The New Deal's New Gold Policy: A Case Study In The Power Of (old) Ideas

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To what extent can developments in economic policy be attributed to developments in economic theory? This question has attracted a variety of treatments. Some authors have pursued this question on the basis of simple models of political and intellectual processes; their approach has been an "*a priori*" one (e.g. Keynes 1936, Friedman 1986). Others, more cautiously, have adopted an "empirical" case-study approach; the extensive scrutiny of the "Keynesian Revolution" in policy making (surveyed by Peden, 1988) is a good example of this approach.

This paper contributes to the empirical, case-study approach to this question by examining the roots of Roosevelt's gold policy experiments of the first year of his presidency. I begin by reviewing two well known examples of *a priori* analyses of the relation between economic ideas and economic policy. I draw attention to the ambiguities which such theoretical analyses yield, and suggest an empirical approach may be more useful. I give reasons why Roosevelt's gold policy is a particularly good case for study, and then dig into the many and tangled roots of this policy.

Two Examples of the a Priori Approach

In any *a priori* approach to our question the author begins by advancing a "vision" of how policy makers behave. The author states his position as to whether government is swayed by "commonsense" or theory; whether it is rational or prejudiced; whether it is public spirited or self interested. The author then adds a vision of the producers and distributors of economic theory: whether economists are rational or prejudiced, public spirited or self interested. The author concludes by drawing from these positions some implications for the influence of theory on economic policy.

The best known example of this *a priori* analysis of the influence of theory on policy is pursued by Keynes in the twenty sixth chapter of the *General Theory*. In that chapter Keynes is pondering the influence his new theories will have on the decisions of Prime Ministers, Chancellors and Presidents. Keynes expresses the opinion that those who make policy are public spirited, and are ruled by theories rather than "commonsense". Unfortunately, the theories which rule them are the ones they were taught in their youth. Consequently they are frequently governed by theories which have lost application; they are the "slaves of defunct economists". For this reason economists making public spirited proposals, based on theories with a current application, may have no immediate success. But as time passes, and as Cabinets and Departments are percolated by younger people with more modern educations, the triumph of more modern theories will ultimately be secured. Evidently, Keynes was optimistic about the power of enlightened theorising to influence policy, at least in the long run. *In the long run we are all rational.*

Another example of the *a priori* approach, but one with much bleaker conclusions, has been provided by public choice theorists, especially Tullock, Stigler, McCormick and Tollison (e.g. McCormick and Tollison 1981). Policy makers, according to these authors, are not public spirited; they are interested in power, prestige and perquisites. Consequently, public spirited proposals of economists will succeed only when the public interest coincides with the private interest of the policy maker, something which these writers think will infrequently occur. Economists who have adopted this position (e.g. Friedman (1986)) are consequently pessimistic about the influence of economic theory on economic policy.

The crucial difference between Keynes and public choice theorists concerns the degree of public-spiritedness of policy makers. I find it difficult to choose the best assumption here; to swing too much in a direction of Tullock etc. is to give too a facile characterisation to policy maker's motivations; but to swing too much in Keynes' direction is to give a too naive characterisation to them. As a referee of this paper put it, policy decisions are "usually some hard to delineate mixture of ideology, opportunism, morality, private and public interest occurring simultaneously".

An Empirical Approach

An empirical approach to our problem may eliminate the difficulties faced by *a priori* reasonings. In this approach the author looks at specific episodes of policy making in an attempt to directly observe what influence theory has had on the decisions made. The episode we will examine is Roosevelt's decisions with regard to the dollar price of gold between 1933 and 1934. More specifically, we will be concerned with (i) Roosevelt's refusal in June 1933 to restore a definite parity between dollar and gold, and (ii) his policy of actively increasing the dollar price of gold in the latter part of 1933.This is an interesting case study for several reasons:

(i) Roosevelt's decisions were genuine decisions. Here we are not studying pseudo-decisions which merely validate what has happened, or what must happen. None of Roosevelt's decisions were forced on him, or were inevitable. His decision to scupper the orthodox gold standard was not dictated by events. One proof of that is the shock, indeed wonderment, which his decisions provoked. They were without precedent; "Never before had a government deliberately cut the gold (or silver) value of a nonmetallic currency that stood at or near parity in the foreign exchange markets, that was backed by ample international liquidity and that was no longer threatened by a panic". (Palyi, 1972, p. 280)[1].

