

Introduction

Imagining a Fed in the Making

When I was a professor of money and banking I used to wonder how Federal Reserve officials could be so stupid. Now that I've had some years as a central banker with responsibility, I often wonder how professors of money and banking can be so naïve.

—Karl Bopp, President of the Federal Reserve Bank of Philadelphia

Karl Bopp, the longtime president of the Federal Reserve Bank of Philadelphia, addressed the Federal Open Market Committee (FOMC) for the final time on February 10, 1970.¹ The FOMC is the venue where representatives of all the Federal Reserve System's elements, twelve regional Federal Reserve Banks and the Washington, D.C.-based Board of Governors, come together to forge monetary policy. Bopp welcomed the new chair of the Board of Governors, Arthur Burns, and bid him farewell. After twenty-nine years at the Philadelphia Fed, Bopp was retiring. He used his parting remarks to weigh in on pressures which were forging the Fed into its modern form: an insular, board-centered technocracy. Bopp criticized a three-year-old mandate to “bring about the reduction of interest rates,” which he considered futile. Unfunded wars in Vietnam and against domestic poverty fostered an inflationary environment that pushed interest rates ever higher. Bopp then turned to internal Fed politics, urging recent board appointees to “concentrate on policy” and not micromanage the Federal Reserve Bank of New York employees who implemented FOMC policy directives. Over the past decade, an influx of economists into appointed positions had transformed the Board of Governors from an occupationally diverse body into an economist stronghold.

Bopp's last remark impugned economists' ambition of consolidating Fed power. He cautioned that economists still lacked "comprehension of the linkages among financial and real economic variables . . . ignorance of the connections was colossal." Until Fed policymakers better understood monetary policy's impacts, they should "hesitate . . . to follow recommendations as to policy that might be provided by a computer."

Bopp's criticisms were not new. Five years earlier, he wrote, "The simple truth is that no one comprehends enough to be an expert in central banking. . . . Central banking is an infant, as human institutions go."² Economists found Bopp's critiques puzzling. Central banks had existed for centuries. Milton Friedman and Anna Schwartz had recently published *A Monetary History of the United States: 1860–1867*, which pioneered a new technique for analyzing central bank behavior by measuring monetary aggregates.³ The Board of Governors' technical staff was expanding, forging new models and forecasts, and integrating those tools into the monetary policy process.⁴ Economists believed central banking was evolving from an art to a science.

Bopp and other members of the Fed's old guard were skeptical of this notion, and believed human cognition and judgment remained crucial central banking elements. Bopp could relate to the board's new upstarts. An economics professor as a young man, Bopp had navigated the transition from academia to Federal Reserve service in the 1940s. Unlike his new colleagues, however, Bopp worked his way up through the Philadelphia Fed ranks through decades of hard work, often in deference to inherited practices and ideals he found questionable. Bopp's views carried weight among a retiring generation of Fed officials. Chief among these was William McChesney Martin Jr., the Fed chair often credited with establishing the modern Fed.⁵ Martin became chairman of the Board of Governors in 1951, when the system regained independence after decades of treasury dominance. Martin had championed a "historic democratization" of the FOMC, growing its ranks to include the presidents of all twelve reserve banks in addition to the seven appointed board governors. This vacated a board advantage established in 1935, when the FOMC was constituted as a twelve-member body with seven votes reserved for the board.

Martin's diffuse Fed order was sustained through deference to the New York Fed's expertise. From the time the open market committee first formed in 1922, New York had acted as the system's agent for buying and selling government securities, the main mechanism through which monetary policy is implemented. New York's position at the commanding

heights of finance and America's global trade nexus endowed its officers with a cosmopolitan outlook. They believed America had a national interest in fostering a liberal world order based on free trade and the gold standard and called for directing Fed power externally to promote dollar stability. This book identifies this ideology as Hamiltonian, reflecting an updated application of Alexander Hamilton's financial principles to a world shaped by American primacy.

The economists who invaded the board in the 1960s rejected this philosophy, and the inclusive Fed Martin fostered. The new technocrats believed monetary policy should be directed toward domestic goals, such as accelerating growth or stabilizing prices. They saw New York's aim of directing monetary policy toward sustaining international monetary stability as outdated, harmful even. Various economists had called for the system to turn its attention inward since its 1913 origin, but they were denied positions of Fed authority before the 1960s. This reflected a resilient Federal Reserve Act (FRA) clause requiring the board's ranks to reflect the "different commercial, industrial and geographical divisions of the country."⁶ In practice, this meant appointed governors traditionally hailed from different regions and occupations. The law's denial of any form of central banking expertise was intended to prevent capture by Wall Street. It instead staved off an economist takeover for over half a century, when the modern Fed emerged.

Imagining the Fed traces a struggle for power that began at Jekyll Island in 1910 and ended six decades later with the establishment of a durable Fed technocracy. It shows that before 1970, the Federal Reserve was a site of institutional diversity, contestation, and change. Institutional instability grew from legal ambiguity rooted in compromises among clashing ideals, interest-based conflicts inherent in federalism, the institution-building efforts of Fed visionaries to overcome these faults, and agent-led initiatives to dismantle inherited systems. This book traces the rise and fall of three extralegal Fed regimes which predated Fed technocracy. The modern Fed was built on the legacies of these earlier Feds, which came before.

