DIARY

Book 120

April 20 - April 25, 1938

- A -

- B -

- P -

- R -

- S -

- T -

- U -

- W -

FORM 8-37

1

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 20, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF ENGLAND.

FROM L. W. Knoke

I called Mr. Bolton at 10:00 a. m. today. We discussed a great many things. As regards silver I told him there was nothing new in the situation that I knew of. With respect to our new spending program Bolton thought the impression prevailed in Europe that Congress might dampen it down. I pointed out that Congress had never been a friend of economy and that the feeling here seemed to be that Congress would go along but might conceivably insist on earmarking the funds voted. In Europe Bolton thought there was a very marked feeling of pessimism as to the spending program and no conviction at all that it would ultimately bring about a real improvement of business. Europe, he continued, was much interested in rumors as to the Roosevelt-Garner rift and I replied that all I could do was to refer him to the press.

I mentioned the continued shipment of gold from Japan. Bolton saw therein a sign that Japan was beginning to feel the pinch. I made reference to the two gold accounts which we have with the Bank of England, Account A and Account B, and explained that the question had recently been raised here whether in cases of sales by us of sterling we could convert gold from both accounts. Bolton replied that they wanted us to do just as we pleased. I spoke of the premium on gold coin which according to recent reports from Europe was gradually disappearing. Bolton explained that for a time this premium had reached almost 6 per cent or equivalent to a gold price of about 150s per ounce. Gold coin had been heavily offered in London by Uruguay, FORM 13 AM 1-37

2

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 20, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF ENGLAND.

FROM L. W. Knoke

Venezuela, Holland, Switzerland, Belgium, Canada (about 30/40 million dollars worth) and quite recently also by British India. These silver supplies had greatly exerted such a pressure on the market that the premium had tended to sag away. With a substantial improvement in the situation of France which up to recently had absorbed by far the largest amount of the supply, the picture had changed so that today gold coins in Paris were almost offered flat with a premium in London and Amsterdam of from 1 to 1 1/2 per cent. The principal demand was now coming from European refugees who would ordinarily put their money into dollars but were now inclined to go into gold coin. At the Bank of England they had been studying this problem for many months and today they were feeling very strong in their disapproval of very high premia if for no other reason than that it led to the rich getting their gold at low prices and the poor at high. Bolton asked whether the gold to be desterilized by our Treasury would show in the Federal reserve figures and I explained the details.

I enquired about the French situation and the way he felt about it. Bolton replied that personally he thought the French had turned the corner at last but that they were not as yet on the up grade. The new Prime Minister was highly respected at home and seemed to enjoy the confidence of most Frenchmen. Whether this confidence was completely justified remained to be seen. Meanwhile the country was completely sold out, down to rock bottom. However, people in

SC. 3.2 60M 9-37

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 20, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF ENGLAND.

FROM L. W. Knoke

general were beginning to wonder whether it was sound policy for them to keep their money abroad. As a result there had been a small but evident trend of repatriation. I suggested that quite possibly our spending program had been decided upon at a moment when it might do France considerable good. Bolton seemed to agree with this thought.

LWK:KW

HM

GRAY

London

Dated April 20, 1938

Rec'd 2:01 p.m.

Secretary of State,

Washington.

325, April 20, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

One. What reply should I make to the inquiry transmitted in paragraph one my 298 April 11, 7 p.m.?

Two. The dollar has been bid all day. Various explanations are being banded about the market it being particularly emphasized that with gold at a substantial premium the main source of supply of dollars is removed. There are also rumors of Japanese buying after New York opened. The French control took sterling at 158.20-22 most of the day but the amount was small. Towards the close the franc became offered, the control supplying sterling at 158.32.

KENNEDY

CSB

HM

GRAY
Paris
Dated April 20, 1938
Rec'd 2:15 p.m.

Secretary of State,
Washington.

626, April 20, 5 p.m.

FROM COCHRAN.

Paris exchange market active today with control apparently acquiring good amount of sterling. Dollar not so much offered and by 3:30 p.m. Guaranty had acquired only 400,000 for the control. Bank of Indo-China continues to buy dollars presumably to cover short position. Acting as the French control Guaranty today sold sterling against belgas since French railways have to meet 50,000,000 belga maturity. Guaranty succeeded in obtaining over 20,000,000 of the required amount, provided principally by Credit Lyonnais acting for Belgian banking syndicate.

Following yesterday's boom when all offers for shares could not be supplied, and influenced by Wall Street's example of last night, Paris Bourse today reacted, with Internationals particularly weak, excepting gold shares.

French

-2- #626, April 20, 5 p.m. from Paris

French bankers state that customers including those in the provinces are selling foreign exchange; some of their franc deposits are increasing but most of proceeds used for investing in stocks or French rentes. Demand for national defense bonds continues active. Press intimates that because of extent to which Treasury is now receiving subscriptions and renewals to its securities, the Government is not obliged to hasten to use its special powers to borrow further at the Bank of France or open the new public loan and that consequently no announcements on these two points followed today's Cabinet meeting. One Paris American Bank tells me that its customers who have investments in the United States are mostly estates or big holders who do not alter their portfolios frequently and are taking no action in present circumstances. This bank's clients who fled from the franc bought sterling almost exclusively and are now beginning some liquidation. Gold coins, large French bank notes and foreign paper currency are coming onto the market evidencing dishoarding.

WILSON

CSB

April 20, 1938

For the Secretary:

Duffield told me today that in writing the story which appears in The Wall Street Journal this morning on the possible use of desterilized gold for retiring Treasury bills, he talked with several people at the Federal Reserve Board. He said he talked with two members of the Board, Mr. Davis and Mr. Szymczak, but that Davis was of no help at all and Szymczak very little. He talked to Larry Clayton, Assistant to the Chairman, and learned that Clayton agrees with the Treasury viewpoint that some bills should be permitted to run off weekly.

His major discussion was with Elliott Thurston, Special Assistant to the Chairman, who reviewed the whole series of steps leading up to the present situation. He congratulated Duffield on his previous story which had revealed the possibility of some bills being allowed to run off. Thurston referred to this earlier story as constructive and helpful in that it had served as a warning to the financial community and had stirred up those persons and groups which opposed using the desterilized gold to pay off bills.

Later in the day after the 11 o'clock meeting in the Secretary's office with the Executive Committee of the Open Market Committee of the Federal Reserve Board in which the Secretary had referred to the Duffield story and intimated that he must have talked with someone, Mr. Duffield was requested by Mr. Thurston to inform the Secretary that he had not talked with Chairman Eccles and that he had not discussed the subject of desterilized gold with Mr. Thurston. Mr. Duffield told Mr. Thurston that while he couldn't understand the reason for Chairman Eccles' request, he would be glad to convey the message to Secretary Morgenthau that he had not talked to Chairman Eccles. Later, Chairman Eccles informed Secretary Morgenthau over the telephone that Duffield had agreed to report to the Secretary that he had not talked to him or any other Board member or to Thurston.

Upm

RE FINANCING PLANS

April 20, 1938.
10:45 a.m.

Present: Mr. Taylor
Mr. Bell
Mr. Haas
Mr. White
Mr. Gaston
Mr. Lochhead
Mr. Upham
Mr. Seltzer
Mr. Harris

H.M.Jr: Well, listen, all you goddam experts.

Bell: Economic experts.

H.M.Jr: I've spent 40 minutes with the President, 30 of it on this subject, and I gave him everything that I had, plus Duffield's story in today's Wall Street Journal, which I thought was very good, plus the article in the Tribune and the Times, so he had all of those, the background. I told him that the Federal Reserve owned 700 million dollars of the billion 800 million dollars worth of bills outstanding, that we have four alternatives of what we could do; that my recommendation was that we only borrow 50 million a week from now on of bills because I thought that that carried out the spirit of his message, but I wanted to explain how I arrived at it; that if we did nothing, between now and the 15th of June, Bell informed me that 300 million dollars worth of gold would go to work; that it was just a question how fast he wanted this thing to go. And I said that the Federal Reserve found themselves in a very embarrassing situation, because since Saturday morning through last night they had sold a hundred million dollars worth of bonds, had to replace them with bills, it was extremely difficult, and that they might find themselves in the position where they would have to let that portfolio run off, which in a sense would offset what we did, that is, it would decrease the reserves; but that the depositing of a billion dollars worth of gold was Mr. Eccles' plan, he'd been advocating it for two or three months, and as far as I know the difficult situation which we now found ourselves in had never been raised by them.

The President said, "When I last saw Mr. Eccles last week, he never pointed this out to me."

So I said, "Well, it's just a question, Mr. President - I've tried to do everything that's mentioned in your speech just as promptly and as cheerfully as possible. I think I have done it."

He said, "You have."

"Now," I said, "it's a question of who's going to find themselves in an embarrassing situation, the Treasury or the Federal Reserve." I said, "I'd rather have it be the Federal Reserve."

Well, he thought this thing over pretty carefully. And I said another thing. I said, "The inflation spirit has not caught on, and if the Treasury hesitates and flutters at this time, why, it may just add to the difficulties and make people think, 'Well, the Treasury isn't so sure about this program.'"

And then I told him what I had in mind, which is for you fellows only. I mean I'm not going to tell the Fed this at this time - that I wanted to make an offering in June for the September note holders, so that September will be completely blank, and at that time we could, if we wanted to, go out for about a billion dollars worth of new money, in order to get ready for the money when it did go out and also for the big March maturity. But I don't want to tell it outside the Treasury. That would leave us completely free.

Then the President said, "Well, I don't know whether this makes sense, but couldn't you sell a 20-year $2\frac{3}{4}$ bond which would be callable any time by the Treasury after five years, and advertise it as a bond for widows, orphans and trustees?" So I told him about the Farm Credit bond which had a 20-year spread; that it was perfectly possible and we'd study it.

And I tried my best to tell him everything that Burgess talked about last night. I told him that everybody was "agin" me but I felt that this was the way to do it, in view of his message; now it was up to him. And especially in view of the fact that somebody in the Federal Reserve has been talking, and talking plenty. They certainly gave Duffield an earful, didn't they?

Taylor: (Nods yes)

H.M.Jr: And I said, "Now, Mr. President, I can't guarantee it, but if this idea works of building up these balances in the Federal Reserve and the pressure becomes hard enough, it's possible that it may start these fellows investing."

"Now," I said, "New York Edison announced late last night they're going to get out a 60 million dollar issue."

I said, "To show you how hungry they're going to be, Mr. Burgess said to me, 'Do you suppose it would be all right for the Federal Reserve to buy some of Jesse Jones' Commodity Credit bills?' He said, 'Do you think as a central bank we can own them?' I said, 'I don't think so. Of course, if you want to do what the Bank of Mexico did - that's what they did.' He said, 'Well, I'm just looking around. What we going to put our money in?'"

So I said, "If this idea of piling this stuff up to make them so hungry that they'll go out and invest and put the money to work - why then, the quicker we do it the better."

I tried to be fair in presenting it, see?

Bell: I think that's a fair statement.

H.M.Jr: What?

Bell: I think that's a fair statement.

H.M.Jr: What? Especially inasmuch as he had Duffield's article, the Tribune article, and the New York Times article. I took them all over. Huh? Is that a fair ....

Bell: I think it is.

H.M.Jr: Huh? And I explained to him that we'd have to go to the market twice between now and September, because these things are only 90-day; so we'd have to go to market twice. And that my great reluctance to spend taxpayers' money, even though it was very little, in the form of interest on borrowed money that I had no use for - I said, "It just goes against my grain and everything else."

So the long and short of it, after a full 30 minutes - he's taken plenty of time to think and plenty of time to read - that I'm not going to kid around with the Open Market Committee, I'm just going to tell them that this is what the President and myself - this is what we're going to do.

Bell: That's 50 million a week.

H.M.Jr: Yes.

Bell: And retiring ...

H.M.Jr: Well, we offer 50 million a week instead of 100.

Bell: Retire 100.

H.M.Jr: The 50 million really meets the 9-months coming due.

Bell: 9-months coming due?

H.M.Jr: Meets the 9-months coming due.

Bell: No, no, we started rolling over, the 23d of March, I think.

H.M.Jr: Well ....

Bell: Well, it doesn't make any difference. There's a 90-day and a 9-month bill maturing.

H.M.Jr: Isn't that what it is?

Bell: Yes, that's right.

H.M.Jr: What? 90-day and 9-months, and we're offering 100 million to meet those two.

Bell: Present time, yes.

H.M.Jr: And what I'm saying is that we'll offer 50 million a week, so there will be 50 million a week which will mature. Huh?

Bell: That's right.

H.M.Jr: Now, the discussion that - the thing we ought to spend the time on with these boys: "Now here's the problem. What the hell you going to do about it?" I mean I never kid with you people. Once I've made up my mind, there's no use taking your time - "What do you think of this?" and all the rest of it, when it's already decided. I've never done that. If I ask people's advice, I ask their advice with my mind open. As long as I've made up my mind, no use kidding. I've never done that with my own crowd.

Do you (Taylor) think from what I said it sounds fair?

Taylor: (Nods yes)

H.M.Jr: Certainly reading him all that stuff gives him the background, because Duffield did a very fine job.

Taylor: Thought you gave him everything you could give him.

Lochhead: The last paragraph in the announcement of the original sterilization program made that statement.

H.M.Jr: Incidentally, the Times referred to that.