(ii) Roosevelt's decisions do seem to be the product of economic theorisings. However, they were the product of economic theorisings which were on the margin of academic economics.

Orthodoxy did not approve of these ideas; and neither did the developing counter-orthodoxy of Keynes and his followers. The provenance of Roosevelts ideas were, to a large extent, a tiny band of agricultural economists, whose theories have since then been ignored, and treated as almost crank[2].

A Brief Chronology of Events

The episode under study begins with the Inauguration of Roosevelt in first week of March 1933. During March 6-10 1933 the orthodox Gold Standard suffered its first blow, when a Presidential executive order prohibited gold payments by banks and non-banks. But the dollar price of gold was not affected; it remained at "par" (Friedman and Schwartz, 1963, p. 471). On April 20 Roosevelt indicated to a news conference that, in order to raise commodity prices, he would welcome and would allow a depreciation of the $US. Shortly afterwards, the free market in gold began to depreciate the dollar against gold (Friedman and Schwartz, 1963, p. 465). This depreciation was generally seen as a temporary measure. It was, additionally, an irritant to the governments of France and Britain, which urged stabilisation. There emerged a general expectation that at the World Monetary Economic Conference in June 1933 the US would restore some stable parity between the dollar and gold. It was an expectation which Roosevelt did not discourage. (Davis, 1986, p. 157). And it was the expectation which Roosevelt's delegation to the Conference carried with them. They were to be surprised.

Roosevelt did not attend the World Monetary Economic Conference. Between June 17 and July 4 he was sailing on a 45 ft schooner, the Amberjack II. At the end of this nautical excursion, on July 2, Roosevelt sent a Message by telegram to the Conference which destroyed the hopes of a return to stable parities. In it he dismissed the stabilisation of dollar price of gold as a "fetish" of "so called international bankers", which should be replaced by "efforts to plan national currencies with the objective of giving these currencies...a purchasing power which does not vary in terms of the commodities ... of modern civilisation". (Davis, 1986, p. 193).

This Message was greeted by dismay and outrage by the politicians of the UK, France, Germany and Italy, "who were generally convinced they had been deliberately deceived and misled" by Roosevelt's earlier comments (Davis, 1986, p. 194). Raymond Moley, a Roosevelt adviser, recalls meeting Ramsey Macdonald at this time; "I have rarely seen a man more distraught than he was that morning. He turned a grief-stricken face to me as I came in and he cried out, 'This doesn't sound like the man I spent so many hours with in Washington. This sounds like a different man. I don't understand'" (Moley, 1938, p. 263). The message destroyed the Conference; it broke up several weeks later, never to reconvene.

But Roosevelt was to throw a second "bombshell". Beginning in 22 October 1933 he ordered dollar purchases of gold in a deliberate attempt to increase the price of gold. The depreciation of the dollar up till October had been the work of the market; henceforth the US government would deliberately engineer a further depreciation. This policy ceased at the close of 1933, and on 30 January 1934 the value of gold was stabilised at $35 per oz. What was behind Roosevelt's two decisions ?

Sir Basil Blackett

Raymond Moley in his memoirs claims to have "known" that Keynes' *Treatise on Money* "had greatly influenced F.D.R." in the months preceding his decision to thwart a restoration of the gold standard at the World Monetary Economic Conference. (Moley, 1938, p. 236). Presumably, Moley is referring to Keynes' mockery of the "mystique" of gold in the thirty fifth chapter of the *Treatise* (printed as "Auri Sacra Fames" in *Essays in Persuasion* 1931). However, Keynes does not actually advocate the termination of the gold standard in the *Treatise*; he prefers an "internationally managed gold standard" (1930, Volume II, p. 338). Therefore, a more direct source for Roosevelt's discontent with the gold standard should be sought before ascribing it to Keynes' own diffident evaluation of it. In seeking this source, it should be kept in mind that Roosevelt made the decision on his yacht, removed from the usual flood of advice from officials and cabinet. But he was not insulated from all suggestion. On the yacht he was given by Colonel House a book (Friedel, 1973, p. 478): *Planned Money* by Sir Basil Blackett. Who was Blackett and what does *Planned Money* say?

