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## Manuscript Review of "A History of Interest Rates" by Homer

Hyman P. Minsky Ph.D.

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# RUTGERS UNIVERSITY PRESS

NEW BRUNSWICK, NEW JERSEY

December 4, 1961

Dr. Hyman P. Minsky  
National Bureau of Economic Research  
261 Madison Avenue  
New York 16, N. Y.

Dear Dr. Minsky:

Miss Helen Stewart has shown me both your letter to her of November 27 and the extremely interesting report which you have rendered to us on Sidney Homer's A HISTORY OF INTEREST RATES. I could wish that we had sent the manuscript in its earlier versions and its incomplete drafts to you along with the reports of the two scholars that we did consult since a great deal of what you say in your report makes a lot of sense. Whether Sidney Homer can be induced to take another look at his mass of material and give it one final set of polishes, I don't know. It is certainly something that I shall have to approach with great caution because he has begun to get a sense of impatience about progress.

We are putting through an honorarium for you and when our battery of IBM machines gets around to generating a check, my assistant will forward it to you. Once again, our very real thanks for a perceptive and highly intelligent report.

Cordially yours,

William Sloane

WS:elc

P. S. We shall preserve your anonymity.

November 27, 1961

Miss Helen Stewart  
Rutgers University Press  
New Brunswick, New Jersey

Dear Miss Stewart:

Attached you will find my comments on Sidney Homer, A History of Interest Rates.

I ended up reading almost all of the manuscript. I did not do an editing job. One needs to be done even if the manuscript is published in its present narrative history format, for there are quite a few errors and inconsistencies in the text. However, as I indicate in my comments, the basic weakness of the manuscript is that this useful information and discussions are hidden or obscured by a mass of essentially trivial and irrelevant detail. I recommend that the manuscript be revised before publication: the basic data and charts should be in a separate "compendium" and the textual material should be in the form of essays that examine either the history of special aspects of the subject or review specific historical heads or epochs. More attention to the significance of what took place and less emphasis upon the recording of events is needed.

Non-professionals have made interesting contributions to economics, but their contributions have rested on special knowledges that the author possessed. Mr. Homer not only has special knowledge of financial markets but he has collected interesting data. I believe that a typical rather than a strictly historical framework will enable you to achieve an interesting volume.

Incidentally in my work in New York City, I may meet Mr. Homer. I hope you will not reveal my identity to him.

Sincerely yours,

Hyman P. Minsky

HPM:rm

Comments on Sidney Homer, A History of Interest Rates

The contents of the manuscript can be best described as a narrative history of interest rates from the beginning of recorded time to the present. A great deal of the narrative material is casual and superficial: what I call gossip. Particularly unsatisfactory and essentially unnecessary to the author's main purposes are the various sketches and comments on the general historical framework within which particular observations were generated. The emphasis upon the historical framework by the author is associated with a neglect, (perhaps underemphasis is better than neglect, for a great deal of this material is contained in the manuscript) of the really significant background material needed for an appreciation and understanding of the data.

The data collection and generation job that the author has done is valuable and should become public property: the tables and charts should be published. As I see it the question is whether the present narrative framework is the best format within which to present this material. My view is that the massive narrative obscures what is important, both in the data and in author's comments. I therefore recommend that the data, in both tabular and chart form, be presented as a separate section, a compendium of our knowledge of

interest rates. This section should be fully annotated and accompanied by an essay describing the content and limitations of the data.

In addition to the "compendium" and its accompanying notes and essay, and in lieu of the narrative history, a number of essays summarizing the data and dealing with special topics related to interest rates and transactions in which interest rates enter should be prepared. It is obvious from the manuscript that the author is not a trained economist but rather that he is knowledgeable about the ways of financial markets and usages. Hence, even though the data cry out for analytical interpretation, I suggest that the essays should present in a systematic form the author's considerable insights into the nature, behavior and evolution of financial markets: they should capitalize on his special knowledge.