"This will be accomplished by the sale of additional public debt obligations, the proceeds of which will be used for the purchase of gold, and by the purchase or redemption of outstanding obligations in case of a movement in the reverse direction."

Upham: They refer to that as an implied promise, though.

Taylor: Of course, the movement isn't in a reverse direction.

Upham: Gold in a reverse direction.

H.M.Jr: And while we're on this thing, another thing I told the President, also extra extra confidential, was that one Sumner Welles and one Herbert Feis came over here begging me to jiggle the price of silver the next couple days, to help them in their deal with Mexico, and I refused point blank to do it. I said silver was strong in London, I just wasn't going to do it. So he said Senator Pittman didn't care about the world price of silver. I said, "All right, you get Senator Pittman to make a speech on the floor of the Senate that he doesn't care about the world price of silver and I'll promise that when the newspapermen come around to see Gaston he'll say, 'Well, if Pittman doesn't care about the world price of silver, it's all right with the Treasury.'"

So I said, "How does the President feel about it? You better ask him. You tell the President for me I'm not going to jiggle the price of silver. But if Senator Pittman makes a speech on the floor of the Senate saying it's entirely up to Congress - if they don't care, they'll revoke the law - why, we'll carry out the law and stop buying. Now, if that's the way you want to do it, O.K., but it's up to you and Senator Pittman."

"But," I said, "I won't call them." But I refused - oh, it started - "make it half a cent." I said, "I won't make it an eighth of a cent." I said, "It's the silliest thing. I just wouldn't do it."

Taylor: Oh, have you (Gaston) been reporting the receipt of the letters on that subject to the boss?

Gaston: On silver? Haven't seen any.

Taylor: Well, you answer them, then send me what you have answered.

Gaston: Well, somebody upstairs has answered them - just a perfunctory acknowledgment, I guess. I haven't seen them.

Taylor: After the first - about three days, they've been a hundred percent opposed to what we did.

H.M.Jr: They were? Well, let Mrs. - I'd like to have a synopsis of it - I mean a .... Against us?

Taylor: (Nods yes)

Kieley: Eccles and all of them.

H.M.Jr: Yes.

to the President by H.M. Jr.

15

NEW YORK TIMES
APR 20 1938

TOPICS IN WALL STREET

Government Bond Market

The new influences now at work in the market for United States Government securities, notably the increase in excess bank reserves and the possibility that the Treasury will retire maturing discount bills in cash from the proceeds of the gold "desterilization" program, continues a major topic of discussion in financial circles. That the price structure of the government bond market appears assured, with a strong tendency for further substantial appreciation, is a consensus among important observers, who interpret the absence of new Treasury flotations and the lack of demand for commercial loans leaving banks—with their enlarged supply of excess reserves—with no alternative but to turn to the existing government issues. In other words, the banks are being forced into the government bond market, especially the market for long-term bonds. It became generally apparent that the Federal Reserve "put the breaks" on the spectacular rise in "governments" on Saturday and Monday by heavy selling of their bonds from portfolio. One important trader said yesterday that had not the Federal Reserve sold in such volume, the market could easily have risen a full point higher on the movement under the impetus given it by the credit measures taken last week.

Debt Retirement With Gold

One of the important questions which the Federal Open Market Committee must have discussed in its meeting in Washington yesterday is the advisability of using some of the proceeds of gold desterilization to retire outstanding government debt. There were rumors in the market yesterday that some or all of the $618,000,000 of Treasury notes due on June 15 might be retired in this way, and some sections of the market have believed since the desterilization plan was first announced that the Treasury would at least retire some weekly bill issues. Conservative opinion does not favor such a course because of the danger that it would overstimulate the market for government securities. From the Treasury's point of view, however, the use of desterilized gold to retire debt and the issuance at a later date of new debt to meet the spending program would have two advantages: First, it would quickly get the proceeds of the gold out to the banks as excess reserves; second, it would give a partial answer to those critics of its policy who say that using desterilized gold to defray general or relief expenditures is a violation of the implied pledge made when sterilization was started that securities issued to pay for incoming gold would be retired when gold was drawn from the inactive fund.

NEW YORK HERALD TRIBUNE

APR 20 193[illegible]

Wall Street Comment

Spending-Lending

The Administration moved with exceptional rapidity to [illegible] its gold [illegible] and to get action from the Federal Reserve Board on reserve requirements, but the working out of the details of the program is taking some time. The bond market has been awaiting with the greatest of interest the news of the Treasury's plans for passing the proceeds of the desterilized gold over to bank reserves. Since the Administration has decided not to leave the inactive gold fund unbalanced until gold is exported from this country, the money market believes that a more stable market for government issues could be maintained if the desterilized gold proceeds were passed along through the channel of regular Treasury expenditures than by interrupting the series of discount bill offerings. Bankers would have been better pleased if an increase in the public debt could have been avoided. But since the Administration has decided to resume spending, the preference is for leaving the present debt structure undisturbed and for tapping the market later when the need arises. The Treasury also has not worked out its plans for handling any exports of gold that may develop. The behavior of the dollar yesterday seemed to indicate that gold exports would not immediately take place, but the market believes that the trend of the dollar yesterday was not indicative of what the near future holds in store.

C. & O. Proxies

The agreement reached yesterday to postpone the Chesapeake & Ohio Railway meeting for three weeks gives the opposition to the management that much additional time to obtain proxies or to win over some of the 41.92 per cent already held by the Young group. Because of the unexpectedly large showing by the management to date, some quarters are inclined to view the opposition's job as extremely difficult, a view which may have dictated the plea made at the meeting by unidentified interests for adjournment to May 30 instead of May 10.

Financing Perks Up

Reflecting a firmer bond market, Consolidated Edison Co. last yesterday announced plans for floating [illegible] a refunding issue of $80,000,000 3½ per cent debentures, largest public utility financing since the Appalachian Electric Power Co. floated $97,000,000 bonds and debentures on February 2 last. Consolidated Edison has been contemplating this financing for some weeks to redeem at a premium of 5 per cent on June 1, 1938, $80,000,000 principal amount of Consolidated Gas Co. of New York twenty-year 4½ per cent gold debenture bonds due June 1, 1951. The opportunity has now arrived for such an undertaking, partly as a result of the government's easy credit program which has increased bank reserves. This program has brought a spurt in the market for government bonds, as banks rushed to invest their idle cash, and the strength has extended to municipal and the better grade corporate issues.

New Governors

The nominees for governors of the Stock Exchange already are being besieged by colleagues and interested outsiders who want to be on the inside track with pet schemes and favorite sons for the paid presidency and the public representatives on the governing board when the new board takes office. Some committee nominees are bewildered by the mass of suggestions and reports that will be awaiting the immediate attention of the governors when they assume command May 9. One week will be allowed, during which the present committee members will continue to function, allowing time to appoint new committees, select the public representatives and the paid president. Informal conferences are being held to discuss prospective candidates for the new posts, but this preliminary work will not get into full swing until after the end of the week. Independent candidates must be nominated by petition before next Monday, and if none has been placed in the field the nominees are assured of election and can begin active preparation for the tasks awaiting them.

Short Selling

It has been assumed that short selling is being [illegible] odd lot [illegible] to avoid the government regulation that [illegible] lot short sales can only be made at a price above the previous sale. Informed circles admit that there is just enough truth in the statement to cause a lot of misunderstanding. Until the S. E. C. passed its short trading rules last February there were no reliable statistics on odd lot short selling, but researchers have disclosed that something over 5 per cent of average odd lot sales were short sales. Since that time definitive data show that the proportion of odd lot short sales to total short sales runs around 13 per cent. As the error in the early data is all on the side of understatement, about all that can be said with precision is that some increase in this type of trading is indicated. The S. E. C. is in possession of all statistics on the matter and is studying them carefully to judge the success of the rule.

15 Most Active Stocks

The fifteen most active Stock Exchange issues on April 19 were:

	Volume	Close	Net Chg.
Anaconda Copper	[illegible]	[illegible]	[illegible]
U. S. Steel	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]
U. S. [illegible]	[illegible]	[illegible]	[illegible]
Int. Tel. & Tel.	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]
Gen. Motors	[illegible]	[illegible]	[illegible]
Unit. Airc.	[illegible]	[illegible]	[illegible]
Kennecott	[illegible]	[illegible]	[illegible]
Beth. Steel	[illegible]	[illegible]	[illegible]
Chrysler	[illegible]	[illegible]	[illegible]
Gen. Motors	[illegible]	[illegible]	[illegible]
Boeing Airplane	[illegible]	[illegible]	[illegible]
Douglas Airc.	[illegible]	[illegible]	[illegible]
Curtiss-Wright	[illegible]	[illegible]	[illegible]

[illegible]

Capital Statistics

The Federal Reserve Bank of New York has now sent out the questionnaire, in preparation for some time, which will bring in information as to the capital market's inventory position, commitments and prospects for future financing. The questionnaire has gone out to thirty investment firms and will be answerable as of Friday of each week. The questions have to do with prospective financing, actual commitments where the underwriting agreement has not been terminated and in cases where it has been terminated. In addition the Reserve Bank is asking the firms to supply it with data at least once a quarter on capital position, credit used and funds tied up in inventories. The need for gathering this information obviously exists and it is to be hoped that the Reserve Bank will see fit, in time, to make the data public at regular intervals. There has been a wide difference of opinion as to whether the supply of investment banking capital is adequate to the most satisfactory functioning of the capital market in times of stress. All such arguments have been conducted, however, without sufficient information for the forming of a valid opinion. The figures which the Reserve Bank here is collecting will not be as comprehensive as one might desire, but they will represent at least a start toward giving a factual basis to opinions on the state of the capital market.

Rail Results

Early reports of railroad earnings for March and the first quarter exhibit the expected poor showing compared with a year ago and emphasize anew the need for constructive and immediate action to relieve the position of the carriers. In the absence of traffic revival and new increases, the roads now are pinning all their efforts to a reduction in wage costs. The difficulty with that program, recognized by the rail managers, is that effective relief there may be so long in coming that some roads cannot survive.

OPEN MARKET MEETING

April 20, 1938.
11:00 a.m.

Present: Mr. Taylor
Mr. Bell
Mr. Haas
Mr. White
Mr. Gaston
Mr. Lochhead
Mr. Upham
Mr. Seltzer
Mr. Harris
Mr. Eccles
Mr. Harrison
Mr. Burgess
Mr. Williams
Mr. Szymczak
Mr. Piser
Mr. Davis
Mr. Goldenweiser
Mr. Sinclair

H.M.Jr: Do you gentlemen want to know what the budget picture is from now until October 1, or have you already had it? I mean has it been transmitted to you?

Burgess: I think we'd like to have it again, as far as I'm concerned.

H.M.Jr: All right.

Bell: Well, this picture contemplates retiring 250 million dollars of Treasury bills in June. Those are the special tax bills. Present indications are that we'll go out of April with two billion two, out of May with two billion 80, June one billion 930, July one 750, and August one 600, September one 650, going into October with one billion 650 million dollars. Carrying that on through until the end of the year, we'd go out of December with a billion 180 million, no more bills being retired other than 250 in June.

Eccles: If you didn't retire the bills in June, that is, if you put out tax bills again for December, then before you go - you'd go into the end of the year with nearly a billion and a half, wouldn't you?

Bell: That's right, a billion four plus.

H.M.Jr: When I've met with you gentlemen before, I've always told you that my mind has been open, and we've talked the thing over together. So, in order to be entirely fair and frank with you people, I want to explain to you gentlemen that I had a long talk with the President this morning and went over the whole situation with him to find out what his wishes were in this matter. It's a question of carrying out the program as laid down in his message to Congress and his radio talk. I tried to be as fair as possible in giving all sides of the question and pointing out the difficulties and everything else, also my own recommendation if he wanted the thing carried out properly. And the result of that talk this morning - he and I both decided ~~on the~~ part of the Treasury that we'd let 50 million dollars a week run off. And as I say, I have never - I thought just in fairness I shouldn't ask you to advise me, having made up my mind. And that was the decision which was made this morning.

Eccles: That would be indefinitely. That would take you on through June. See, in June you'll have 150 fall due commencing on the 22d.

H.M.Jr: Well, I was - I didn't go beyond that; I was talking from now until the 15th of June.

Eccles: You were figuring while you had a hundred million of bills a week that you'd pay off half of them.

H.M.Jr: Pay off half of them. And that would take us through until the 15th of June. I can't think beyond that. I mean we'd have to reconsider in light of whatever our June financing was going to be.

(Harrison comes in)

Eccles: We discussed the matter yesterday from various angles and are all agreed that the problem it presents to both the Treasury and ourselves is that if anything is paid off it means that the Reserve System will get cash, of course, in lieu of bills and thus would reduce its portfolio to the extent of those bills unless it goes into the market to replace them; now, the problem is, if you pay 50 million of bills off, is it going to be possible to replace those bills? Where can you go to replace them?

It would do another thing. To the extent that any bills are paid off, it will naturally affect the Government bond market to the extent that they'll go up higher. Now, the question is, should there be any effort to keep them from going just as high as they want to go, with the later expectation, of course, that there may be another adjustment. That, of course, is in the future. To the extent that anything is paid off, it does mean a stronger bond market, a bond market less easy to keep from going up rapidly, and it also seems to me to put the Reserve in a position where it might have to let some of its portfolio run off to the extent of the amount of just the bills paid; in other words, don't replace the bills that are paid off.