Blackett was a British Civil Servant of considerable distinction. The word "first" tends to recur in a summary of his career. After obtaining a first at Oxford in 1904, he came first in the civil service examination and joined Treasury, where he eventually became "first controller" of finance. (*Dictionary of National Biography*, 1931-1940). It may also be worth noting that in 1913, in his capacity as Secretary of the Royal Commission on Indian Currency and Finance, Blackett came to know J.M. Keynes. It was Blackett who, in the first days of the First World War, invited Keynes to join Treasury. (Skidelsky, 1983, p. 289).

On leaving the civil service in 1929 the patronage of his friend, Montagu Norman, secured for Blackett a directorship of the Bank of England. We may wonder whether Norman would have had desired his appointment if he foresaw how, with the onset of the Great Depression, Blackett's counsel would depart drastically from traditional Treasury wisdom. In the early 30s Blackwell became an advocate of deficit finance. He rejected Say's Law, since saving "has[3] too often meant simply adding to the unemployed". (Blackett, 1, 1932, p. 111). He also advised Lloyd George on his "New Deal".

More pertinent to our own concern here, he advocated the abandonment o the pre-war international monetary arrangements. He expounded his views in *Planned Money*, published in 1932. In *Planned Money* Blackett asserts the gold standard was obsolete. He complains of "... the extraordinary hold which the gold mentality has obtained, especially among the high authorities of the world's Central Banks. The gold standard has become a religion for some of the Boards of Central Banks in Continental Europe, believed in with an emotional fervour which makes them incapable of an unprejudiced and objective examination of possible alternatives" (Blackett 2, 1932, p. 71). In Blackett's analysis, adherence to the gold standard meant the sacrifice of price level stability for the sake of exchange rate stability, and the sacrifice was not worth it.

Blackett's own alternative was not precisely articulated. But he favoured a fiat currency which would (somehow) be managed to obtain price level stability. (Blackwell quotes approvingly Plato's suggestion in the *Laws* Bk V of an inconvertible, fiat currency). The fiat currency would be linked to other currencies by fairly rigid parities. This may seem like a pseudo-gold standard. The crucial difference, however, was that the world's supply of gold was a matter of accident; it was not "planned". The fiat currencies would be "planned" to ensure stable prices; stable exchange rates would emerge as a consequence.

Blackett's book is well written. The prose is clear. The tone achieves confidence without stridence. It went through two printings. The *Times* obituary suggests "his book powerfully influenced sections of American opinion in favour of the voluntary devaluation of the dollar, which took place a few months later" (*Times*, August 16 1935). Whether it influenced Roosevelt's opinions can't be proved. For that matter, it can't be proved he read it, though one of his biographers points out he had "ample time" to do so (Davis, 1986, p. 183). But Roosevelt's Message does contain one trace that suggests he did read it; Roosevelt at one point in his Message advocates efforts to "plan national currencies". "Plan" was something of a motif for Blackwell, whose book was entitled *Planned Money*. However, Blackett only recommended the abolition maintaining the dollar value of gold. He never recommended intervention to increàse the dollar value of gold. The source of that second policy seems to have been largely two agricultural economists from Cornell; George Warren and Frank Pearson.

Warren and Pearson

The senior of these two was George Warren (1874-1938). The following profile gives us a flavour of the man;

> "Dr Warren was - or he convincingly impersonated - the archetype of the American hayseed, down-to-earth in every sense. Born on a farm in Nebraska in 1874, he had graduated from the State University of Nebraska with a degree of farm management, had written a number of books and pamphlets with earthy titles such as "Elements of Agriculture", "Alfalfa", "An Apple Orchard Survey of Orleans County", and "Some Suggestions for City Persons who Desire to Farm", and had received his Ph D from Cornell in 1905, remaining there to teach. Photographs taken of him in 1933 show a stocky smooth faced man approaching 60 who peers through round, black-rimmed spectacles with a steady vacuous gaze slightly reminiscent of Calvin Coolidge's and who invariably has a clutch of pencils sticking out of his breast pocket. He was given to careless dress, homely witticisms and pithy irrefutable sentences like "Here is a farm, here is a farmer and here are the facts" (Brooks, 1969. p. 109).

