FEDERAL OFFENSES

Doug Henwood

In 1939, Texas Congressman Wright Patman came upon an imaginative way of harassing what would be his lifelong enemy, the Federal Reserve System: he'd caught the central bank cheating on its taxes. Its new headquarters, a neoclassical temple of finance overlooking the Washington Mall, wasn't government property, because the Fed wasn't an agency of government—so the system was improperly claiming exemption from District of Columbia property taxes. The building, Patman observed, was owned by the twelve regional Federal Reserve Banks, themselves owned by private commercial banks. So, Patman concluded, the Fed owed the D.C. government property taxes, like any private enterprise.

Patman's argument inspired the District's tax authorities to bill the Fed for taxes. The Fed's lawyers fought back, arguing that they were indeed part of the government, citing legislative history and judicial precedent. The D.C. authorities showed the Fed's lawyers the 1935 deed, under which the U.S. Treasury had signed over "all the right title and interest of the United States of America." Only days before Pearl Harbor, the D.C. government published a notice of imminent auction: they were going to seize the building and sell it to the highest bidder. It took three years of litigation for the Fed to win its case.

As Patman said twenty-five years later, "A slight acquaintance with American constitutional theory and practice demonstrates that, constitutionally, the Federal Reserve is a pretty queer duck." It's a profitable and self-financing enterprise that need never go to Congress, hat in hand. Though the system is governed by a Board whose members are appointed by the President and confirmed by the Senate, their fourteen-year terms insulate them from immediate political concerns, and they share power with the presidents of the twelve Reserve Banks, who serve at the pleasure of their regions' commercial bankers. Credit policy is set by the Federal Open Market Committee, which consists of the seven presidentially nominated members of the Federal Reserve Board and five of the privately nominated regional Bank presidents. The FOMC meets every forty-five days or so, in deep secrecy. When Congress passed the Freedom of Information Act, the practice of recording a transcript of the meeting—to be released five years after the fact—was discontinued, lest ambitious litigants expose the deliberations of the money mandarins to premature public scrutiny. After each FOMC meeting, carefully euphemized summaries of the previous powwow are released. As William Greider says in his book *Secrets of the Temple: How the Federal Reserve Runs the Country* (Simon & Schuster), "No other agency of government, not even the Central Intelligence Agency, enjoyed such privacy."

While CIA-watching is sport practiced by scores of journalists, intellectuals and academics with an intensity ranging from idle curiosity to *engagé* hostility, Fed-watching is limited largely to the friendly eyes of Wall Streeters and their allies in academe and the business press. Of the nearly eighty books on the Fed listed in *Books in Print*, only a handful are intended for a general audience; the rest are either highly specialized university-press tomes, or fervid screeds with titles like *The Federal Reserve Hoax* and *The Federal Reserve Conspiracy and the Rockefellers.* Both these titles are published by the Noontide Press of Costa Mesa, California, a division of Willis Carto's Institute for Historical Review, which believes the Holocaust never happened. According to this line of thinking, the central bank is part of that international brotherhood of Communists, Jews, Trilateralists and London bankers that secretly rules the world. The Fed deserves better critics. It's found one in Greider.

Patman spent almost fifty years in Congress attacking the Fed, the last twelve of them as chairman of the House Banking Committee. But there are no Patmans in Congress today. When Fed chairman Alan Greenspan testified before our representatives earlier this year, no one challenged his assumptions that anemic growth is good for the economy, or that signs of workers finally sharing some fruits of the Reagan boom should be viewed with alarm. Like all central bankers, Greenspan views any outbreak of prosperity as a riotous threat to economic order, to be suppressed with tighter credit. Rather than challenging these assumptions—or looking into Greenspan's intellectual history, notably his admiration of Ayn Rand—our elected representatives exchanged Jewish-mother-and-chicken-soup jokes with the Superintendent of Money.