The Argument: Mapping the Fed's Struggle for Power

Imagining the Fed explains an intergenerational struggle to shape the Fed's policy regime. The title is meant to shine light on an anachronism problem common in Fed studies, and to highlight the creative element in

institution building. Scholars routinely project presumed Fed identities and powers deep into the past, before such elements emerged historically. Fed analytic frames are often ideologically charged, portraying the Fed alternatively as: (1) an independent central bank, (2) a state agency charged with regulating monetary growth, or (3) the vehicle of a banker conspiracy. This book classifies these views, respectively, as progressive, populist, and Jeffersonian. It also identifies a fourth Fed genre articulated in the writings of generations New York Fed officers and researchers.⁷ This latter perspective sees Fed power and responsibilities through a global lens. Hamiltonians view New York as “first among equals” within the system, owing to its unique vantage and expertise gleaned from working at the pinnacles of finance.⁸

Imagining the Fed shows that all four of these Fed images were woven into the FRA, yielding an ambiguous blueprint. The system’s federalism tied representation to territory, both among the reserve banks, which governed discrete territories, and on the national board. This dispersion of power was intended to prevent New York from establishing Fed hegemony.⁹ This plan would fail within a few years, however, with the first hierarchical Fed emerging in the 1920s with New York at its center. This order would be toppled by the end of the decade, however, amid internal critiques that the system was behaving like a central bank and undermining the letter and spirit of the law. A similar sequence would unfold two decades later, when William McChesney Martin Jr. tore down an inherited order to democratize the Fed.

This book argues that this developmental sequence was no coincidence. It reflected the interplay of agency and political time, set against a backdrop of institutional memory. By agency, this book means purposeful actions by individuals to change policies or institutions. This book focuses on the agency of two types of actors: Fed officials and U.S. presidents. Fed insiders are the main protagonists in the system’s struggle. They build and dismantle the extralegal regimes analyzed throughout the book. Presidential agency shapes Fed institutions through its impact on political time. Stephen Skowronek developed the concept of political time to explain a recurring pattern of hegemonic parties dominating U.S. national politics, capturing the state, and directing policy for an era.¹⁰ This book broadens the political time clock to incorporate a second developmental pattern wrought by transitions between war and peace. It identifies four political moments, partisan ascent and decay, and war and peace, and argues that

each empowers an ideological reform script, which reshapes the Fed and lays the seeds of future struggles.

The rest of this chapter develops this argument. It first reviews the Fed governance literature, before theorizing the roles of ideology, agency, and political time in shaping the Fed's developmental path. The book's core claim is that "the Fed" we know today congealed in 1970, marking the culmination of the system's political development, understood as "a durable shift in governing authority," with "shift" meaning "a change in the locus or direction of control."¹¹ It was only at this late juncture that the board consolidated FOMC agenda control. *Imagining the Fed* makes three contributions to the American Political Development (APD) literature. The first is its theorization of the role of international factors, including wars, regimes, and interests, as driving recurring patterns of Fed conflict. The second is an agentic notion of political time, which sees the discretionary choices of presidents and central bankers as impactful. Finally, the book also contributes to an emerging literature that stresses the durable impacts of ideas and agents that lose out in reform battles at critical junctures.¹² It shows that the contemporary Fed landscape contains vestiges of all four of its founding ideologies, even though changing times have rendered some Fed value systems incomprehensible within the modern world.

Fed Governance Studies and the System's Vanishing Struggle for Power

This section introduces the Federal Reserve's struggle for power as a contest to shape its policy regime. The FRA imagined two policy instruments, the discount rate and open market investments, and splintered control of each among the reserve banks and board. The law left unclear where institutional control resided, implying alternatively that it lay with the board, the treasury, or the reserve banks.¹³ Founding board member Paul Warburg reflected later that the law established a "system of checks and counter-checks—a paralyzing system which gives powers with one hand and takes them away with the other."¹⁴ It was an invitation to struggle.

The law did not imagine a central committee where system stakeholders would come together to forge policy. The first such committee, the FOMC's forebear, was established in 1922 through a reserve bank

agreement. The first committee was exclusionary, controlled by the five governors of the wealthiest reserve banks. This structure was contested immediately, and intermittently for decades thereafter. Milton Friedman and Anna Schwartz argue one proximate outcome of this struggle, a 1930 “diffusion of power” which grew the committee to twelve, foreclosed an expansionary bond-buying policy that would have steered the economy away from the Great Depression.¹⁵ This institutional story was debunked, but the argument that Fed policy mistakes worsened the Depression remains influential.¹⁶ Since Friedman and Schwartz wrote, the Fed’s power struggle has been progressively scrubbed from the literature. Today, economists see the system’s original twelve bank structure as a static source of “coordination problems,” which contributed to Depression-era mistakes.¹⁷ Most see primitive ideas as playing a more important role in leading Fed policymakers astray, however.¹⁸ The conventional Fed history sees Congress as ending its struggle in 1935 by elevating the Board of Governors to a position of Fed primacy, reflected in an FOMC voting majority. While the new Fed would be dominated by the treasury for another decade and a half, the 1951 Treasury-Fed Accord durably restored its operational independence.¹⁹ Afterward, new Board of Governors chair William McChesney Martin Jr. enacted procedural reforms which some argue heralded the modern Fed.²⁰