Now, that raises this question, however. If you let the portfolio run off, of course, in our explanation - we'd have to make one - the only explanation we could make would be that we're not selling anything, it is merely a case of the Treasury paying - reducing its debt, and to the extent that we hold bills that they are paying, we are not replacing them, because it is practically impossible to replace them in the market due to the scarcity of the bills.

H.M.Jr: Well, as I say, that's the problem that you're faced with, and that's the problem, and that's the result of this ....

Eccles: Well, that's the way we could meet it, let some of the portfolio run off.

Szymczak: In other words, we'll decrease the excess reserves by that amount after having increased them, turn right around.

H.M.Jr: Your responsibility. And as I said, people that have been working four months to have us release this billion dollars worth of gold - nobody raised the trouble it would make in handling this situation, and this is what they wanted. Now we've got it, and it's just a question of who's going to have the troubles, the Treasury or the Federal Reserve. Now, this has been going on for months, and for months it's been advocated that a billion dollars worth of gold be desterilized. Well, it was a billion four - doesn't make much difference - and now we're plump up against this thing and nobody's thought it through.

Eccles: It's the decrease in the reserve requirements that's putting the strength in this bond market. You've got this 750 million throughout the country, and your pressure on the bond market is the decrease in the reserve requirements. Of course, it is something that none of us wanted, but it was made a part of the program and there wasn't anything else to be done about it. If it were merely a question of desterilizing a billion of gold, it would be a very different problem than desterilizing a billion four of gold and decreasing reserve requirements by 750 million. That gives you two billion 150 million and not a billion, which makes a very different problem.

H.M.Jr: Well, the Federal Reserve Board recommended it.

Eccles: We didn't recommend it.

H.M.Jr: Oh yes, you're on public record.

Eccles: Well, we did it, but we didn't recommend it. Nobody took action to recommend it.

H.M.Jr: Well then - I haven't got the President's speech, but I ....

Davis: Well, isn't it perfectly idle to argue about who did this and why this fellow did that and whose responsibility it is? I mean we've got a problem and we're both of us interested in the state of the Government bond market in the future, and that's the angle that bothers us over there, Henry, I'd say. I mean I'm not interested, and I don't think you are, to follow through who was responsible for this or that or the other.

H.M.Jr: Well, I think it's pretty important, because I don't know what's going to happen next.

Davis: Well, we're jointly interested in the state of the bond market.

H.M.Jr: I don't know what the recommendation is next. The next one I've already heard - and I don't know where this one comes from and I don't get a chance - is, how about taking another billion dollars out of the Stabilization Fund.

Davis: Well, of course, I never heard anything about that.

H.M.Jr: Well, they start in - that one's already started, and so it does become a matter of responsibility and interest when these things - they keep working, burrowing, working, then suddenly you're faced with this thing and everybody says, "Oh my God, what are we going to do about it?"

Eccles: Well, the decision has been made on this matter. I don't know that there is anything for us to discuss.

H.M.Jr: Well, it's this - there is this to discuss. I mean the Executive Committee of the Open Market Committee is here and you people own a quarter of a billion dollars worth of Governments - I don't know how much we own - and I'd like to ask the managers of that fund if they're prepared to say how they're going to handle this situation and what they're going to do, and then we'd be glad to discuss that with them, because my mind on that is entirely open. We've got some bonds, we've got some cash, and I'd like to - I think it would be an advantage if we moved simultaneously and not at cross purposes on that.

Eccles: Well, what bonds do you refer to?

H.M.Jr: Well, I mean we've got - I don't know - Harris, how many bonds have we got in our various investments? Must have - how many Governments do we own?

Harris: Well, including those special twos and ....

H.M.Jr: Not the - exclusive of those.

Harris: We own over two billion.

Sinclair: Two billion, you say, Mr. Harris?

Lochhead: Trust funds.

H.M.Jr: We've got over two billion. Some of them can be sold. And we've got some cash.

Eccles: Well, I think that if you don't want the market to go higher - it's just a question of, after all, whether we would let this market go just where it naturally will go, let it go down to a two percent yield or wherever it might want to go, and whether there should be any effort in keeping it from going there.

H.M.Jr: Well, I can answer that very simply, and I'm sure the people in the Treasury agree. I'd like to see just as orderly a market as possible. I'd like to see just as orderly a market as possible. And I'd like to hear from Dr. Burgess and ask him what cooperation he'd like to call on from the Treasury to keep the market orderly.

Burgess: Well, Mr. Secretary, it's a good deal - in Chester Davis's language, a good deal like saying, "Some one else will fix the size of the crop and all we have to do is control the price." I think that one should say first, it is a perfectly impossible situation, there isn't any way of controlling the price of Government securities in this situation.

Now, we can have some influence on it. The only way we could have any real influence is by letting some of our portfolio run off, and that would tend to restrain the rise in prices. What the effect of that would be in confusing people's minds and whipsawing the market one way and another, or its relation to the general program, I think, is very problematical. I think we'd have to be very reluctant about using that method, because it would appear to be a direct contradiction to the program that's been announced. And what the effect on the market would be I don't just dare say. It would be very depressing, but it is about the only instrument we have left that would make any impression in keeping this market orderly.

H.M.Jr: Well, would this be a fair thing to do? In view of what we're going to do, would you people like to meet and then come back and talk it over again? Because we wouldn't normally announce this thing until 10:30 tomorrow morning. Is that when the press conference is, Herbert?

Gaston: Yes.

H.M.Jr: And you might have a plan or suggestion. And as I say, I've got to raise the money eventually, whatever this thing is going to cost, and I don't want to see the Governments get too much out of line, whatever that means, and we've got a big program ahead of us next year; and there's the old saying, "Whatever goes up has to come down." And we're trustees for some sixty different accounts, of which one is Postal Savings. And as I say, we've got over two billion of Governments. So for every reason we're tremendously interested.

And whatever the decision is - I mean proposal - I mean I think it's important that we buy and sell at least at the same time, so that we're not at cross purposes. I mean if you people are buying, we don't want to be selling, or vice versa.

Eccles: I don't know that we could accomplish anything more by meeting. It seems to me the problem is quite a clear one. To the extent that the Treasury anticipates - pays off bills rather than turn them over, it puts more money immediately in the market and puts less bills in the market, which gives strength to the market now - at least temporary strength until you have to do a lot of financing next year. In the meantime we could sell bonds, but we have great difficulty in replacing them with bills if you're reducing the amount of bills.

H.M.Jr: I explained that to the President. I was just as fair as I knew how to be. I went all around.

Eccles: Now, if you'd sell bonds that would help - sell bonds from the trust funds. But then, you'd get cash which would nullify the effect of your - in other words, if you'd pay off your bills 50 million a week and then you should sell 50 million of bonds in order to keep the market from going down, you merely add to the General Fund the 50 million that you paid out in payment of the bills, so that the excess reserves are just the same as if you hadn't paid the bills. That's the effect that would be if you sell bonds from your trust funds.

White: Not if you put the cash back in the depositaries, which you might do.

Burgess: They wouldn't take it.

Bell: They'd want to pay it in.

White: I thought you were going to deprive them of that privilege.

Eccles: They won't pay the F.D.I.C. assessment.

Burgess: They elect whether they'll take new deposits.

Lochhead: They won't take Postal Savings account.

Eccles: Early next year you've got some very large maturities, and it will be at that time likely that the revenue based on this year's income will be falling off and the expenditures will be increasing, so that the Treasury will - it would seem to me that with the large cash balance they have now, if they could go into next year at a time when they have a huge refunding together with the possibility of raising new money, that would be the time to have large balances. Personally, it would make a much more orderly situation if the 50 million were rolled over - I mean the hundred million a week. It would be, of course, that much less pressure on the market and it would be that much easier to keep an orderly market than if you take that out of the market.

If that is taken out, it does create some problem that could be met by the Reserve's portfolio running off. But that hardly seems desirable. I think we might be able to explain the running off of just the bills that the Treasury pays. Such portion of the bills that the Treasury pays off - we might well let the portfolio diminish by that amount, with the expectation that when they come back in next year we would increase the portfolio at such a time as they started to increase their borrowing.

H.M.Jr: Well, when do you think you people could work out a policy as to how you're going to handle the situation? I mean we've got several alternatives.

Eccles: Well, we couldn't work out one on reducing the portfolio before next week. We'd have to have a meeting of the full Committee, which has the responsibility. The Executive Committee doesn't have that. To reduce the portfolio ....

Szymczak: Or increase it.

Eccles: ... or increase the portfolio - we would not want to take that responsibility without a meeting of the full Committee. We could get that meeting within a - well, it would be difficult to get it before the first of the week.

H.M.Jr: Well, what will the policy be for the balance of this week?

Eccles: Well, we discussed the matter yesterday, and it was merely to continue what we're doing, attempting to maintain as best we can an orderly market. I don't think there is any immediate problem of maintaining an orderly market, because we have over 600 of bonds. I am merely thinking that by a continuation of selling long bonds to maintain a market, we could completely run out of long bonds in the course of, say, several months. But for the course of the next week or two weeks, I don't think that it - it may not be such a problem to maintain an orderly market, the market showing a continuous strength.

H.M.Jr: How do you feel about this, George?

Harrison: Well, Mr. Secretary, I'm in a somewhat different position, I think, from some of the others. First, my advice was not asked as to whether gold should be desterilized or whether reserve requirements should be reduced. I have taken no position on that and therefore my judgment is not prejudiced by those past decisions in any way. Had my advice been asked, I think I would have been in opposition to both acts. But that's water over the dam. The policy was determined and we have now increased excess reserves by some 750 millions, so that the total in the System is two billion and a half. With your desterilization program it is probable that excess reserves will be increased to three billion eight before the end of the year, even if you take the slowest method of paying out the gold that you have released. In face of the large increase in excess reserves that has already taken place, plus the probable further increase that will take place before the end of the year, it is our judgment - that is, it is certainly my judgment - that the tendency for the Government bond market is to go up. Already it's been very strong - very strong. The first flush of purchasing by those who have gotten larger excess reserves has made for a very rapid increase in the bond market. We have done the best that we could, with the powers at our hands, to make that market an orderly one, in face of a huge increase in demand.

I would like to think that the Reserve System would continue to do what it can to make that market orderly and provide bonds to satisfy some of this demand. I think that it is in the interest of the Treasury, in the interest of the market, it is in the interest of the member banks who are buying the bonds and who, if this is allowed to go through the roof now, will suffer later a large loss when the inevitable downward movement comes - that being so, I think it should be the responsibility or the interest - put it that way - of all of us to see that that market is maintained as orderly as possible over the future.

Now, what can we do to make it orderly? I think we ought to continue to do what we're doing. I would like to think that, for the time being anyway, you would continue to roll over your bills, not only because it provides a means for us to replace the bonds that we sell in the event that we decide not to let the portfolio go down, but also from the point of view of the Treasury because it is probable that you won't have to borrow any new money through the rest of the year, but it is likely that you will have to borrow increasing amounts next year, and I should think that your position would be better if you should maintain as much stability through this year as you can, and then finance your requirements next year on as stable a market as we have been able to maintain through this year. Otherwise, if you reduce your bills now and reduce your total obligations outstanding, you will have a drop down through this year and then a sudden increase next year, due to two factors: large maturities plus larger and increasing expenditures.

I am myself of the opinion, although circumstances develop to prove that we are often wrong, that this market is going to continue to get stronger and stronger. Now, if my judgment is right on that, we have only a limited capacity to sell bonds - limited by the amount that we've got, and to conserve our ammunition and to make our action most effective, it might well be possible, if not likely, that in a few weeks the best step that the System could take would be to let the portfolio run off, on the theory that that is the most effective way of exerting the downward pressure on the market.

I admit that if we let the portfolio go off it decreases or sops up excess reserves to the extent that we let the portfolio decline, and it might appear to be in conflict with the program that has been agreed upon to increase excess reserves; but after all, I don't know that the program contemplated that you must have three billion 800 million excess reserves or any particular amount. Query: whether we couldn't make a perfectly satisfactory explanation of the action, in the light of the actions that have been taken, by saying that we're going to in a measure offset the increase in excess reserves by some reduction in the portfolio and reduction in excess reserves to that extent, not with the purpose of sabotaging the program but rather solely for the purpose of accepting the responsibility of maintaining an orderly market. And if it is necessary, in order to maintain an orderly market, that the portfolio should drop somewhat, I should think that it would be possible adequately to explain it both to the Congress, if there is a political inquiry about it, and certainly to the public.

Now, I know that others feel a little differently about that, but it was only a year ago that we increased reserve requirements and reduced excess reserves, and in the face of that turned around and bought about a hundred millions of Government securities, which tended to offset the action that we had previously taken. Conversely, I don't see why we couldn't do the same thing now, if in the light of the next few weeks that seems to be the most effective and economical way of carrying out the responsibility we've got.

I don't think we've got to decide that today. We in the Executive Committee can't decide it today, because we haven't got the authority. I think we ought to have an early meeting of the full Committee so that we can discuss the method by which we're going to carry out our responsibility of an orderly market: whether we're going to do it by replacements or whether we're going to do it by liquidation of some of the portfolio.

H.M.Jr: I should think the sooner you had your meeting, the better.

