We're going on a duck hunt

SUSIE J. PAK

Michael D. Bordo and William Roberds, editors

A RETURN TO JEKYLL ISLAND
The origins, history, and the future of the Federal Reserve
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On the centenary of the meeting that led to the founding of the US Federal Reserve, a distinguished panel of economists gathered to ponder the legacy and history of America's central bank. The conference was held at the Jekyll Island Club, the location of the original convening, where Senator Nelson Aldrich and Assistant Secretary of Treasury A. Piatt Andrew Jr spent ten days with a group of the nation's top bankers, including J. P. Morgan & Co partner Henry P. Davison, Kuhn, Loeb & Co partner Paul M. Warburg, and National City Bank President Frank A. Vanderlip, discussing a proposal for a central bank. Unlike the 1910 meeting, which was secret, the 2010 proceedings have been documented by an engaging volume of essays. Taken together, the papers in *A Return to Jekyll Island* highlight the complicated relationship between history and policy as well as the challenges of reconstructing the past in order to predict the future.

The decision to meet at Jekyll Island reflected the conference organizers' desire to analyse the legacy of the Federal Reserve from the perspective of its founders. What did the founders envision? What were their intentions? Determining the answers is neither simple nor straightforward. Because of the long history of controversy over central banking in the United States, and given the anti-banking fervour after the panic of 1907, when a collapse in the stock market was followed by a run on a number of banks, the 1910 party felt compelled to hide their plans under the guise of a duck-hunting expedition so that even the record of who attended is not entirely clear. As Frank Vanderlip later wrote, the party believed that "If it were to be exposed publicly that our particular group had got together and written a banking bill, that bill would have no chance whatever of passage by Congress". For this reason, Paul Warburg explained, "The results of the conference were entirely confidential. Even the fact that there had been a meeting was not permitted to become public".

The meeting and its details only began to emerge when Senator Carter Glass began to publish a series of twenty-three articles in the *New York Evening Post* on the history of the Federal Reserve Act in 1927. Glass seems to have been primarily concerned with the question of who could claim credit for the Federal Reserve System, and, in one of his articles, he wrote that Warburg had engaged in an unsuccessful publicity campaign to impress his views on Congress in 1913, and that Warburg could not claim rightful credit as the father of the Federal Reserve system. In response, Warburg began to write his personal recollections of the Fed's history, and in 1930, he decided to publish his manuscript despite what he called a "strong distaste for allowing myself to be drawn into a discussion of phases in our banking history in which I had played an active part".

By that time, the country was also in the midst of the Great Depression, and Warburg had become "convinced that the Federal Reserve System had entered upon a gravely critical period in its career, and that for the discussion about to ensue it was highly important that certain vital facts in the origin and growth of the System be adequately understood". Yet while he finally acknowledged that a meeting had in fact taken place, Warburg offered very little detail. "Though eighteen years have since gone by", he wrote, "I do not feel free to give a description of this most interesting conference concerning which Senator Aldrich pledged all participants to secrecy." Warburg only broke this pledge because he had learned that Nathaniel Wright Stephenson was about to publish a biography of Senator Aldrich, which included "an authorized account of this episode".

Although Stephenson's biography offered a basic description of the meeting, the passage of time limited the information that could be gathered from the key participants. By the time the news of the meeting became public, Aldrich had been dead for fifteen years. Henry Davison died in 1922, and it was left to Davison's protégé, Morgan partner Thomas W. Lamont, to write the story of his involvement. Lamont was able to cull other details from Warburg before Warburg died in January 1932, but he actually told Lamont that he was not even sure who originated the meeting, though his own personal belief was that it was Davison. Two years later, Vanderlip filled in some of the details by publishing a series of autobiographical articles in the *Saturday Evening Post*. Vanderlip's account of the meeting differed, however, in one significant way from all the other versions. In his recollection of Jekyll Island, one person in particular was there, who was not mentioned by Warburg, Stephenson or Lamont: Benjamin Strong, who became the head of the Federal Reserve Bank of New York in 1914. The reasons for not including Strong, who died in 1928, in the other accounts remain unknown.

The unfortunate by-product of the secrecy is that when the meeting did come to light, it only served to confirm the very perception the participants had tried to avoid. Speculation was also heightened by the location of the meeting, which gained its own legendary status. Founded in 1886, the Jekyll Island Club had "a membership limited to 100", and was a vacation destination for the nation's leading families located on a privately owned island off the coast of Georgia. (Jekyll Island only became part of the state of Georgia in 1947.) More of a resort than a club, Jekyll Island was also home to private apartments "attached to the Club House" and larger private residences called "cottages". The Club had segregated schools for the children of white and black employees, a chapel, a golf course, a garden, a stable, tennis courts, and "11 miles of beach". Because none of the attendees was a member of the club at the time, another party or parties would have had to make a request on their behalf to use the club in the off-season. Though the party travelled to Georgia in Aldrich's private railway car, Aldrich did not become a member of the Club until 1912.