An emerging Fed governance literature downplays the Fed’s early power struggle, however, as well as the impact of Martin’s reforms. Peter Conti-Brown’s *The Power and Independence of the Federal Reserve* dismisses early Fed skirmishes as “institutional chaos” wrought by a flawed federal design, and explains Martin’s legacy as mainly rhetorical, a language of independence.²¹ In *The Myth of Independence*, Sarah Binder and Mark Spindel argue that Congress shapes Fed governance through the law.²² In their view, the system’s decentralized coordination problem-prone design grew from compromises among central bank champions and opponents, representatives of the nation’s core and periphery, Republicans and Democrats. When later economic shocks revealed these fragilities, lawmakers responded by rationalizing the Fed. In this view, the system’s structure flows entirely from the law, and agent-led reform efforts are insignificant. Lawrence Jacobs and Desmond King’s *Fed Power* similarly omits any discussion of the system’s internal divisions and power struggle, and portrays Martin as working to grow the Fed’s power and autonomy, bureaucratic motives they claim guide all Fed officials.²³

None of these works discuss the 1960s Fed transformation this book identifies as the culmination of its political development. Conti-Brown acknowledges that Fed power today is concentrated in an alliance between the board chair and staff, but doesn't explain the origin of this extralegal regime.²⁴ Jacobs and King argue that the modern Fed emerged in 1980, when it was allegedly freed from democratic oversight and embraced finance over other sectors.²⁵ Binder and Spindel argue that Congress changes the FRA whenever the economy tanks, and thus see the Fed as forever in the making. Yet, emerging research suggests that the 1960s reforms identified in this book are significant. Fed insiders have long recognized that decade as a time of rising board sophistication, but as two scholars recently observed, how "this transformation was engineered, by whom, and how it unfolded . . . remain a blind spot of the flourishing literature on central banking."²⁶ Another scholar observes that in the 1960s "the Federal Reserve System took on a new name—"The Fed."²⁷ This book shows that these developments were intertwined, and that a unified Fed identity was unthinkable just a few years before. The diffuse Fed order Bill Martin fostered emphasized inclusion, consensus, and deference to New York's expertise. The modern Fed shattered each of these pillars. While Martin's egalitarian norms were dismantled, his beliefs that the Fed should be inclusive and nonpartisan endured. The modern Fed is a composite of the institutional legacies and vestiges of the Fed regimes that came before.

The Struggle to Build a Durable Fed Regime

Imagining the Fed explains the evolution of the Fed policy regime, understood as the institutional process and values that shape its policy decisions. It analyzes the development of its two main policymaking bodies, the Board of Governors and the FOMC, from the perspective of the individuals who occupied them and remade them through time. This departs from how central banks are analyzed by economists and builds on a growing literature which interrogates how internal attributes of central banks interact with their ideational and global settings.

Many economists see central bank independence, the degree of legal separation from political authorities, as the main variable that shapes monetary policy outcomes.²⁸ In this view, the key to central banking success, understood as delivering low rates of inflation, is to build high

legal walls separating central banks from politicians. Another literature focuses on the state of economic knowledge as the key lever that shapes monetary policy outcomes.²⁹ A third line of thought sees central banks' structural-institutional environments as shaping their behavior. A critical vein of this literature, which this book identifies as embodying Jeffersonian thought, sees central banks are structurally flawed due to their reliance upon elected politicians for survival.³⁰ A sunnier version of this theory sees the Fed as a democratically accountable central bank, which lawmakers rationalize and empower in response to economic crises.³¹

These latter approaches offer a broader view of the political forces that shape central banks and sometimes lead them astray, but they remain underdeveloped and prone to anachronism; imagining central banks as closed systems, populated by homogenous technocrats, governing strictly domestic realms. Friedman and Schwartz problematize the first assumption by arguing that the structure of policy committees shapes their policy outputs.³² In *Bankers, Bureaucrats, and Central Bank Politics*, Christopher Adolph challenges the view that banks are populated by benevolent planners, showing that individuals' monetary policy beliefs and preferences are shaped by their experiences and career trajectories.³³ In this view, the policies and natures of central banks are shaped by the agents who populate them. Finally, a growing literature emphasizes global regimes as determinants of, and constraints on, central bank power.³⁴

Imagining the Fed integrates these insights into its analysis. It differentiates among Fed regimes by their degrees of fragmentation, centers of expertise, power resources, and embeddedness. Fragmentation is a measure of the diversity of interests represented and number of veto points in collective decisions. As fragmentation grows, policy becomes harder to change.³⁵ When fragmentation falls, change becomes easier. This book shows that in the Federal Reserve, fragmentation entails a tradeoff between regime legitimacy and policy flexibility, as institutions that reduce fragmentation (such as committees) necessarily exclude claimants to policy authority. Expertise is a measure of where ideational authority lies within the system. It can be centralized on the board, in the treasury, or in New York, or it can be deemphasized altogether. The next section explains that these constellations of authority correspond with different ideological Fed images. Power resources refer to globally valuable goods that central banks stockpile and deploy to enact policies which shape their environment. At the system's origin, this was gold and British sterling,

today it is flexible dollars. Embeddedness refers to the system's environment, including a domestic political system and a global economic regime.