Harrison: I think so too, with this possible reservation, that while our judgment is that this is going to be a continued strong market, you never can tell when you might get a reaction of opinion which will tend to offset some of the present strength. I don't expect to see that reaction myself, but it may come, and there may be some advantage in not deciding whether you want to reduce the portfolio for a couple weeks yet.

H.M.Jr: Well, I think this is a perfectly fair request on the part of the Treasury, that the minute you people are thinking of changing the policy which you have been following since last Saturday, I'd like to be among the first to know it.

Harrison: I should think you should be. And I don't know - I'm speaking only my personal view, and I think we all have to here - I don't know that the majority would think it would be wise to reduce the portfolio; I don't know that two weeks from now I would vote for it either. But it looks to me, projecting our views forward, that that might be the best policy in spite of the fact that it appears to be going counter to the general program of increasing excess reserves.

I think that is only an appearance, it could be explained. You and I know that except for psychology, in fact, to reduce or to offset three billion eight by a reduction of two or three hundred million in our portfolio wouldn't have any real impact upon our economy at all, except for psychology. And if we're going to rely upon psychology, perhaps that is just the thing we want - in other words, to sell smaller amounts and get the aid of psychology rather than try to offset the strong market by continued sales of Governments, plus replacements which tend to strengthen the shorter-term Government market.

But as far as I see it today, I think we have got to go on replacing, because we haven't got the authority to do differently. And apart from that, whichever we do, if you ask my judgment, I think the best policy for the Treasury, for the reasons I have mentioned, would be to continue to roll over the bills for the time being, leaving for future judgment the question of what you want to do about the June maturities. I don't think you have to decide that today.

Lochhead: Mr. Harrison didn't get here in time for your opening statement.

H.M.Jr: You didn't get the statement.

Harrison: I apologize for being late, Mr. Secretary.

H.M.Jr: I said that before when you people came in to these meetings I've always asked your advice, always came in with an open mind. But I made the statement that I just came from the President, had been with him a long time going over with him all this thing, and at that meeting with him it had been decided to let 50 million a week run off.

Harrison: Oh, I didn't know that.

H.M.Jr: I'm sorry, I thought somebody had told you.

Harrison: Well, I was just giving you what I thought would be the best program.

H.M.Jr: Because, I said, I didn't want to sit here, having made up my mind, and then ask your advice, because I had never done that.

Harrison: Well, I think if that's definitely decided there is more rather than less to be said for allowing our portfolio to run down somewhat, both for practical reasons and also for purposes of policy and objectives.

Burgess: Mr. Secretary, from the point of view of the market, I think one thing ought to be said before we break up. If you announce that you're going to pay off 50 million of your bills, that will affect the market very strongly on the up side. If we announce at some time that we're going to use our portfolio flexibly, let some run off, that would affect it on the down side. I think if either of those steps is to be done that it would be much wiser to do them simultaneously than separately. That is, if in connection with your announcement that some of the debt would be paid off, the Board were to announce - or the Open Market Committee - that we would make that flexible use of our portfolio, you wouldn't be whipsawing the market one way and then the other.

H.M.Jr: Well, I'm obligated - have a press conference twice a week, have one Thursday morning at 10:30 - I'm obligated to make an announcement at 10:30 tomorrow morning as to what the Treasury proposes to do about bills. So my time is fixed, and that is why I was asking whether you people didn't want to meet, and in view of the decision which the Treasury has made whether you wanted to make an announcement of your own at the same time.

Harrison: When is that, tomorrow morning?

H.M.Jr: Every Thursday morning at 10:30.

Eccles: Pretty difficult for us to do it. In fact, we couldn't do it tomorrow morning.

Szymczak: Why not, Marriner?

Eccles: Got to get your full Committee here.

Szymczak: (Nods no)

Eccles: Supposed to communicate with them by telephone and eventually - certainly not be a very satisfactory thing for them or for us.

Szymczak: I think this is really important enough to contact them at once by telephone, get some decision on it. You're only speaking ....

Harrison: We can at least do this: we can make an effort to see how far those of us who are here are in agreement, or ....

Eccles: We can do that.

Harrison: We might come to a definite agreement among ourselves. Or there may be a majority of the full Committee here who are opposed to doing anything about the volume of the portfolio anyway, in which event there is no use consulting the others. That will at least enable us to report to the Secretary that all we're going to do is continue our present practice of replacements.

Szymczak: We could have a meeting immediately after retiring from the Secretary's office of the Board and the members of the Executive Committee that are here, and then contact the rest by telephone, and we could have some information by late this afternoon.

Eccles: You mean as to advising the Treasury whether we're going to let our portfolio run off or not?

Szymczak: That's right, and also as to our action in the market - selling bonds in the market.

Harrison: May I ask, Mr. Secretary, whether it is any part of the Treasury program to let some of its two billion of bonds go in an effort to maintain this orderly market, whether that has been decided one way or the other?

H.M.Jr: Hasn't even been discussed.

Harrison: Of course, to the extent that you did that, you would be offsetting this increase in excess reserves, too. I don't know whether that's any worse than having us do it, or better.

Eccles: Well, we can reverse our action on excess reserves - if we could go back and get this 750 million we have released, we'd be all right.

Sinclair: Think we'd better look into our ammunition a bit here.

Harrison: Well, you've got a strong market here now. As we say, we think the announcement tomorrow morning will tend to make it still stronger, and that tends to make our present program of shifting from long to short less and less effective. And it may be that if we're going to continue that, we might need some help from the Treasury. We might want to recommend that; I don't know.

Sinclair: May I ask, what is the market doing this morning? I haven't checked.

Burgess: Quiet and firm.

H.M.Jr: I'd say up one or two thirty-seconds. Harris, go get it fresh for them, will you please.

(Harris goes out)

Find out, Burgess, whether we've sold anything?

Burgess: Not yet. That is, we hadn't.

H.M.Jr: Industrials off about two and a half points. Commodities are off.

Harrison: It's a great world: threat of an inflation program, bonds go up and stocks go down.

H.M.Jr: Sterling is weak.

Harrison: It's cock-eyed.

H.M.Jr: Well, the only thing that is strong is Government bonds and silver.

Harrison: Silver.

H.M.Jr: Silver's strong.

Burgess: Your two babies.

Harrison: Might replace our bonds with silver.

H.M.Jr: That's what I had in mind.

(Hearty laughter)

Lochhead: Well, we can sell it at $1.29 an ounce.

Harrison: Put the word "laughter" after that remark.

Sinclair: Can't buy silver, George.

(Harris returns)

H.M.Jr: What is it, Harris?

Harris: Very quiet. Prices unchanged to one and two better. The stock market is very quiet.

H.M.Jr: Did the Fed do anything?

Harris: Not yet.

Burgess: We hadn't up to a quarter of 11.

H.M.Jr: Did you ask whether the Fed had done anything?

Harris: They hadn't up to a few minutes ago.

H.M.Jr: They had not.

Harris: No.

H.M.Jr: Well, George Harrison asked - I'm more than willing to be propositioned. How's that? I mean ...

Sinclair: Fair.

H.M.Jr: Because after - without drawing any pictures - I mean I don't have to. Of course, this thing .... So if you people should do anything, come to any decision or want a proposition on anything, why, we're more than willing to sit down with you.

Harrison: Mr. Secretary, I don't want to ask an impertinent question, especially since I think you have clearly answered, but is it too late to reconsider the question whether you might make your announcement next Tuesday rather than Thursday, or next Thursday rather than this Thursday, because as Mr. Burgess says, after all we're interested in a common problem here, and it does seem that it would be unfortunate for you to make an announcement that tends further to boost the market and then we, say, next week, possibly making another announcement that tends to depress it; and there are too many gyrations in it already without creating artificial ones.

H.M.Jr: No, your question is a perfectly proper one, and I'll give you a perfectly courteous answer, that the decision was made, as I said, before I came into the room, and I thought in fairness to you people - I've never done that before - that I ought to tell it to you. I mean every other time ...

Taylor: Applies to time, too; in other words, that means tomorrow.

Szymczak: The announcement must be made tomorrow morning.

Harrison: I mean has nothing been developed today that would warrant reconsideration on the time, not on the policy necessarily?

H.M.Jr: No. And I'd like to say this. I mean I can say it very calmly and judiciously. I mean the fact that the Wall Street Journal prints pretty fully what is reported to be the position of the Federal Reserve System in this morning's paper makes it rather difficult not to give the newspapermen publicly tomorrow a clean-cut answer.

Harrison: I haven't seen the Wall Street Journal.

H.M.Jr: Well, I suggest you read Mr. Duffield.

Szymczak: And the editorial.

Eccles: I haven't seen it. Chester called it to my attention on the way over here.

H.M.Jr: I suggest you read Mr. Duffield.

Harrison: Our policy or your policy?

Burgess: Got the whole story.

H.M.Jr: Yes, the whole story.

Davis: Well, he's got more of a story than exists, Mr. Secretary.

H.M.Jr: True.

Davis: And it is one of the extremely embarrassing things that sometimes happens.

H.M.Jr: I said I'm saying it very calmly. I've worked with the Board and with the Committee together - well, for a little over four years, and it's my desire to continue to do so. As I have often said, I think the most important thing, aside from any action, is that towards the public we present, if possible, a united front. I've always said that's the most important thing. I think it still is. I'm willing to do my part. But certainly in the Treasury here ever since I came in - I mean we've clamped down on that kind of thing just as hard as it is possible. But I'm - I mean it sort of - but having made the decision at the President's bedside this morning, I feel it is necessary to announce it tomorrow morning.

Harrison: Of course, it doesn't - assuming that we're all after coordinated action and agreement, it makes it awfully hard for us to get an agreement where we haven't got the whole committee here, with such short notice of your policy.

H.M.Jr: Well, again I say calmly and without any feeling that I think that some of this should have been thought about the last couple months. The Board were the people who have worked so hard for it and got it.

Harrison: Well, it might have occurred to me that somebody would desterilize gold, or alternatively that somebody might decrease reserve requirements, but I don't think any of us not on the inside could have possibly guessed through advance thinking that both would be done at the same time.

Eccles: No, that's the - I did all in my power to avoid changing this reserve requirements picture. You recall yourself at the luncheon down here with Hopkins and Jones - and you know what request came to me with reference to the question of changing reserves; and the only choice we had about it was to be put in a position of not cooperating with the program or do it. And that was a pretty tough decision for - I couldn't say that we - either question of cooperating, it seemed to me, or move out. What has happened as a result of it is quite inevitable, because you couldn't dump 750 million in the lap of these banks over night and not get ....

Szymczak: Marriner, can't we go back to our Board room and confer with the rest of the Board members and decide upon something and then contact the other members of the Open Market Committee and contact the Secretary this afternoon on what we're thinking about? Get together either this afternoon or perhaps ....

H.M.Jr: Before you go, may I raise one thing with Burgess. Are you making progress with R.F.C. on their coming issue Monday?

Burgess: (Nods yes)

H.M.Jr: Could you tell us about what you think it would look like, as far as you have gone?

Burgess: Well, the last we talked the program was to put out 175 million, which includes 60 million of refunding, which would be simply an exchange offering, and that it would be two issues of perhaps nine months and twelve months notes, and that the rates for the year issue would be around three quarters of one percent, and the nine months we haven't discussed very much - .0065, .0060, something like that. Those rates are changing so fast under this program that we can perhaps reduce them by the time we talk again. Particularly with your announcement, those rates will go to the ....

H.M.Jr: What date is it? May 1 the last day?

Burgess: May 2.

Bell: Ought to be announced next Monday.

Burgess: Should be announced Monday morning.

H.M.Jr: But is everything going smoothly?

Burgess: I think so. We've set the wheels in motion.

Bell: The Treasury is working on an issuing circular and R.F.C. is doing the same thing, and they will combine those.

Burgess: I think it is very important that before the end of this week, preferably the next two days, the R.F.C. should give a preliminary indication that it is going to do financing of this sort - the general character - just as you give advance information so the market may be thinking it over; and should give the facts about tax exemption and the fact that these are guaranteed, give the facts of the obligation. There was a great misunderstanding on that last time.

H.M.Jr: Well, would that be carried in Monday morning's papers for offering on Monday, is that the idea?

Burgess: Final offering, yes. What I am talking about also is the advance statement.

H.M.Jr: Well, Taylor will phone Jones and tell him.

Burgess: I think he already suggested that to him.

Bell: We hope to have the circulars ready to go out Saturday afternoon, just the same as we would if it were a Treasury announcement - release Monday morning.

Taylor: I've talked to him about everything except the day and so on, as to when he ought to feed it out, and I'm going to call him this morning and say this afternoon is probably a good time to start feeding that out.

H.M.Jr: Well, is there anything else, Marriner?

Eccles: I don't - I don't think of anything else.

Burgess: There is the question of your War Loan deposits, Mr. Secretary, as to whether the banks should have the privilege of prepayment. I think that your decision with respect to repaying 50 million of bills somewhat alters that case from our preliminary discussions, and on the basis of that I'm inclined to agree with Mr. Bell that we ought to give the banks some continued privilege of prepayment. Now, it may be we could limit that in some way and have them do it only over a period of days, but not ...

Bell: Not pile it up in a few days.

H.M.Jr: Well, that would be by word of mouth, wouldn't it?

Burgess: Yes, simply be continuing our present practice of making no change in it, but on all amounts over two million dollars consulting with the Treasury and arranging this schedule.