This appreciation, however slanted, communicates two truths; Warren was an agronomist first and an economist second, and had a predilection for "facts" over theorising. Warren obtained a bachelor's, master's and doctor's degree in agriculture at Cornell. In 1906 he became a professor of agronomy there. And in 1910 he became professor of farm management. His specialism was statistical studies of agricultural prices and quantities. This gave him some prominence in the early econometrics of farm prices. One of his books, *Inter-Relationships of Supply and Prices*, was reviewed by Keynes in 1929 in the *Economic Journal*. Keynes praises the "great skill and completeness" of this work of Warren and his co-author Pearson. But he notes that the authors are "strangely free from attempts to philosophise, except in the most elementary way, about the results..." (Keynes, 1983, p. 229). Keynes also notes that "It is curious that whilst this book is almost entirely concerned with calculations as to the elasticity of demand, this technical term is not, I think, anywhere mentioned therein" (Keynes, 1983, p. 230). Certainly, Warren and Pearson's books display only the rudiments of economic theory, and even those rudiments are sometimes mishandled.[4]

Warren and Pearson acquired a far greater renown during the Great Depression through their remedies for economic distress. They believed, as did many others, that a recovery would require a restoration of money prices of commodities. What made their position distinctive was the means by which it could be achieved. They believed it could be done by raising the dollar price of gold. Their reasoning began with the arbitrage relation governing the dollar price of goods, the dollar price of gold, and the gold price of goods.

$$P = E\,Pg$$

P = $ price of goods, E = $ price of gold, Pg = gold price of goods.

The next premise in their theory was that, Pg, the value of gold in terms of commodities, was determined by the demand and supply of gold. Finally, they assumed that government set the money (ie dollar) price of gold, as under a gold standard. This assumption completes their model. In this model money prices are set by (i) the demand and supply of gold and the (ii) the dollar price government gives to gold. Because gold is the key variable in this theory of prices we will call it "metalism". Metallism has the implication that by increasing the money price of gold government could increase the money price of commodities. Metalism was an unorthodox theory of prices in 1933: to Keynes mind it was "rubbish". (Brooks, 1969, p. 112). Metalism is also antagonistic to the non-Keynesian view which emphasises the quantity of money, or monetarism, which sees money prices as determined by the demand and supply of money.

Warren and Pearson were well aware of the antagonism of their theory to monetarism; they saw their theory as a rival to it. They did not deny a proportionality between money and prices, but they appear to have believed the direction of causality in that relationship ran from prices to money. It was their theory, not the Quantity Theory, which isolated the *causes* of price fluctuations.

Metalism and Monetarism in The Classical Economists

Despite its distance from some far more popular rivals, Warren and Pearson's theory of price determination should not be dismissed as crank; it has very respectable Classical roots. Classical economics does contain both Metalism and Monetarism.

Consider, first, David Ricardo. It was his doctrine that the gold price of commodities was determined purely by technological factors (1951, p. 352). He also recognised the arbitrage relation between the money price of commodities, the money price of gold and the gold price of commodities. Consequently, Ricardo believed a change in the "value" (ie labour content) of gold would change money prices. All this would be quite congenial to Warren and Pearson. But Ricardo was also a monetarist who stressed the importance of the quantity of money for prices, even under a gold standard. (1951, pp. 353, 354) Mill shared these two stances with Ricardo, and, of the two, I think Mill was more aware of the need for a reconciliation. How did they reconcile their Monetarism with their Metalism?

I think we may summarise Ricardo and Mill's reconciliation as follows; monetarism is the relevant doctrine for the short run, and metalism is the relevant doctrine for the long run. To put this in the language of Classical economists, the *market price* of goods, in terms of money, was determined by the quantity of money, but the *natural price* of goods, in terms of money, was determined by the technology of gold production. This position is advocated clearly, if diffusely, in Chapters 8 and 9 of Book 3 of Mill's *Principles of Political Economy* (1852).

