

Rothbard's America's Great Depression, Chapter 4, Part 2

Treasury Currency

- Rose appreciably only from 1921-1923
 - Mostly silver certificates
 - Pittman Act of 1918 allowed Treasury to send silver to Britain for wartime
 - Then Pittman required Treasury to buy silver at \$1/oz. to replenish reserves
 - Massive subsidy to domestic silver miners
 - Harding admin. could have repealed, but didn't

Bills Discounted

- 1923, 1925, 1928
- Rescued banks when Fed was selling gov't bonds
- Fault of Fed's "Lender of Last Resort" policy
- Lots of rediscounted business paper, too
 - Fed both relaxed max. length of discount **and** lending standards
- Penalty rate set very low
 - Penalty rate should be high to prevent banks from borrowing, loaning borrowed funds, and pocketing difference
 - Was actually set very low, to where prime commercial paper sat
 - Lending was continuous, not just in emergencies (i.e. insufficient reserves)
 - Pierre Jay fought for emergency lending only until 1926
 - Fed stopped listening to him completely in 1924
 - Jay himself repudiated his position in 1926
- Fed failed to raise rates
 - Policy of free lending to "legitimate business"
 - Secondary loan market makes such segregation impossible
 - 1926, Gov. James of Federal Reserve Board (FRB): Fed is supposed to prop up agriculture, industry, commerce
- Calvin Coolidge bad on this—speech during election on Oct. 22, 1924
- Lots of political pressure to continue inflation
- "Moral suasion" policy to avoid funding speculation
 - But more loans = more inflation regardless!
- 1. Quantity is a problem all its own
- 2. Extra loans in 1 area overstimulate it and lead to more malinvestment, problems during depression
- Call loan rates kept low
- Coolidge and Treas. Secretary Mellon cheerleading
 - **Don't underestimate the power of the bully pulpit!**

Bills Bought – Acceptances

- **An acceptance is:**
 - **Agreement between bank & 3rd party for bank to pay a certain amount by a certain date**
 - **Generally used in import/export businesses**
 - **Importer with good credit gets bank to send acceptance to exporter**
 - **Exporter can now ship goods with assurance he will be paid**
 - **Once goods arrive, contract concludes**
- These led inflation in 1921, 1922, 1924, 1927, 1928
- Fed bought acceptances, providing reserves to banks w/out obligation to repay
- Acceptances common in Europe, but new to U.S.
 - Fed created the whole market

- Massively subsidized and encouraged by Fed
- Mostly to benefit of Paul M. Walburg and large acceptance banks
- Rapid rise in limits to bank acceptance purchases
- Rapid expansion of what kinds of acceptances were allowed
 - Eventually moved from shipping goods to warehoused goods!
 - **A new market means more places to loan!**
- Lots of German bonds/acceptances
 - Hurts Americans by inflating their currency
 - Hurts Germans by letting German government buy more goods to squander

U.S. Government Securities

- Big deal in 1922, 1924, 2nd half of 1927
- Fed buying government securities
- Holdings tripled \$193M -> \$603M from Nov. 1921-June 1922
 - Wasn't understood this was inflationary at first, but once that fact was known, was continued with inflation in mind!
- Supported by Benjamin Strong
 - Purchases dropped in 1923 when he was ill for most of the year
- Boom in short-term debt and refinancing encouraged by Fed

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