This book distinguishes between secular and political time to explain the Federal Reserve's evolution. Secular time refers to periods of normal politics, when actors have time to interpret legal texts, build reform coalitions, and conceptualize their interests. These processes occur in relation to inherited institutions and agent experiences. In secular time, America's checks and balances hold, and political cleavages organize around parochial interests.³⁶ Political time, by contrast, refers to national traumas which change the parameters of American politics. The rise of a party to ascendancy in Washington. An economic crisis that implicates the ruling establishment. Marches to war. Returns to peace. These moments enable bursts of state building, which shatter regimes in and out of the Fed. As crises fade and secular time returns, Fed agents are forced to reconcile inherited institutions, which veer from the law, with a changed world.

Ideology, Interests, and the Battle over the Gold Standard

Congress established the Federal Reserve System in 1913, after a long dialogue over America's normative financial institutions which dated to the nation's founding. On the eve of the system's establishment, four visions vied to shape the nation's monetary authority and its purposes. Jeffersonians saw central banks as incompatible with America's constitutional order. Hamiltonians wanted a central bank modeled on the private Bank of England. Progressives looked to the German Reichsbank as a model, a joint public-private enterprise that blended public authority with private expertise.³⁷ Populists wanted a monetary authority constituted as an arm of the state to emit "legal tender," paper currency whose value derived from sovereign authority, to grow the money supply to create a more equitable capitalism.³⁸

Support for these visions varied across America's regional divides. The industrializing Northeast was rising on the world stage, emerging as one of the world's most economically advanced regions.³⁹ America's abundant hinterland regions, by contrast, remained capital poor and occupied lower rungs in the international division of labor. Hamiltonian and progressive central bank champions were clustered in elite New York financial circles.⁴⁰ Most Americans were unaware of the nuances of their

arguments, and many interpreted their calls to build a central bank as a plot to entrench Wall Street's power. In the South and West, populist and Jeffersonian ideologies were common. Citizens either wanted a public currency-emitting monetary authority to remedy historical grievances, or they preferred the central bank-less status quo and a gold standard regime they considered natural.

Congress's territorial makeup ensured that an elite plan to build a central bank would be defeated.⁴¹ This book shows that changing partisan dynamics further repudiated the central bank idea, however. The Republican Party had dominated U.S. national politics since the Civil War. Its governing orthodoxy emphasized a Hamiltonian partnership between political authorities and industrialists, reflected in a mercantilist economic program, which united the gold standard, protectionist tariffs, and domestic *laissez-faire*.⁴² This Gilded Age order was contested by a series of populist movements, culminating in William Jennings Bryan's ill-fated 1896 presidential bid on a platform to monetize silver. Bryan was defeated decisively in that contest. Republicans retained national power and legalized the gold commitment with the Gold Standard Act in 1900.

At the dawn of the twentieth century, however, the ruling party soon developed a fissure as progressivism emerged as a counterweight to mercantilism. Progressives called for lowering tariffs to improve consumer welfare and called for regulating the industrial economy. Intraparty tensions boiled over at the 1912 Republican National Convention in Chicago, where party elites nominated incumbent William Howard Taft as the party's presidential candidate over Theodore Roosevelt, the leader of the progressive wing. Roosevelt ordered his followers to leave the convention and form a Progressive Party behind his presidential candidacy. The Republican vote fractured in the fall national elections, delivering Democrats an unlikely landslide victory.

The Democratic Party was split into populist and Jeffersonian wings and anchored to a southern base. William Jennings Bryan led a populist bloc which remained committed to using state authority to regulate currency expansion. The party's Jeffersonian wing hoped to restore a more virtuous classical liberal order by breaking up trusts, lowering tariffs, staying on gold, and devolving federal power. At the Democratic convention in Baltimore, Bryan played kingmaker by endorsing New Jersey governor Woodrow Wilson as the party's nominee after several inconclusive ballots. Wilson won the presidency alongside broad Democratic majorities in both houses of Congress, but Wilson knew Democrats' grasp on national

power would be ephemeral if it didn't expand its geographic base. Wilson sought to establish a new era of Democratic partisan rule by claiming the mantle of progressivism and attracting Western progressives into a broadened coalition.⁴³ The next chapter explains how these changing partisan dynamics resulted in a series of design compromises that layered all four central bank ideologies into the FRA.