Market prices in terms of money were supposed to gravitate to natural prices, in terms of money, by adjustments in the quantity of money. There were two adjustment mechanisms. The first was the Humean one: any increase in the quantity of money would increase prices, (monetarism), but this increase in prices would lead to a balance of trade deficit which would eliminate the increase in money, and so induce prices to drop back to their natural level (Ricardo, 1951, p. 358). But the more fundamental adjustment mechanism was a Smithian adjustment of production to discrepancies between market and natural prices; if money prices were such that the actual purchasing-power of money was above its natural level, then gold production would increase, consequently increasing the the money stock, and thereby driving the purchasing power of money back to its natural level. In the long run, the value of money is determined by the technology of gold production, and the money-gold parity. Thus we see that the position which Warren and Pearson took was not crackpot; they had distinguished precedents. They could be interpreted as advocates of a Classical model with infinitely swift speeds of adjustment.

The Intellectual Transmission Mechanism

Warren was introduced to Roosevelt in December 1930, by Henry Morgenthau, who had been a student of Warren at Cornell. Roosevelt was then Governor of New York, Morgenthau was heading a New York State agricultural commission, and Warren was serving on that commission (Schulyer, 1958, p. 968). Initially, therefore, Warren was only an adviser on agricultural matters. But he managed to interest Roosevelt in his price theories and (apparently) his publications advocating them. (Fusfeld, 1957, pp. 193-194). In May 1932 Roosevelt wrote "I am doing a lot of studying down here on the fluctuating dollar. If we don't do something for stabilisation we are all headed for trouble" (Fusfeld, 1957, p. 194).

Morgenthau restated the Warren-Pearson case to Roosevelt on board the Amberjack II voyage of June 1932. On June 30, just 2 days before Roosevelt's "bombshell" telegram, "Morgenthau expounded to Roosevelt more fully that he had done before the price theory of George Warren and Frank Pearson. He had with him, this time, charts and graphs, which he displayed to show how purchases of gold by the government at variable prices somewhat higher than the going market rate might be used not only to raise commodity prices but also to manipulate them in such a way as to achieve, ultimately, a permanently stable "commodity dollar". There was lively discussion of all this and (though vaguely) of the possibility of establishing a new international monetary system along the same lines" (Davis, 1986, p. 187). The responsibility of an idea for policy decisions could hardly be plainer. But it may not be necessary to give all the credit to Warren and Pearson. There was one other economist who pressed the Warren and Pearson proposal on the President. This man was not a hayseed, but the preeminent monetary economist of his day, America's principal advocate of Monetarism, Irving Fisher.

Irving Fisher's Role

Fisher was an embodiment of the alliance between Monetarism and Metallism, for which Ricardo and Mill provide precedents. Fisher was heedful of the arbitrage relation between the gold price of commodities and the dollar price of goods, and he had a clear vision of how changes in the gold value of commodities would change the dollar price of goods under a gold standard. (See, for example, Fisher, 1913, Chapter 6). These changes in gold values, he believed, were a source of instability in money prices. To eliminate this source of price instability he had, since 1913, proposed tying the value of the dollar to commodities rather than gold. (Fisher, 1913, pp. 337-348) Fisher did not propose the monetary authority actually buy and sell commodities at pegged dollar prices. The dollar would still be pegged to gold; but the peg would be adjusted as the purchasing power of gold went up and down. If the commodity purchasing power of gold went up; the gold purchasing power of the dollar would be decreased; keeping constant the commodity purchasing power of the dollar. *This was essentially Warren and Pearson's proposal.* It is therefore not surprising that Fisher held the work of Warren and Pearson in high regard. In May 1932 Fisher wrote to his wife; "Warren and Pearson's work seems to me of a very high order. I cannot agree with you that his work is wrong or useless. It is I believe convincing to those who have read it with an open mind". In a letter to Jacob Viner Fisher described their work as "splendid", "admirable" and "striking". (Allen, 1977, pp. 570-571).

Thus Warren and Pearson's proposals can be traced to Fisher. And since Fisher virtually claims to be the originator of his adjustable gold peg scheme (Fisher, 1920, p. 113), it would seem that Roosevelt's gold policy find their source in the bright, optimistic scheme-making mind of Irving Fisher. Between 1912 and 1934 Fisher pressed his adjustable gold peg scheme proposals in "99 addresses, besides 39 letters to the press, and 161 special articles, as well as 9 testimonies at hearings held by government bodies and 12 privately printed circulars, together with 13 books bearing on the subject" (Fisher, 1956). He presented his views in person to Woodrow

Wilson in 1912, and gave him an early draft of *Stabilising The Dollar*. (Fisher, 1956, p. 189).

