Levy Economics Institute of Bard College

January 28, 2013

One–Pager | No.37

Lessons from an Unconventional Central Banker

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Eighty years ago, a millionaire banker from Utah told the Senate Finance Committee that "only bold and courageous leadership" could end the Depression. All the other invited speakers from banking and industry preached the gospel of balanced budgets, but Marriner S. Eccles told Congress that government spending on a sufficient scale would fix the unemployment problem. A sharp increase in the purchasing power of ordinary people would get the economy back on track. Increased effective demand financed by government borrowing would create employment and generate income and investment.

Eccles argued forcefully that only the US government had the money-creating powers to end the Depression. Individual states could not act in the same way; they could not call men to war or provide billions for public investments. Only the federal government had this power. It should use its powers of taxation to jump-start the economy and mobilize the resources of the nation for the benefit of its people. He even proposed a five-point program that might resonate today, with public support for the unemployed, refinancing of mortgages on an immense scale, and extra funds for public investments.

Eccles was accused of being a socialist. His proposals would, according to his opponents, surely destroy the good credit standing of the US government. But he responded that his critics failed to see the economy as a whole. When the government borrows money, according to Eccles, we borrow from ourselves, and when we pay interest on, or pay back, the principal of the debt thus created, we are paying ourselves. In a June 1932 speech before the Utah State Bankers Convention, he said, "If a man owed himself, he could not be bankrupt, and neither can a nation. We have got all of the wealth and resources we ever had, and we do not have the sense, the financial and political leadership, to know how to use them."

Eccles was offered a position at the US Treasury soon after his appearance in Congress, and President Franklin D. Roosevelt then called on him to become the chairman of the Board of Governors of the Federal Reserve. Thus began a long and distinguished public career that would last for almost 20 years in Washington, D.C. Eccles was instrumental in drafting key banking legislation in the mid-1930s, including the new National Housing Act of 1934, and he played a key role in the events that led up to the 1951 Treasury–Federal Reserve Accord.

The Treasury–Federal Reserve Accord is a milestone in central bank history. It led to a lasting separation between monetary policy and the Treasury's debt-management powers and established an independent central bank focused on price stability and macroeconomic stability. Eccles's role in the Accord drama is somewhat surprising, since he started his career at the helm of the Fed as a "fiscalist" and preached deficit financing and monetization of government debt. But in a broader cyclical perspective, his position was quite consistent, contrary to what some historians have stated, as he was equally concerned with inflation and deflation.

In a new Levy Institute working paper ("Marriner S. Eccles and the 1951 Treasury–Federal Reserve Accord"), I revisit the Accord history and elaborate on the role Eccles played in the events that led up to the Accord. The global financial crisis has generated renewed interest in the Accord and its lessons for central bank independence. This new working paper shows that Eccles's support for the Accord—and central bank independence—was clearly linked to the strong inflationary pressures in the US economy at the time. During the Depression, he was equally supportive of central bank financing of New Deal programs.

Eccles's strong support for the Accord was thus linked to the inflationary policies of the Truman administration and should not be interpreted as unconditional support for central bank independence at all times. This broader interpretation of the Accord holds the key to a more balanced view of Eccles's role at the Federal Reserve, where his contributions from the mid-1930s up to the Accord are seen as equally important.

Eccles favored countercyclical fiscal and monetary policies and close coordination between the central bank and the Treasury. The history of the Accord should teach central bankers that independence can be crucial for fighting inflation, but also encourage them to be more supportive of government efforts to fight deflation and mass unemployment. Eccles argued correctly that a nation that borrows in its own currency can never go bankrupt, since "it owes the debt to itself." Central banks should therefore support strong fiscal efforts through monetization, as there is currently no immediate risk of inflation.

A more detailed discussion of the issues can be found at www.levyinstitute.org/publications/?docid=1675.

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