The ideologies differ in how they imagine monetary authorities should be constituted and the ends they should pursue. Populists want a state-controlled monetary authority to emit paper currency. To do so, political authorities need to jettison the gold standard and prioritize domestic economic goals over international monetary stability. After William Jennings Bryan's 1896 presidential defeat, these ideas were taken up and refined by economist Irving Fisher and his students Milton Friedman and Anna Schwartz, who posited a stable causal relationship between the quantity of money in circulation and the domestic price level.⁴⁴ Since monetarism endorses regulating monetary growth for domestic purposes, this book identifies it as a right-leaning strain of populism. This distinction matters because it stands in stark contrast with the other three central bank ideologies, which at the time of the Federal Reserve's origin were united in support of sustaining the gold standard. Progressives wanted a public-private central bank with authority lodged in an independent board to modernize America's financial practices and integrate it within the international gold standard.⁴⁵ Hamiltonians shared these same ends, but believed a central bank structured as a private oligarchy was necessary to achieve it. Jeffersonians opposed a central bank but embraced a vision of the gold standard as an automatic institution.

These four visions vied to order the Federal Reserve's components into a system. Populists and progressives envisioned the board in Washington as the Fed's head, but populists saw it as an arm of the treasury, while progressives wanted the board constituted as an autonomous bastion of expertise. The law supported each of these views. The populist Fed vision rested on provisions that limited banker representation on the board and installed the treasury secretary as its *ex officio* chairman. It was also supported by a passage that read, "[W]herever any power vested by this Act in the Federal Reserve Board . . . appears to conflict with the powers of the Secretary of the Treasury, such powers shall be exercised subject to the supervision and control of the Secretary."⁴⁶ These design features reflected concessions made to populists.⁴⁷ They were countered, however, by progressive structures which insulated the board from

politics, including lengthy, staggered terms for board members (originally five of seven members); private reserve bank ownership; and budgetary autonomy.⁴⁸ The next chapter shows that as it was being constituted, the board immediately divided into populist and progressive factions.

The law also contained passages that implied that the reserve banks were intended to be the system's leading authorities. Jeffersonian ideals infused the law's decentralization of power and deemphasis of expertise. Reserve banks were spread widely across the country and tasked with governing discrete territories. The gold standard's alleged automaticity lent plausibility to an imagined system of devolved power where reserve banks functioned as "self-regulating adjunct[s] to a self-regulating gold standard."⁴⁹ Jeffersonian thought also shaped the board requirement that its members reflect the "different commercial, industrial and geographical divisions of the country."⁵⁰ This built the nation's sectional and sectoral divisions into the board.

The FRA lent weakest support to the Hamiltonian central bank ideal. Hamilton endorsed private governance, with the bank wholly controlled by shareholders with common "experience guided by interest."⁵¹ This design was engineered to advance Hamilton's purposes for the bank, which included lending out a stable currency to unlock commercial growth and acting as a source of government energy by helping elected officials navigate "certain emergencies." Hamilton warned that if lawmakers kept the currency-issuing power to themselves, they would be tempted to respond to crises by expanding the currency and debasing its value through inflation. He wrote, "The stamping of paper [is] so much easier than the laying of taxes, that a government in the practice of paper emissions would rarely fail in any such emergency to indulge itself too far . . . [resulting in an] inflated and artificial state of things incompatible with the regular and prosperous course of the political economy."⁵² In Hamilton's view, the bank's credibility would spring from the diverging interests of its owners and elected officials.

Hamilton believed that to be effective in safeguarding the currency and spurring lawmakers to tackle looming problems, the central bank needed to be structured in the opposite way of the American government. Rather than dividing authority vertically among national and sub-national units, or apportioning representation inside the bank by territory or in response to national elections, the bank's corporate structure would empower shareholders with shared, long-term material interests. "To attach full confidence to an institution of this nature," Hamilton wrote, "it

appears to be an essential ingredient in its structure, that it shall be under a *private* not a *public* Direction, under the guidance of *individual interest*, not of *public policy*.”⁵³ The FRA decisively rejected this Hamiltonian vision. The law’s architect, Rep. Carter Glass (D-VA), explained that the Federal Reserve was “modeled upon our Federal political system. . . . The regional banks are the states and the . . . Board is the Congress.”⁵⁴

The system’s Hamiltonian tradition would be pioneered by Benjamin Strong, the New York Fed’s founding governor. As the FRA neared final passage, Strong complained that Democrats had thrown “the central bank idea . . . upon the brush-heap.”⁵⁵ Their “mongrel institution” was “nothing but a central bank with some of the most vital advantages of such an institution so bound up with red tape . . . that it would fall down in its practical working and bring disaster upon the country.” Strong would spend the rest of his life forging cooperative linkages among the reserve banks, enabling them to act more like a central bank, and with central banks overseas. The law’s two concessions to Hamiltonian ideals included the location of a Federal Reserve Bank in the nation’s financial capital, as well as its endorsement of the gold standard. The Hamiltonian theory of the Fed shares with its Jeffersonian counterpart an emphasis on reserve bank autonomy. Instead of imagining each reserve bank as sovereign and independent, however, reserve banks are understood as united by a national interest in preserving the gold standard, understood as a working international regime. In this vision, New York is imagined as “first among equals,” owing to its position atop America’s financial capital and global trade nexus.⁵⁶

