Volume Title: The Great Contraction, 1929-33

Volume Author/Editor: Milton Friedman and Anna J. Schwartz

Volume Publisher: Princeton University Press

Volume ISBN: 0-691-00350-5

Volume URL: http://www.nber.org/books/frie65-1

Publication Date: 1965

Chapter Title: Director's Comment

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Chapter URL: http://www.nber.org/chapters/c9281

Chapter pages in book: (p. 125 - 130)

Director's Comment

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THE National Bureau affords its directors the privilege of submitting a "memorandum of dissent or reservation" to a manuscript accepted for publication. What I am submitting are neither dissents nor reservations, but a questioning comment. I have read the manuscript twice, in original draft and in final galley proof. I eagerly await the more pleasant reading afforded by a published volume, where tables appear in context and charts, by their presence, remove that need for faith, defined by St. Paul as "the substance of things hoped for, the evidence of things not seen." This volume, if my judgment is sound, is one of the truly great ones published by the National Bureau. Its breadth of scope, its penetrating use of analytical tools to set forth, dissect, and in a sense reconstitute, as it might have been, nearly a century of the monetary history of the United States, has created a finished product that I will reread more than once with enjoyment coupled with a conviction that time so spent is profitably employed. My questioning is not of the logic of a brilliant presentation, but of an underlying assumption. My brief comments will be based largely upon the period 1929–33. The authors state, in their summation of the period, "There is one sense—and, so far as we can see, only one—in which a case can be made for the proposition that the monetary decline was a consequence of the economic decline. That sense is not relevant to our main task of seeking to understand economic relations, since it involves relying primarily on psychological and political factors" (p. 691).

We are inevitably, in varying degrees, influenced by our background and environment. Mine compels me to place much greater weight upon these "psychological and political factors" than the authors would be willing to concede. I am a businessman by profession, an amateur economist by avocation. My doctor's degree in economics regrettably lies nearly half a century in the past; my few years of university teaching are almost as remote; competitive business, a combination of industry and finance, has been my profession since 1926. To me, business is simply decision making and calculated risk taking. Decisions are not always easy, and the risk taking is real; I survive by virtue of my competitors' mistakes—if they did not make about as many as I do. I would be an ex-businessman. It has been burned in upon me that monetary policy, in final analysis, acts on men whose conduct is not predictable; it neither operates in vacuum nor in a world in which all other factors can be taken as constant.

The difficulty of predicting the impact of economic measures was faced in the *Third Report* of the British Council on Prices, Productivity and Incomes, generally assumed to have been written by Sir Dennis Robertson.[1] After some 72 sections attempting to analyze the situation and weigh the probabilities, there follows: "But no precise judgment of the balance of all these factors is possible; economic restraints and incentives operate on men's minds where it is not possible to forecast their precise effects; they operate also in circumstances which are constantly changing." And Lord Keynes, here a "decision maker." told the 1931 annual meeting of the investment trust of which he was chairman: "I have reluctantly reached the conclusion that nothing is more suicidal than a rational investment policy in an irrational world" (quoted from memory, without verification of exact phraseology). He also states in his *Treatise on Money:* "To diagnose the position precisely at every stage and to achieve this exact balance may sometimes be, however, beyond the wits of man."[2] One final example: Sir Henry Clay's biography of Lord Norman[3] tells of the head of the Bank of England. physically exhausted but feeling that the international monetary system was temporarily under control, yielding to doctors' orders and taking a brief cruise on the Mediterranean—to be greeted when the ship put into port with the news that Britain had gone off gold!

The authors of this volume in discussing the silver situation (1893–97) recognize the importance of psychological and political factors when they say. "the entire silver episode is a fascinating example of how important what people think about money can sometimes be. The fear that silver would produce an inflation sufficient to force the United States off the gold standard made it necessary to have a severe deflation in order to stay on the gold standard" (p. 133).