Few politicians show lasting interest in matters of money and credit. When interest rates are high, as they were in the early 1980s, some Congressmen will say harsh and vaguely threatening things about the Fed, but their attention drifts with the turn in the business cycle. Only the occasional eccentric Congressman betrays any lingering fascination with the mysteries of money—like goldbug Jack Kemp, who lulls audiences to sleep with his paeans to the stern, objective discipline of a gold standard. Or like Representative Bill Dannemeyer, a spiritually inclined right-wing Californian who shared this bit of wisdom with his constituents: "It is not an accident that the American experiment with a paper dollar standard, a variable standard, has been going on at the same time that our culture has been questioning whether American civilization is based on the Judeo-Christian ethic or Secular Humanism. The former involves formal rules from God through the vehicle of the Bible. The latter involves variable rules adopted by man and adjusted as deemed appropriate." And you thought gold, like any form of money, was a social convention, not the Word made Coin.

It wasn't always thus. The "money question" was a guiding obsession of late nineteenth-century populists, who argued the merits of gold, greenbacks and credit with an intensity and detail now reserved for barroom analyses of pro sports. The populists were well aware that money matters, now safely obscured behind a veil of technological mystification, were a highly effective form of class warfare—of rich against poor. "The money question was the political expression of a struggle over shares," as Greider says.

The money question was inspired by the punishing deflation of the last third of the nineteenth century.

The Civil War was financed with easy money and a limitless supply of greenbacks. Prices and production zoomed, and Yankee farmers prospered. After the war, however, Eastern bankers demanded a return to sobriety in the form of a valuation of gold that would enforce a return of pre-war prices. It succeeded all too well. Wheat that sold for $2.06 a bushel in 1866 sold for less than 60¢ thirty years later. As prices fell, farmers borrowed to increase output and stay afloat, a strategy that only fed the deflation. Under the burden of falling prices and heavy debts, farms failed in droves, to be ceded to creditors, combined into larger operations and resold. Farmers expressed their displeasure in the populist rebellion, one of the greatest examples of spontaneous, radical revolt in our history. A group of hayseed autodidacts organized themselves and plumbed the mysteries of political economy.

The populist agenda—praised decades later by no less than John Maynard Keynes, though scorned by all "thoughtful" contemporaries–envisioned an activist Federal government spreading the wealth and protecting small fry from distant creditors: railroad and telegraph regulation, a progressive income tax, legal rights for unions, price stabilization and easy credit. The latter was to be guaranteed by democratic control of money and credit—an "elastic currency" that would expand to accommodate the growth of commerce, instead of the rigid currency, gold, which limited growth and assured that wealth flowed upwards and misery trickled down. The nineteenth-century populist ideal of an elastic currency was ironically realized in 1913, with the creation of the modern populist's nemesis, the Federal Reserve.

Wall Street overcame its objections to the idea of a central bank when J. P. Morgan and his cronies failed to refloat the banking system during the panic of 1907 and were forced to turn to the government for a bailout. Gone were the halcyon days when the House of Morgan could refloat the Treasury on onerous terms. Though Progressive reformers thought they were getting a grasp on the money trust by creating the Fed, bankers had other plans. What was created was the first public-private partnership, run by technocratic, managerial precepts. The Fed's subsequent history shows that the public is typically the junior partner in such arrangements, something worth recalling in the light of contemporary neoliberalism, which speaks glowingly of partnerships among business, government and labor.

The new Fed was charged to maintain "sound credit conditions, and the accommodation of commerce, industry, and agriculture." The language was vague because nobody in Congress really understood central banking; since the gold standard would continue, the Fed was conceived as the lender of last resort in a panic, not the regimentarian of credit. The young Fed was quickly captured by Benjamin Strong, the "Morgan man" who was president of the New York branch. At age seven, the Fed deliberately provoked its first recession, to end the postwar inflation. It was the first of many it would provoke in an effort to manage the business cycle. The ideal was to avoid the wild swings between boom and panic characteristic of the nineteenth-century business cycle–to rein in a boom to keep it from turning outlandish, and to "flood the street with money," in Strong's phrase, just as a bust was about to degenerate into a disaster. William McChesney Martin, chairman of the Fed in the 1950s and '60s, described the Fed's mission in two oft-quoted phrases: "leaning against the wind," or, alternatively, "[taking] away the punch bowl just when the party gets going." Father knows best.

