	1,786	47,100	100.00	.....	39.11	.....
1929	No. 1	51,189	63.09	100.00	1,274	40,181	90.86	100.00	32.98	36.30
	No. 2	10,237	12.62	36.91	3,399	3,012	6.81	9.15	2.47	3.32
	No. 3	5,244	6.46	24.29	7,970	658	1.49	2.34	.54	.85
	No. 4	7,417	9.14	17.83	22,140	335	.76	.85	.28	.31
	No. 5	7,121	8.69	8.69	180,769	39	.09	.09	.03	.03
	Total	81,136	100.00	.....	1,835	44,225	100.00	.....	36.30	.....

(*Continued on next page*)

TABLE XI (*Continued*)

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1930	No. 1	52,998	70.28	100.00	1,391	38,110	91.13	100.00	30.92	33.94
	No. 2	9,206	12.20	29.72	3,178	2,897	6.93	8.87	2.35	3.02
	No. 3	4,514	5.99	17.52	8,192	551	1.32	1.94	.45	.67
	No. 4	5,488	7.28	11.53	22,867	240	.57	.62	.20	.22
	No. 5	3,204	4.25	4.25	160,300	20	.05	.05	.02	.02
	Total	63,247	100.00	.....	1,662	41,818	100.00	.....	33.94	.....
1931	No. 1	45,979	72.70	100.00	1,320	34,827	91.52	100.00	27.96	30.56
	No. 2	8,257	13.05	27.30	3,134	2,635	6.92	8.48	2.12	2.60
	No. 3	3,503	5.54	14.25	8,380	418	1.10	1.56	.34	.48
	No. 4	3,748	5.03	8.71	28,486	162	.43	.46	.13	.14
	No. 5	1,760	2.78	2.78	160,000	11	.03	.03	.01	.01
	Total	63,247	100.00	.....	1,662	38,053	100.00	.....	30.56	.....
1932	No. 1	34,503	70.58	100.00	1,140	30,254	88.64	100.00	24.19	27.29
	No. 2	9,022	18.45	29.42	2,563	3,520	10.31	11.36	2.81	3.10
	No. 3	2,144	4.38	10.97	8,542	251	.74	1.05	.20	.29
	No. 4	2,235	4.57	6.59	22,806	98	.29	.31	.08	.09
	No. 5	990	2.02	2.02	128,571	7.7	.02	.02	.01	.01
	Total	48,894	100.00	.....	1,433	34,131	100.00	.....	27.29	.....

[1] Explanation of groups:
Group No. 1—Those with incomes too low to make reports.
Group No. 2—Those with incomes below $5,000 but required to make reports.
Group No. 3—Those with incomes more than $5,000 but less than $10,000.
Group No. 4—Those with incomes more than $10,000 but less than $50,000.
Group No. 5—Those with incomes above $50,000.
Total—Total of all groups.

[2] Total number gainfully employed and total income of those gainfully employed taken from Tables II and VIII, pages 50 and 74 respectively, of *The National Income and Purchasing Power*, by W. I. King, for the years 1922 to 1928, inclusive. For the years 1929 to 1932 the total number and total income of those gainfully employed taken from Tables VI and XV, respectively of *National Income, 1929-1932*, a report on national income, Senate Document 124.

[3] Cumulative: Greater than the lower limit of that group.
Group No. 1: Number gainfully employed and income data obtained by subtracting the "all groups" data of those making returns in Table X from the total number and total income, respectively, of those gainfully employed in Table XI.
Groups No. 2, 3, 4 and 5: The number gainfully employed and total income of those gainfully employed for the years 1922 to 1928, inclusive, taken from Tables VII and VIII, pp. 50 and 74 respectively, of *National Income and its Purchasing Power*, by W. I. King. For the years 1929-1932 the corresponding data taken from Tables VIII and XV respectively of *National Income, 1929-1932*, a report on national income, Senate Document 124.

TABLE XII

Trend of Development in Manufacturing Industries

1914 to 1931

(Factories, excluding establishments with products valued at less than $5,000)

YEAR	NUMBER OF ESTABLISHMENTS[1] (000)	NUMBER OF WAGE-EARNERS: AVERAGE FOR YEAR[1] (000)	TOTAL WAGES[1] (000,000)	WAGES PER LABORER	VALUE OF PRODUCTS[1] (000,000)	VALUE ADDED BY MANUFACTURE[1] (000,000)	VALUE ADDED BY MANUFACTURE PER LABORER	PER CENT OF VALUE OF PRODUCT ADDED BY MANUFACTURE	PER CENT OF VALUE ADDED BY MANUFACTURE PAID AS WAGES
1914	177	6,896	$4,068	$589.91	$23,988	$ 9,710	$1,408.06	30.47	41.89
1919	214	9,000	10,462	1,162.44	62,042	24.809	2,756.55	39.98	42.17
1921	196	6,947	8,202	1,180.65	43,653	18,332	2,638.83	41.99	44.74
1923	196	8,778	11,009	1,254.15	60,556	25,850	2,944.86	42.69	42.58
1925	187	8,384	10,730	1,279.81	62,714	26,778	3,193.94	42.69	40.07
1927	192	8,350	10,849	1,299 28	62,718	27,585	3,303.59	43.98	39.33
1929	211	8,839	11,621	1,314.74	70,435	31,885	3 607.30	45.26	36 44
1931	175	6,523	7,186	1,101.64	41,350	19,867	3,045 68	48.04	36 17

[1] Source: *Statistical Abstract of the United States*, 1934, p. 697.

TABLE XIII

GAINFUL WORKERS TEN YEARS OLD AND OVER

BY GENERAL DIVISIONS OF OCCUPATIONS AND SEX, CONTINENTAL UNITED STATES

(Per cent not shown where less than 0.1)

YEAR AND GENERAL DIVISION OF OCCUPATIONS	NUMBER			PER CENT DISTRIBUTION			PER CENT OF TOTAL	
	Total	Male	Female	Total	Male	Female	Male	Female
1920	41,614,248	33,064,737	8,549,511	100.0	100.0	100.0	79.5	20.5
Agriculture	10,665,812	9,582,666	1,083,146	25.6	29.0	12.7	89.8	10.2
Forestry and fishing	270,214	269,541	673	.6	.8	.....	99.8	.2
Extractions of minerals	1,090,223	1,087,359	2,864	2.6	3.3	.....	99.7	.3
Manufacturing and mechanical industries	12,831,879	10,901,527	1,930,352	30.8	33.0	22.6	85.0	15.0
Transportation and communication	3,096,829	2,872,559	224,270	7.4	8.7	2.6	92.8	7.2
Trade	4,257,684	3,585,701	671,983	10.2	10.8	7.9	84.2	15.8
Public service (not elsewhere classified)	738,525	727,939	10,586	1.8	2.2	.1	98.6	1.4
Professional service	2,171,251	1,154,221	1,017,030	5.2	3.5	11.9	53.2	46.8
Domestic and personal service	3,379,995	1,193,313	2,186,682	8.1	3.6	25.6	35.3	64.7
Clerical occupations	3,111,836	1,689,911	1,421,925	7.5	5.1	16.6	54.3	45.7
1930	48,829,920	38,077,804	10,752,116	100.0	100.0	100.0	78.0	22.0
Agriculture	10,471,998	9,562,059	909,939	21.4	25.1	8.5	91.3	8.7
Forestry and fishing	250,469	250,140	329	.5	.7	.....	99.9	.1
Extraction of minerals	984,323	983,564	759	2.0	2.6	.....	99.9	.1
Manufacturing and mechanical industries	14,110,652	12,224,345	1,886,307	28.9	32.1	17.5	86.6	13.4
Transportation and communication	3,843,147	3,561,943	281,204	7.9	9.4	2.6	92.7	7.3
Trade	6,081,467	5,118,787	962,680	12.5	13.4	9.0	84.2	15 8
Public service (not elsewhere classified)	856,205	838,622	17,583	1.8	2.2	.2	97.9	2.1
Professional service	3,253,884	1,727,650	1,526,234	6.7	4.5	14.2	53.1	46.9
Domestic and personal service	4,952,451	1,772,200	3,180,251	10.1	4.7	29.6	35.8	64.2
Clerical occupations	4,025,324	2,038,494	1,986,830	8.2	5.4	18.5	50 6	49.4

Source: *Statistical Abstract of the United States*, 1934, p. 55]

TABLE XIV

GOVERNMENTAL CORPORATIONS AND CREDIT AGENCIES, FEBRUARY 28, 1935

(In millions of dollars)

