Challenge

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The Growlery

Ending the Debt-Money System

John H. Hotson (Professor of economics)

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THE GROWLERY

Ending the Debt-Money System

President Reagan, for all his references to Franklin Roosevelt, has lessons to learn from FDR's war economics. In World War II, the United States hit all its macroeconomic targets. From 1941 to 1944 unemployment fell to almost nothing and real output rose 42 percent, while the rate of inflation fell from 10 percent in 1942 to 2.4 percent in 1944 and 1945.

In contrast, the first three years of Reaganomics saw unemployment increase drastically and real output grow only 4 percent, while the rate of inflation fell from 9 percent in 1981 to 4 percent in 1983. From 1941 through 1944 the U.S. price level increased 19 percent while output and employment increased drastically. From 1980 through 1983 the price level increased 21 percent while real output increased hardly at all and unemployment ballooned, from 7 percent in 1980 to 10 percent in 1982 and 1983 before falling below 8 percent in 1984.

Why these great differences in economic performance? There are two basic reasons why Roosevelt's policies so greatly outperformed Reagan's. The first of these has been much discussed; the second has been virtually ignored. The more discussed reason Roosevelt was able, during World War II, to combine full employment, rapid growth, and stable prices was that he enacted and enforced comprehensive wage, price, and credit controls. Reagan has not.

The neglected reason for Roosevelt's better performance during the war was that he was able to "draft" the Federal Reserve System to serve the general purpose; Reagan has not. Because he had drafted the Fed, Roosevelt was able to finance his huge wartime deficits in a close to optimum way. Reagan is financing his deficits in the worst possible way.

Why should the U.S. government borrow from foreigners, at 12 percent interest, money the Fed should have been required to produce at 0.37 of a percent, as it did in World War II? A government deficit in an underemployed economy, such as ours, is not a bad thing if it is financed in a prudent and sober manner. However, a foreign deficit, if it continues very long and is very large, can lead a country into grave difficulties; witness the cases of Argentina, Mexico, and Brazil.

According to the conventional wisdom, the current federal budget deficit of some $180 billion is a very great problem. All join in scolding President Reagan and in telling him he must "do something" lest interest rates remain too high for recovery from the present world depression.

Do any of these critics ask themselves *why* a deficit of 5 percent of U.S. GNP in 1984 is a problem, when deficits of 13 percent of GNP in 1942, 29 percent of GNP in 1943, and 22 percent of GNP in 1944 and 1945 were no problem? "High deficits cause high interest rates," says the conventional wisdom; then how come Roosevelt was able to finance his huge deficits at 2 percent interest, while Reagan has to pay 10 percent to finance his relatively much smaller deficits?

Too much "bad" money and too little "good" money

The U.S. central bank, or Fed, is today controlled not by the government, but by the very commercial banks it is supposed to control. These bankers have greatly reduced the proportion of our total money