Federalism structured uneven support for the law’s embedded ideologies across its envisioned units (see Fig. I.1 on page 14). Because the United States had been without a central bank for nearly eight decades when the Federal Reserve was established, early officials had “little understanding of central banking theory and . . . no experience of central bank administration except that gained on the spot.”⁵⁷ Because the system was composed of thirteen separate entities, however, each tied to a separate location, central banking lessons were learned unevenly. Barry Eichengreen observes “officials of the Federal Reserve Bank of New York, the seat of international finance, were better attuned to the advantages of international cooperation than . . . the Board of Governors” and reserve banks in the “interior of the country.”⁵⁸ Eichengreen sees these differences as “doctrinal,” but Jeffrey Frieden maps them onto diverse sectoral interests regarding national currency policy.⁵⁹ To maintain currency stability in an

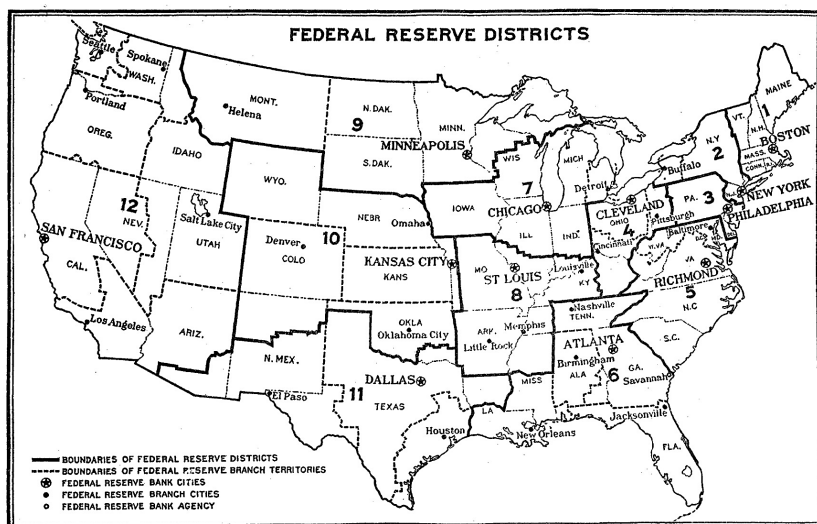


Figure I.1. Map of the Twelve Federal Reserve Banks and Districts. Map by Federal Reserve Board, Federal Reserve Bulletin, January 1925, Washington, DC.

open economy, monetary policy must be directed entirely toward replicating foreign monetary conditions.⁶⁰ In hard times, however, individuals whose fortunes are tied to the state of the domestic macroeconomy prefer expansionary monetary policies to maintain their incomes.⁶¹ These discretionary policies cause domestic inflation rates to surpass those prevailing abroad, however, causing the currency to become overvalued. To stabilize an overvalued currency, states can enact austerity to push down domestic prices, devalue the currency, or float it on foreign exchange markets.⁶² Internationally oriented sectors, including exporters and international traders and investors, prefer to forego monetary stimulus in downturns to maintain currency stability. When the Federal Reserve was established, these interests were clustered in New York and along the eastern seaboard.⁶³ Territorial representation thus hard-wired currency conflict into the system.

This problem would be compounded by Americans' gold standard naiveté. Many imagined the gold standard as an automatic, self-enforcing institution. Jeffersonians believed the gold standard was natural, following David Hume's price-specie-flow mechanism. In this view, when gold enters a country, the money supply automatically expands, causing local prices

to rise relative to foreign prices, making imports cheaper. Rising imports are paid for with an outflow of specie, which contracts the money supply, pushing down prices and restoring international equilibrium. These simple beliefs jarred against the way classical gold standard operated in practice, however. Scholars sometimes argue that central banks administered the gold standard by applying “rules of the gold standard game.” Arthur Bloomfield has shown, however, that no such rules existed when the classical gold standard operated.⁶⁴ Central banks prioritized maintaining gold convertibility above other goals, but their policies routinely flouted supposed “rules of the game.” This layer of discretion was essential for sustaining ongoing patterns of international central bank cooperation, where central banks could call on their foreign counterparts for support in emergencies.⁶⁵ This cooperative regime was crucial for the sustaining the gold standard by preventing financial contagion and promoting global financial stability.

The central bank-less United States was a pariah within this cooperative system. Instead of presenting the world with a unified face, the Federal Reserve had thirteen separate heads. To beneficially engage central bank networks and promote international monetary stability, the system would need to select a diplomatic interlocutor, which would lead the system to adopt unified policies that bent in response to monetary developments overseas. Whether monetary policy would be aimed externally to promote dollar stability or inward toward domestic goals would hinge crucially on the constitution of the Fed policy regime. The median citizen in any democratic country is employed in domestic sectors, which favor monetary policy flexibility over currency stability.⁶⁶ Consequently, the more the Fed regime approximated the political order, fragmented by veto points and parochial interests and ideas, the less likely it would be to make the timely policy adjustments needed to sustain dollar stability. To contribute to world monetary order, the system would need to devise institutions to reduce its fragmentation and empower New York to shape the system’s policy agenda.