	TOTAL	FINANCED WHOLLY FROM GOVERNMENT FUNDS								
		Total	Reconstruction Finance Corporation	Commodity Credit Corporation	Export-Import banks	Public Works Administration	Regional Agricultural Credit Corporations	Production Credit Corporation	U. S. Shipping Board Merchant Fleet Corporation	Other[1]
Assets										
Loans—total	7,548	2,027	1,374	40	4	276	82	.....	112	139
Preferred stock, capital notes, and debentures	868	868	865	.....	.....	.....	.....	.....	.....	3
Cash—total	337	107	4	....[2]...	10	.....	2	2	18	71
Investments:										
United States securities	467	24	.....	.....	.....	.....	.....	2	.....	22
Obligations guaranteed by United States	226	10	.....	.....	.....	.....	....[2]...	10	.....	.....
Other investments	762	124	.....	.....	.....	.....	.....	99	21	4
Accounts and other receivables	155	50	31	....[2]...	....[2]...	.....	4	....[2]...	9	6
Real estate and other business properties	141	133	1	....[2]...	....[2]...	.....	....[2]...	....[2]...	50	83
Other assets	488	383	299	....[2]...	....[2]...	3	....[2]...	....[2]...	1	80
Total assets other than interagency	10,992	3,727	2,574	40	14	279	88	114	209	408
Liabilities										
Bonds, notes, and debentures:										
Obligations guaranteed by United States	3,596	251	251	.....	.....	.....	.....	.....	.....	.....
All other	2,405	72	.....	.....	.....	.....	.....	.....	.....	72
Other liabilities (including reserves)	224	55	19	....[2]...	....[2]...	.....	1	1	17	17
Total liabilities other than interagency	6,225	378	270	....[2]...	....[2]...	.....	1	1	17	89
Excess of assets over liabilities, exclusive of interagency transactions	4,767	3,349	2,305	40	14	279	88	113	193	318
Privately owned interests	327	.....	.....	.....	.....	.....	.....	.....	.....	.....
U. S. Government interests	4,439	3,349	2,305	40	14	279	88	113	193	318
Distribution of Government interests:										
Capital stock	6,573	5,515	500	3	14	400[3]	45	112	50	[3]4,391
Surplus	337	240	69	1	....[2]..	.....	11	1	143	15
Interagency interest (net)	−2,471	−2,405	1,736	36	.....	−121	32	.....	.....	−4,088[3]

(*Continued on next page*)

TABLE XIV (*Continued*)

	FINANCED PARTLY FROM GOVERNMENT FUNDS									
	Total[4]	Federal land banks	Federal intermediate credit banks	Federal Farm Mortgage Corporation	Banks for Co-operatives	Home Loan Banks	Home Owners' Loan Corporation	Federal Savings and Loan Insurance Corporation	Federal Savings and Loan Associations	Federal Deposit Insurance Corporation
Assets										
Loans—total	5,520	2,047	158	665	29	77	2,544	.....	.....	.....
Cash—total	230	24	14	18	6	30	122	1	.....	15
Investments:										
United States securities	443	67	34	.....	25	1	.....	.....	.....	316
Obligations guaranteed by United States	215	16	41	.....	58	1	.....	100	.....	.....
Other investments	638	1	....[2]....	627	10	....[2]....	.....	.....	.....	.....
Accounts and other receivables	105	40	4	19	1	....[2]....	37	1	.....	2
Real estate and other business properties	8	5	....[2]....	....[2]....	....[2]....	....[2]....	3	....[2]....	.....	....[2]....
Other assets	105	84	....[2]....	1	....[2]....	....[2]....	....[2]....	.....	18	2
Total assets other than interagency	7,265	2,284	251	1,330	130	110	2,706	102	18	335
Liabilities										
Bonds, notes, and debentures:										
Obligations guaranteed by United States	3,346	.....	.....	1,089	.....	.....	[5]2,256	.....	.....	.....
All other	2,333	1,835	175	.....	.....	.....	322	.....	.....	.....
Other liabilities (including reserves)	169	82	4	36	....[2]....	3	39	....[2]....	.....	5
Total liabilities other than interagency	5,847	1,917	179	1,126	....[2]....	3	2,617	....[2]....	.....	5
Excess of assets over liabilities, exclusive of interagency transaction	1,417	366	72	204	130	106	89	102	18	331
Privately owned interests	327	121	.....	.....	2	24	.....	.....	.....	[6]181
U. S. Government interests	1,090	245	72	204	128	82	89	102	18	150
Distribution of Government interests:										
Capital stock	1,058	114	70	200	125	82	200	100	18	150
Surplus	97	65	34	4	3	1	−11	2	.....	.....
Interagency interest (net)	−66	66	−32	.....	.....	.....	−100	.....	.....	.....

[1] Includes interagency interests held by the Treasury Department.
[2] Less than $500,000.
[3] Non-stock (or includes non-stock proprietary interests).
[4] Includes also War Finance Corporation not shown separately.
[5] Includes unissued bonds covering loans in process.
[6] Includes $41,000,000 of assessments paid in by member banks and trust companies formerly included under United States government interests.
Source: *Federal Reserve Bulletin*, April, 1935, p. 221.

TABLE XV

RECONSTRUCTION FINANCE CORPORATION

LOANS, SUBSCRIPTIONS, AND ALLOCATIONS

(Amount outstanding at end of month. In thousands of dollars)

	PROCEEDS DISBURSED, LESS REPAYMENTS							PROCEEDS NOT YET DISBURSED	
	Feb. 28, 1934[2]	Oct. 31, 1934	Nov. 30, 1934	Dec. 31, 1934	Jan. 31, 1935	Feb. 28, 1935	Mar. 31, 1935[3]	Jan. 31, 1935	Feb. 28 1935
Loans and Subscriptions									
Loans under section 5 of the Reconstruction Finance Corporation Act as amended:									
Banks and trust companies (including receivers, liquidating agents, and conservators)	690,471	583,452	599,397	632,209	595,717	568,814	538,431	117,970	113,005
Building and loan associations	59,552	25,205	23,259	20,082	15,640	13,567	12,281	21,367	21,367
Insurance companies	54,059	29,982	29,420	24,829	24,023	22,664	22,035	135	135
Mortgage-loan companies	167,315	159,327	155,874	160,591	156,292	155,367	151,796	101,317	99,226
Credit unions	499	388	387	386	367	361	343	.....	.....
Federal land banks	193,618	115,263	110,997	78,647	77,023	74,670	72,318	.....	.....
Joint stock land banks	13,158	7,323	7,132	6,495	5,530	5,031	4,078	634	621
Agricultural credit corporations	1,214	605	600	863	863	863	861	.....	.....
Regional agricultural credit corporations	29,145	2,673	866	.....	.....	.....	.....	.....	.....
Livestock credit corporations	2,071	1,546	1,464	1,334	1,314	1,272	1,256	.....	.....
Railroads (including receivers)	345,178	353,170	361,506	376,555	379,087	379,713	380,199	1,504	753
State funds for insurance of public moneys	5,055	1,233	811	541	.....	.....	.....	.....	.....
Fishing industry	.....	.....	25	25	43	53	53	85	78
Processors or distributors for payment of processing taxes	13	2	2	1	1	1	1	.....	.....
Total	1,561,348	1,280,168	1,291,739	1,302,558	1,255,900	1,222,374	1,183,651	243,011	235,184
Other loans:									
For self-liquidating projects, section 201 (a) (including repairs to property damaged by earthquakes, etc.)	71,217	112,291	117,027	122,743	125,408	127,839	132,908	101,336	97,588
For financing exports of agricultural surpluses, section 201 (c)	10,053	15,271	14,992	15,176	15,176	15,164	14,953	3,095	3,088
For financing agricultural products, section 201 (d)	4,448	5,717	6,090	4,258	4,177	4,719	5,332	4,202	3,689
To commodity credit corporation	153,525	42,969	30,242	33,362	36,139	35,905	39,552	376,506	372,034
On preferred stock of banks	10,757	18,849	18,965	19,124	19,487	19,674	20,304	1,534	1,345
On preferred stock of insurance companies	4,375	25,785	25,785	30,033	29,933	29,933	29,933	.....	.....
To drainage levee and irrigation districts	2,414	11,147	11,321	12,298	15,410	16,978	21,292	65,489	65,147
To public school authorities	.....	22,300	22,300	.....	.....	.....	.....	.....	.....
To industrial and commercial businesses	.....	3,248	4,166	6,627	8,516	10,649	12,740	23,247	24,050

(Continued on next page)

TABLE XV (*Continued*)

To mining, milling, and smeltering businesses	.....	.....	.....	.....	.....	.....	.....	.....	168
On assets of closed banks	.....	23	22	20	34	79	150	171	219
To Public Works Administration on security transactions	.....	.....	.....	1,529	71	1,356	17,311	7,098	2,407
Total	256,788	257,600	250,911	245,169	254,350	262,296	294,475	582,677	569,734
Purchases:									
Preferred stock of banks	261,438	562,410	571,193	585,858	598,112	621,055	627,876	60,954	36,835
Capital notes and debentures of banks	192,897	256,671	259,662	260,102	256,622	256,316	254,666	68,127	65,914
Preferred stock of insurance companies	.....	100	100	100	100	100	100	.....	.....
Total	454,335	819,180	830,955	846,060	854,834	877,472	882,642	129,081	102,748
Total loans and purchases	2,272,472	2,356,949	2,373,605	2,393,787	2,365,084	2,362,141	2,360,767[1]	954,770	907,667
Allocations									
For relief:									
Federal Emergency Relief Act of 1932	299,003	298,006	297,774	297,774	297,718	297 718	297,711	15	15
Federal Emergency Relief Act of 1933	478,244	499,590	499,586	499,588	499,987	499,991	499,994	13	9
Emergency Appropriations Act of 1935	.....	215,000	325,000	470,000	500,000	500,000	500,000	.....	.....
Total	777,247	1,012,596	1,122,360	1,267,362	1,297,705	1,297,709	1,297,704	28	24
To other Government agencies:									
To Secretary of the Treasury for:									
Purchase of stock of Federal Home Loan banks	79,146	81,646	81,646	81,646	81,646	81,646	81,646	43,095	43,095
Purchase of stock of Home Owners' Loan Corporation	39,000	200,000	200,000	200,000	200,000	200,000	200,000	.....	.....
To Land Bank Commissioner	147,600	147,600	147,600	147,600	147,600	147,600	147,600	97,400	97,400
To Federal Farm Mortgage Corporation	55,000	55,000	55,000	55,000	55,000	55,000	55,000	.....	.....
To Federal Housing Administrator	.....	15,000	15,000	25,000	25,000	25,000	25,000	.....	.....
To Secretary of Agriculture for:									
Crop loans	115,000	115,000	115,000	115,000	115,000	115,000	115,000	.....	.....
Reallocated as capital regional agricultural credit corporations	44,500	44,500	44,500	44,500	44,500	44,500	44,500	.....	.....
Reallocated to Governor of Farm Credit Administration	40,500	40,500	40,500	40,500	40,500	40,500	40,500	.....	.....
Total	520,746	699,246	699,246	709,246	709,246	709,246	709,246	140,495	140,495
Total allocations	1,297,993	1,711,842	1,821,606	1,976,608	2,006,951	2,006,955	2,006,950	140,523	140,519
Total loans, subscriptions, and allocations	3,570,464	4,068,791	4,195,211	4,370,395	4,372,035	4,369,095	4,367,717	1,095,293	1,048,186

[1] Includes $372,065,000 of loans for distribution to depositors of closed banks. [2] Revised [3] Preliminary

Source: *Federal Reserve Bulletin*, April, 1935, p. 222.