H.M.Jr: Call up Papa Bell and ask him.

Burgess: That's it exactly, let him be the dictator.

Eccles: In other words, you're not going to give them the option; have to get consent.

Bell: Under present arrangements they can pay in anything up to two million dollars without consulting the Treasury, but when it goes over two million dollars, why, they have to send a wire and ask permission to prepay.

Taylor: Why don't you leave it just the way it is?

Bell: That's what the doctor's suggestion is. Then when they ask permission to pay in more, say, up to ten million, we give them permission to pay that in over five days, two million rather than ten million in one day. I think that's a good suggestion myself.

Taylor: I don't think you want - under these circumstances you want to do anything to disturb the present arrangements.

Sinclair: Mr. Secretary, before we go, there is one further question I d like to ask, in view of the question raised by Mr. Burgess about not whipsawing the market with increased reserves and through some other method decreasing reserves. We all seemed to think that was a rather important point. Before we go back to our discussion, I'd just like to make sure that we do think it's an important point. Do I make myself clear?

H.M.Jr: Not quite clear, no.

Sinclair: Well, Mr. Burgess said if the Treasury pays off 50 million a week and then for some reason the Open Market Committee or the Treasury decide to sell bonds or let - on account of it, then you'd be doing one thing one day and four or five days later doing the other thing, and it might, as he expressed it, whipsaw it with decrease and increase. I thought both you and Mr. Burgess attached importance to that. I'd like to make sure that that's a really important point. As a matter of policy, I think we've got enough ammunition for several days probably to handle the surging market; whether we have beyond that point is another question.

H.M.Jr: The only thing I think is important - Bell can talk for himself - is that if there is any change in your policy we be given an opportunity to sit down and discuss it with you. That's the only thing I think is important. I mean if there's any change and there's anything to discuss about it, if you want to discuss it, we'd like to know it just as soon as possible. That's the only thing that I stress.

Bell: It seemed to me desirable that if the Board decides to let the portfolio run off, that decision ought to be announced at the same time that the Treasury's decision is announced to retire 50 million bills.

Sinclair: You do think that's important.

Bell: I think that is desirable from the standpoint of the market.

Eccles: It seems to me we're put in an impossible position. To decrease reserve requirements, which has caused this situation - we decreased the reserve requirements and that has created the excess reserves at the present time that are causing this problem. Now, to turn right around and as an Open Market Committee let some of the portfolio run off, which tends to nullify the effect of that, is rather a difficult thing to justify. If the purpose of this is to get interest rates low and a huge excess of funds, why not let the Government market go where the excess reserves would normally put it. If that isn't the purpose of it, then what is the purpose?

Harrison: Not doing that anyway, because we're offsetting it as much as we can.

Eccles: Well, that's right, but you're tending to do it not by diminishing at all the excess reserves. Now, we were put under requirement to make this change in reserve requirements. We did that. Now, I don't - it doesn't seem to me that on one hand we can agree to give to the market a certain amount of excess reserves and then turn around through an open market operation and reduce that amount of reserves. It just doesn't seem consistent at all. If they wanted the market to have three billion 800 million of reserves, wanted to desterilize a billion four, not a billion; they wanted to decrease reserve requirements 750 million; then, why attempt to offset or nullify that? Let's let the inflationary effect of the thing and the extremely high bond market, extremely low rates - let it have its effect. I don't know why we should be the goats in attempting to offset that kind of a situation. Now, that's the other side of it.

Sinclair: Except we have a fundamental responsibility to maintain an orderly market, as far as we can.

Eccles: But a situation has been created, and I don't think we can assume that responsibility. You can't increase reserves as we have and then assume responsibility of maintaining an orderly market when a disorderly market is created as a result of an action taken. That's the other side of it.

Harrison: You wouldn't stop making shifts?

Eccles: Well, I'd make them as much - to the extent that you can do it. But how can you make shifts if they're going to take these bills out of the market? We're getting this - taking bills out of the market makes the problem - that much more impossible to make shifts.

Burgess: I think the meeting would be interested in knowing that par is now bid for all issues of Treasury bills.

Bell: Go to a premium.

H.M.Jr: Stop printing money. Be cheaper issuing bills.

Burgess: So it wouldn't cost you anything to continue issuing Treasury bills.

H.M.Jr: I say we can substitute them for silver certificates.

Harrison: Mr. Secretary, may I in my effort to stall for time ....

H.M.Jr: Would you like a glass of tomato juice?

Harrison: Would there be any impropriety or difficulty in having your press conference tomorrow at four o'clock rather than 10:30? For two reasons: First, it gives us that much more time, and second, it does seem to me that there might be some advantage in making an announcement of this character after the market closes anyway.

H.M.Jr: That's perfectly reasonable. If that would help you, we're perfectly willing.

Harrison: I don't know that ...

H.M.Jr: I mean if you want that - I mean just between 10:30 tomorrow morning and five o'clock tomorrow night is ....

Burgess: I think from the point of view of the market that's very important. After all, there are a few people who have access to tickers, and they would get an immediate advantage that the country bank wouldn't get.

H.M.Jr: Perfectly willing.

Harrison: I don't know ....

H.M.Jr: No, you're asking me. I told you, "Go ahead, proposition me." I'm all right.

Harrison: I tried two or three of them.

H.M.Jr: All I got to do is listen.

Harrison: It seems to me from the point of view of the Treasury ...

H.M.Jr: I can give you a courteous answer. We're perfectly willing. I say five o'clock on account of San Francisco. Perfectly willing to let it go till five o'clock tomorrow night.

Bell: Still send out the announcement tomorrow morning. The banks have to get ready.

H.M.Jr: What?

Bell: Banks have to get ready.

H.M.Jr: Better hold that.

Bell: I was wondering if we shouldn't send it so they could get it all ready to mail.

H.M.Jr: Which banks you mean?

Bell: I mean Federal Reserve Banks.

H.M.Jr: They won't do anything except through Burgess, will they?

Burgess: It goes to all twelve banks.

Bell: All twelve banks will get notice, and it won't be announced in the press until Friday morning, but they ought to get ready.

Burgess: You can send it to them in the afternoon and they can get it out; they're all prepared. Send it from here at two, something like that; there's going to be no leakage.

Bell: Ought to send it around noon or not later than two.

Gaston: I wonder what will be the effect of an announcement tomorrow morning that the Secretary's disclosure of his bill program has been deferred until the market closes. What effect will that have on the market?

Burgess: I don't think it will have any effect; just be neutral, I think, Mr. Gaston. One can never tell, but I think it would be neutral.

Harrison: You could have a headache in the morning, couldn't you?

H.M.Jr: I hope not. Easiest thing in the world, though, to have. Always have a continuous one.

Burgess: It will obviously be an announcement that will affect the market one way or the other, so there is a very good reason for postponing it.

H.M.Jr: We could postpone the whole press conference until the afternoon, Herbert.

Gaston: Yes, but that wouldn't deceive them. They'd know why.

H.M.Jr: Well, I'm just trying to be cooperative in a small way, just so they don't think ...

Szymczak: I like that "small way" part of it.

H.M.Jr: Do something.

Eccles: Did the President, in feeling that these bills should be paid off - do you think he realized the problem that they create?

H.M.Jr: I did the very best job I could, and I told these fellows before you people came in in detail my conversation; I asked both Taylor and Bell whether they thought I'd been entirely fair in my presentation and they both said I'd covered the ground from all sides just as well as I could, giving him all the difficulties and everything else, and both sides. And then I asked him what he wanted to have done. But I did as good a job as I knew how. Maybe it wasn't very good, but at least I gave him everything I had. I gave him the morning papers, gave him the Wall Street Journal, the Times, and the Tribune, and their comments. Of course their comments were all opposed to this. So he had all of that.

Burgess: Maybe that's why.....

Harrison: All opposed to what?

Taylor: Letting bills run off.

Eccles: It seems to me that there isn't any - we can start temporarily and try to maintain that and keep that market, but as long as you've got these reserves in the picture and continuing reduction in the money market paper, you might just as well, it seems to me, face now the inevitable result of that and expect - let this market take the course that it is going to take as a result of those reserves. That's the way the situation looks to me. For us to try to even think - to assume that we can even approach a control of it with the present reserve picture is foolish. The sooner that the public and Congress know that we can't, the better off we are, the better off the situation is. The idea of trying to give an impression of - that you've got authority to meet a problem that you haven't, and take responsibility for it, is something that I don't want to do.

Taylor: Got a market tip to give you, Marriner. Buy Bayer's Aspirin for use next spring, because ....

H.M.Jr: What did he say?

Bell: "Buy Bayer's Aspirin for use next spring."

Eccles: Of course, you've got that next spring - very likely have the ....

Sinclair: We'll all have another pair of trousers by then.

Eccles: That's another thing, that if we should start letting a small part of - letting the portfolio run off now, you lose the psychological effect of it at such time as you may need to do that. There is a psychology in diminishing it. The minute that you - if you begin to let it run off now, you have lost any effect of doing that at such time as you may want to exercise a restraining influence. We'll be accused, if the program doesn't go ahead, of sabotaging the program.

Taylor: I think George brought it out earlier that about a year ago, why, we got caught the same way, where we had to take market action which was contrary to, let's say, the ....

Szymczak: Increased reserve requirements.

Eccles: But you had a different problem last spring. Didn't have a large spending program, didn't have a huge desterilization along with it. You had a very different - attempted to restrain rather than - whereas this time you have the very opposite type of a program. Well, we can't settle that discussion here. Just speaking out loud there as to what seems to me to be the possible problem with these reserves, as far as we're concerned.

Treasury Department
Division of Research and Statistics

Date 4/20 1938

To: Secretary Morgenthau

From: Mr. White

Should you at any time this evening find yourself "mulling over" this morning's finance conference, you may be interested in glancing at the attached, which I do not feel received sufficient emphasis at the meeting.

I hesitate to intrude on your "rest" period, but since some action is to be taken tomorrow I thought I had better risk it.

April 20, 1938

Some Thoughts Pertaining to this morning's Finance Meeting

onclusion

An orderly market does not mean a fixed market.

The yields on Government bonds should be permitted to fall to the lowest level possible now - even though bills go almost to par and bonds to 2 percent yield - and monetary policy should be directed towards keeping those yields at the low level attained until we have recovery. The Federal Reserve Board and the Treasury have ample weapons at their disposal to keep bond yields low until that time comes - or until the spending program has been continued for another year at least.

Therefore, the Open Market Committee is not justified in reducing the portfolio of the Federal reserve banks at this time except to the minor extent necessary to eliminate the hour to hour or day to day fluctuations and to slow up the rate of rise - not to check it. Nor should the Treasury sell bonds from its trust funds except to the extent that is necessary to cooperate with the Open Market Committee in order to insure an orderly rise.

1. The less bankers and investors are able to obtain on their investments in Government securities the more pressure there will be for them to turn to private investments. This is exactly one of the principal justifications for lowering reserve requirements and embarking upon a desterilization program. This is an essential part of the recovery program and is that part of the program which is particularly the Secretary of the Treasury's responsibility to push as much as he can.

2. An orderly market is, of course, desirable. But an orderly market does not mean an unchanging level of bond prices. It means only a gradual and smooth rise or fall to the level justified by the underlying economic conditions and by the recovery program. To accomplish that smooth and gradual movement is the Open Market Committee's job. There is no reason to believe that the job will be too difficult to handle with the resources available.

3. It is true that bond prices will rise during the next few months, but it is not true that they must fall when the Treasury has to increase its borrowings from the market this Fall or next Spring. Bond prices can be kept at approximately the level they will reach this Summer and Fall by appropriate open market and reserve requirement policy next Spring. If excess reserves tend

to decline next Spring because of the increased borrowing of the Treasury and because of expansion of private business, then the Federal Reserve Board can correct the situation (and thus prevent downward pressure on bond prices) by: (a) Again lowering reserve requirements; (b) Purchase of Government securities in the open market. (Moreover, the Treasury itself has powerful instruments to increase excess reserves if desirable.)

4. The $1.4 billion of desterilized gold permits the banks to absorb not only $1.4 billion of Government securities, but several times that amount when the Government resumes borrowing and spending in the Fall and Winter. These amounts should be contrasted with the expected volume of deficit financing during the next fiscal year.

In addition, a half billion or so of gold is very likely to come in and likewise can make possible under similar circumstances absorption by the banks of several times that amount - without diminishing excess reserves (and without increasing the downward pressure on Government borrowing and bond prices).

5. Eventually Government bond prices will fall, but that can only take place after recovery has been in full swing or (a contingency which, in my opinion, is very remote and in any case has no relevance to the present problem) if we do not get recovery in the next few years.

If, to be sure, recovery develops at a rapid rate and there is a large increase in bank loans to industry, then bond prices will tend to fall. At such a time the Treasury might be perfectly willing to permit it and possibly even encourage the decline.

(There is, it must be remembered, one other possibility. So far we have been speaking exclusively of economic factors. But political and psychological developments -- engendered overtly or subtly for political considerations -- may cause a break in the Government bond market before recovery is attained. Should that happen, it will matter little whether the yield of bonds prevailing at the time happens to be 2½ percent or 2¾ percent.)

(White)

ADDRESS OF JAMES ROOSEVELT, SECRETARY TO THE PRESIDENT,
at the Jackson Day Dinner, Hotel Manchester, Middletown,
Ohio, on April 20th, 1938.

