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- Hello, this is Rose Friedman, inviting you on behalf of Instructional Dynamics to another of our biweekly conversations with Milton Friedman, Professor of Economics at the University of Chicago. We are taping this interview on Wednesday July 24th, 1974. Yesterday, Mr. Nixon formally confirmed the rumor that has been making the rounds, that Alan Greenspan is being named Chairman of the Council of Economic Advisors, what is your reaction?

- Well Mr. Greenspan is an excellent person for the job, the question, and the crucial question, is whether the job is one in which even an excellent person can, under present circumstances, have much of an impact. Alan Greenspan has, in the first place, very close links to many of the top figures in Washington. He was one of the first people who joined Mr. Nixon's pre nomination staff in 1967, when the first person onboard that group that worked in advance of the convention in outlining and developing Mr. Nixon's programs and policies, the first member of that group I believe was Pat Buchanan, who is still at the White House as a speech writer, a second early member was Martin Henderson, a young man who subsequently worked at the White House as a special assistant to the President, and also in the first year of the Nixon administration, as a special assistant to Arthur Burns, who was at that time Counselor to the President, I believe that Alan Greenspan was about the third of that group of people who joined, though I'm not sure, but at any rate, he was with that group as, more or less, director of research for the campaigning staff, he worked after the convention, during the campaign, in the same position, he has not up to now held a formal position within the Nixon administration, though I am sure he has been offered a number, he has preferred to stay on the outside, but he has certainly been a close informal advisor to Mr. Nixon, to the people in Washington. In addition, he was a student of Arthur Burns' at Columbia, although he never, never has received a doctoral degree, primarily because he went on into the business consulting world, rather than into the academic world. So in terms of his links with people in Washington, he certainly knows them well, they know him, he has confidence in them and they have confidence in him. With respect to his general political economic philosophy, he started out essentially as a, what's come to be called an objectivist, a follower of Ayn Rand, this is a doctrine in which for the present purpose, and a major point about it is that it stresses non-intervention, it's a very libertarian point of view. Alan I think has moved somewhat away from the extreme, from the full position which Ayn Rand and her followers would hold, they would give government a much smaller place than he would, but he would give it a much smaller place than most people. He is a strong believer in the free market, he has been consistently and persistently opposed to price and wage controls, he never was one of those people who jumped on the band wagon for price and wage controls in 1971, he was a believer in cutting government spending as much as possible, he is a believer in the importance and role of money in determining economic developments and in the importance of a moderate rate of monetary growth. He has one other feature which distinguishes him, sofar as I can see, from every other former chairman of the council of economic advisers, with one exception, all past chairman of the council have been academic economists, the one exception is Leon Keyserling who is not an economist at all, but a lawyer, and who I may say was not one of the more impressive chairmen, in the main therefore, the council's chairmen have been not only economists, but academic economists. Alan Greenspan is certainly a very well trained, very knowledgeable economist, but he is not an academic economist, his career has been with a firm of Townsend-Greenspan, though which really means a firm of Greenspan, it was originally, there was originally a man, Townsend, who had set up a Townsend consulting firm that Alan joined shortly after he finished his graduate work, the firm was expanded and became Townsend-Greenspan, Mr. Townsend died, and essentially it's Greenspan's company, his own personal company, this has been a consulting firm that has been, that writes and puts out reports on current business conditions, does special analysis for particular industries and so on, and has obtained over the years an extraordinarily high reputation, indeed I would say, probably, it has the highest reputation of any of the large number of private economic consulting firms, its clients are a number of some of the very biggest businesses in this country, as well as brokerage houses in New York and so on. So that Alan Greenspan comes to the position of Chairman of the Council of Economic Advisors with a much closer connection with the business world, a much more pragmatic background than the academic economists, but I don't want to give the wrong impression, he's pragmatic in the sense of means, but not in the sense of objectives or ends, the values I've described he holds very strongly, I am morally certain that Mr. Greenspan would not have joined the administration unless he had had assurances from them, and that they proposed to follow the old time religion they've been talking about, of fighting inflation through trying to cut down the government budget, through a moderate monetary stance, and through, and with the avoidance of price and wage controls, now that doesn't mean they will do so, after all, prior to 1971, Mr. Nixon was following that policy then, but that didn't prevent him in the summer of 1971 from going in for voids and price controls, but if he did, if there were any such change, I would think it highly likely that Mr. Greenspan would resign rather than go along with a change in that direction. Now, this, I may say also that Mr. Greenspan is a very attractive person personally, in the sense that he is reasonable, not at all aggressive or abrasive in any way, gets along very well with people, so I think he's an ideal person for the job. The question that bothers me is not about him, or not about his views, but about whether anybody under present circumstances can exercise much influence in that position, partly this is because the administration is now, in its sixth year, the lines of been more or less set, but partly it is because, there is so little the administration can do except exhort, when it comes to the crucial elements needed for a proper sensible economic policy now, there is, and it's hard to say that they are anything other than on the one hand, and the three things I've mentioned, first, reduction in government spending, second, a moderate rate of monetary growth, and third, the avoidance of wage and price controls. The one thing the administration can pretty clearly do is to avoid wage and price controls, in that negative sense, it has some scope fraction. But beyond that, what can the President do? He can exhort congress to reduce spending, it is hard for me to believe that he can, under present political circumstances, do anything very effective in the way of impounding funds that congress legislates. He can plead with the Federal Reserve to reduce the rate of monetary growth, the Federal Reserve is technically independent, but more important, at the moment, it is from a purely political point of view, far more independent of the President than he is of them, that doesn't mean that the Federal Reserve is independent, but its political links, the things that will affect it are much more likely to come via congress, and via its constituency the banking community, than it is via the President, and therefore it is very hard for me to say that the President is at the moment in a position to exert much influence on the course of events accept by exhortation and by, what I must say, would be a very very important thing, avoiding wage and price controls, after all, as I have stated repeatedly on these tapes, I believe our present parlor situation dates directly from the imposition of price and wage controls on August 15th, 1971, and hence, that there is no action that Mr. Nixon could have taken that would have done more good for the country than the negative action of avoiding putting on those controls, so I do think that is an important, but beyond that as I say, Mr. Greenspan can primarily exert an influence as so far as he is more effective than his predecessors, or than anyone else, in persuading congress to keep down spending, or in persuading the Federal Reserve, to slowdown the rate of growth, I certainly wish.