TABLE XVI

PART I—FAMILIES AND PERSONS RECEIVING EMERGENCY RELIEF, CONTINENTAL UNITED STATES

MONTHS	RESIDENT FAMILIES AND PERSONS RECEIVING RELIEF UNDER THE GENERAL RELIEF AND SPECIAL PROGRAMS					NUMBER OF TRANSIENTS RECEIVING RELIEF[2]
	Families	Single Persons	Total Families and Single Persons	Total Persons	Per cent of Total Population[1]	
1933						
January	3,850,000[3]	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
February	4,140,000[3]	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
March	4,560,000[3]	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
April	4,475,322	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
May	4,252,443	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
June	3,789,026	.....[4]	.....[4]	.....[4]	.....[4]	.....[4]
July	3,451,874	455,000[3]	3,906,874	15,282,000[3]	12	.....[4]
August	3,351,810	412,000[3]	3,763,810	15,077,000[3]	12	.....[4]
September	2,984,975	403,000[3]	3,387,975	13,338,000[3]	11	.....[4]
October	3,010,516	436,000[3]	3,446,516	13,618,000[3]	11	.....[4]
November	3,365,114	461,315	3,826,429	15,080,465	12	.....[4]
December	2,631,020	438,431	3,069,451	11,664,860	10	.....[4]
1934						
January	2,486,274	456,469	2,942,743	11,086,598	9	.....[4]
February	2,599,975	532,036	3,132,011	11,627,415	9	126,873
March	3,070,855	563,138	3,633,993	13,494,282	11	145,119
April	3,847,235	590,007	4,437,242	16,840,389	14	164,244
May	3,815,926	617,735	4,433,661	17,228,458	14	174,138
June	3,757,971	559,502	4,317,473	16,833,294	14	187,282
July	3,867,047	542,362	4,409,409	17,301,734	14	195,051
August	4,059,605	569,877	4,629,482	18,187,193	15	206,173
September	4,096,725	656,215	4,752,940	18,410,334	15	221,734
October	4,106,681[5]	720,853	4,827,534[5]	18,450,567[5]	15	235,758
November[6]	4,225,000	750,000	4,975,000	18,900,000	15	266,000

[1] Based on 1930 *Census of Population*.
[2] Middle of month figures, excluding local homeless which are included under general relief program.
[3] Partially estimated.
[4] Not available.
[5] Partially estimated to cover the rural rehabilitation program on which reports are not yet complete.
[6] Preliminary.
Source: Division of Research, Statistics, and Finance, Federal Emergency Relief Administration.

PART II—CASES[1] RECEIVING EMERGENCY RELIEF—DIRECT, WORK, SPECIAL PROGRAMS

1934	GRAND TOTAL	GENERAL RELIEF			SPECIAL PROGRAMS[2]
		Total	Work Programs	Direct Relief Only	
April	4,437,242	4,437,242	1,176,818	3,260,424	.....[3]
May	4,433,661	4,320,187	1,343,214	2,976,973	113,474
June	4,317,473	4,237,425	1,477,753	2,759,672	80,048
July	4,409,409	4,368,195	1,723,295	2,644,900	41,214
August	4,629,482	4,582,434	1,922,029	2,660,405	47,048
September	4,752,940	4,619,496	1,950,728	2,668,768	133,444
October	4,827,534	4,654,402	1,998,167	2,656,235	173,132
November[4]	4,975,000	4,785,000	2,150,000	2,635,000	190,000

[1] Cases include each family or single person on relief, not counting transient single persons.
[2] Rural rehabilitation program, emergency education program, student aid; excludes transients.
[3] Cases aided under special programs in April were included in the general relief program.
[4] Preliminary.
Source: Division of Research, Statistics, and Finance, Federal Emergency Relief Administration.

TABLE XVII

OBLIGATIONS INCURRED FOR EMERGENCY RELIEF FROM ALL PUBLIC FUNDS BY SOURCE OF FUNDS, JANUARY 1933 THROUGH NOVEMBER 1934, BY MONTHS AND BY QUARTERS[1]

	OBLIGATIONS INCURRED FOR EMERGENCY RELIEF						
	Total	*Federal Funds*		*State Funds*		*Local Funds*	
		Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
1933							
January	$60,827,160.86	$31,175,001.46	51 3	$8,898,288.71	14.6	$20,753,870.69	34.1
February	67,375,423.32	39,850,235.88	59.1	5,921,376.42	8.8	21,603,811.02	32.1
March	81,205,631.61	51,355,220.07	63.2	5,212,394.33	6.4	24,638,017.21	30.4
First quarter	209,408,215.79	122,380,457.41	58.4	20,032,059.46	9.6	66,995,698.92	32.0
April	73,010,800.68	45,373,968.80	62.1	8,182,877.70	11.2	19,453,954.18	26.7
May	70,806,338.08	48,803,456.80	68.9	5,017,248.11	7.1	16,985,633.17	24.0
June	66,339,206.68	42,523,714.87	64.1	8,038,872.89	12.1	15,776,618.92	23.8
Second quarter	210,156,345.44	136,701,140.47	65.0	21,238,998.70	10.1	52,216,206.27	24.9
July	60,155,873.87	37,482,328.17	62.3	7,576,554.71	12.6	15,096,990.99	25.1
August	61,470,496.37	39,781,831.27	64.7	8,726,266.40	14.2	12,962,398.70	21.1
September	59,346,338.14	36,289,188.33	61.1	11,093,954.69	18.7	11,963,195.12	20.2
Third quarter	180,972,708.38	113,553,347.77	62.8	27,396,775.80	15.1	40,022,584.81	22.1
October	64,888,913 42	40,415,353.15	62.3	10,186,795.50	15.7	14,286,764.77	22.0
November	70,810,514.27	39,796,429.13	56.2	18,633,766.17	26.3	12,380,318.97	17.5
December	56,526,330.37	27,755,055.43	49.1	18,768,833.14	33.2	10,002,441.80	17.7
Fourth quarter	192,225,758.06	107,966,837.71	56.2	47,589,394.81	24.7	36,669,525.54	19.1
Total, 1933	792,763,027.67	480,601,783.36	60.6	116,257,228.77	14.7	195,904,015.54	24.7
1934							
January	53,880,834.01	29,065,736.51	54 0	16,124,460.00	29.9	8,690,637.50	16.1
February	57,668,212.60	26,462,858.11	45.9	21,832,729.56	37.9	9,372,624.93	16.2
March	69,794,802.92	32,522,395.84	46.6	25,615,747.44	36.7	11,656,659.64	16 7
First quarter	181,343,849.53	88,050,990.46	48.5	63,572,937.00	35.1	29,719,922.07	16.4
April	113,134,286.74	82,299,551.45	72.7	17,642,023.89	15.6	13,192,711.40	11.7
May[2]	129,222,770.62	96,741,145.12	74.9	12,647,639.02	9.8	19,833,986.48	15.3
June[2]	125,198,649.88	92,084,137.06	73.6	11,777,402.31	9.4	21,337,110.51	17.0
Second quarter[2]	367,555,707.24	271,124,833.63	73.8	42,067,065.22	11.4	54,363,808.39	14.8
July[2]	130,953,215.11	95,146,288.68	72.6	13,061,941.23	10.0	22,744,985.20	17.4
August[2]	149,424,555.07	113,308,571.80	75.8	12,226,882.75	8.2	23,889,100.52	16.0
September[2]	143,227,846.44	108,559,186.27	75.8	11,406,614.12	8.0	23,262,046.05	16.2
Third quarter[2]	423,605,616.62	317,014,046.75	74.8	36,695,438.10	8.7	69,896,131.77	16.5
October[2]	156,747,867.63	121,949,841.00	77.8	13,950,560.23	8.9	20,847,466.40	13.3
November[3]	172,750,000.00	139,430,000.00	80.7	10,670,000.00	6.2	22,650,000.00	13.1
Total, 1934[3]	1,302,003,041.02	937,569,711.84	72.0	166,956,000.55	12.8	197,477,328.63	15.2
Total, 23 months[2]	2,094,766,068.69	1,418,171,495.20	67.7	283,213,229.32	13.5	393,381,344.17	18.8

[1] Includes obligations incurred for relief extended under the general relief program, under all special programs, and for administration; beginning April, 1934, these figures also include purchases of materials, supplies, and equipment, rentals of equipment (such as team and truck hire), earnings of non-relief persons employed, and other expense incident to the work program. Does not include about $990,000,000 expended for the CWA, of which $840,000,000 was derived from Federal funds and $150,000,000 from state and local funds.