CAUTION: NOT TO BE RELEASED FOR PUBLICATION UNTIL DELIVERED ABOUT 9:30 P.M., EASTERN STANDARD TIME, WEDNESDAY, APRIL 20th, 1938

In celebrating the birthday of Andrew Jackson tonight we are a few months late if we persist only in looking at the calendar. But in the situation which confronts us today I feel that Old Hickory would be more at home with us than ever. That hard-bitten old warrior was a direct man and a bold one. He first calmly decided what needed to be done and, once his mind was made up, he did it. No amount of conversation could dull his appetite for getting results. If we measure him by the test of current events, Andrew Jackson is never out of date. The one problem which was uppermost in his mind is the one in which we are most interested.

What to do for the man out of a job?

How to restore this nation to a prosperous basis?

Certainly the name and most of the origins of our present-day Democratic Party come from the days of Jackson. He liked a good fight better than anything else in the world, he loved to be alive and ready for action. I wish that he could stand with his party today. Today as then, it stands ready to do battle -- a battle not against individuals, not against personalities, but for a definite cause, that cause to make the capitalistic system of the richest country in the world run smoothly. The New Deal is going forth to war against depression once more.

Last week the President said in his message to the Congress, "The National Administration has promised never to stand idly by and watch its people, its business system and its national life disintegrate."

Coupling that statement with action, he has recommended to the Congress a new Public Works and Relief Program, which after many weeks of deliberation and study has been carefully designed to rectify what he considers to be the ills under which our system is now burdened. He has asked for these relief appropriations to insure that the men and women of America — the man without a job — shall, so long as the New Deal shall stand, never go hungry. He has called for a program of public works, the primary purpose of which is to give industry a new chance to sell its products and to give workers a new chance to find jobs. As to the need for such a program, I think there is little disagreement. The secondary purpose, we all know — the creation of useful and necessary projects, such as schools, playgrounds, bridges, hospitals and so on; I need not call the roll. An added appropriation for CCC camps will prevent the reduction of 300 of these, and thus guarantee that our young men will receive useful training for their future citizenship. In like fashion, the National Youth Administration will remove existing gaps in the education of many of our young men and women. And as WPA is to our urban and town life, so is the proposed program of the Farm Security Administration to our farm life -- The American Farmer will be protected.

There is nothing in this program that is new or revolutionary. In 1933 the Democratic Administration, faced with new and hitherto unknown conditions, had to experiment with public works and work relief. That theory has been tried and tested and found successful. Just as Andrew Jackson in his day faced the new and unusual with bold, direct and courageous action, so the Democratic Party in 1933 decided to rely upon the past performance of the American People. In every crisis which history has forced upon them they unfailingly have given full and confident support to bold leadership. From those experiments we have learned many useful and positive lessons. And we know many things today, therefore, that make it unnecessary for us to be hesitant in taking the direct action which is the basis of our present program. I am not implying that we know all the answers or that there may not arise in the future, need for further experimentation. We do know from actual experience that business employs more workers when Government takes action to increase the buying power of the people. The national income produced by a nation is the value of all the goods and services produced by the people in one year. The record shows that this national income -- which after all is the single test of America's wealth -- rose from 38 billion dollars in 1932 to almost 70 billion in 1937. In the span of those years it is an indisputable fact that the income of the American People was greatly increased. That, simply, is the purpose of this program.

I know that all of you who are thinking about it have two questions in your minds:

Can the country afford it?

Since we tried it once, why should we try it again?

Let me try to state simply the answers to those questions.

An automobile needs fuel to make it go. The gasoline which provides the power for our national automobile is the labor of wage earners, farmers, and business men, the people who are working, who are busy creating wealth. But the situation which we face today is very much like the problem of any automobile owner who is tempted to save money on lubricating oil on the ground that it is gasoline and not lubrication which drives the car. He soon finds that while his gas tank may be full, his skimping on oil has stalled the engine.

The Government expenditures which we recommend . have been found by experience to be necessary to lubricate the wheels of business and make them turn. We, the people, have this added advantage over the car owner. His lubricating oil once used is gone, but wise Government expenditures leave behind a permanent addition to the wealth of our cities and towns, -- the playgrounds, the reservoirs, the roads, the forest and soil conservation.

How does this fit in with your hope for a balanced budget? Think back to 1932, when the national income was about 40 billion dollars, or an average of $320 for each man, woman, and child in the country. The Federal Budget was about 4 billions, or $32 apiece for each one of us. If you could have paid the $32, you would have had on the average $288 left. That was too small to live on, and so the people could not pay enough to balance the budget. But in 1937, the Government was spending about $25 more, and your average incomes were about $230 more. Naturally the taxation from revenue was high, because it is a lot easier to pay $57 out of $550 than it is to pay $32 out of $320. The way to make the revenues rise until they equal the expenditures is to push the average income up some more. If we had kept up the advance of last year, the budget would have balanced in 1938.

But the same people who are objecting to a spending program now were saying last year that business could go ahead under its own steam and that it was time to taper off the Federal spending. Nobody knew for sure what the effect would be, but the majority of the American people seemed to be in favor of tapering off, so the experiment was tried. Business quickly went into a tailspin and the national income dropped about 12 billion dollars. Your average income fell from $550 to about $450 a year.

The Administration believes that this experiment in tapering off has gone far enough. We have learned that when we go ahead with public works and work relief, your average income goes up, and we come closer each year to balancing the budget. When we taper off, your income goes down and we go farther away from a balanced budget.

I am not making any apologies for these experiments. They prove that the Federal Government can pull the country out of depression by spending and can drop the country in again by economizing. We had to prove that by experiment because hardly anybody believed it in 1933. Now that this relationship is proved by experience, many people still can't believe it, but we are not in favor of delaying action any longer.

What makes national income? Production.

What makes production? Orders from dealers.

What makes orders from dealers? People spending their money.

Spending makes the market, the market makes the factories run and gives employment, the employment gives wages to spend. That is the wheel of industry. When it stops turning no one person dares to spend to try to start it up again. We have to act together, and the only way we have of pushing all together is by using the Government as our agent.

Some people will tell you that you are going to be ruined by the terrible burden of taxes, even if you do get jobs and prosperity. But think for a minute of what you have left over after your taxes are paid. Why not cut out all our spending, public and private, and have no expenses and no income at all? Then everybody's budget would balance at nothing equals nothing. The only way to get out of depression is upward. It will cost you some money, but you will make a profit on it, and will have more left for yourself afterward than you have now. If you have to double your taxes in order to double your income, is it not worth the price? Or would you rather cut your taxes in two and let your income go back to what it was in 1932? Ask that question when someone tells you that spending our way out is going to ruin the country.

Our experience boils down to this: When the Government spends more money, you all have more money and your taxes are easier to pay. When the Government spends less money you have a lot less money and the taxes are more than you can carry.

We believe that most of you who have no jobs will go back into private employment when business gets going again. And it will, with a little teamwork. The Government is doing all in its power to encourage business to go ahead without running off the track as it did in 1929. Those fears which business may have in spending money, in enlarging the plant of America are being dealt with by the Administration swiftly. I may mention for example, the renovation of the present tax structure, which is taking place in Washington now. I may mention the simplification of administrative regulations relating to the issuance of securities which business has claimed are too restrictive in scope. These and others like them are matters of administrative management. I believe that the great majority of the American People agree with me that the necessary changes are matters of administrative improvement and that we don't want to go back to the mistakes that were made before 1933. There are few business men, not to mention citizens in other walks of life, who today would wish to sacrifice the gains which America as a Nation has made since 1933. Do you in your own acquaintance know of anyone who wants to give up the general principles of the changes the New Deal has made, such as social security, the securites and exchange acts, the regulation of public utilities, the elimination of slums, or the strengthening of our banking structure?

No, I don't think any of us want to go back to 1929. Then we had a philosophy, if it could be called that, of "Do-Nothing". We tried that once and I do not need to remind you of the results. There is no desire to repeat that pattern of thinking, that policy of drift, of governmental inaction. We do not propose to blind ourselves to the facts, to indulge in the wishful thinking that by mere inertia a miracle will come to pass. We cannot content ourselves hoping plaintively for the best and looking "around the corner" without making any effort to get there.

51

You, the people, and your Administration cannot afford to wait for one year, or for four long years. We cannot "stand idly by". The time for action has come. Just as important as the doing is the time of doing it. We will not postpone this program until the good it can do will come too late. The essence of the New Deal has been to strike at a time when that action will get results. We propose to follow that policy, to act now, before conditions reach a point at which this program would be a futile palliative.

You know and I know of many people who have repeated over and over, "Something should be done." We are faced at this crossroads with the policy of doing that something or doing nothing. To the best of my knowledge, only the Democratic Party has been willing to say what should be done or to do it.

This is not the time to dwell upon partisan politics. But as Democrats who look to the future of our party, we must realize that it prospers only if our country prospers. What has befallen our Republican colleagues on the national scene can easily befall us if we go to sleep at the switch the way the Republicans did. "Do-Nothingness" will never again be the main attribute of Government in America. We have no touch-stone, no talisman of success — except that of intelligence and an understanding of our people. A new concept of security has grown up in the minds of the people. They have learned to demand much from their public servants. It is my hope that we will live up to their expectations.

As we read our daily papers, and listen to our radios, there must come home to everyone of us earlier or later, this simple truth. Our country has come of age. In a nation where men can no longer escape depression by moving westward to the frontier, in a country where land is no longer to be had for the asking, those of our citizens who through no fault of their own are overcome by the problems of a complicated economic system, have only their Government to look to for assistance. The vast majority of our citizens have come to realize as an established fact that they cannot allow their agent, the Federal Government, to be blind to conditions of suffering amongst their fellow-citizens. For what other reason have we created the organization of the Government? Throughout our history whatever the disaster, whether it be flood or fire, crop failure or danger from a foreign enemy, it has been natural for people to look to their common agent for protection. That is a basic reason for its existence.

To paraphrase the statement a great president made many years ago, the object of government is to do for a community of people whatever they need to have done, but which they cannot do as well for themselves as individuals. The Western Frontier was made available only through the aid of Federal troops. When the pioneers who settled the West began their long trek the movement was a community proposition. The Federal Cavalry detachments were the very life blood of the Old West, performing a hundred functions. Without the early Army Posts, the post roads, the pony express riders, civilization would never have come to the frontier.

Time changes many things. After a few short years, the Federal Government changed from a symbol of adventure to a symbol of protection and of help. The Government helped the farmer by providing facilities for shipping his goods to market, by getting lower railroad rates, building highways, creating land banks, and so on. It is the Government today to whom the Ohio Valley, for instance, looks not alone for flood control, but for flood prevention. And more than anything else it is the Government today to whom the man without a job must turn when all other resources fail. I am sure you join with me in the belief that he will never turn in vain.

It is nonsense, of course, to pretend that Government can do it all. Government's share is only to create conditions sufficiently attractive and sound so that the business man will spend, the investor will spend, and so that you will be able to spend. A large factor in creating that confidence for investment over a long period is the determination and the confidence of the American People as a whole in their own inherent capacity. Such confidence will not allow men to stand idle so long as there is work to be done. Those who have idle funds which they are unwilling to use are practicing self-delusion, if they really believe they save while they sit on their money. That money itself will melt away if the workers and machines are idle and wealth is not produced.

But our problems are not settled by simply shouting about danger. Our liberty is easily lost unless we act - together, unless we meet our problems boldly, unless we prove to our people that the powers of Democratic Government are equal to the task of protecting our security. As one of our wisest Americans has said: "If we would govern by the light of reason, we must let our minds be bold."

It is only a Government which draws its strength from the consent of the governed that can make vital decisions to act intelligently. I believe that we made this decision to act when we voted in 1932. We reaffirmed that decision 1936. From that unified Democratic will, the voice of a people which has spoken, we have drawn our strength. With that strength we must meet our problems.

We have won several big battles against this war upon depression. We have found, however, that the war is not yet over. But an enduring victory lies ahead. We Americans will retain the privilege of liberty -- liberty to think and to speak, liberty to act, -- and the liberty of lasting security.

- - - - - - -

April 20, 1938

Memorandum for the Secretary:

Col. Harrington's office telephoned the following figures:

Employment for week ending April 16 - - -	2,532,448
Increase over week ending April 19 - - -	27,965

APR 20 1938

Dear John:

I have gone over the matters which we discussed in our meeting of April 15th and have reconsidered the Treasury position in the light of this discussion. It is my feeling that in view of the far-reaching character of the other amendments contained in the proposed legislation it will not be possible for me to give you an affirmative answer either on the proposed Treasury guarantee of Home Loan Bank debentures or on the proposed purchase by the Treasury of Home Loan Bank debentures. It is my thought that the problems facing the development of the Home Loan Bank System require very careful study with a view to producing a comprehensive and constructive answer. As I wrote you on March 18, I realize that these problems are serious and I wish again to assure you of my desire to cooperate in producing an orderly solution.

However, in view of the unfavorable comments on the proposed amendments which have been expressed by other Governmental agencies, and in view of the comments of my own staff, I cannot recommend the submission of this legislation to Congress in its present form. It is my impression that under present market conditions the ability of the Home Loan Bank System to sell its consolidated debentures plus the resources of the Home Owners' Loan Corporation available for the purchase of shares of building and loan associations and the purchase of bank debentures should be sufficient to take care of any immediate problems.

