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FROM THE PAST TO THE FUTURE: IDEAS AND ACTIONS FOR A FREE SOCIETY

CHAPTER TWELVE

FED CHAIR AGONISTES

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Fed Chair Agonistes
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A sure bet in 2020 is that President Donald Trump will bully Fed Chairman Jerome Powell, pressuring Chairman Powell and the Open Market Committee to set interest rates lower than Fed wants them. Chairman Powell wants them. In fact, the only dispute is how brash President Trump will be. After all, the President already got out a few zingers last year. "China is not our problem, the Federal Reserve is," President Donald Trump said after Mr. Powell led his board in lowering interest rates 25 basis points, a smaller increment than the President desired. Last summer the President suggested that Mr. Powell's interest rates were so high that they were preventing the economy from zooming forward "like a rocket ship."

Such audacity feels uniquely Trumpian. It isn't. Though our modern political culture holds that the Federal Reserve is independent, other postwar Presidents have bullied Fed chairmen, whether directly or through loyal proxies. The names of the bullies include Lyndon Johnson and Ronald Reagan. At this event, we are mourning Paul Volcker, the Fed chairman with the greatest fortitude. Volcker didn't complain loudly about Reagan at the time. But he wrote a memoir before he passed away. In that memoir Volcker details the level of the pressure placed upon him. In the summer of 1984 Treasury Secretary James Baker summoned Volcker to the White House. "The president is ordering you not to raise interest rates before the election," Baker told Volcker. The worst example of Fed bullying however is President Richard Nixon's successful campaign to coerce "his" Fed chairman, Arthur

Burns, into leading the Fed in policy that guaranteed devastating inflation.

The story of Burns at the Fed is worth reviewing, because it provides us with a reminder of how politics and personality prevail over character and trade. For if anyone seemed likely to withstand the pressure from Richard Nixon, it was Arthur Frank Burns. In the 1950s, when Nixon was a young vice president, the older Burns chaired the Council of Economic Advisors, winning the admiration of young politicians, including Nixon, for his professionalism. In 1960, when Nixon ran for president the first time, it was the pipe-puffing Arthur from whom Nixon took counsel. Burns warned Nixon that unless Congress and the Fed moved taxes and interest rates down substantially, voters would turn away from the Republican Party and elect John F. Kennedy. The taxes and interest rates did not come down dramatically, and Nixon did lose. But Burns had supplied Nixon with that gift most precious to politicians: a plausible explanation of why the politician's defeat was not the politician's fault. The grateful Nixon never forgot, and in turn gave Burns a gift just as precious, at least to a proud professional: Nixon listened to him. Burns was sure Nixon liked him, and wrote in his diary at one point that he considered himself Nixon's "best friend."

Outsiders placed confidence in Burns for another reason: the high respect paid him by the guild of professional economists. Early on, Burns had won has his peers' approval as a star data cruncher and wizard forecaster. It was said that Burns predicted the strength of the 1955 recovery by the thickness of the cigarette smoke in the General Motors salesrooms. Burns' work on inflation was hawkish, and included a monograph, "Prosperity Without Inflation." He appeared admirably independent, contradicting colleagues with an early and genuinely prophetic determination that corruption in the Soviet regime would kill the Russian economy. Nixon's decision to bring Burns into his administration in 1969 was regarded as a sign of the integrity of both men. People commented that men like Burns with his retro, center-parted, hair and pipe seemed like grownups, a welcome shift from the whiz-kid hires of Johnson and Kennedy.

But after Nixon moved Burns Burns over to the Fed in 1970, Burns found his friend suddenly cooler. Nixon wanted lower interest rates. After a time Burns and his board did lower rates, but as Mr. Powell and colleagues today, the Burns Fed moved in modest increments of 25 basis points. Burns believed he could convince Nixon of the merit of gradualism if he could get the president's ear. Yet this time he could not. Instead Nixon dispatched emissaries such as John Ehrlichman to deliver threats: "The president will take on the Fed publicly if its Open Market Committee retaliates." Or: "responsibility for a recession is directly on the Fed."

By early 1971 Nixon was introducing yet another blocker, this time the new Treasury Secretary, John Connally. Connally was a Democrat, an unorthodox choice for a president, but the real sin in the nomination from Burns' point of view was that Connally was no economist, not even a banker, just, as Burns put it, "a most smooth politician." The offense of the Connally hire was compounded when Connally took a crash course in monetary theory not from Burns but from his predecessor, William McChesney Martin. Connally ordered all White House hands to follow White House policy—and included Burns as a "hand."

Far from making an exception of Burns, the now hardening Nixon simply watched the torture of Burns with amusement. Bullies look for vulnerability. Burns' vulnerability, Nixon thought, was his Jewish background. "You know I think Connally is anti-Semitic," Nixon rambled to Ehrlichman. "It probably troubles him to deal with Herbert Stein and Arthur Burns and Henry Kissinger and [speechwriter William] Safire. Too bad." "The government is full of Jews," Nixon told another aide, H.R. Haldeman. There was "a Jewish cabal" in government. "And they all only talk to Jews." In Burns' case, this was hardly so. The person Burns *wanted* to talk to was Nixon.

As the year 1971 progressed, economic news did not improve sufficiently to please the White House, and Nixon and his men continued to give Burns the treatment. Burns goosed the money supply, irritating Milton Friedman, but not enough to please the insatiable Nixon. Later, Ehrlichman would record the standard scolding he was sent to deliver: "The President made you chairman of the Fed, Arthur," Ehrlichman would say. "You are deeply in his debt. He expects you to be loyal." No move was too petty for Nixon. In those days White House Sunday church services provided a chance for presidential access. Nixon's staff moved to block Burns' attendance: "keep him off Church," read one memo.