[2] Breakdown partially estimated.

[3] Preliminary.

Source: Division of Research, Statistics, and Finance, Federal Emergency Relief Administration, January 7, 1935. Table based on reports from state and local relief administrations.

APPENDIX B

PRICES IN THEORY AND IN PRACTICE

THAT "prices are set in a free market by the equalization of supply and demand" is a widely accepted statement of how prices are determined; this statement of price determination is based upon the assumption that practically all business enterprises are operated under conditions of free and unrestrained competition. The theory of the determination of prices of reproducible goods, produced for a highly competitive market, is the heart of the classical theory of prices. This supply-and-demand competitive price theory holds that, under competitive conditions, the price of each commodity will tend to be fixed in the market at the point where the market supply and market demand will be equalized or balanced. This statement is unintelligible unless one has a thorough understanding of the meaning of both "market supply" and "market demand" and of how they may be equalized or balanced.

The market supply of a commodity at any given time is conceived to be the number of units of that commodity that sellers would be willing to sell at stated prices per unit. The number of units which would be offered for sale at different stated prices would vary *directly* with the magnitude of the stated price per unit. The actual quantity which would be offered for sale might range from zero at a low price offer per unit, to the total physical quantity in the hands of the sellers at a very high price offer per unit. The higher the market price, the larger will be the market supply (number of units offered for sale); the lower the market price, the smaller will be the market supply.[1]

1 Also, a change in the market price will bring about a change in the physical supply (amount produced) as well as in the market supply. It may be argued that a change in the price does not cause an immediate change in the market supply, it only causes sellers to sell more or less because of variations in the price. But a change in the quantity sold will influence the quantity produced.

The market demand for a commodity (at any given time) is conceived to be the number of units of the commodity which buyers would buy at any stated price per unit. The number of units which would be purchased at each stated price would vary inversely with the magnitude of the price per unit. The actual physical quantity which would be purchased might range from zero at a very high price per unit, to the total physical quantity in the hands of sellers at a very low price per unit. The higher the market price, the smaller will be the market demand (the number of units which would be bought); the lower the market price the larger will be the market demand.

The individual's market demand for a particular commodity depends upon two things: First, the individual must have a desire for the commodity and a willingness to buy at a particular price a certain number of units of the commodity; and second, he must have the purchasing power with which to purchase the commodity at the market price. The intensity of an individual desire for a certain commodity at a particular time is dependent (1) upon the want-satisfying qualities of that commodity as compared with the want-satisfying qualities of other commodities, and (2) upon the number of units of the commodity it will be necessary to acquire to satisfy his urgent desire for additional units of it. A change in the social habits and customs of an individual will change the intensity of his desire for a particular commodity. The individual's ability to buy a given number of units of various commodities at the market price of each will depend upon his current money income. The total market demand for a commodity is made up of the sum total of the individual market demands for it.

The market demand for non-consumption goods or producers' goods is dependent upon the business needs for those goods. The business needs for producers' goods are ultimately dependent upon the demand for the consumers' goods into which the producers' goods are converted. However, the day to day demand for producers' goods is not directly related to the day to day demand for consumers' goods.

The market supply of, and the market demand for, each commodity, at any particular time, are supposed to be equalized by the *specific price* which will cause the *greatest number*

of units of the commodity to be bought and sold in the market. If a price lower than the equalized price temporarily prevails in the market, the number of units of the commodity which sellers would offer for sale at this lower price would be *less* than the number of units which buyers would be willing to buy at that price; in short, the *market demand* at that lower price *would exceed the market supply*, and the market prices would be raised by the unsatisfied buyers offering a higher price in the market. On the other hand, if a price above the equalized price should prevail temporarily in the market the number of units which sellers would offer for sale at the higher price would exceed the number of units which would be bought by buyers at the higher price; in short, because of the high price, the *market supply would exceed the market demand*, and the unsatisfied sellers would lower the market price by offering to sell at a price lower than the one prevailing.

The competitive price theory holds that the price at which the demand for and the supply of a commodity will be equalized in the market, will be the price which will equal, or tend to equal, the cost of production of the least efficient business enterprise in the industry. The least efficient enterprise or the one with the highest cost of production engaged in producing the market supply of any commodity is generally referred to as "the marginal producer." The conclusion that the price of each reproducible commodity is determined largely by the cost of production of the marginal producer in each competitive industry is based on the following process of reasoning:

The total physical supply of a reproducible commodity over a long period of time will be only slightly greater than the total quantity of the commodity sold in the market; a large surplus physical supply cannot be held indefinitely by producers. Therefore, every unit of each commodity produced will be sold in the market eventually at the market price at the time of each sale. The lowest price at which a particular business enterprise is able to sell its goods, and at the same time remain in business an appreciable length of time, is a price which is equal to the cost of production. If a business enterprise is unable to secure a price for its products above their cost of production, it must sell at a lower price as long as it stays in business.

In any industry, the enterprises with the lowest cost of production are able to sell at much lower prices per unit of product than are those with the highest cost of production. In order to increase the volume of their sales, and for the purpose of securing a larger percentage of the business in their respective industries, the efficient low cost enterprises tend constantly to lower the price offers they make in the market. Therefore, the efficient enterprises in each industry tend to lower the market price of the products of the industry below the cost of production for the least efficient or marginal enterprises. The marginal enterprises thus become submarginal and because of heavy losses eventually are forced out of business.

The forcing of submarginal producers out of business reduces the immediate available market supply; the efficient enterprises then are able to gain a temporary increase in their sales possibly at a slight increase in price and certainly without further decreases in price. If all the enterprises in an industry, including the marginal and submarginal producers, are selling all they produce at the prevailing market price, a decline in the total production would decrease immediately the available market supply and cause a slight rise in the price. This shortage in market supply and rise in price would stimulate the efficient enterprises to increase their production, and as a result the market supply would increase and the price would tend to decline to its former level. The efficient enterprises would thus gain a larger volume of sales because of failure of the submarginal enterprises.

The competitive price theory holds that if for any reason in an industry the cost of production of a commodity should increase, the resulting decreased profits of the active enterprises in the industry sooner or later would eliminate some of the marginal and submarginal enterprises, and thus bring about a temporary decrease in the market supply of the commodity. The decrease in the market supply of the commodity would then cause some increase in its price. The price of the commodity would again be stabilized at a point which would equal the new cost of production for the least efficient producer in the industry. On the other hand, the theory holds that if the cost of production of a commodity in an industry should de-

crease, the resulting higher profits in the industry would bring about an increase in the production of the commodity. The increase in production would increase the market supply and thus bring about some decrease in the price. Again, the price would be stabilized at the point which would equal the lowest cost of production for the least efficient producer.

Again, according to the theory, if the market demand for a reproducible commodity increases, there will be an immediate rise in the market price of that commodity. The rise in the market price will either increase the profits or decrease the losses of all the producers. This rise in price then will stimulate an increase in the production of the commodity. The resulting increase in the market supply of the commodity will tend to cause a decline in its market price, and the market price again will tend to be stabilized at a price which will equal the cost of production of the least efficient producer.

On the other hand, if the market demand for a commodity decreases, the market price of the commodity will decline. The decline in the market price will bring about a temporary decrease in the production of that commodity because it will force some of the marginal producers out of business. The decrease in production may be so great as to bring about a slight shortage in the market supply at the prevailing lower price. But, according to the theory, the supply of and the demand for the commodity again will tend to be stabilized at a price which will equal the cost of production of the least efficient producer remaining in the industry.

It is recognized by all price theorists that this competitive supply and demand price theory does not apply to the determination of the prices of all classes of goods. They recognize the fact that the prices of non-reproducible goods, such as the works of art of the old masters, can not be determined by cost of production or of reproduction. The physical supply of such goods being definitely fixed, their prices will be determined entirely by the extent of the market demand for each of the commodities. However, most price theorists recognize the fact that the great bulk of commodities purchased by the public are reproducible; it then is assumed by many of them that the

prices of the great bulk of the goods sold in the market are determined in accordance with the competitive price theory.

Also, it is recognized by all competitive price theorists that some reproducible goods are produced under conditions of non-competition or monopoly. They have a well developed monopoly price theory to apply to goods produced under such conditions. This theory holds that monopolists will tend to set the prices of their products at the level which will return to them the *highest net profits*. The managers of monopolized industries exercise practical control over the supply of goods reproduced by those industries. They, therefore, will tend to regulate the market supply in relation to the market demand in such a manner as to secure the greatest net profits from their businesses. This policy often results in unreasonable curtailment of production and unjustifiably high prices in the industries that are dominated by monopolistic enterprises.