This effort, however, bore little fruit. By the late 1920's Fisher's own reliance in the gold peg as a remedy of inflation had receded and he had become interested in the possibilities of new monetary instruments of the Fed; open-market operations, and the manipulation of discount rates and required reserve-ratios. (Barber, 1985, p. 25). But the election of Roosevelt promised Fisher a new opportunity for all his schemes. Between 1933 and 1939 Fisher conveyed his views on various topics in 100 letters to the President. He also met Roosevelt in early August 1934 at which he explained the advantages of flexible gold content of the dollar. On this occasion Roosevelt asked Fisher whether he agreed with Warren and Pearson that inflating the dollar price of gold would raise the dollar prices of commodities; Fisher unhesitatingly agreed (Fisher, 1956, p. 279). After the meeting he told his wife "at last there is a statesman who has the audacity as well as the understanding to do the things which for twenty years, I've been trying to get done" (Fisher, 1956, p. 281).

The Importance of Being Unimportant

In the previous sections I have shown the direct intellectual roots of Roosevelt's gold policy are fairly easily identifiable. But attention should also be paid to the broader mental outlook which predisposed Roosevelt to take unorthodox advice. A.W. Coats (1958, p. 77) has written aptly of the "the contemporary supremacy of economic heterodoxy" in the United States at this time[8] A broad range of unorthodox policies were touted as remedies for economic depression. This range included the inflationism of William Rogers, who favoured substantial bond purchases by the Fed, as well as a determined and politically significant lobby which favoured the remonetisation of silver (Friedal, pp. 323-325, Everest, 1950). There were additionally a considerable number of fiscal activists, which included many so-called orthodox economists, such as Frank Knight and Jacob Viner (Davis, 1971, pp. 16,40). American institutionalists (e.g. Wesley Mitchell) were also prominent at this period. Rather than "gold" being the single voice of dissent from a uniform orthodoxy, it was one voice amidst a chorus of dissent.

Coats has attributed this profusion of heterodoxy to the pragmatism of American mental attitudes, a pragmatism which found its philosophic articulation in the writings of John Dewey (e.g. 1929). To quote from the *International Encyclopedia of Social Science*, "Much of Dewey's work consisted of polemics against . . . the usual message of classic philosophy. . . . that behind the everyday world of change and irrationality there is an unchanging and rational world". (Sills, 1968, p.157). The incompatibility of this outlook with neoclassical theorising is plain. But it lends itself well to Institutionalists,[9] and to other proponants of unorthodox activist remedies. Therefore, the ascendancy of Deweyian pragmatism presents us with a paradox. Dewey was concerned to dethrone "intellectualism", to raise the prestige of action relative to thought. But this attitude actually gave a greater power to ideas. It did this by eroding the various inhibitors on the use of new ideas; by removing checks of a "logical" nature, by reducing the importance of the fine intellectual pedigree, and by letting the success or failure of ideas be the only criteria by which they are judged. Dewey's pragmatism actually emancipated new ideas from the hindrance of orthodoxy and "sound judgement", and gave them space to prove their mettle. Thus Deweyian Pragmatism bears some responsibility for the adoption of supposedly "crank" policies, like those of Warren and Pearson.[10] But the question remains open as to why gold was chosen, rather than any of the other unorthodox remedies. One factor which may have favoured the Warren and Pearson proposals was that Roosevelt had actually heard something like these doctrines before: in the economics courses he took at Harvard between 1900 and 1904.

Roosevelt's Education

By the standards of the time Roosevelt had received a significant formal education in economics. 18 of the 121 credits he earned at Harvard were in that subject. His note books survive and are in the Harvard archives, and have been consulted by Fusfeld (1957). The archives indicate the future president took two courses in Money and Banking by Professor Andrews. Andrews, like Mill, seems to have been both a Monetarist and a Metallist simultaneously. Andrews taught Roosevelt that "the general level of prices and the price of gold move together" (Fusfield, 1957, p. 263). The causation ran from the dollar price of gold to the dollar price of goods. An increase in dollars per gold; i.e. an increase in the dollars a unit of gold could buy, increased US exports and that lead to higher demand and higher dollar prices for commodities. This is in the spirit of Mill, and need not be antithetical to Monetarism.[11]