Yours very truly,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Mr. John H. Fahey,
Chairman,
Federal Home Loan Bank Board,
Washington, D. C.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

TO Secretary Morgenthau

FROM Mr. Taylor

Subject: Suggested letter to Mr. Fahey concerning proposed legislation

Upon careful reconsideration of the legislation proposed by the Home Loan Bank Board, it seems advisable for the Treasury to continue its disapproval. The far-reaching character of the proposals makes it impossible to consider separately the questions respecting the Government guarantee of obligations of the Home Loan banks and the authorization for the Treasury to purchase these obligations.

Attached hereto is a suggested letter from you to Mr. Fahey, outlining briefly the position of the Treasury after reconsideration in the light of the meeting held with representatives of the Home Loan Bank Board on April 18. There are also attached a memorandum discussing the general issues involved in the light of the comments in the Board's memorandum written in rebuttal of your letter to Mr. Fahey of March 18, and a copy of the letter of March 5 to the Acting Director of the Budget, discussing in detail the Treasury's objections to the specific provisions of the proposed legislation.

Wayne C. Taylor

Attachments

Comments on Proposed Home Loan Bank Legislation

Three main proposals are involved in the proposed legislation together with a number of subsidiary provisions which collectively would effect important changes in the operation of building and loan associations under the jurisdiction of the Federal Home Loan Bank Board. Each of the three main provisions is summarized below and is followed by comments on the Treasury's position thereon.

(1) (a) A Government guarantee of obligations of the Federal Home Loan banks would be provided with respect to both principal and interest.

It is contended by the Home Loan Bank Board that a Government guarantee of obligations of the Home Loan banks is necessary to protect the Home Loan Bank System, in which the Government has a substantial interest. It is said that this guarantee would be further justified both because of the necessity of preventing a financial crisis in the urban mortgage market and because similar assistance has been extended to other segments of our financial economy.

The Treasury has maintained, on the other hand, that a Government guarantee has not heretofore been extended to the bonds of an agency not fully owned by the United States, and that it would appear to be unwise to depart from this policy. Although the Government now owns almost 80 percent of the banks' stock, the Treasury has pointed out that the statute contemplates the ultimate withdrawal of all the Government capital in the banks.

Perhaps a more fundamental question, however, than the rather technical issue of ownership of stock is the highly important matter of the scope and character of the activities of the Home Loan Bank System, for consideration of the extension of a Government guarantee to obligations of the banks must of course be viewed in the light of the nature of the activities of the system.

In the first place, the assumption seems to underlie the proposed legislation that shares in building and loan associations ought to have a degree of liquidity comparable to that of bank deposits, and the proposal to have the Government guarantee the obligations of the banks is one of a series of provisions intended to implement this. We do not believe that this principle should be established. Shares in building and loan associations have generally been understood to be means for the investment of long-term savings, and not liquid instruments. The assets of the associations, consisting almost entirely of mortgages and derivative real estate, are of a character suitable to this concept of their shares and provide no means for furnishing any considerable degree of liquidity. If this concept is to be changed and shares in building and loan associations made liquid instruments, such shares will become for practical purposes indistinguishable from bank deposits; and building and loan associations and banks may be expected to compete actively for all funds now held in banks where the checking privilege is not essential. It would appear, moreover, that liquidity for building and loan associations would be furnished almost entirely at the expense of the Government -- whereas, existing banking institutions supply their own liquidity under all ordinary circumstances and depend upon Government aid only in case of genuine emergency.

Second, the proposed legislation appears to open the way for national banks and other commercial banks to become members of the System. Aside from the fact that this would render even more complex than at present our already overlapping systems of supervision of banks, the expansion of the Home Loan Bank System to include such banks would greatly increase the magnitude of the probable contingent liability of the Government should the guarantee be extended.

Third, the proposed legislation would extend the scope of operations of the Home Loan Bank System by expanding the types of collateral eligible for securing advances from the banks. This liberalization of eligibility requirements applies to the number of families housed per dwelling; the restriction to mortgages on homes, the restriction to collateral specifically itemized in the statute, and the restriction limiting the size of home mortgages. These changes would tend to rob building and loan associations of their character as "local, mutual, thrift and home financing institutions" and would seem to be unwise. In any event, the effect of these proposals in increasing the scope of the Home Loan Bank System makes a Federal guarantee of the obligations of the banks even more questionable.

(1) (b) The Secretary of the Treasury would be authorized, in his discretion, to purchase obligations of the Home Loan banks.

The Treasury has opposed this proposal on the ground that political pressure would tend to force the Treasury to exercise its option against its will, and on the basis that with only one exception, present authorizations to purchase obligations are confined to those possessing a Government guarantee.

The Home Loan Bank Board has contended that the option to purchase debentures may be considered as an alternative to a Government guarantee, and that it would be an advantage to the Treasury to have the option of utilizing either, depending upon circumstances. The Board has also stated that there has been no political pressure to force the Treasury to make purchases in the case of other authorizations to purchase, and that there is no likelihood of such pressure in the case of the Home Loan banks.

Even if the matter of political pressure is ignored, the arguments cited above in connection with the proposed guarantee of the obligations of the banks apply as well to the proposal to authorize the Treasury to purchase such obligations.

(2) The insurance premium rate of the Federal Savings and Loan Insurance Corporation would be reduced from 1/8 of 1 percent to 1/12 of 1 percent per annum.

The Treasury has taken the position that the Federal Savings and Loan Insurance Corporation has not been in business long enough for its operations to give any significant indication of the adequacy of its premium rate, but that *a priori* considerations indicate that the rate should be higher than that charged by the Federal Deposit Insurance Corporation.

The Home Loan Bank Board, however, maintains both that the experience of the Federal Savings and Loan Insurance Corporation justifies a reduction in its premium rate and that the rate should be as low as that of the Federal Deposit Insurance Corporation because, in its opinion, the risk incurred in insuring building and loan associations is less than that in the case of banks.

Analysis of the gross income of the Federal Savings and Loan Insurance Corporation from date of organization through December 31, 1937, indicates that the interest received on the Home Owners' Loan Corporation bonds originally obtained in exchange for the capital stock of the insurance corporation has provided most of the income. Out of the aggregate gross income of $14.1 millions, a total of $10.5 millions consisted of interest received on the above-mentioned Home Owners' Loan Corporation bonds. Only $3.2 millions was received in insurance premiums. This certainly indicates that the subsidy provided the insurance corporation by the Home Owners' Loan Corporation (for the insurance corporation is not now paying dividends on its stock owned by the Home Owners' Loan Corporation) has been by far its largest source of income, and that insurance premiums have provided only a relatively small amount of the accumulated reserve.

The risk involved in insuring building and loan shares would appear to be substantially greater than that involved in insuring bank deposits. Banks are required by law to hold a substantial volume of legal reserves and in addition customarily carry considerable amounts of nonreserve cash and of liquid securities and hold large portfolios of Government securities. The amount of deposits held <u>per contra</u> to these assets is included in the base for the payment of insurance premiums, but entails no risk whatever to the insuring corporation. In addition, the relative volume of uninsured deposits held by banks, which deposits nevertheless form part of the base for the payment of insurance premiums, is much greater than in the case of accounts in building and loan associations.

The proposed legislation would also further reduce the adequacy of the present premium through changes in the method of settlement on insured accounts by the insurance corporation. It is proposed that such settlements shall consist of "at least" instead of "not to exceed", 10 percent in cash, and that debentures shall bear 2 percent interest instead of being noninterest-bearing. The corporation would also be empowered to make settlement in full in cash in its discretion.

3. Federal Savings and Loan Associations would be made exempt from all State and local taxes except real and tangible personal property taxes; and shares of Federal Savings and Loan

Associations would be made exempt, both as to value and income, from State and local taxes (except surtaxes, estate, inheritance and gift taxes).

The Treasury has maintained that such tax exemptions would constitute hidden subsidies and would be undesirable forms of financial assistance, inasmuch as they would escape the scrutiny and safeguards generally present in connection with ordinary expenditures entering into the budget of a political unit; and that the granting of such tax exemptions would give an unfair competitive advantage to Federal associations. In any event, now that the President has announced his intention to attempt to eliminate intergovernmental tax exemptions, the subject proposal would be in conflict with the program of the Administration.

March 5, 1938

My dear Mr. Bell:

Reference is made to your letter of January 29, 1938, with which there was enclosed a copy of a draft of a proposed Bill "to amend the Federal Home Loan Bank Act, the Home Owners' Loan Act of 1933, the Federal Reserve Act, Title IV of the National Housing Act, and for other purposes," and a memorandum containing a summary of its provisions by sections.

The proposed Bill goes far beyond technical or clarifying amendments to the acts referred to in its title, and would fundamentally alter the place in our financial structure of the institutions supervised by the Federal Home Loan Bank Board, change materially the character of the business of these institutions, and extend the probable scope of the supervision of the Board to additional types of financial institutions, as well as open new and wide avenues of tax exemption. Because of the far reaching character of the proposed legislation and because, in my opinion, most of the proposed changes would be unfortunate and would constitute precedents for further changes of similar character, I have thought it best to discuss briefly the broad issues involved before commenting more particularly upon the various sections of the Bill of interest to the Treasury.

First, the assumption seems to underlie the proposed legislation that shares in building and loan associations ought to have a degree of liquidity comparable to that of bank deposits. The proposed Bill consequently provides for substantially supplementing the ability of the Federal Home Loan Banks to make the advances to their members which would be necessary in order to permit them to maintain in times of stress the status of their shares as quasi-demand deposits, and also provides for revising the insurance of the Federal Savings and Loan Insurance Corporation so that shareholders in defaulted building and loan associations may be paid off in cash or in interest-bearing debentures rather than being asked to wait for a substantial period without interest as is the case at present.

I believe that this attempt to provide a liquidity comparable to bank deposits for shares in building and loan associations is unsound, and I am consequently opposed to legislation intended to implement it. Shares in building and loan associations have been generally understood to be means for the investment of long-term savings and not liquid instruments. The assets of the associations, consisting almost entirely of mortgages and derivative real estate, are of a character suitable to this concept of their shares and provide no means for furnishing any considerable degree of liquidity.

If this concept is to be changed and shares in building and loan associations made liquid instruments, such shares will become for practical purposes indistinguishable from bank deposits; and building and loan associations and banks may be expected to compete actively for all funds now held in banks where the checking privilege is not essential. If, in making their adjustment to such a situation, building and loan associations endeavor to maintain liquid assets comparable in extent and character to those customarily maintained by banks, the effect of the tendency strongly evident in the proposed legislation will be to transform them into a competing system of banks - operating, however, under different supervisory authorities and under different fundamental statutes from the existing banking institutions. In the more likely case that building and loan associations fail to build up their proportion of liquid assets, notwithstanding the changed character of their shares, they would still constitute a competing system of banks except that in this case their liquidity would be furnished almost entirely at the expense of the Government - whereas, existing banking institutions supply their own liquidity under all ordinary circumstances and depend upon Government aid only in case of genuine emergency.

Second, the proposed legislation would expand the types of business which Federal savings and loan associations may engage in and would likewise expand the types of collateral eligible for securing advances from Federal Home Loan Banks. These changes pertain to the maximum size of loans which may be made by Federal savings and loan associations and the percentage of the total assets of such associations which may be employed without regard to statutory restrictions limiting loans to "home" mortgages of a stipulated maximum amount and within fifty miles of the home office of the association. The liberalization of eligibility requirements applies to the number of families housed per dwelling; the restriction to mortgages on homes, the restriction to collateral specifically itemized in the statute, and the restriction limiting the size of home mortgages. These changes would tend to rob building and loan associations of their character as "local, mutual, thrift and home-financing institutions" and in my opinion would be unwise.

Third, the proposed Bill removes the present restriction which limits membership in the Federal Home Loan Bank System to building and loan associations, savings banks, and insurance companies, and opens it to all types of home financing institutions which meet certain conditions, the principal one of which is that they secure their funds on a basis which the Board judges to warrant the making of long-term mortgage loans. This provision, if so desired by the Board, would throw membership in the system open to commercial banks; and so raises broad questions with respect to the possibility of conflict between the Federal Home Loan Bank Board and the authorities at present supervising the operations of these banks.

Fourth, the proposed legislation extends sweeping tax exemption privileges to Federal savings and loan associations. These associations are already exempt from all Federal corporation taxation, and dividends on their shares are exempt from the normal income tax of the Federal Government. It is now proposed that they also be exempted from all State and local taxation except real and tangible personal property taxes and that their shares and the income thereon also be exempted from all State and local taxation, (except surtaxes, estate, inheritance and gift taxes). It is also proposed that the wording of the exemption provision be so sweeping as to include within its scope indirect as well as direct taxation.

I am deeply concerned by the increasing demands for tax exemption privileges constantly being urged for various classes of enterprise, and feel that this request for additional tax exemption upon the part of a class of institution already exceptionally favored in this respect ought to call for a reconsideration of our entire policy in granting such exemptions in the past. Tax exemptions are concealed subsidies, particularly undesirable in that their cost is not annually brought to the attention of the appropriating authorities and the public, as is the case with outright subsidies. The proper occasion for a consideration of the granting of exemptions from taxation ought to be in connection with general tax legislation rather than in connection with legislation relating to specific classes of institutions.