The gold vault at the Federal Reserve Bank of New York

At the time of the meeting, J. Pierpont Morgan, the senior partner of J. P. Morgan, was one of the directors of the Club. He was also one of the original 1886 members, as was William Rockefeller, the president of Standard Oil who sat on the board of National City and whose nephew, John D. Rockefeller Jr, was Aldrich's son-in-law (Rockefeller was an owner of a private cottage on the island). James Stillman, the chairman of the board of National City and whose two daughters married two of William Rockefeller's sons, had also been a member of the Club since 1892. Whether Morgan, Stillman or Rockefeller was actually involved with the meeting, we do not know, but the idea that those present were acting as lieutenants for the senior members of their firms or for powerful family interests has become part of the popular lore feeding the perception that the Federal Reserve was created for and by Wall Street's elite.

The fact that the papers of the 2010 conference were published is one way in which the meetings at Jekyll Island clearly differ. The decision to hold the meeting there and the desire to share the proceedings are themselves signs of the extent to which the Federal Reserve has become the status quo. Even though the historical conditions of the Federal Reserve's work have changed, however, the proceedings indicate that certain questions remain, such as those of public trust, the Fed's independence, and the theories and intentions of its leaders.

The papers review the major debates on the Fed and monetary policy. Charles Calomiris's paper ("Volatile Ties and Persistent Conceptual Errors: U. S. monetary policy in 1914–1951") sums up the overarching historical questions: "What did the monetary authority do, why did it behave the way it did, what effects did its policies have, and what should it have done differently?" In other words, what can we learn, how can we learn, and have we learned from the history of the Federal Reserve?

Because the Fed's history has been the subject of extensive analysis, it is important to consider how this volume is a contribution to the literature. The papers range from the intensively archival (Marc Flandreau and Stefano Ugolini, "Where It All Began: Lending of last resort at the Bank of England monitoring during the Overend-Guerney Panic of 1866") to econometric models (Lawrence J. Christiano and Daisuke Ikeda, "Government Policy, Credit Markets, and Economic Activity"). Questions include: did the action (or inaction) of the Fed create conditions that led to financial crisis? (Eugene N. White, "'To Establish a More Effective Supervision of Banking: How the birth of the Fed altered bank supervision'"); and why did the Fed fail to act as lender of last resort during the Great Depression? (Michael D. Bordo and David C. Wheelock, "The Promise and Performance of the Federal Reserve as Lender of Last Resort, 1914–1933")? Many of the papers focus on the Fed's failures and ask why the mistakes were made. The answers range from a lack of understanding or misconceptions of economic principles as they are now understood, to the cultural biases of American society, and political interference.

One of the book's unique features is that it is structured as a conversation between the authors of the articles and their commentators. It is in this interplay between papers and critique that the book is most engaging. Perhaps the volume could have gone even further to transcribe and capture the questions and comments from the audience that must have been spontaneously volunteered on the day of the

event. As often happens in academic conferences, the critiques also raise important questions and point out potential future research. In his response to Flandreau and Ugolini's article on the Bank of England, for example, Barry Eichengreen emphasizes the importance of studying the historical and political context in order to understand why central banks allow members of the banking community to fail. Allan Meltzer's response to Calomiris's article on reoccurring conceptual mistakes by the Fed highlights possible research into the unintended consequences of non-member banks being allowed to fail. In general, two larger themes emerge from the papers and their critiques. The first is the relationship between political and economic power, which as the participants point out has historically been expressed as the tension between the Fed and the state (whether Congress or the Treasury) or of the fear of politics intruding on the market and on monetary policy. The second is the importance of trust, a point made by several papers that was also repeated during the concluding panel discussion, whose transcript serves as the final piece of the book.

Moderated by Raghuram Rajan, the panel discussion was introduced by Dennis Lockhart, began with video commentary by Paul Volcker, and featured Ben Bernanke, E. Gerald Corrigan and Alan Greenspan. Collectively, the group represented the leadership of the Federal Reserve for the past thirty-odd years. The discussion centred on the major challenges of a financial crisis, from the "Volcker disinflation" of the late 1970s to the Great Crash of 1987 and the Panic of 2008. As in the conference papers that preceded the discussion, the panellists expressed disagreements about the Fed's actions, problems, failures or policies. That much was evident, for example, in Greenspan and Bernanke's responses to the question of whether the Fed had done all it could in times of panic, and whether they had a sufficient response for their critics, who included other participants at the conference. One commonality between the panel discussion and the papers, however, was the way in which the conversation of monetary policy incorporated a discussion about the importance of trust and respect. This is particularly interesting given the long-standing debate about the proper attitude of a central bank with regard to impersonal relations or the "anonymous' dealing with the market".