However, the price which will give a particular monopolist the highest net profits may not be a price which would give him a very large profit on each unit of product sold. In other words, it may be to the interest of a particular monopolist to depend on a large and growing volume of sales at a small profit per unit of product rather than on a smaller volume of sales at a larger profit per unit of sales. The amount of profit to be secured on each unit of product sold, theoretically, would be determined by the nature of the market demand for the commodity and the relative changes in the cost of production resulting from an increase or a decrease in production or output:

If there is a highly elastic demand for a monopolized commodity—that is, if a slight increase in the market price of the commodity causes a large decrease in the number of units which would be purchased, or, if a slight decrease in the price causes a large increase in sales—the market price which would give the highest net profits to the monopolist would be one that would return only a moderate profit per unit sold. To make a slight increase in the price in order to secure a larger profit per unit, likely would cause such a large decrease in the volume of sales that a decrease in the total net profits would result. But, a slight decrease in the price might cause a sufficient in-

crease in the volume of sales to cause an increase in the net profits, even though a slightly lower profit per unit of sales was received. If the technique of production in a monopolized industry is such that an increase in the volume of production will lower the cost of production per unit of product, and if the market demand for the product is highly elastic, the price which would give the largest net profits to the monopolist would be one which would return only a moderate profit per unit of product. In that case the monopolist could secure large net profits from a large volume of sales at a fairly low profit per unit.

On the other hand, if the demand for a monopolized commodity is quite inelastic—where either a large increase or decrease in the market price would cause only a slight change in the number of units of the commodity which would be purchased in the market—the monopoly price which would return the highest net profits to the monopolist is likely to be one which would give a large net profit per unit of product. A substantial increase in the market price would not result in a material decrease in the volume of sales; neither would a slight decrease in the price result in a significant increase in the volume of sales. Therefore, for a monopolized commodity with an inelastic demand, the highest net profits could be secured at a price level far above the unit cost of production.

Unquestionably, the competitive price theory is a reasonably sound explanation of how, *in the long run*, prices are, or would be, determined for goods which are produced under conditions of competition without any monopolistic restraints. But, many economists make two false assumptions in applying the competitive price theory to the price structure of the modern industrial world. First, many of them falsely assume the monopoly and monopolistic restraints are rare exceptions and that free and unrestrained competition exists in all but a few industries. Second, the majority assume that, if, in the long run, competition tends to set the market price at a level which will equal the cost of production of the marginal producer, it should do so at any given period of time. Because

of these two false assumptions, the prices which actually prevail in our markets are rarely anywhere near equal the cost of production of the marginal producers in the various industries.

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The traditional factor "land" was purposely omitted in the enumeration of the factors of production for which payments are to be made. As a matter of practical accounting land owned by a productive enterprise is treated as "capital investment" upon which interest is to be paid. When the land used by the enterprise is not owned but rented under a contract, the payments therefor are made under the second class of cost factors (payments made to other business enterprises for use of property and for services). The traditional theorist might logically object to the omission of land as a separate factor of production on the ground that "land produces economic rent," which is a surplus return quite different from interest on capital, in which class it is here placed. I am willing to admit the validity of this objection, and then justify my omission of land as a separate factor on the ground that whatever "economic rent" the enterprise may receive from the use of the land in excess of imputed interest on its cost, will go to "pure profit," which is also a surplus return. The fact is that if land owned and used by a business enterprise does not return an economic rent, the enterprise must otherwise earn more than enough to pay the imputed interest on the capital (money) invested in the land in order to secure any pure profits. The same would be true in reference to the use of a building or a piece of machinery purchased and used by the business enterprise. All costs of production must be met before there can be any profits.

The technical student might raise several objections or at least ask several questions concerning our threefold classification of the cost of production factors. He might ask in which class the payments for transportation service would fall. Or, why taxes should be placed in the class with the factors of production.

It is not my intention to enter into a long theoretical defense of this classification but a few words of explanation may be in order. Cost of transportation generally is charged to the price of the goods sold or added to the net price, when it is paid directly by the enterprise selling the goods. If cost of transportation is paid by the buyers of goods or materials purchased, it usually is added by them to the cost of those goods.

If transportation payments are not put into the prices of the goods bought or sold, they should be placed in class two, as payments made to other business enterprises for services rendered.

It may be argued that taxes are payments to the government for services rendered and should, therefore, be placed in class two as payments for services rendered by other enterprises similar to insurance payments. For that matter, it may be argued that taxes should be added directly to the price paid by the buyer just as cost of transportation usually is added directly to the price paid by him. On the other hand, it may be argued that the activities of the government for which taxes are paid do not aid in the creation of new value by the business enterprise as does the use of services from other enterprises or the direct use of labor or capital. There is an element of truth in all of these contentions, and there would be much uncertainty as to how to classify *taxes* as a cost factor if it were not for one important fact: Taxes paid by enterprises must be paid out of the funds received from the net value (new value) created by the enterprises, if their capital is to be kept intact. In short, the net value created by each business enterprise, after paying taxes, is divided in some manner between those who furnish the management and the other factors of production. Since taxes must be paid out of net value, they are placed in the same class as wages and interest.

In order to better understand the meaning of "net value" created by business enterprises, we may consolidate all costs of production into *two* classes instead of three. The first class would include the money value of all materials used in the production process (the amount of money which must be paid to other business enterprises to replace the goods consumed), and the money value of all services hired from other business enterprises in the production process. This class of expenses represents goods and services acquired by the enterprise for the purpose of operating its business; they were acquired for the purpose of adding value in the productive operations.

The second class includes all the money paid for the use of the factors of production of the enterprise, plus all taxes paid. In the first class of cost expense we have all the payments for

the goods and services purchased from other business enterprises and consumed in the productive processes. The values of the goods and services consumed are not destroyed by the productive processes; they are translated into the value of the goods turned out by the productive enterprise. The productive processes create new values to be added to the goods and outside services consumed so that the new goods and services turned out have much greater values than the goods and services consumed in the processes of production. It is this added value to the goods and services used in production which constitutes the *net value created* by the productive business enterprise. The factors of production (labor, capital—land, and management) are directly responsible for the creation of this new net value. Those who furnish the factors of production receive payment for their services out of the proceeds (money) derived from the newly created value or the net production of the enterprise. The payments for the use of the factors of production plus taxes constitute the second class of cost of production expenses. These expenses are paid out of the net production of the enterprises, and whatever is left is pure profits to the owners.

After paying all the costs of production out of the money received from the goods or services produced, the owners of each business enterprise retain the balance, if any, as "pure profits." In order to comprehend fully the theory of pure profits, it is necessary to understand the meaning of "wage of management" as related to "profits," as well as to know the relationships between "interest" and "profits," as conceived by economic theory.

By "wage of management" is meant the wage or salary received, or which is ordinarily received, by the manager of a business enterprise. The managers of many small enterprises are the owners of the enterprises. Many of these manager-owners do not pay themselves salaries but depend upon the earnings from the businesses for their compensation; if there are no earnings they receive no wages or other income. It is claimed by the classical economists that these small owner-managers should receive wages for their managerial functions, and that the management wages should be charged as a part

of the cost of production. The wage of management of the manager-owner should equal the wages he would receive if he were performing the same kind of work for someone else. The classical economists pointed out that if a manager-owner did not receive a wage of management he could not remain in business. Such compensation, they pointed out, could not be classed as profits received; it is a legitimate cost of production expense. Anything the owner-manager received above the wage of management plus the mere interest on the actual capital he had invested in his business was classed as "pure profits."

As a result of the development of the modern corporate form of business organization, there is little difficulty in separating "wage of management" from profits. The officers of the modern corporation receive definite fixed salaries for their services as managers; these salaries are charged as expenses of operation just as the wages of laborers are thus charged. The high officials of the modern business corporations generally are stockholders in the corporations, but their salaries are paid in the same manner as the salaries of the non-stockholder officials are paid, regardless of pure profits or the payment of dividends on the shares of stock. Too often the salaries of large and influential stockholders of corporations are much higher than those same individuals could receive as managers of other corporations in which they owned no stock. To that extent the modern corporation sometimes confuses "wage of management" and profits. But, a mixture of these two factors by paying excess corporate salaries to influential stockholders is not defensible; it is not fair to the other stock-holders who are not on the corporate payrolls; it is not fair to the public to increase the cost of production in any such manner.

Since the beginning of capital investment in business enterprises it has been difficult, if not impossible, in practice actually to separate "interest" and "pure profits." In theory these two factors are distinct and separate. Interest is the payment which must be made for the use of capital (money); pure profits is the surplus earnings of a business enterprise after all costs of production and taxes of the enterprise have been paid. The owners of a modern business corporation generally invest capital (money) in it, for which they receive shares of

stock; they expect to receive "dividends" upon these shares of stock. Dividends paid upon shares of stock which represent actual capital (money) invested in the corporation may consist in part of interest on the capital invested and in part of "pure profits." Dividends paid on "watered" stock (shares which represent no actual capital investment) could not represent interest payments, for these is no actual investment; such payments must be made from pure profits, and when received they represent undeserved pure profits. Dividends which are no larger than the rate of interest the owner of the shares of stock would have received had he loaned to someone else for use the money actually invested in the stock, represent interest payments only. To the extent dividends exceed the prevailing rate of interest on the amount of capital actually invested, they represent pure profits.

It is claimed by practically all owners of shares of stock and by most theoretical economists that it is not only just for stockholders to have the opportunity and privilege of receiving dividends in excess of the prevailing rate of interest on the actual investment in the shares of stock, but that it is necessary for them to have the opportunity to receive such dividends that they may be induced to invest in corporate shares. It is pointed out that the risk involved in the investment of money in corporate shares is great; the investor has no guarantee of any kind of dividend return and may stand to lose the total amount invested. It is claimed that the stockholder should have an opportunity for a large gain in case the business proves profitable, as compensation for the risk he takes of the business being unprofitable. Unquestionably, the maximum dividends allowed on the actual investment in corporate shares should be greater than the loan interest rate prevailing. But, the extent to which dividend rates should include pure profits is a matter of public policy which has not yet been determined. The interest element of dividends may be measured by the prevailing rate of interest on safe loans or investments, such as high grade corporate bonds and government securities.