- Well, has the Fed being slowing the growth of money?

- Well I sound like a record in which the needle has gotten stuck, because all I can say is the same thing that I have said each time over past weeks when I have taken up this matter, there is as yet no sign whatsoever in the actions of the Fed as opposed to the statements and pronouncements, that there is any real slowdown in the rate of monetary growth, that it is departing in any significant way from the trends of the past three or four years, now this may seem not quite to fit in with some of the recent figures, for example, I have in front of me the report of the Federal Reserve Bank of St. Louis, the latest one available, which is for the week ending July 10th, and it shows that over the prior year, from the week ending July 11th, '73, to the week ending July 10th, '74, the annual rate of growth of the narrow money supply M1 was 5.6%, as I have noted repeatedly, the trend rate of growth over the past four years has been 6.7%, and so anyone who looks at that single figure is likely to say, well now isn't that wonderful if that is really moving? However, if you take a look at the chart that underlies these numbers and look at the more detailed movements, you will find that the base figure of July happens to be a period when the money stock was well above the long term trend, it was abnormally high, in the next four months, the money supply did not grow at all in the United States as the Fed pulled the money stock back down somewhat below the trend, in consequence, that 5.6% really grossly understates the sort of trend rate of growth, what I have done is very different, I have plotted on the chart, the logarithmic straight line which shows a steady 6.7% rate of growth, and I have been plotting that week after week on the chart, the numbers for the money stock, the narrow money stock, over the past four or five months have simply fluctuated around this line, some weeks they have been above it, some weeks they have been below it, but they have shown no systematic tendency to go below it, and that shows up if you look at the rates of monetary growth in numerical values of the table, that St. Louis puts at the foot of that chart, it was 5.6% over the past year, but it was 7.8% over the past nine months, it was 7.2% over the past seven months, it was 9.4% over the past five months, as you can see, these month to month comparisons can give you a very widely varying rate, if you look at the broader money stock M2, which on the whole, I am inclined to regard with greater concern, exactly the same thing is true, that has been growing over the past three or four years at an annual rate of close to 10%, about 9.7, 9.8%, those numbers have been more consistently a little lower over the past year, they are 8.7% for the year, and even the highest, which is for seven months, or I'm sorry, which is for nine months, is only 9.7%, and yet when I plot on the chart the trend line, the actual money stock has been below the trend for perhaps the last two or three weeks, you could, it could be that what's happening in that series is the beginning of a slow deceleration, but I'm very, very reluctant to reach any conclusion at the moment, partly because there is so little evidence of any slowing down, but also because disintermediation, that is to say the tendency for people to cut down on time deposits and convert them into higher yielding market paper, has clearly tended to slowdown the growth of M2 rounded to M1, but if you put it all together, what you can see is, that my best judgment is as yet not proved, no evidence, there is no sign, the one good thing you can say is there is no sign of a recent acceleration in monetary growth, maybe, maybe there are a few clouds in the sky ahead that suggest a deceleration.