I have often wished that Professor Taussig had included, in the economic text I studied, a chapter on the force of momentum. Value, I was taught, was the determining long-run factor. and deviations in price from value, short term and self-correcting. I learned the force of a spiraling downward momentum. feeding on emotional fear, during the 1929–33 period, and experienced a replay during the confidence crisis and stock market debacle of the spring of 1962. A nonstatistical view

[1] London, H.M. Stationery Office, July 1959, p. 25, paragraph 73.
[2] New York. Harcourt, Brace, 1930, Vol. I, p. 255.
[3] *Lord Norman,* London, Macmillan, 1957.

of the psychology of the 1929-33 period was presented in a paper delivered by J. M. Barker (university teacher, banker, and senior official of Sears, Roebuck & Co.) before a midwestern conference of bankers in 1936, from which I quote:

> Whenever you have a group of people thinking the same thing at the same time you have one of the hardest emotional causes in the world to control. The more people that are thinking the same thing the more surely you are at the mercy of unreasoning, emotional mob psychology as a cause, with sometimes dire economic effects. . . . If you consider the universality of the speculative mania of the later days of the last boom, you will see how completely the people of this country, to say nothing of the world, were under the influence of the mob psychology of unreasoning, emotional cupidity. When the break came, cupidity turned into unreasoning, emotional, universal fear. . . . In every city of this country, business men, hard hit or already wiped out in the stock market in the earlier part of the crash, were still watching the quotations every day to see how things were going. They saw the market dropping, dropping, dropping. Is there any doubt they made their decisions from day to day under the influence of the emotional backgrounds formed by their observations of the falling security prices?

The authors are highly critical of Federal Reserve policies. The continuing conflicts within the system are convincingly documented: Board. Open Market Committee, and individual Reserve Banks—they call to mind the line from one of Ibsen's plays that runs: "When the devil decided that nothing be accomplished, he appointed the first committee." The authors' diagnosis: "The bull market brought the objective of promoting business activity into conflict with the desire to restrain stock market speculation. The conflict was resolved in 1928 and 1929 by adoption of a monetary policy, not restrictive enough to halt the bull market yet too restrictive to foster vigorous business expansion" (pp. 297-298). Their conclusion that "the Board should not have made itself an 'arbiter of security speculation or values' and should have paid no direct attention to the stock market boom" (p. 291) is one I am not sure I can accept. With holding company superimposed on holding company, call loans for "others" mounting by the billion, and momentum feeding on itself, the monetary ease that would have "fostered vigorous expansion" might well have cumulated economic maladjustments whose correction was merely postponed. As it was, when the break came, "as in pre-Federal Reserve times, J. P. Morgan and Company assumed leadership of an effort to restore an orderly market by organizing a pool of funds"—yet "by the second week after the crash the phase of organized support of the market was over" (p. 305). This was a different kind of depression.

With possibly unjustifiable oversimplification in description on my part, the basic weapon in the authors' arsenal may be termed their concept of high-powered money. Their treatment of its role is consistent and brilliantly analytical in depth. One point only disturbs me. There is no question as to the mathematical demonstration. If high-powered money could be increased by the Federal Reserve without that very move setting other forces in motion, unpredictable both as to source and intensity, I would have no reservations. I lack competence to pass judgment. This is not a controlled experiment, with high-powered money increased, and all other factors remaining constant. Depositors were watching their banks. "One of the reasons New York City banks were said to be reluctant to borrow from the Reserve Bank was the fear that Europeans would interpret borrowing as an indication of weakness" (p. 317). "The aversion to borrowing by banks . . . was still greater at a time when depositors were fearful of the safety of every bank and were scrutinizing balance sheets with great care to see which banks were likely to be next to go" (p. 318). To borrow from the RFC was the kiss of death: "the inclusion of a bank's name on the list was correctly interpreted as a sign of weakness, and hence frequently led to runs on the bank" (p. 325). It is difficult today to recall "the dominant importance then attached to the preservation of the gold standard and the greater significance attached to external than to internal stability, by both the System and the community at large" (p. 363). Summarizing, in the words of Lord Keynes: "If we are dealing with a closed system, so that there is only the condition of internal equilibrium to fulfill, an appropriate banking policy is always capable of preventing any serious disturbance to the *status quo* from developing at all. . . . But when the condition of external equilibrium must also be fulfilled, then there will be no banking policy capable of avoiding disturbance to the internal system."[4] A parallel reading of Professor Chandler's biography of Benjamin Strong[5] and that of Lord Norman by Sir Henry Clay should leave no doubt that we were dealing with no closed system: the extent of the erosion of newly created high-powered money would be one measure of the "disturbance to the internal system" that I (with what justification I am not capable of answering) would not treat lightly.