As indicated already, pure profits are surplus returns to the owners of business enterprises. The amount of pure profits which any particular business enterprise will be able to earn,

according to the theory of profits, will depend upon its relative efficiency as compared with the efficiency of the marginal enterprise in that industry. As already indicated, pure profits are often justified upon the ground of the risk owners take in investing their money in their businesses. Pure profits also are justified on the ground that the receivers contribute superior productive efficiency to industrial society and should be compensated accordingly. This justification of profits assumes, first, that the products of each enterprise are sold in a highly competitive market, and, second, that there is a uniform expense per unit for each factor of production to all competing enterprises and that all their supplies are purchased in a highly competitive market. That is, the theory assumes that all enterprises in an industry sell at the same prices, and that they buy supplies and services in the same markets at the same prices and pay the same rates of wages to laborers and the same interest rates on capital used. Under such assumed conditions the profits of any one enterprise would depend on the relative efficiency of the managers of the enterprise in utilizing the factors of production while fabricating the goods or services turned out. The manager who used the greatest skill in combining and utilizing the raw materials, the labor, and the capital employed, would make the largest profits. Therefore, theoretically, pure profits are due to efficiency of management.

Upon the basis of the competitive theory of profits some theoretical economists have concluded that, as industry approaches maturity, pure profits tend to become less and eventually will disappear. They claim that competition will eliminate the inefficient enterprises and that the standardization of products and the methods and technique of production will tend toward a uniform cost of production for all remaining enterprises. It is thought that competition in the sale of products will keep the price at or near the cost of production and pure profits for all will disappear.

The trend of the development in the industrial world under the laissez-faire policy for the past half-century has shown the fallacy of the theory that profits will become less and eventually disappear. Contrary to the theory, the standardization of goods and the mechanization of methods of production in certain

industries have resulted in increase rather than decrease of pure profits. The fundamental reason why profits have increased rather than decreased in the standardized industries is because the growth of mass production and the standardization of products have been attended by restraint of competition in the sale of the products of those industries. In short, the assumption of the existence of unrestrained competition in the sale of products in each industry (which is one of the fundamental assumptions upon which "the theory of pure profits" is based) has proved to be false as applied to the development of mass production in modern industry. The growth of monopolistic restraints in the sale of goods has more than kept pace with the development of standardization of goods and improvements in methods of production. "Profits" in modern big business partake more of the nature of monopoly gains and special advantages than they do of pure profits.

Of course, the assumption of equality of opportunity as between competing enterprises was never actually true as applied to the business world. The theory of pure profits assumes that each business manager has the same opportunities and advantages as all his competitors in purchasing or hiring goods, services, labor, and capital in the market. This assumption was never actually true and is less true today than it was a half-century ago. The development of "bigness" of business enterprises in most industries has given big enterprises many advantages over their little competitors in purchasing goods and services, and in the employment or hiring of labor and capital. Because of these advantages, the *big* enterprises often are able to make larger profits than their smaller competitors even though the small enterprises may have managers equal or superior in efficiency to the managers of the big competitors.

The advantage in buying, except in a completely monopolized or regulated market, has been always with the large buyer. Ordinarily the seller is willing to sell a large quantity of goods at a lower price per unit than he would a small quantity. The costs and uncertainties of selling are reduced to a minimum when a producer is able to sell his total output to one or a few buyers. For this reason, the large buyers are able often to

purchase both goods and services at lower prices than could the small buyers. In buying goods the large manufacturers and the large merchandizing establishments (chain stores) have a great advantage over their small competitors.

Also, in the employment of capital (borrowing money) the large business enterprises have a definite advantage over their small competitors. Because of the comparative safety of security and wider market in which to borrow, the large enterprises in each industry are able to borrow money at lower rates of interest than the small competitors are compelled to pay for the money they borrow. The chain store may sell its notes in the national discount market at a low rate of interest, while the local merchant may be compelled to borrow from the local bank at a comparatively high rate of interest.

Frequently, the large business enterprises are able to employ laborers at smaller wages than their competitors pay. This is particularly true in the large cities in retail merchandizing business, where the large department stores pay their clerks less than do the smaller stores. It is true also in some of the monopolistic manufacturing industries, where the "trusts" cut wages below the wages paid by their smaller competitors. There are, of course, instances where small enterprises in some industries pay lower wages than do the larger enterprises in those industries. But, on the whole, the large enterprises pay a smaller rate of wages for the same class of work than do the small enterprises.

Those enterprises which make profits by paying lower wages than their competitors have been called "chiselers." In much of the popular discussion of "chiselers" it has been assumed that those guilty of paying very low wages were the small enterprises only. That assumption has never been proved, and in my opinion, it is untrue. An enterprise which buys at lower prices than those paid by competitors may be called "chiselers" also. The "chiselers" of this class certainly are the large business enterprises. To secure goods and services below the prices paid by competitors may be said to be "chiseling" a profit out of the selling business enterprises.

Profits may be due partly to superior efficiency in management. They may be due to monopoly advantages, or they may

be due to advantages in purchasing the factors of production. But the large profits in the modern business world certainly are due less to superior efficiency in management than they are to advantages in selling in a restrained or controlled market, and to opportunities of purchasing materials, labor, and capital at prices below those paid by competitors.

It has been pointed out that there is a definite theoretical distinction between interest and profits; that interest is the payment for the use of capital (money), and that profit is a surplus return which goes to the owners of business enterprises after all costs of production are paid. While the return on capital has no theoretical connection with pure profits, in the world of practical business finance, capitalization and profits are intimately connected. There is a tendency for business managers to assume that the investment in a business (the capital) is worth whatever the business is able to earn. It has been a fairly definite business policy to capitalize business corporations upon the basis of their current or prospective earning power, regardless of the amount of actual capital (money) invested in the enterprise or the corporation by the stockholders. If the amount of money actually paid into a corporation for its shares of stock is one millon dollars and it is able to earn sufficient profits to pay substantial dividends on two million dollars capitalization, the nominal capital often will be raised to that amount by issuing an additional one million dollars of shares of stock as a stock dividend. Frequently, also, the organizers of business corporations over-capitalize their concerns by issuing shares of stock with a par value much in excess of the money actually paid for the shares. They do this with the expectation that their concerns will earn profits sufficient to pay dividends on this "watered stock." In order to avoid the odium attached to issuing "watered stock," many of the organizers issue shares of stock with no par value. In this manner they completely merge "interest" on capital (invested in the stock) and "profits." Most shareholders look upon dividends on shares of stock as being profits only, yet they look upon their shares as being so much capital invested.

As a result of the frequent capitalizing of current or prospective earnings, the capitalization of many large business

corporations has no relation to the actual amount of money invested in the corporation by the shareholders. This procedure has enabled many business enterprises to cover up the actual excess profits made, and to convert those excess profits into a normal charge upon "cost of production" as if the dividends were interest on actual capital invested in the businesses. In accounting procedure, dividends are paid out of "profits," and do not constitute a part of the "cost of production." But from the legal point of view at least, public utilities have a right to a reasonable return on their capital investment. In court decisions, "capital invested" is too frequently confused with "earning power" and "capitalization," as they were in the O'Fallon rate case. There is a tendency for investors and the public in general to make a similar mistake, and regard dividends as earnings on capital invested, regardless of the actual amount of money received by the corporation for its shares of stock. That part of dividends which equals a fair return on the money received by the corporation for the stock, should be looked upon as a legitimate return on actual capital invested, all in excess of that return is a surplus return not easily defensible. This surplus return should not be concealed by overcapitalization or the issuance of watered stock.

APPENDIX D

WAGE AND PROPERTY INCOME

ONE of the most important problems today confronting our capitalistic economic society is that of the division of available national money income (the proceeds of production) among those who furnish the factors of production. This problem generally is referred to as the problem of the "*distribution of wealth*"; it might better be referred to as the problem of the "*division of the national money income among the factors of production.*" It is the problem of dividing the proceeds of production between those who furnish labor, land, capital, and management in production.

Theoretical economists have developed definite theories as to how the money income is divided or as to how wealth is distributed. Those who furnish labor get a part of the national money income as *wages*, those who supply land in production receive a part of it as *rent*, those who furnish capital receive a part of it as *interest;* and those who operate the business enterprises receive the balance in the form of *profits*. In the competitive profits theory[1] it was assumed that managers of business enterprises entered the market and purchased the needed labor, land, and capital at the prevailing market prices for each factor. There are definite theories of how the market prices for the use of labor, land, and capital are determined. A brief statement and discussion of these theories will give a better understanding of how the national money income is, or should be, divided among the factors of production.