- Clouds? (laughs)

- Well, you're quite right.

- Sun?

- Sun, rays of the sun, but I think that as yet the evidence is very tenuous and you better keep the Scotch verdict.

- Well turning to another subject, does the decline in real GNP in the second quarter mean we can confidently say we're in a recession?

- Many people will be remarking that, have remarked, the papers have been full of it, that we have had two quarters of declining GNP in a row and that means we have a recession. I've never, as I've noted here often, that does not seem to me to be the, either the accepted, or a good definition of a recession, as I mentioned earlier, if we went down 6%, at an annual rate of 6% in the first quarter, and up at 1% in the second quarter, would that make a recession? Would that mean there was no recession? While 2.5% down in each of the two quarters which would leave you at the same end pointing that there was a recession, that's too simple minded a test, the test which really is used by the National Bureau, which has become accepted as the unofficial arbiter of whether there is a recession or not, is a much more extensive one, and has to do with the breadth as well as the depth of the decline, and from that point of view, one has to say, looking at the classical kind of a recession, the kind the Bureau has called in the past, it is still very hard to say that this one has been a recession, the aggregate total output alone shows a substantial decline, if you look at the depth of GNP, real GNP, it is comparable to the decline in earlier declared recessions, 1970, 1960, '61, '57, '58, and so on, however, look at other aggregates, in particular the aggregate that bothers me the most, and that I find most mysterious, is total employment and unemployment, the unemployment rate has only gone up trivially, it's only gone up to 5.2%, a much smaller rise in the unemployment rate than during any of the earlier recessions, in addition, total employment has continued to rise, industrial production has declined somewhat, but the amount of decline in the index of industrial production is much smaller than it has been in earlier recessions, and so you go from one series to another and what you find is that the slowdown has been very concentrated, primarily automobiles and construction, and almost nowhere else, you find very little evidence in the labor market of a great deal of ease, you do not find that evidence either in the level of unemployment, nor do you find it in average hours per week, ordinarily during a recession average hours per week decline with an easier labor market, nor do you find it in any significant slowing down in rates of wage increases, so that I think one has to say that while clearly there has been a slowdown in the economy, there has been what the new, the phenomemon which the Bureau has dubbed somewhat infelicitously in my opinion, growth recessions, there clearly has been a growth recession, that is a decline in the rate of growth, I'm afraid you still cannot give an unambiguous statement as to whether there has been a real recession, now clearly, I should make it clear that my own bias is obviously in the direction of saying there has been a recession, since, as you will recall, I started predicting nearly a year ago, that there was going to be a recession in late 1973, early 1974, and hence, there is a strong temptation to make my prediction self-fulfilling by declaring that there has been a recession, and yet I think if you look at all the figures, you have to say that the verdict here, as in the case of whether the Fed has shifted the monetary restraint is not yet in, if we continue moving along our present lines, if that real GNP continues to decline, it is hard to believe that it will not sooner or later show up in the form of unemployment, so either of two things ought to happen, either the unemployment index ought to start rising fairly rapidly fairly soon, or else we're going to have another one of those many recessions of the kind that we had in '66, '67 that was never called a real recession.