The authors ask, "Why was monetary policy so inept?" and answer, "We trust that, in light of the preceding sections of this chapter, the adjective used . . . to characterize monetary policy during the critical period from 1929 to 1933 strikes our readers, as it does us, as a plain description of the fact. The monetary system collapsed, but it clearly need not have done so" (p. 407). The monetary policy certainly was unsuccessful, and probably the characterization of "inept" is justified. With respect to the final statement that the collapse of the monetary

[4] *A Treatise on Money*, Vol. I, p. 349.
[5] Lester V. Chandler, *Benjamin Strong*. Washington, D.C., Brookings, 1958.

system was unnecessary, this I cannot feel has been proved. To me, each move in the high-powered-money arsenal involves a calculated risk. If its impact on men's minds is favorable, possibly even if it is neutral, the arithmetical results postulated by the authors follow as night after day. I merely cite at this point the earlier quotation from the report of the British Council on Prices, Productivity and Incomes. If those moves were deemed inflationary and "unsound," the results could have been other than those desired. In that day a citizen fearing devaluation could choose gold rather than paper, and the international flow of gold, seeking safety, was as unpredictable as that of a gun loose on a battleship pitching in heavy seas. The authors may well be right; they are outstanding monetary economists—but I would prefer the terms "possibly" or conceivably "probably" rather than "clearly" need not have happened.

If my recollection is correct, the most striking illustration of the potentialities of high-powered money are those cited in connection with the five-month period ended January 1932, in which deposits fell by $5,727 million. "The provision of $400 million of additional high-powered money to meet the currency drain without a decline in bank reserves could have prevented a decline of nearly $6 billion in deposits" (p. 346). Mathematically this was possible. Reviewing the economy in the United States at that time, and the situation in both Britain and Central Europe, I cannot believe that what in theory "could" have happened, in actuality "would" have happened.

There is a well-documented analysis of what would have happened had one billion dollars of additional high-powered money been introduced into the economy during any one of three strategic periods in the great depression: (1) January 1930 to end of October 1930, (2) January 1931 to end of August 1931, and (3) September 1931 to end of January 1932. Were a Lloyds to underwrite the assumed potential turning of the tide, I could rest more easily. If it be permitted to lapse into the terminology of the market place, there is a vast difference between gross income and net income. This would be determined by the reaction on men's minds, not only in this country, but in every monetary center of the world. Had it been favorable, the authors' assumptions are tenable; had it, for instance, been deemed an inflationary threat to the gold standard, the "cost" (in erosion of those high-powered dollars) could have reduced the "net" to such an extent as would have precluded the results confidently anticipated by the authors. Again, I don't know; I am merely questioning.

In Kerrville, Texas, the "Bank of the Charles E. Schreiner Estate" is run by Louis Schreiner, aged about 90, and was founded by his father, old Captain Schreiner, as he is termed in those parts. The old Captain laid down the rule: "The time to call your loan is before you make it," and in almost a century, good times and bad, that bank has never called a loan. High-powered money, intelligently administered by a regulatory body, can, as the authors point out, accomplish much. It cannot accomplish the impossible—there seems to me an analogy in Lord Keynes' rueful remark: "Nothing is more suicidal than a rational investment policy in an irrational world." I would have more hope of its keeping us out of trouble than in its ability to turn an emotional tidal wave after we got into trouble.

I claim no validity for my "questioning comment." During my university days I would have placed little emphasis upon the psychological and political factors: a long life in business has changed my views. The story is told that Bismarck in council, after his staff had scoffed at certain factors which they termed imponderable, reached his decision: "Gentlemen, the Imponderables have it." I have no idea whether his decision was correct, and similarly I have no idea whether the weight I attach to imponderables has validity. My comments are set forth with humility, because I have made too many mistakes to do otherwise.

Over all, my admiration for *A Monetary History of the United States, 1867–1960* is unrestrained.