There are several theories of how wage rates are determined. The oldest of the wage theories is that the rate of wages is determined by the cost of the minimum of subsistence of the

1 Discussed in Appendix C.

corporations has no relation to the actual amount of money invested in the corporation by the shareholders. This procedure has enabled many business enterprises to cover up the actual excess profits made, and to convert those excess profits into a normal charge upon "cost of production" as if the dividends were interest on actual capital invested in the businesses. In accounting procedure, dividends are paid out of "profits," and do not constitute a part of the "cost of production." But from the legal point of view at least, public utilities have a right to a reasonable return on their capital investment. In court decisions, "capital invested" is too frequently confused with "earning power" and "capitalization," as they were in the O'Fallon rate case. There is a tendency for investors and the public in general to make a similar mistake, and regard dividends as earnings on capital invested, regardless of the actual amount of money received by the corporation for its shares of stock. That part of dividends which equals a fair return on the money received by the corporation for the stock, should be looked upon as a legitimate return on actual capital invested, all in excess of that return is a surplus return not easily defensible. This surplus return should not be concealed by overcapitalization or the issuance of watered stock.

ucts or services of the enterprise by the work of the last laborer employed. Represented graphically, the last laborer is the final unit of labor which the employer finds it advisable to add to his staff. The point at which the employer no longer finds it advisable to add an additional employe is determined by the principle of proportionality of the use of the factors of production. According to this principle, the marginal productivity of each additional laborer hired—the last increment of value added to the product or service by the last unit of labor—decreases after a certain proportion between the number of units of labor, capital, and land employed has been reached by a business enterprise.

It is held by many theorists that each employer will continue to employ additional laborers until the marginal productivity of the last laborer added to the staff is just equal to the wages which must be paid to all other workers in that class. When this point is reached, if additional workers are employed, they must be taken on at lower wage rates, it being no longer profitable to pay according to the prevailing rates for non-marginal employes. On the other hand, the theory assumes that if the wage rates are below the marginal productivity of labor in general, and all the laborers are employed, competition between employers for labor will cause higher bidding for laborers and thereby force the rates to rise—in short, there would be a shortage of labor at the prevailing wage rates. The marginal productivity wage theory holds that the supply of labor and the demand for labor is equalized eventually by a scale of wages which is equal to the marginal productivity of the different classes of laborers.

There is an inference of justice in the marginal productivity theory of wages, which inference, if the theory were a correct explanation of how wages are determined, is not true necessarily. The inference is that laborers receive that which they produce—wages equal to their marginal productivity. It is unsound to assume that the marginal productivity is a true measure of what laborers produce. If such were the case a slight increase in the number of laborers resulting in a large decrease in the marginal productivity of laborers in a particular enterprise would result in a great decrease in the productivity of the

laborers in that enterprise. Clearly such would not be the case, even though the employer was enabled to reduce wages because of the decline in the marginal productivity of his laborers.

The whole marginal concept is based on the assumption that the price (value) of the products of each enterprise is set by some outside force and that the division of the money received from the net value of the production of the enterprise will be determined by the marginal productivity of each factor of production. As a matter of fact, the cost of production is one of the most important elements which determine the value or price of the products. An increase in wages will increase the cost of production and may result in an increase in the price or value of the products of the enterprise. An increase in the price of the products of an enterprise will bring about a new marginal productivity of laborers in that enterprise. An increase in wage rates will bring about a readjustment in all cost factors and in prices so that business enterprises may be able to pay the increased wages without operating at a loss. The relationships between prices, wages, interest, and profits are relative, not fixed. As a matter of fact, an increase in wages without a corresponding increase in the price of the products results in a decrease in profits and eventually will cause a decrease in interest and rents. If it is assumed that the new lower rate of profits and interest is normal, the marginal productivity of laborers would be increased as a result of the higher wages. Marginal productivity of labor is not a definitely fixed thing; it is a relative thing. But the marginal wage theory assumes that marginal productivity is an absolutely fixed quantity.

One of the most important practical objections to the marginal productivity theory of wages is, that ordinarily it is impossible for an employer in modern industry to measure accurately the additional value added as a result of the work of a particular laborer. Again, the theory is incorrect in assuming that there is always a gradual decline in the marginal productivity of laborers as additional laborers are employed in a business enterprise. Generally such is not the case in modern industry. The factory at a given time has a given number of machines to be operated and a given amount of work to be performed to keep the plant operating at full capacity. If the factory is short one

laborer, it may be very expensive to the management—the marginal productivity of that laborer would be high, but if this one place is filled, an additional laborer would be practically useless.

Laborers may be displaced by new machines (capital) because the cost of the machines is less than the cost of the laborers displaced. Such displacement of laborers occurs principally because of the invention of new machines or improvements in existing machines, not because wages were above the marginal productivity of laborers. New and improved machines result in an increase in the production per laborer employed, and therefore logically increases the productivity of labor as a whole, as well as the illusive marginal productivity of laborers employed. Certainly, technical improvements in capital equipment enable employers to pay higher real wages to laborers; but, the displacement of laborers caused by the technological improvements may create a surplus of laborers and permit employers to reduce real wages rather than increase them. Such a result is contrary to the marginal productivity theory of wages.

At any given time a definite number of laborers would be necessary to operate the different business enterprises of the country at full capacity at eight hours per day. Assuming that the number of laborers was just short of the number required to operate all the enterprises at full capacity, there would be a shortage of labor, if business conditions were such that all the enterprises attempted to operate at full capacity. Wage rates would rise as a result of the bidding of employers for additional laborers. But, if business conditions were such that business enterprises operated at 75 per cent of capacity, there would be a surplus of laborers and a decline in wages, because laborers would bid against one another for jobs. Also, suppose that technological improvements in methods of production (new automatic machinery) made it possible for industry to operate at full capacity with 25 per cent fewer laborers, there would again be a surplus of laborers and a decline in wages because of competition for jobs. The relative bargaining power of employers and employes has far more to do with determining wage scales than the theoretical marginal productivity of laborers.

It is true that the amount of productive capital equipment at any one time will limit the number of laborers who may be employed. An increase in the number of business enterprises and in the amount of capital employed may tend to increase the number of jobs. But, for the time being, an improvement in the character of the capital equipment will tend to decrease the number of jobs available. If an improvement in the nature of the capital equipment occurs simultaneously with an increase in the amount of employed capital, the effects of the first may nullify entirely the effects of the second, and there would be no increase in the number of jobs, though there would be a great increase in production. If there is a decrease in the number of jobs there will be a decline in wage rates regardless of changes in the theoretical marginal productivity of laborers. Again, we may repeat that the relative bargaining power of employers and employes in reference to wages has more to do with setting the prevailing wage scales than any other force.

Economic rent as originally discussed by the classical school is a surplus return which good land gives the owner as compared with poor land or marginal land—land that will just pay for cultivation. According to modern economic theory, the amount of economic rent which a particular piece of land will yield is measured by the difference between the value of the products produced and the capital and labor cost of producing those products. The maximum economic rent on a piece of land can be secured by cultivating the land up to the margin of intensive cultivation; that is, where the last laborer and the last unit of capital added will produce just enough additional products to pay for those last units.

A substantial share of the national money income is supposed to be paid out on account of economic rent. In agriculture this is supposed to be particularly true. Lands can be rented by the acre, under a contract for so much per annum because those lands produce an economic rent as great as or greater than the contract rent. Both the economic and contract rents received from agricultural lands are generally absorbed either as interest on the investment in the lands or as interest on the mortgages covering them. Unquestionably, the fertility of agricultural lands make them valuable because they produce

an economic rent. Because of the repeated sales of agricultural lands the present and prospective economic rent of those lands has been fully capitalized, if not overcapitalized, so that the rent income from land is looked upon by the present landowners as a return on capital invested in the land. There are many cases where the interest on the mortgages on the land is much larger than the economic rent derived from the land. In such cases the rent has been overcapitalized.

Except in cases of royalties paid on natural resources used in production, the returns on lands used by industrial enterprises are so interwoven with the return on capital and with profits that it would be impossible to separate the different elements into rent, interest, and profits. The land and natural resources owned by business enterprises are purchased for business uses and become a part of the capital investments of those enterprises. The economic rent derived therefrom becomes *earnings* on capital investment and may be paid out as interest on borrowed capital or as dividends to owners. When the economic rent of land or resources owned by business enterprises increases, the capital investment appreciates (or is written up in value), just as the sales price of agricultural land rises with an increase in its economic rent. Just what part of the appreciation of the capitalization of business enterprises has been due to the rise in the value of natural resources owned is not known. It is known, however, that a large part of the capitalization of the railroads is due to appreciated land values. A large part of the earnings of many business enterprises is due to advantageous site value of the resources they own. In this sense rent does absorb a substantial proportion of the money income paid out by business enterprises. Many present-day economists see rent not merely as a surplus derived from the productivity of the better grades of land over the marginal land, but a surplus return that any factor of production may return to its owner because of its superiority of quality on productivity.

Interest is what is paid for the use of money when borrowed. Pure interest is paid for the use value only, and does not include any payment for insurance against loss of principal. The interest rate upon a United States government bond is generally referred to as a good example of pure interest without

any charges against possibility of loss of principal. Most interest charges, such as the interest charged individuals by banks on loans, include insurance charges against losses. The interest rates paid by business enterprises to lenders include charges against possible losses on the principal loaned. In practice it is not always possible to separate insurance charges and pure interest in loan contracts.

Interest must be paid because owners of capital (money) would not give up its use unless they received some compensation in return. Interest can be paid because the use of capital goods into which money can be converted produces new value—because capital is productive. In terms of the economic theorist, the rate of interest at any one time will be that rate which equalizes the demand for new capital and the supply of new savings (or of loanable funds). According to accepted economic theory, at any one time the demand for new capital is limited by the marginal productivity of new or additional units of capital in each business enterprise borrowing. The business manager could not afford to pay an interest rate in excess of the marginal productivity of the new capital he borrowed; he might pay a rate almost as great as the marginal productivity if competition forced him to do so.