- We've been holding a question from Mr. Parker which we have for some time now, but it seems particularly relevant now, in view of all the financial difficulties, to answer it, Mr. Parker's question is as follows, I recall some years ago a tape which you made on the failure of the Bank of the United States, on several occasions since then you have mentioned this failure, but the original tape which I am unable to locate mentioned the part that J. P. Morgan and his antisemitic posture had on this failure, for your more recent subscribers, I wish you might consider repeating what you said at that time.

- Well the reason why this is kind of appropriate and timely, and it's not simply repetition, is because there is, I suppose amusing, I suppose disturbing coincidence, between the experience of the Bank of the United States in the one hand and of the Franklin National Bank on the other, let me recall to you that the Bank of the United States which failed on December 11th, 1930, I believe in one of the former tapes I made a mistake and said 1931 and somebody called my attention to it, but it was December 11th, 1930, that the original Bank of the United States which failed on that date, was not an official bank, the title of Bank of the United States made it sound like an official bank, because there was,

- You mean it was not a government bank?

- It was not a government bank, quite right, it was official, but it was not a government bank, there were two banks of the United States in the early years which were formed and the one of which terminated in 1860 and then one in 1836 when there was a big bank war between Biddle and Jackson over whether the charter of the Bank of the United States should be extended, but that bank having disappeared, this new Bank of the United States was a purely private bank, it was the largest bank in the United States that had ever failed up to that time, there were some very special features associated with its failure, and that's what brings out the coincidence with the Franklin National Bank, the Franklin National Bank has not yet failed, but clearly it's in great difficulties, the Bank of the United States was one which was not very popular with fellow bankers in New York, and the major reason it was not popular was its name, because of its name it was interpreted as being an official bank, particularly by immigrants, and that it was a new aggressive, rapidly developing bank, which had attracted a great many customers among the immigrant and foreigner population of the United States, now the Franklin National is not quite in that position, but it has certain similarities, it is a new bank, it was an aggressive bank, it was a bank that was expanding very rapidly, that was having lots of branches, particularly in Long Island, and that was regarded by other banks as rather a brash newcomer, the second special feature of the Bank of the United States and the feature that Mr. Parker is recalling, is that it was one of only two banks in New York at that time, I say two banks, and I'm sure it's two sizable banks, maybe there were some small banks, but of the major banks, it was one of only two, in which the board of directors and the ownership was predominately Jewish. The reason this is highly relevant, for several reasons, one of which was the general antisemitism on the part of the banking community, the other special feature of J. Piermont Morgan that I'll come back to, but the Bank of the United States got into trouble because of alleged speculation by some of its directors, in this case it was, and if I remember rightly, in copper, it wasn't foreign exchange, Franklin National Bank, the extensible reason for its trouble was speculation in foreign exchange, at this time, the New York Clearing House, Federal Reserve Bank of New York, in the case of banks that got into trouble, had a strong tendency to develop a plan to save the bank, and indeed just a week or two before the Bank of the United States got into trouble, another bank about the same size, which was in trouble, had been saved by a plan involving a guarantee fund put up by other banks in the Clearing House, the crucial feature in these rescue operations was the role that J. Pierpont Morgan played at that time, there was generally a tripartite business, a bipartite business, J. Pierpont Morgan on the one hand and the Clearing House banks on the other, it was J. Pierpont Morgan having put up I think it was 25 million dollars in the case of the bank a week earlier, and the original plan which the Federal Reserve Bank of New York developed for saving the Bank of the United States, involved J. Pierpont Morgan participating in a guarantee fund, and involved merging the Bank of the United States with another New York bank, and this is where the second coincidence with the Franklin National Bank comes in, of all the banks in New York, which bank do you suppose they chose to merge? The Bank of the United States, the other bank which had predominately Jewish ownership and Jewish board of directorship, namely, that what was then called the Manufacturers Trust Company, now with respect to the current Franklin National Bank, what bank do you suppose is being talked of as the most prominent merger partner for Franklin National Bank? Well, what is now being called familiarly Manny Hanny, namely Manufacturers Hanover Trust Company which is the bank that resulted from the merger of the