The Times that Tried Men's Economic Souls

BY LAWRENCE W. REED

Two hundred and thirty years ago this month in Valley Forge, Pennsylvania, the brutal and storied winter of 1777–78 came to a long-awaited close. Nearly a quarter of George Washington's Continental Army troops encamped there had died—victims of hunger, exposure, and disease. Almost every American knows that much, but few can tell you why Congress was as much to blame as the weather.

For six years—from 1775 until 1781—representatives from the 13 colonies (*states* after July 4, 1776) met and legislated as the Second Continental Congress. They were America's de facto central government during most of the Revolutionary War and included some of the greatest minds and admirable patriots of the day. Among their number were Thomas Jefferson, Benjamin Franklin, John and Sam Adams, Alexander Hamilton, Patrick Henry, John Jay, James Madison, and Benjamin Rush. The Second Continental Congress produced and ratified the Declaration of Independence and the country's first written constitution, the Articles of Confederation. It also ruined a currency and very nearly the fledgling nation in the process, proving that even the best of men with the noblest of intentions sometimes must learn economics the hard way.

Continental currency

Governments derive their revenues primarily from one, two, or all three of these sources: taxation, borrowing, and inflating the currency. Americans were deemed to be in no mood to replace London's taxes with local ones so the Second Continental Congress, which before March 1781 faced no legal prohibition to tax, opted not to. It borrowed considerable sums by issuing bills of credit, but with few moneyed interests willing to risk their capital to take on the British Empire, the expenses of war and government could hardly be covered that way. What the Congress chose as its principal fundraising method is revealed by this statement of a delegate during the financing debate: "Do you think, gentlemen, that I will consent to load my constituents with taxes when we can send to our printer and get a wagon-load of money, one quire of which will pay for the whole?"

Reports of the deliberations that led to the printing of paper money are sketchy but indications are that support for it was probably not universal. John Adams, for instance, was a known opponent. He once referred to the idea as "theft" and "ruinous." Nonetheless, he and Ben Franklin were among five committee members appointed to engrave the plates, procure the paper, and arrange for the first printing of Continental dollars in July 1775. Many delegates were convinced that issuing unbacked paper would somehow bind the colonies together in the common cause against Britain.

In any event, not even the skeptics foresaw the bottom of the slippery slope that began with the first \$2 million printed on July 21. Just four days later, \$1 million more was authorized. Franklin actually wanted to stop the presses with the initial issue and opposed the second batch, but the temptation to print proved too alluring. By the end of 1775 another \$3 million in notes were printed. After war erupted, the states demanded more paper Continentals from Congress. A fourth issue—this time for \$4 million—

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was ordered in February 1776, followed by $5 million more just five months later and another $10 million before the year was out.

In the marketplace the paper notes fell in value even before independence was declared. The consequences of paper inflation at the hands of American patriots were no different from what they ever were (or still are) when rampant expansion of the money supply is conducted by rogues or dictators: prices rise, savings evaporate, and governments resort to draconian measures to stymie the effects of their own folly. As author Ayn Rand would advise in another context nearly two centuries later, "We can evade reality, but we cannot evade the consequences of evading reality."

Americans increasingly refused to accept payment in the Continental dollar. To keep the depreciating notes in circulation, Congress and the states enacted legal-tender laws, measures that are hardly necessary if people have confidence in the soundness of the money. Though he used the power sparingly, George Washington was vested by Congress with authority to seize whatever provisions the army needed and imprison merchants and farmers who wouldn't sell goods for Continentals. At harvest time in 1777, with winter approaching and the army in desperate need of supplies, even farmers who supported independence preferred to sell food to the redcoats because they paid in *real* money—gold and silver. Washington ordered guards placed along the Schuylkill River to stop supplies from reaching the British.

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Another 13 Million Paper Dollars

Congress cranked out another 13 million paper dollars in 1777. With prices soaring the Pennsylvania legislature compounded the effects of bad policy: it imposed price controls on precisely those commodities required by the army. Washington's 11,000 men at Valley Forge froze and starved while not far away the British army spent the winter in relative comfort, subsisting on the year's ample local crops. It wasn't the world's first, nor would it be its last, experiment with price controls.

Congress recognized the mistake on June 4, 1778, when it adopted a resolution urging the states to repeal all price controls. But the printing presses rolled on, belching out 63 million more paper Continentals in 1778 and 90 million in 1779. By 1780 the stuff was virtually worthless, giving rise to a phrase familiar to Americans for generations: "not worth a Continental."

A currency reform in 1780 asked everyone to turn in the old money for a new one at the ratio of 20 to 1. Congress offered to redeem the paper in gold in 1786, but this didn't wash with a citizenry already burned by paper promises. The new currency plummeted in value until Congress was forced to get honest. By 1781 it abandoned its legal-tender laws and started paying for supplies in whatever gold and silver it could muster from the states or convince a friend (like France) to lend it. Not by coincidence, supplies and morale improved, which helped to bring the war to a successful end just two years later.

The early years of our War for Independence were truly, as Tom Paine wrote, "times that tr[ied] men's souls" and not just because of Mother Nature and British troops. Pelatiah Webster, America's first economist, summed up our own errors rather well when he wrote, "The people of the states had been . . . put out of humor by so many tender acts, limitations of prices, and other compulsory methods to force value into paper money . . . and by so many vain funding schemes, declarations and promises, all of which issued from Congress but died under the most zealous efforts to put them into operation and effect."

History texts often bestow great credit on the men of the Second Continental Congress for winning American independence. A case can also be made, however, that we won it in spite of them.