When the Federal Reserve was born, these contradictions were not yet apparent. Since America had not had a central bank under the classical gold standard, Americans were blissfully ignorant as to its operations. As the system was first being established in 1914, World War I broke out, collapsing the international gold standard. It would only be after that crisis passed and the fixed currency regime remained broken that Fed agents would begin grappling with contradictions among its federal structure and international monetary order.

Agency, Political Time, and Fed Reform Catalysts

Stephen Skowronek developed the concept of political time to describe a recurring American pattern where ascendant parties dominate national politics for an extended era before being supplanted by a new hegemonic party.⁶⁷ Wesley Widmaier has extended the concept to explain the rise and fall of international economic regimes.⁶⁸ Both theories are structural, envisioning regimes as born with built-in half-lives. Partisan regimes unravel as factions diverge, governing orthodoxies grow stale, and minority parties regain strength. International regimes devolve as their embedded ideas are converted from pragmatic principles into rigid policy scripts. In each theory, regimes collapse when their policies and ideals are implicated in crises and repudiated, and the political time cycle begins anew as new regimes are formed.

Conspicuously missing from these theories are factors that bridge domestic and international realms, such as wars and societal interests. Consequently, political time theories miss crucial contingent relationships between actors and their environments. For example, the outbreak of war overseas presents U.S. presidents with strategic choices of whether to engage or abstain from conflicts, which impact their domestic political survival.⁶⁹ Similarly, individuals form economic policy preferences in response to assessments of whether the world economy is opening or closing.⁷⁰ These relationships impact the health and vitality of both global and domestic regimes. Presidents who lead the nation into unpopular wars see their parties punished by voters, potentially cutting short a partisan regime. Waning foreign participation in global regimes can similarly weaken domestic support. These relationships are crucial in the monetary realm, where fixed currency regimes rely on ongoing patterns of mutual international adjustment.

An agent-centered theory of political time looks to the rhetoric and actions of regime leaders to explain how they navigate a changing structural landscape.⁷¹ In this view, regimes are not born with built-in half-lives, but survive or fail based on their capacity to maintain authority and popular support amid changing circumstances. Leaders make choices that shape regime longevity, including questions of war and peace and how to respond to crises. Once these choices are made, however, they set in motion patterns of state building and demolition which move beyond a leader's control. These political moments penetrate the Federal Reserve and reshape its environment, setting the stage for its next round of

Table I.1. Political Time Impacts on the Federal Reserve

	Partisan Ascent	Partisan Decay	War	Peace
Reform Script	Populist	Progressive	Hamiltonian	Jeffersonian
Autonomy	↓	↓	↓	↑
Capacity	↓	↑	↑	↑
Locus of Authority	Party	Board	New York	System Agents

struggle. This book conceives of political time as four moments: partisan ascents and implosions, war and peace. Each event shifts the parameters of U.S. politics and empowers an ideological state-building script. Table I.1 (above) theorizes how each moment reshapes the Federal Reserve's attributes and environment.

Partisan Regime Origin and Collapse: Wellsprings of Populism and Progressivism

The rise of a newly ascendant party unleashes populist forces throughout the polity. Partisan regimes are founded by presidential candidates who successfully link the old regime's ideas and policies to emergent crises. The transition to unified government reduces the political system's veto points, opening reform opportunities.⁷² Legislative reforms are shaped by factional compromises, but are often pushed past the finish line by invoking the "democratic wish," a populist reform script that promises to strip power from corrupt elites and restore it to "the people."⁷³ This invites the construction of sprawling federal agencies, which splinter authority across regions and institutional borders, sowing the seeds of interest-based conflicts and power struggles. The populist impulse also reshapes the bureaucracy and courts. Party activists are tapped to fill vacancies in state agencies and the judiciary.⁷⁴ Partisans first clash with holdovers from the old regime, but as partisan appointments accumulate the bureaucracy and legal system bends to the ruling party's priorities.⁷⁵

This book shows these same dynamics reshape the Federal Reserve Board of Governors. Board appointees serve lengthy, staggered terms, which expire biennially, to ensure that individual presidents cannot load

the board with loyalists. Presidents nevertheless see these appointment opportunities like all others, as opportunities for patronage and shifting policy priorities.⁷⁶ Partisan implants first grow the board's fragmentation, as newcomers clash with holdovers beholden to older visions of the board's mission. If partisan rule is sustained across multiple electoral cycles, however, the board grows more unified as old members cycle off and are replaced with like-minded partisans, remaking the board's value system.

In America's competitive electoral environment, ruling parties inevitably lose their grip on national power. As partisan regimes mature, agencies of state are increasingly seen by the party faithful and opponents alike as an extension of the ruling party.⁷⁷ In the face of emergent crises, however, America's inherited state is often revealed as parochial and lacking capacity.⁷⁸ When confronted with such a crisis, declining partisan regimes grapple toward progressive reform. Presidents look to delegate authority to public and private actors to contain the crisis. New agencies are also forged, but the shadow of future elections hangs over bipartisan legislative negotiations, so new agencies are constituted as independent and located outside the executive branch, to prevent them from becoming instruments of the ruling party.⁷⁹

Partisan regime collapses remake the Federal Reserve and its environment. Scholars have identified a recurring pattern whereby lawmakers respond to a faltering economy by changing the FRA to reshape its powers, governance, and mandate.⁸⁰ This book shows that Fed empowerment processes begin earlier in the political time cycle, before crises spiral to slay partisan regimes. Presidents commanding declining regimes push their thumb on the system's internal power struggle to elevate the board's status. Likewise, crisis-induced progressive state building is an open-ended process. New financial agencies are layered onto an unwieldy state, shrinking the Fed's autonomy, muddling its responsibilities, and often taxing its resources.