Part IV, Chapter XXI, "A Summary and Analysis of History Rates in Western Europe and North America" is an example of the essays that should be prepared which summarize and draw inferences from the historical trends.

In addition interpretive essays, showing how the data reflects the evolution of contracts and institutions, as well as histories of special topics, should be prepared. I will suggest some subjects that I feel the author should explore: the order in which they are

stated is not of any significance. I believe much of the material for these essays is contained in the text: the material will have to be extracted and rewritten. However I am sure that additional research will be necessary if any such program is undertaken.

1. Interest contracts have always had two attributes, one being to shift consumption over time, the other being to divide the participation in some productive venture among units: we might call these consumption and production "loans". (Pure consumption loans in which both sides shift consumption over time are possible, but in a production loan one side the lender is conceptually shifting his consumption as well as participating in a productive venture). As the government does not have to meet its commitments out of the revenue <sup>if any</sup> generated by the project, ~~if any~~, which is financed by the loan, government debt is a form of consumption loan. A broad review of the type of borrower at different periods, the varying significance of production loans in the form of participation interests, mortgages, or bonds as against consumption loans in the form of government and private household debt would be of great interest. The invention of the corporation and its effect upon the financing of productive ventures is part of this story.

2. In production loans the interest rate that can

be offered is related to the value of the output that the project is expected to generate. As railroads and other durable capital goods users entered the loan market for funds, the calculation of expected future returns became a part of the evaluation procedure used by both the borrower and the lender. A study of how the profitability of projects and the quality of assets were estimated during different periods would be important and relevant to many problems being discussed at present. The author has thought about this subject for he discusses the interest rates attached to new issues of high grade railroad debt at various points in his manuscript.

3. The source of the funds being loaned at different periods would make a most interesting essay. Starting with the medieval orders and philanthropies and continuing down to the present day institutional investors, the sources of the supply of funds side should be traced. It is my guess from the existing narrative history that the mechanism generating the supply of long term funds will turn out to have been better organized for much of modern times than the market generating the supply of short term funds. A historical sketch of the underwriting, distribution and security market institutions would be interesting

and really is essential to the understanding of interest rates.

4. Missing in the narrative history is any descriptions of the circumstances in which the present set of financial contracts which involve interest calculations were invented and adopted. Inasmuch as these various contracts determine not only many of the institutional attributes of the financial market but also particular specialized terms which are available for financing the control over particular resources, such a study would be of real importance. Some contracts whose origin should be traced are straight line life insurance, life annuities, amortized mortgages, callable and redeemable bonds, and the various classes of savings deposits. (The shift from perpetuities redeemable at the initiative of the issuer to bonds with a due date is a special part of the "history" of interest rates that needs writing.)

5. In the discussion of interest contracts by economists, the distinction between real and nominal rates of interest is made. A major conclusion of the narrative history, as it now stands, is that during the nineteenth century a secular decline in interest rates took place. What was happening to prices as the decline took place? If my memory is not wrong, over much of



this period prices were also declining so that although the nominal rate fell toward 2 $\frac{1}{2}$ % during the nineteenth century the real rate remained somewhat higher. Similarly if secular inflation is expected long rates must rise if real rates of return are to be maintained. The recent bear market in bonds may reflect this secular stagnation; and the term structure of interest rates may also reflect such price level expectations.

6. At various points in the narrative history risk rates are mentioned. An essay examining the prime-risk rate structure during various eras would be interesting and important. Such an essay should examine the activities that were financed at the various risk rates in the different periods. An interesting aspect of such a study would be to examine how risk differentials for particular classes of assets changed over time.

Charter 7-1766

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Rutgers University Press  
New Brunswick New Jersey

October 9, 1961

Mr. James F. McRee, Jr.  
National Bureau of Economic Research  
261 Madison Avenue  
New York 16, N. Y.

Dear Jim:

Herewith the Homer manuscript, HISTORY OF INTEREST  
RATES for Mr. Minski. Thank you for helping us  
get a reader.

Yours,

Helen Stewart

HS:f