original Manufacturers Trust with the Hanover Bank, so that the merger partner is exactly the same this time, the proposed merger partner as it was in 1930, now, let me go back to J. Pierpont Morgan and how that affected this, because this is itself a long and interesting story, back before World War One, J. Pierpont Morgan senior had been pillar rating an insurance investigation in New York by a lawyer, I now forget whether it was Brandeis or some other famous, Cordoza or one of the other, it was one of the very famous Jewish lawyers, and he had really been pillar rating, we have on record, thanks to a great gossip, Hamlin who was on the Federal Reserve Board, and who kept his diaries, of a lunch which he had with J. Pierpont Morgan junior during World War One, 1918, when there was a great controversy going on about whether Felix Warburg should be made a member of the Federal Reserve Board, and the campaign was extensively on the ground that Warburg had too many German interests, but the real reason was that Warburg was Jewish, and J. Pierpont Morgan says to Hamlin in the course of this lunch, now I'm gonna get even with those Jews for what they did to my father, well comes 1930, comes the Bank of the United States and the proposal that it be saved and that J. Pierpont Morgan contribute 25 million dollars to this, I don't guarantee that number, but a substantial sum to the guarantee fund as he had to other bank funds, and he refused to do it, now, in and of itself that's only a circumstantial case for saying that it was antisemitism that was responsible for his not going along, but the case is much stronger than that, because it turned out that there was an insurance, there was a banking commissioner of the state of New York who was sued in the courts on the grounds that he should have closed down the Bank of the United States earlier, and part of his defense was that the Bank of the United States was really a very solid, sound bank that would have been perfectly alright if this rescue plan had gone through, and he testified in the course of the court hearing, as in it's open and the record and the public record, that racial considerations, and I think he used the word racial and not religious, played a very large role in the unwillingness of Morgan and the others to go along and saving the Bank of the United States, I might note to complete the story, that the Bank of the United States was undoubtedly a perfectly sound and solid bank, and that if indeed the rescue operation had gone through, it probably would have survived in perfectly good shape, it was liquidated during the worst years of the depression from 1930 to '33, but it ended up paying off 92.5 cents on the dollar for every deposit, a dollar a deposit, and that was under the adverse circumstances having to be liquidated and liquidated under those conditions, approximately the failure of the Bank of the United States was a major event, it set off a train of bank failures that really started a sharp intensification in the depression in early 1931, I don't mean to say that if the Bank of the United States had been saved, you might not have had such runs, some other bank might have failed and the same thing might have happened, but from a proximate point of view, December 11th, 1930, marks a drastic change in the character of the depression, from being a severe recession without liquidity and banking problems, it was turned into a major financial collapse, that's why I remember that date so well. Now let's come back to Franklin National Bank today, many people have been concerned and there has been widespread discussion of the possibility that it might also trigger off a great depression and a financial collapse of this kind, I do not believe that that is likely to be the case, the crucial difference between the situation then and now, or I should say there are two crucial differences between the situation then and now, the fist crucial difference is the existence of FDIC, thanks to FDIC there is simply no chance that you are going to have runs on perfectly good banks by ordinary depositors lining up for blocks long trying to take out their money, because even if Franklin National were allowed to go broke, as it should have been allowed in my opinion to do, the second big difference is that the attitude of the Federal Reserve and the monetary authorities, they have in my opinion swung too far from the one extreme to the other, from the viewpoint of staying out, they have gone to the viewpoint of going in on too large a scale, I think it would be a healthy thing at the moment, assuming, maybe I'm wrong, maybe Franklin National is a perfectly good and sound and solid bank and it can be preserved without any undo government intervention or without any undo subsidy, but if not, if it really is a bad bank, if it's really in a poor condition, why I think there is, it would be a good thing if it were allowed to go broke, but I think those two differences are very crucial, and they make it almost inconceivable that you could now have a banking collapse of the kind that was triggered by the failure of the Bank of the United States in 1930.

- I think this brings us to the end of our tape, thank you very much, remember subscribers, if you have any questions or comments please send them to Instructional Dynamics Incorporated, 430 Ohio Street, Chicago, Illinois, 60611. We shall be visiting with you again in two weeks.