In 1979, with Americans on gas lines and the financial markets in a funk over double-digit inflation, Jimmy Carter announced his diagnosis of a national malaise and shuffled his cabinet as a cure. Wall Street was not impressed; investors shunned bonds and chased gold. Though gold has no intrinsic value—neither interest nor dividends accrue to its owner—it is the security blanket of nervous speculators, who cling to it with special fervor in times of war, monetary panic or inflation. How to calm Wall Street? wondered the hapless administration. The Street's answer: Paul Volcker.

Volcker, then president of the New York Fed, was a long-time financial bureaucrat. He worked in the Treasury under three Presidents, Kennedy, Johnson and Nixon. A nominal Democrat, he nonetheless worked closely with John Connally, Nixon's Treasury Secretary, engineering the world's final liberation from fixed exchange rates and the gold standard. Volcker's high-level financial diplomacy endeared him to central bankers and to finance ministers around the world. Though he was a wheeler-dealer at the highest levels of high finance, he seemed utterly indifferent to accumulating personal wealth. Connally once threatened to fire him if he didn't get a haircut and a new suit. It pained him to dine in the expense-account restaurants where lobbyists seduce our public servants.

Carter ignored Bert Lance's warnings that he was mortgaging his electoral future to the Fed and nominated Volcker as chairman. Only months after taking office, Volcker announced to an uninformed public that the Fed was changing its basic operating procedures. Instead of manipulating interest rates, the Fed would aim to stabilize the supply of money and credit. The Fed had apparently converted to monetarism, a doctrine repeatedly discredited in the eyes of all but Milton Friedman. The conversion to monetarism was a cover for an austerity program the likes of which the United States had never seen. The Fed would drive interest rates to record levels for an unprecedented length of time. Though the professed goal was ending inflation, the hidden agenda was restructuring the political economy to assure a permanent redistribution of income, from labor to capital, and from small capital to large.

Now, there's an enormous gap between what ordinary folk mean by inflation and what the creditor classes mean. When the former complain about rising prices, they're really complaining about a decline in their standard of living. The inflation of the 1970s masked a decline in real wages for most Americans, a trend that has continued in the noninflationary 1980s. Yet for some—middle-class homeowners, real-estate speculators, independent oilmen —inflation was a gold mine. They were able to borrow at low real interest rates to buy quickly appreciating assets. But these gains were creditors' losses. Real interest rates—that is, actual interest rates less inflation—were low or even negative for much of the decade, which meant that *rent-*

iers were losing doubly, as inflation ate away at the value of their principal, and the tribute collected in the form of interest was barely enough to make up the loss. Restoring the soundness of the dollar was the creditors' Holy Grail.

Since debtors far outnumber creditors, the politics of austerity demands deviousness and secrecy. Over half of U.S. households have a net worth of zero or less, while the top tenth own 86 percent of all financial assets held by individuals, and the top 2 percent owns over half. As the Fed itself, which collects these statistics, put it, "Fewer than 10 percent of families provided more than 85% of the net lending by consumers, and more than half of all families were net borrowers." Or, as Greider puts it, indulging in his curious practice of phrasing eternal verities in the past tense, "The few lent to the many." Volcker had fired the opening round in the revolt of the haves; the United States was about to throw the world into its worst slump in fifty years. Since it was all phrased in the cool language of technocrats—"monetary aggregates," "target cones," "velocity"—virtually no one noticed, and the press wasn't asking any hard questions.

Dearest to the Fed's cold heart is the profitability of large banks; of less ardent concern is the health of large industrial concerns; of least interest is the fate of the working classes. Thus it mattered not a whit that unemployment reached a post-Depression high of 10.8% in late 1982, that factory workers lost their jobs by the millions, plants closed and farms failed throughout the heartland—or that International Harvester nearly went bust. (The Reagan administration and a pliant Congress worked the fiscal front of the war, cutting social spending and fattening the wallets of the already rich through tax cuts, deregulation and a military binge.) "If disinflation . . . is to work, there must be losers," as E. F. Hutton told its clients. (Poor Hutton, which never recovered from its check-kiting scandal, joined the party of losers when it was absorbed into the Shearson Lehman/American Express empire in late 1987.) It was only the threat to the banking system, extravagantly symbolized by a series of financial shocks that included Mexico's near-bankruptcy in 1982, and the failure and subsequent nationalization of the Continental

Illinois Bank in 1984, that persuaded the Fed to relent. Tight money was fine while it squeezed producers and consumers to the breaking point—but if the *rentier* class was threatened, then a change of heart was called for.