Theoretically, the supply of loanable funds is limited by the amount of the current savings of the population. Over a long period of time the new additions to the nation's capital fund must come out of savings from the national money income. The saving of a part of the current money income is accomplished by foregoing the spending of all of it to satisfy immediate wants. Saving, therefore, is supposed to be a sacrifice for which the individual must be rewarded by the possibility of the satisfaction of a large want in the future. It is claimed by some theorists that the current interest rate must be high enough to compensate the savers for their sacrifice in postponing immediate consumption. Doubtless, high interest rates will have some influence in inducing greater savings on the part of many people; but the most positive influence of high interest rates is that they result in higher incomes for those who are able to make great savings.

Little personal sacrifice is experienced by those who make the bulk of the current saving in the United States. The bulk of our industrial savings is made by people and by corporations that have very large incomes, who are able to satisfy normal wants and make large savings from their surplus incomes. It would indeed be a sacrifice for many of the large income receivers to spend all their incomes. Large national savings are made during periods of prosperity, not because larger sacrifices are made at that time, but because incomes are larger. At such times large savings would be made regardless of the interest rates which prevailed.

Over short periods of time, the supply of loanable funds is not limited by the current savings of the public. A large part of the expansion of loans during prosperous periods comes from the increase in bank credit, and not from current savings. During depression periods current savings are used to pay off bank loans previously secured. The demand on the part of profitable business enterprises to borrow money will greatly increase the supply of loanable funds by inducing an expansion of bank credit. It is doubtful if the quantity of current savings has any appreciable influence on interest rates. Certainly the current rate of profits in business has more influence in causing interest rates to rise or fall than does the flow of current savings.

While the level of the interest rate has fluctuated widely over short periods of time, the average level has hardly changed for the past four hundred years. It is doubtful if this fact can be explained on the ground that savings have just about kept pace with the demand for new capital. It would be truer to say that the demand for new capital has adjusted itself to current savings loanable at a fairly constant rate of interest. Unquestionably, the general rate of interest has been influenced considerably by the general level of profits in business. The owners of loanable funds have had the option of investing in business enterprises as owners or of loaning the funds to others. If the probabilities of safety and profits from direct investment in business were very favorable, the owner of loanable

funds would lend them only at a high rate of interest. As we have seen, the theory of profits is that competition will keep profits from rising much above the level of the wage of management. We have seen, also, that the theory is fallible.

APPENDIX E

A portion of the public statement on the proposed banking act of 1935, issued on April 21, 1935, by Senator Duncan U. Fletcher, Chairman of the Senate Committee on Banking and Currency.

IN MY opinion, the proposed banking act of 1935 is, in all probability, the most important piece of banking and monetary policy legislation with which this or any other Congress has dealt. This statement is based upon the importance of title II alone; and, curiously enough, title II of the bill is bearing the brunt of almost all the opposition made to the entire piece of legislation. Please be advised, however, that all of those who are offering concerted opposition to the bill on the basis of the incorporation of title II are almost spontaneous in their clamor for the enactment of titles I and III.

"Hence, I shall deal only briefly with the first and third titles of the bill. The first title provides for the merging of temporary deposit insurance funds into permanent funds, that $5,000 be designated as the maximum insurable deposit for assessments, withdrawal from the fund, buying assets of insured closed banks, and a number of other important matters. The third title provides for 'accidental' holding-company affiliates, security affiliates in liquidation, security dealers accepting deposits, employes' deposits, liquidation of assets of banks in voluntary liquidation, termination of double liability, examinations, and a number of other important matters.

"Title II, on the other hand, deals almost wholly with the creation of machinery for the effective regulation of a definite monetary policy in accordance with the campaign promises of President Roosevelt based on the Democratic platform of 1932 which advocated 'a sound currency to be preserved at all

hazards' and proposed to put an end to 'the indefensible expansion and contraction of credit for private profit at the expense of the public.'

"Moreover, it is a definite attempt to accomplish the ends which the President had in mind when on July 3, 1933, he stated to the American delegation to the London Economic Conference and again re-affirmed on October 22 in his address to the American people in which he stated that 'when we have restored the price level, we shall seek to establish and maintain a dollar which will not change its purchasing and debt-paying power during the succeeding generation. I said that in my message to the American delegation last July and I say it now once more.'

"This bill among other things provides that:

"(1) 'The offices of governor and chairman of the board of directors of each Federal Reserve bank shall be combined.' In their places a governor and vice governor 'shall be appointed annually by the board of directors, subject to the approval of the Federal Reserve Board. The governor shall be the chief executive officer of the bank.'

"Whereas in the original Federal Reserve Act the executive head of the bank was to have been known as chairman of the board of directors and at the same time act in the capacity of Federal Reserve agent, the active head in control of purely banking operations was to function in the capacity of a bank manager. The Federal Reserve banks gave to the bank manager the high-sounding name of 'governor.'

"Since that time it has developed that the governor of each Federal Reserve bank has not only superseded the chairman and agent as the executive officer of the bank but has also become the virtual dictator of the Federal Reserve bank to the extent of practically controlling the election of directors who are presumed to be independent in the exercise of their power in the election of said governor. The results are obvious.

"The above provision of the bill merely merges the two offices and at the same time provides for the retention of all governors and chairmen—if they are qualified and if, subject to the approval of the Federal Reserve Board, the various boards of directors elect them governor and vice governor. At the same

time the language of the bill makes it clear for once that banks cannot evade or over-ride the law through the creation of a high-sounding office and wrest control from the Board by creating a dictatorship within the Federal Reserve System.

"The bill further provides that:

"(2) Prior to July 1, 1937, the Federal Reserve Board may waive the capital requirements for the admission of non-member state banks as members of the Federal Reserve System.

"It is intended through such a provision to recognize the fact that small banks—that small state banks—are not mere 'pawn shops.' It is in recognition of the fact that smallness and bigness in a bank's capitalization, deposits, investments, or loans is not an indelible evidence of either soundness or weakness. The success or failure of a bank depends primarily on its management and not on its size.

"It is a recognition of the fact that there are thousands of small state banks in this country which are worthy of membership in the Federal Reserve System. On the other hand, it absolutely does not provide a license for, or inducement to, the inclusion of unsound banks, or of undercapitalized banks, within the Federal Reserve System. Assuming an unbiased and unprejudiced administration of the act in accordance with the intentions of Congress, there should result no unfair treatment of, or impositions on, either state banks or national banks under the provisions of this section.

"The next provision to which I wish to call your attention is:

"(3) 'In selecting the six appointive members of the Federal Reserve Board the President shall choose persons well qualified by education or experience or both to participate in the formulation of national economic and monetary policies.'

"Moreover, each director is to receive a salary equal to that of a member of the President's Cabinet, and shall be retired at the age of seventy upon a retirement wage to be paid out of funds derived from levies on Federal Reserve banks.

"Such a provision is conceived in the public interest. It provides for no favoritism between bankers, lawyers, economists, manufacturers, or men from any other profession. The administrative duties of a Board member are such as to require a far broader experience and basis for the exercise of

sound judgment than that derived from the narrow confines of any one profession. Please note that the section reads: 'The President must [shall] choose persons well qualified by education or experience, or both, to participate in the formulation of national economic and monetary policies.'

"That is a mandate.

"The next three points to which I wish to direct your attention are of the greatest vital importance. They have to do with the Federal Open Market Committee, flexibility of reserve requirements, and discounts.

"They are, in order of sequence, numbered (4), (5), and (6).

" '(4) The creation of a Federal open market committee consisting of five members, three of whom shall be members of the Federal Reserve Board, the other two to be governors of the Federal Reserve banks selected by all the governors of said banks. Their terms of office shall expire at the end of each calendar year. Said committee shall have supervisory control over the open market operations of the Federal Reserve banks.'

" '(5) The Federal Reserve Board is empowered to change the reserve requirements of member banks as to any or all Federal Reserve districts and/or any or all classes of cities and as to time and/or demand deposits.'

" '(6) Subject to such requirements as to maturities and other matters as the Federal Reserve Board may prescribe, any Federal Reserve bank may discount any commercial, agricultural, or industrial paper and may make advances to any such member bank on its promissory notes secured by any sound assets of such member bank.'

"The first question which arises in connection with these three provisions is as to whether they involve a radical change in the present powers and functions of the Federal Reserve Board and the Federal Reserve System as it is now constituted. The second question is as to whether there will be established a political dictatorship of banking.

"The unequivocal answer to the first—aside from a technical splitting of hairs—is no. To the second an unequivocal answer of no must be given.

"It is a fact that all of the powers which are by this bill centralized in the Federal Reserve Board have since the enactment

of the original Federal Reserve Act existed within the Federal Reserve System. That is, all open market powers dealt with in title II of this act exist in the present law, and were so read into the original act by the 'governors' of the Federal Reserve banks, as I shall subsequently point out. But it also must be mentioned that when any or all the Reserve banks, the Reserve Board, or the Treasury, through its stabilization fund, engage in open market operations, they depart from and transcend the field of banking and become engaged in operations foreign to banking per se.

"That is, when banks or the Board engage in open market operations, they are buying and selling money; they are expanding and contracting the total volume of money; they are laying the foundation for inflation, deflation, and economic chaos if intelligence and prudence are not exercised in accordance with the sound principles of monetary science.

"Such principles are not one and the same with even those of sound banking, where private profit is predominant. On the other hand, the principles of monetary science to which I refer are the principles of national monetary policy operations which absolutely must be made to conform with a public interest which oftentimes is directly opposed to the private-interest motives of bankers if they are to be administered in the interest of the general public."

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UNIVERSITY OF OKLAHOMA PRESS

PUBLISHING DIVISION OF THE UNIVERSITY

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