War and Peace: Founts of Hamiltonian State Building and Jeffersonian Repudiation

War empowers Hamiltonian state-building scripts.⁸¹ Only in the face of grave national emergencies do Americans set aside their antistatism and consent in the construction of coercive institutions imported from

Europe, including armies, taxes, and central banks.⁸² War reshapes the Federal Reserve in three ways. Wars are costly and financed through a combination of taxes, loans, and monetary expansion. The Fed assists with each of these tasks. As banker to the state, it mobilizes and deploys revenues, helps the treasury gain access to capital markets, and creates reserves to provide subsidized credit. The process of drafting the Fed into providing war finance is enabled by constitutional provisions that grant the U.S. president greater wartime authority. A Hamiltonian alliance between the New York Fed and the treasury is forged, centralizing Fed authority along a New York–Washington axis. Congress rewards the Fed for wartime service by removing legal restrictions on its actions. By strengthening the system and concentrating its power, war makes the Fed “more like a central bank.”⁸³ War also transforms the Fed’s global setting. Wars destroy fixed currency regimes and catalyze shifts in economic power. These shifts occur across national borders but also within them. War increases the power of New York compared to other Fed outposts, setting the stage for future institutional skirmishes.

Returns to peace empower Jeffersonian critiques that war-swollen institutions depart from foundational ideals.⁸⁴ Claims of presidential authority lose force as the wartime emergency fades. Fragmentation re-emerges as other actors reassert their governing prerogatives. Fed actors seize onto these fragmenting currents to demand restoration of the system’s autonomy. Once independence is restored, however, Fed agents inherit a central bank that concentrates power in New York. Antistatist sentiments flare throughout the country, and Americans demand dismantlement of a war-swollen state.⁸⁵ These forces are also projected inside the Fed, especially when demobilization is accompanied by economic problems. The system’s struggle reemerges as actors in and out of the Fed invoke Jeffersonian scripts to attack Fed hierarchies and policies.

Wars leave behind several legacies that shape the Federal Reserve’s problems moving forward. One is debt. Congress readily approves wartime deficits, but its fragmented structure makes it hard to develop fiscal plans to pay debts in war’s aftermath.⁸⁶ If taxes are not raised or spending cut, the Fed can find itself pressured into monetizing debts and fueling inflationary forces. The second legacy concerns world order. Throughout this book, the United States emerges from wars in a hegemonic position, giving it opportunities to shape the peace and rebuild fixed currency orders. After World War I, the United States spurned overtures to rebuild a liberal international order, setting the world on a path toward crisis.⁸⁷ It took the

opposite approach after World War II, spearheading international order building. These choices crucially shape the Fed's environment.⁸⁸ If political authorities endorse projects of rebuilding fixed currency regimes, the Fed must direct its powers externally. Even then, its capacity to stabilize the dollar is shaped by fiscal and trade policies.⁸⁹ If politicians enact policies that generate inflationary or deflationary pressures, the Fed must counter them to keep the dollar stable. This book shows that policy changes in the name of dollar stability (or other goals) are not always feasible, however, and the system's uneven integration into the world economy was a recurring source of policy gridlock and institutional conflict.

A final impactful war legacy is voters' verdict on the ruling party's decision to lead the nation to war. If, looking back, voters decide that war was too costly or corrosive of American ideals, they punish the leaders who led them there at the voting booth. Minority party leaders can foster their own party's ascendancy by successfully painting the war as a failure. When this happens, the polity-shaking impacts of partisan regime formation are layered atop the traumas of demobilization. This book shows that this sequence occurred three times during the Fed's maturation, each time recasting its developmental path. Democratic presidents led the nation to wars in World War I, Korea, and Vietnam, which resulted in Democrats losing power. Each time, budding partisan regimes were cut short, and the Fed's problems and possibilities shifted.

Ideas and Agents: The Struggle to Shape Fed Institutions in Secular Time

The FRA imagined an amorphous, fragmented landscape. In underinstitutionalized, complex environments, agents have incentives to devise rules and procedures to advance shared goals.⁹⁰ Some such goals are universal, such as institutional survival and prestige. Others are more particular, like institutions that enfranchise certain actors while excluding others. Reform-minded agents can package ideas into "common carrier" reforms to unite coalitions with diverse goals.⁹¹ Enacting or changing extralegal rules requires building internal majorities. Ideas play important roles in constructing, stabilizing, and contesting such regimes.⁹² The FRA's embedded ideologies are resources agents can invoke to attack or defend the institutional status quo, or which can be fused creatively to imagine a Fed with different processes and purposes.⁹³