Even as Volcker was engineering the triumph of capital, he also presided over a massive deterioration in the national balance sheet, in which the budget deficit plays a relatively minor role. Corporations borrowed to finance dubious buyouts and restructurings, consumers borrowed to buy gizmos, and the nation collectively borrowed to buy imports—all with no guarantee that the debts would be serviced by those who spent the proceeds. Early in his term, Volcker did nothing to stop the banks from their promiscuous lending to the Third World; later in his term, when the crisis broke into the open, Volcker deferred its resolution by encouraging the banks to lend strapped debtors enough to cover their interest payments. The banks assume, not irrationally, that should the Third World "blow," as Volcker liked to put it, the Fed will be there to cover their losses at public expense. The Reagan-Volcker régime gutted the social safety net—but not for big banks, who enjoy a freedom from failure that is the envy of other businesses. Volcker, who likes to talk about discipline, sacrifice and pain, showed no interest in prescribing such harsh medicine to bankers.

Greider's intention is to restore the "money question" to the center of political discourse, and through it, the class question. Yet by focusing narrowly on money, and specifically on the Fed, Greider avoids confronting the economic system that generates these giant pools of cash. The populist world view too often collapses into a Manichean conflict between virtuous producers and parasitic bankers. What to do with old-line industrial companies like Ford, with its $9 billion cash hoard and a banking subsidiary, or General Electric, with its giant financial services division? Are they producers or *rentiers*? Distinctions blur. In the words of Rudolf Hilferding, "Industrial capital is God the Father, who sent forth commercial and bank capital as God the Son, and money capital is the Holy Ghost. They are three persons united in one, in finance capital."

Like all populists, Greider lends too much credence to the idea that easy credit, rapid growth and an energizing inflation can resolve all the contradictions inherent in capitalism itself. The "reckless, booming anarchy" of Jacksonian America—as the Fed's historian, Bray Hammond, phrased it, disapprovingly—charms Greider. Although he admits that unchecked growth was its own undoing: "The impersonal corporations that Jackson despised proved to be the most effective vehicle for organizing the far-flung activities of the emerging national markets. Quite naturally, the national financial system grew with them, developing its own parallel networks to finance the new order. . . . Fifty years after Jackson, the Populist farmers on the plains and prairies found themselves encircled by its awesome complexity." And unable to sell profitably all the food they could produce.

The Fed—like Freud's superego, which draws its psychic energy from the very id it aims to repress—merely harnesses and redirects forces arising spontaneously within the guts of capital. So it's extremely dubious that a democratic Fed could promote limitless growth through easy credit: the demand for borrowed money would eventually exceed its supply, driving interest rates to punishing levels quite independently of any central bank. The Fed follows the money market as often as it leads it.

And who would control a democratized Fed? Congress—that generous friend of the CIA, the Contras and the arms industry? Elected officials love the Fed as it is; it contains and disposes of any public hostility to the creditor classes by dulling the money question with a deadly barrage of theology and technique. The Fed may act as if it's not part of a democratic government, but so do the executive, legislative and judicial branches.

In the context of American politics, however, these are quibbles. Readable, impassioned books that radically 'question the assumptions by which our political consensus operates don't come along every season. The popular media's interest in money is largely pornographic, be it spying on the boudoirs of the rich and famous or sharing the secrets of their portfolios. In the quality press, opinion leaders have shown little interest in acknowledging, much less responding to, the substance of Greider's book. Wall Streeters are amused by the gossip Greider unearthed; pundits miss Greider's emphasis on class and dismiss him as just another inflationeer. For example, the weighty Hobart Rowen, writing on the *Washington Post* Op-Ed page, praises the book as "impressive and detailed," then devotes most of his article to repeating the usual indictments of inflation. Reviews in the business press celebrate the gossipy stuff—central bankers aren't exactly loose of lip—and mourn the lack of attention to technical matters: Should the Fed release its minutes more promptly? Should the Fed continue to defer to the Treasury on the value of the dollar? Is there a conflict of interest in the Fed's dual role of bank regulator and monetary controller?

Did somebody say something about class war?