But Andrews put on his reading list a monetary economist who was rather more pointedly anti-monetarist, and put much more stress on the role of the dollar price of gold; J. Laurence Laughlin, Head Professor of Political Economy at the University of Chicago from 1892 until 1916. Laughlin was a "hard-money" man, who would have rejected Warren and Pearson's inflationist schemes as "fraudulent and dishonest" (Laughlin, 1919, p. 185). Yet his theoretical position was much less antagonistic to these two writers than his policy stance. Firstly, Laughlin was, in the judgement of Milton Friedman, in "rigid and dogmatic opposition to the quantity theory of money" (Friedman, 1988). Specifically, Laughlin, like Warren and Pearson, rejected any causal role for money; "...the quantity of the actual media of exchange...is a result and not a cause of the price-making process....The media of exchange may rise or fall in quantity without themselves affecting the general level of prices" (Laughlin, 1919, p. 182). Like Warren and Pearson, Laughlin believed that if an increase in bank notes has any effect on prices it is mainly indirectly, through the economisation of the demand for gold (Laughlin, 1919, p. 181). Secondly, Laughlin like Warren and Pearson, believed that it was "absolutely plain" that an increase in the dollar price of gold would raise money prices (1919, p. 184). Thus, Laughlin's theoretical scheme was very similar to Warren and Pearson's. Is it possible that Warren and Pearson's doctrines awoke a teaching which had laid dormant in Roosevelt's mind for 30 years? In adopting these Warren and Pearson's strategies was Roosevelt here exemplifying Keynes' practical man, who was ruled by the ideas taught in his youth? It is an interesting possibility.[12]

Implementation

On 25 October what the *Times* called "the boldest economic experiment in history" began. Each day the price of gold was inched up erratically according to Presidential whim. However, the response in wheat and cotton prices was disappointing to the architects of the scheme.[13] The index of wholesale prices stood at the same level in December 1933 as it did in September 1933. (Crawford, 1940, p.337). And the policy became a topic of public dispute. The American Chamber of Commerce and the American Federation of Labour condemned it. Montague Norman told the New York Federal Reserve Bank that "the whole world will be put into bankruptcy" (Blum, 1959). Respectable opinion from two prestigious centres of learning also expressed their dissatisfaction. Late in November 1933 Roy Harrod, James Meade, R.G.D. Allen and several other Oxford economists submitted a memorandum to Roosevelt which welcomed the abandonment of the gold standard, but added "we do not believe that the purchasing power of the dollar can be... reduced by depreciating its value in terms of... gold". They suggested a more likely consequence would be a reduction in the gold price of commodities (Freedman, 1967, p. 172). In December Keynes published an open letter to Roosevelt in the *New York Times* which dismissed the advice of Warren and Pearson as "crack brained and queer" (Freedman, 1967, p. 178); it is foolish "to believe that there is a mathematical relation between the price of gold and the prices of other things...the recent gyrations of the dollar have looked to me more like a gold standard on the booze than the ideal managed currency of my dreams". (Freedman, 1967, p. 181). In December 1933 Roosevelt abandoned his policy; and in January 30 1934 it was fixed at $35 by proclamation. Varying the dollar price of gold never again became a policy with any popularity.[14]

Concluding Comment

The episode of Roosevelt's gold policy tends to vindicate some elements of Keynes' perception of the relation between theory and policy . Firstly, Ideas seem to have been more powerful than Vested Interests. It is true that the American Farm Bureau Federation did urge the Warren and Pearson program on Roosevelt at the time of his inauguration.[15] But can we reasonably doubt that Roosevelt's purpose was to revive an entire economy, and not to merely redistribute its income between particular sections?[16] Secondly, Ideas were more important than Common Sense. Roosevelt was not the sort of practical man who is ruled by common sense and precedent; he grasped a theoretical speculation and pursued it with some determination. Thirdly, the Ideas which were powerful did have a sort of academic lineage. Ricardo and Mill do have a remote responsibility for the events in this period.