By June of 1971 the consumer price index was increasing at an annualized 6% rate, and Burns was desperate. Though a free marketeer, Burns wanted the approbation of his peers. Let someone else – anybody else – deal with the inflation problem. Burns therefore told Nixon that inflation, or its appearance, would abate for a time if Nixon and Congress placed some government restraints on wages and prices. If they didn't, Burns would have to raise interest rates and further irritate his chief executive. Come

July, Burns finally and momentarily heeded conscience and colleagues and led the Fed in raising the discount rate 25 basis points. The President retaliated by allowing his aides to sneak a smear story—adumbration of Watergate!-- in *The Wall Street Journal*. The story included a leak suggesting that Burns was demanding that his own salary be raised 50%. This was false. The story also announced that the "furious" president was considering legislation that would "specifically would bring the Federal Reserve into the executive branch." Burns saw, as he wrote in his diary, that "I would be accepted in the future only if I suppressed my will…" Here Burns had a choice. He could do what the economy needed, or he could, as he put it, "suppress his will." Burns suppressed his will.

What came next, over the summer of 1971, demonstrated the extent of that suppression. For Nixon had indeed absorbed the 1960 lesson, perhaps better than Burns liked. His eye now firmly on the 1972 election, the president mooted a preposterously incoherent stimulus plan: tariffs, a wage-and-price freeze, targeted tax cuts, and closing the gold window, the last vestige of the gold standard. Burns might have lived with individual components, but taken together the plan was professional anathema. Yet when Nixon invited Burns to join the economic team for a Camp David retreat to formalize the plan, Burns was so relieved to be included that after a pro-forma protest against one move – the gold standard suspension – the Fed chairman simply went along. The president, Burns told speechwriter William Safire, had his "wholehearted support."

What followed, too many Americans still remember. For Burns, a momentary elation: the Fed chairman was back in his president's good graces. For Nixon, a political victory – the measures masked the inflation and goosed growth that reelected Nixon in 1972. But great lows followed these short-term highs. Nixon's imperiousness cost him the presidency. It cost the U.S. its economy. A storm of inflation followed when the price controls ended. The 4.5%, 5% or 6% interest rates that Burns in his denial told himself were high enough proved nowhere near the level needed to stop the inflation, which within a few years would surpass 10%. The tragedy was practically Grecian: Burns, the prophet who had spent a career warning of inflation, had promulgated policy that caused it.

The Nixon-Burns story is a saga of personal vanity and human ambition. But it also reflects a political cycle common to nations the world over. Voters reward politicians who give them good times. Presidents want Congress to supply those good times, by voting into laws tax cuts or new entitlement programs. But sometimes – in Nixon's era – Congress doesn't want to cooperate. After all, spending more now makes it even harder for the government to meet long-term commitments – Social Security payments, Medicare – later. So Presidents in their frustration turn to the Fed, knowing that dumping money into the economy will supply those good times – short term, before the inflation kicks in. Since Burns' day, a change in our monetary laws has made it even easier for the Fed chairman to succumb to president's demands that they help the general economy. The Humphrey-Hawkins Act made the Fed's responsibility for the entire economy more explicit by requiring that the Fed pursue, along with the goals of stable money and low interest rates, maximum employment.

What can a meeting of MPS make of all this? We cannot change human nature. Paul Volcker, the Fed chairman who made the right choice, is mourned almost to the point of deification by both citizens who support both political parties. But Volcker was that exceptional benign dictator familiar from history books. What stories like that of Johnson, Nixon and Burns generally show is that leadership at the Fed cannot be conducted with true integrity without more rules governing Fed operation – the kind John Taylor has advocated – so that the Fed does not operate ad hoc. New statute is necessary to remove the employment and growth component of Fed policy. The Burns of 1970 thought he was in charge of the whole economy, a kind of vainglory. But the general assumption then was that the Fed was responsible, and that reinforced the arrogance of an otherwise thoughtful man.

Limiting inflation's likelihood in the future would be easier if the Fed's assignment were more modest: not rocketship captain, but perhaps engineer, assigned to watch meters and monitor money. As a young scholar wrote six decades ago, "all that may be reasonably expected of the federal reserve system is that it will do everything, within its limited powers, to keep the price level from rising further." That scholar's name was Arthur Burns.

AMITY SHLAES

CALVIN COOLIDGE PRESIDENTIAL FOUNDATION

Amity Shlaes chairs the board of the Calvin Coolidge Presidential Foundation, based in Plymouth Notch, Vermont, the birthplace of the thirtieth US president, with an office in the Georgetown area of Washington, DC. The Coolidge Foundation is the sponsor of the popular Coolidge Scholarship, a full college scholarship for academic merit, and the Coolidge Senators program, which exposes gifted students to the values of President Coolidge.

Her newest book is *The Great Society: A New History* (November 2019, Harper Collins). Shlaes is the author of five previous books, four of which are *New York Times* bestsellers: *Germany: The Empire Within*; *The Greedy Hand: Why Taxes Drive Americans Crazy*; *The Forgotten Man: A New History of the Great Depression*; *Coolidge*; and *The Forgotten Man Graphic Edition*. She was a syndicated columnist for ten years, first at the *Financial Times*, then *Bloomberg*.

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