In his remarks, Volcker talked about the leadership of the Fed and the respect for the Fed. "It's that respect and that trust that, at the end of the day, is vital to the acceptance of its independence and to support for its policies. It's those intangibles – to me more important than any technical analysis or intellectual brilliance – that in times of crisis makes it possible for the Federal Reserve to step in, to act, and to act forcibly in the national interest." Corrigan reiterated these points, emphasizing the importance of trust and "collegiality": "I talk a lot about the culture of the Federal Reserve. And I do think that, especially in these trying times, we should recognize, even for our critical friends in the academic community, that the culture of the Federal Reserve is strong, it's been that way for a long time, and I think it will continue to be that way at the end of the day. The maintenance of that culture, including the feature of collegiality that I've spoken about, that I think at the end of the day is the name of the game . . .".

Taken together, the chapters and panel discussion suggest that the issue of trust persists over time and place and remains as relevant today as it did in Britain in the 1860s or the United States in the 1910s. Even when discussing the most recent panic, Greenspan talked about how the lack of trust creates economic instability. While explaining the "two fundamental reforms" he felt were needed in the wake of 2008 ("One is to get adequate capital, and two, to get far higher levels of enforcement of fraud status"), Greenspan said, "Fraud creates very considerable instability in competitive markets. If you cannot trust your counterparties, it won't work, and indeed we saw that it didn't".

Trust and respect also play their part in the foundation story of the Fed. The participants' personal stories suggest that the popular view of Jekyll Island, of an establishment working together in their own interests, does not reflect reality. There was a history of co-operation between the different firms represented at the original meeting on Jekyll Island, but social and personal differences among the individual men who represented those firms would have been readily apparent. Paul Warburg, for example, was a partner in Kuhn, Loeb & Co, a German Jewish bank led by his brother-in-law and senior partner, Jacob H. Schiff, who was Pierpont Morgan's primary rival in private banking. The Kuhn, Loeb partners had socially distant relations with the partners of J. P. Morgan & Co and the firms were fundamentally competitors, but they also had strong co-operative working relations because they were able to manage religious and ethnic conflict within their respective spheres of influence. Personally, Warburg had great respect for Davison, but they were not close friends. A gifted economist with a vast knowledge of European banking practices, Warburg left Kuhn, Loeb & Co to join the Federal Reserve board, but his tenure did not end well. During the First World War, he felt compelled to resign when his German origins and his familial ties to Germany gave critics an opportunity to cast suspicion on his loyalty and patriotism.

Like Warburg, Frank Vanderlip also lacked the social capital of men such as Aldrich and Davison, the only two members of the party who became members of the Jekyll Island Club after the meeting in 1910. An Illinois native and the son of a farmer, Vanderlip had been a journalist and treasury official before joining National City. At the time of the meeting, he had only been president for about a year, and for most of his tenure, he worked under the close scrutiny of James Stillman. In February of the year he went to Jekyll Island, Vanderlip had a series of conflicts with J. P. Morgan & Co, believing that the Morgan partners were trying to undermine National City's position by building up the rival National Bank of Commerce. Though Vanderlip also had great respect for Davison, he fundamentally saw the banks as competitors and was territorial about National City's position. His dedication to the bank was not reciprocated, however, and by 1919, he left the bank because of conflicts with Stillman and William Rockefeller after he was also denied the opportunity to become a majority shareholder.

Relating personal micro-histories to the macro-economic history of monetary policy is not straightforward or simple. But if trust, respect and collegiality are as important to the history of the Federal Reserve as its contemporary leaders believe, then the historical basis for that trust and collegiality between the persons who collectively form the institution of the Federal Reserve seem worth investigating. At the very least, the stories raise other questions, such as whether the relationships between banking institutions reflect those of their leaders. If, as the conference participants suggest, the relationships and culture of the Federal Reserve do affect the ways it interprets its responsibilities, understanding that process would, like the study of its past, also help us to understand how the Federal Reserve arrived at decisions that it has made and will make in the future.

Lines to an Old Statue

From pagan ruins I dug you.
Oh, how terrible were those maimed body parts:
smoke-blackened arms, burst lips, splintered legs –
fragments, to be put back together!

Tiredness I disregarded. I toiled day and night
until you were remade:
such joy when you began to walk,
such mad happiness when you started speaking!

I breathed the blush back into your limbs,
and voluptuous heat; I poured blood into your heart,
the seething, hissing, incandescent river of molten metal:
I was father to your thoughts.

See: even now, as I walk in the wilted garden,
I think of this strange miracle. The Master
turns his clouded gaze from departing swallows
back to you. Don't leave me now.

JENŐ DSIDA
Translated from the Hungarian by Clive Wilmer and George Gömöri

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