At the same time, I'm not sure whether the episode evinces the power of *rational* thought. It is not clear how much Roosevelt understood these policies. Fisher complained that the President saw no distinction between raising the dollar price of gold and reducing crop acreage (Fisher, 1956, p. 282). Roosevelt's own final defence of the proposal was always to ask what alternative existed. So rather than suggest the power of rational thought, the episode might be a manifestation of the urge to action in a time of crisis.

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Notes

1. It is true that he was under a great deal of pressure to do something to relieve the Great Depression.
2. See, for example, Joan Robinson (1973, p. 102).
3. James Harvey Rogers (1938, p. 41) recalled meeting in 1933 a Director of the Bank of England who told him that "we need a deficit so badly in this country I have recommended that, if it can be secured no other way, we return all the taxes". Is it implausible to suppose this unidentified Director was Blackett?
4. Consider, for example, the naivety of this statement. "If the supply of gold were doubled it would halve the price of wheat' (Warren and Pearson, 1935, p. 82).
5. Spahr, the most copious critic of Warren and Pearson, identifies the pair as "pure, unqualified, undiluted bullionist theorists" (Spahr, 1934, p.5).
6. Harrod pointed out this kinship to Roosevelt in the Oxford economists memorandum. (Freedman, 1967, p. 172).
7. The English economists can claim a degree of precedence here. Marshall in his 1887 paper "Remedies for Fluctuations of General Prices" proposed a Standard of Value Independent of Gold and Silver. This was essentially a legal arrangement whereby all money debts would be regularly adjusted in the light of inflation. This arrangement could be interpreted as tying the monetary unit direct to the Consumers Price Index. However, the gold price of the monetary unit which is the critical policy variable for Fisher's and Warren and Pearson's schemes, is entirely absent from Marshall's schema. This doubtless reflects Marshall's view that *even under a gold standard* the commodity value of gold has little relevance for money prices (1925, pp. 193, 194). Keynes shared Marshall's doubts on the importance of movements in the value of gold for price movements, and was correspondingly cool to Fisher's proposal. In the *Tract on Monetary Reform* Keynes wrote of Fisher's scheme "I doubt the wisdom and practicability of anything so cut and dried. Professor Fisher's method may be adapted to deal with long period trends in the value of gold but not with the, often more injurious, short-period oscillations of the credit cycle. (1971, p. 148). Nevertheless, he, in sympathy with Fisher's proposal, favoured an adjustment of the money price of gold whenever a change in the commodity value of gold was actually responsible for a price disturbance (1971, p. 150).
8. This heterodoxy has been described by Barber (1985) and Davis (1971).
9. The *New Palgrave* entry on Institutionalism attributes a stimulative influence to Dewey's philosophy.
10. In Coats' judgement Roosevelt's piecemeal approach did not merely reflect the expedience of the politician but his "remarkable capacity for absorbing current ideas - he had a flypaper mind"; his was a Deweyian mind.
11. In Fusfeld's judgement, "The thread running through the discussion was the general validity of the quantity theory" (Fusfeld, 1957, p. 131).
12. But only a speculation. There is no positive evidence that Roosevelt, an indifferent student, paid attention to Laughlin or his teacher's reading lists.
13. Contrary to the general impression of failure, Friedman and Schwartz believe that the gold purchase policy did succeed in inflating commodity prices (1963, p. 466). Blum musters some statistics in favour of this view (1959, p. 74).
14. But Roosevelt's experiment may have had distant reverberations in later policy advice. In several papers in the 1950s and 1960s (eg Harrod, 1965, pp.58-85) Harrod, who had played a small role in the original episode, recommended increasing the dollar price of gold. But his was only proposed as a remedy for a shortage of exchange reserves. It was not intended to manipulate the price level. (Johnson, 1970, pp.

266-293).

15. Schulyer *et al* (1958, p. 696). It is also worth noting that Friedal's comment: "James Warburg, who had no sympathy for Warren, remembered that the President was fond of using cotton, wheat, silver and gold as illustrations in his conversation. 'Those were the four commodities', Warburg explained, 'that had political pressure behind them and they were always the ones that came up.'" (Friedal, p. 325).
16. Another favourable aspect of the policy was that its cost of failure was low. It might not do much good, but it would not do any harm either. This was the attitude of one of Roosevelt's "Brain Trusters", Raymond Moley (1938, p. 282).

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