Turning to a more detailed statement of my objections to certain provisions of the proposed Bill, Section 1 declares certain findings and outlines a policy, including a statement that there is need to strengthen ".....the existing provisions of:

"(a) The Federal Home Loan Bank Act.....

"(b) The Home Owners' Loan Act of 1933 with respect to the more than 1,300 nationally-chartered local mutual thrift and home-financing institutions as Federal instrumentalities in which the people may safely invest their funds.....

"(c) The National Housing Act with respect to the insurance by a Federal instrumentality of the savings of the people invested in thrift and home-financing institutions....."

It seems unwise to state in a Federal statute that the people "may safely invest their funds" in Federal savings and loan associations. Although these associations are given a Federal charter, there is no guarantee by the Government, implied or otherwise, that investments in them are safe. It is true that the share accounts of all Federal savings and loan associations are insured to a limited extent by the Federal Savings and Loan Insurance Corporation, but even the solvency of this Corporation is not guaranteed by the Government. The same point arises in connection with Section 18 of the proposed Bill which would amend subsection (a) of Section 5 of the Home Owners' Loan Act of 1933, as amended. This particular section authorizes the Federal Home Loan Bank Board to charter Federal savings and loan associations, "In order to provide local mutual thrift institutions in which people may invest their funds....." The proposed amendment would insert the word "safely" before the phrase "invest their funds."

It would also appear to be undesirable to state that there is need to strengthen Federal savings and loan associations "as Federal instrumentalities". As you know, the Government is interested in a construction of the present Act which would leave no room to doubt that Federally-chartered savings and loan associations are under present law "Federal instrumentalities". To make this statement affirmatively at this time might lead to the interpretation that such associations are not now Federal instrumentalities.

Section 2 of the proposed Bill would amend subsection (6) of Section 2 of the Federal Home Loan Bank Act, as amended, to permit the Federal Home Loan Bank Board to broaden the eligibility requirements on real estate collateral for loans of the Federal Home Loan Banks to include mortgages on dwellings housing more than four families. The effect of this provision would be to permit member institutions to obtain loans from the Banks with collateral consisting of mortgages on large-scale housing projects, thus encouraging building and loan associations to make such mortgage loans. This practice would appear to be an unwise extension of the operations of building and loan associations, inasmuch as such loans might represent an undue concentration of assets, and would tend to rob the associations of their character as local mutual thrift and home-financing institutions.

Section 4 of the proposed Bill would amend subsection (a) of Section 4 of the Federal Home Loan Bank Act, as amended, to provide that membership in Home Loan Banks, now open only to building and loan associations, savings and loan associations, cooperative banks, homestead associations, insurance companies and savings banks, is open to other types of institutions engaged in making home mortgage loans if approved by the Federal Home Loan Bank Board. In spite of the fact that certain restrictions are set down with respect to the eligibility of institutions for membership, as, for example, that loanable funds must be obtained on a basis which the Board judges to warrant the making of long-term mortgage loans, it would appear that this liberalization might open the way for national banks and other commercial banks to become members of the system. In my opinion, this would be unfortunate, since our already overlapping systems of supervision of banks (leading to conflicts in policy standards such as those relating to rediscounting) would be rendered even more complex than at present.

Section 7 of the proposed Bill would amend subsection (a) of Section 10 of the Federal Home Loan Bank Act, as amended, to extend the list of eligible collateral for advances of the Federal Home Loan Banks to include obligations of the Banks and of the Federal Savings and Loan Insurance Corporation and other obligations approved by the Board. In addition, all amortized mortgages would be made eligible for advances instead of only "home mortgages" as now provided. Section 8 of the proposed Bill would amend paragraph (3) of subsection (a) of Section 10 of the Federal Home Loan Bank Act, as amended, to make the same liberalization with respect to nonamortized mortgages as Section 7 makes with respect to amortized mortgages. The effect of these changes would be to increase greatly the list of eligible collateral for Bank advances, since mortgages on structures other than homes would be eligible, as well as other obligations approved by the Board. As a result, the Banks might duplicate the existing discount facilities of the Federal Reserve Banks, which would be especially serious if membership in the Federal Home Loan Bank System is open to commercial banks as might be the result of Section 4.

Section 10 of the proposed Bill would amend provision (2) of subsection (b) of Section 10 of the Federal Home Loan Bank Act, as amended, to increase the maximum size of home mortgages eligible for collateral for Bank advances from $20,000 to $30,000 or such greater amount as may be fixed by the Board. This proposal would appear to be subject to the same criticisms cited with respect to Section 2, namely, that an undue concentration of assets might result, and that the associations would tend to be robbed of their character as local mutual thrift and home-financing institutions.

Section 11(b) of the proposed Bill would amend Section 11 of the Federal Home Loan Bank Act, as amended, to provide a Government guarantee, with respect to both principal and interest, of obligations of Federal Home Loan Banks issued with the approval of the Secretary of the Treasury. In my letter to you, dated May 17, 1937, discussing the provisions of a draft of a proposed Bill submitted to you by the Vice-Chairman of the Federal Home Loan Bank Board under date of March 18, 1937, I expressed my opinion ".....that the outstanding contingent debt of the United States should be reduced as rapidly as possible rather than increased .....". Since I see no reason to change my opinion at this time, I feel it necessary to record my disapproval of the present proposal. Furthermore, even though this were not my general position, I should still feel it necessary to oppose this particular guarantee. Although the Federal Government, at the present time, owns almost 80 percent of the Banks' stock, the provisions of section (g) of the Federal Home Loan Bank Act, as amended, contemplate the ultimate withdrawal of all of the Government capital in the Banks. To date, the Federal Government has not guaranteed the bonds of any agency not wholly owned by the United States, and I think it would be unwise to depart from this policy in this case.

Section 11(b) also would authorize the Secretary of the Treasury, in his discretion, to purchase and sell obligations of the Federal Home Loan Banks and of the Federal Savings and Loan Insurance Corporation, such transactions to be treated as public debt transactions. This proposal is not acceptable to this Department. While it is true that the Government has already contributed substantially to the financing of the Banks, it was pointed out in the preceding paragraph that the provisions of the Act contemplate withdrawing the governmental assistance rather than supplementing it.

Section 11(d) of the proposed Bill would amend Section 13 of the Federal Home Loan Bank Act, as amended, in two ways: (1) It would add to the items at present enumerated in Section 13 as being tax exempt (except from surtaxes, estate, inheritance and gift taxes), the stock of Federal Home Loan Banks as to both value and income; and (2) it would add the words "and the burden thereof" after the word "taxation", apparently in an effort to enlarge the present tax exemption so as to include the incidence from indirect taxation. If, in fact, it is intended to enlarge the tax exemption by the use of these new terms, such action would give the Banks a tax advantage over all other Federal instrumentalities. If, on the other hand, the intention is merely to spell out with greater particularization the legal effect of the present exemption, I fear that the long standing construction given to similar tax exemption provisions without the new language might thereby be prejudiced.

Section 17 of the proposed Bill would amend subsection (n) of Section 4 of the Home Owners' Loan Act of 1933, as amended, to authorize the Corporation, subject to the approval of the Secretary of the Treasury, to purchase up to $300 millions of obligations of the Federal Home Loan Banks. This authorization and the present one of $300 millions for either purchases of obligations of the Banks or investments in building and loan associations would constitute a revolving fund. In my letter to you, dated May 17, 1937, referred to above, I said in connection with a proposal to utilize the unused portion of the authorized bond issue of the Home Owners' Loan Corporation for purchase of obligations of the Federal Home Loan Banks, as follows:

> "The Government will fully guarantee the principal and interest of such of the Home Owners' Loan bonds as will be issued, and since I feel that the outstanding contingent debt of the United States should be reduced as rapidly as possible rather than increased, as might be the result of this amendment, I think it would be desirable to refrain from extending the use to which such bonds, and the authorization therefor, may be put. No evidence has been given to show the necessity for additional funds available for the purchase by the Home Owners' Loan Corporation of Federal Home Loan Bank debentures and other obligations, and at least until such time as that action may become necessary, I am opposed to that provision in the Bill."

My opinion at this time remains the same. In addition, I should like to point out that the Home Owners' Loan Corporation was organized as an emergency agency to do one particular job — make mortgage loans to financially distressed home owners — while the Federal Home Loan Banks were set up as permanent agencies to aid in the financing of building and loan associations. It seems quite illogical to me to use the facilities of a temporary agency to aid in financing a permanent agency in this manner.

Section 18 of the proposed Bill would amend subsection (a) of Section 5 of the Home Owners' Loan Act of 1933, as amended, to permit Federal savings and loan associations to be known as "Federal Saving Associations", if the Federal Home Loan Bank Board so determines. In my opinion, the present title aptly describes the type of business which these organizations conduct, while the proposed title might well result in a misunderstanding of the nature of the organizations. The terms "building and loan association" and "savings and loan association" have long served to describe the class of organization to which Federal savings and loan associations clearly belong and the present title therefore conveys to the public the idea of a financial organization making mainly long-term home-mortgage loans, and accepting savings for this purpose. The proposed title, however, would more likely give the impression of an organization like a mutual savings bank. Mutual savings banks, moreover, are fundamentally different from Federal savings and loan associations in the character of their relationship to the investor. The investor in a mutual savings bank is a depositor, and if his claim for withdrawal is denied, the bank is deemed insolvent. The investor in a Federal savings and loan association, on the other hand, is a part owner, and if his claim for withdrawal is denied, he must wait until such time as the association may have sufficient funds to repurchase his shares.

The proposed title is also objectionable because of the possibility of confusion on the part of purchasers of United States Savings Bonds, inasmuch as under existing Treasury regulations, Federal savings and loan associations have been designated to assist in the sale of Savings Bonds. The public may be misled into the belief that Savings Bonds are in some manner identified as obligations of the associations.

Section 19 of the proposed Bill would amend subsection (c) of Section 5 of the Home Owners' Loan Act of 1933, as amended, to increase the maximum size of loans of Federal savings and loan associations from $20,000 to such figure as may be prescribed by the Board, but not less than $30,000. In addition, the percentage of total assets of Federal savings and loan associations which may be employed without regard to limitation (1) on size of loans, (2) a 50 mile lending area, and (3) on loans on improved property other than homes or combination homes and business property, would be raised from 15 percent to such figure between 15 percent and 30 percent as may be determined by the Board. These proposals would appear to be subject to the same criticism cited above in connection with Sections 2 and 10, namely, that an undue concentration of assets might result, and that the associations would tend to be robbed of their character as local mutual thrift and home-financing institutions. Moreover, the objection is even stronger in the case of Federal savings and loan associations, since the Federal Government is more directly concerned in their operation than in the case of other associations which are members of the Federal Home Loan Banks.

This Section would also provide that any portion of the assets of Federal savings and loan associations may be invested "in obligations of, or guaranteed as to principal and interest by, the United States."

The present authority of the associations is to invest "in obligations of the United States." This Department has had occasion to consider the provisions of the present law in a case where an association had invested most of its assets in Home Owners' Loan bonds, guaranteed as to principal and interest, and inferentially, at least, interpreted the words "obligations of the United States" as used in this section (Section 5(c) of the Home Owners' Loan Act of 1933, as amended) to include obligations which were fully guaranteed as to principal and interest by the United States. I understand that the General Counsel for the Federal Home Loan Bank Board rendered an opinion in which the same conclusion was reached.

Section 20 of the proposed Bill would amend subsection (h) of Section 5 of the Home Owners' Loan Act of 1933, as amended, to provide tax exemption for Federal savings and loan associations except from real and tangible personal property taxes levied by any territory, dependency, or possession of the United States, or by any State, county, municipality, or local taxing authority. Present law provides complete exemption only with respect to Federal taxes while State taxes are applicable to Federal associations to the same extent as they are applicable to State-chartered associations. The proposed amendment would also make shares of Federal savings and loan associations exempt both as to value and income from State and local taxes (except surtaxes, estate, inheritance, and gift taxes). The same exemption is already given with respect to Federal taxation. Such tax exemptions would constitute hidden subsidies, and would be, in my opinion, undesirable forms of financial assistance, inasmuch as they would escape the scrutiny and safeguards generally present in connection with ordinary expenditures entering into the budget of a political unit. It would appear to make no difference whether the activity being assisted by a hidden subsidy is worthy or unworthy; the important point is that the assistance to be provided would take place without ever being recorded as an expenditure.

In addition to this general criticism of the proposed tax exemption, this particular proposal is undesirable for two specific reasons. In the first place, the Federal Government would be granting an exemption from taxes levied by <u>State and local governments</u>, and granting the exemption to private institutions and their shares. This would seem to be an unwise extention of the sphere of reciprocal tax exemption which would result in the introduction of new tax conflicts with State and local governments.

In the second place, the granting of the tax exemption proposed would give an unfair competitive advantage to Federal associations. National banks (which are also Federally chartered) and their shares, receive no tax exemption, either as to Federal or State and local taxes; and as a matter of fact, the statute specifies that national banks shall be subject to State and local taxes, but only to the same extent as State-chartered banks. Federal credit unions are exempt from corporation income taxes, but their shares and dividends received thereon are subject to full taxation in the hands of the recipient. If State-chartered building and loan associations and their shares are not now granted exemption from State and local taxation, this proposal would favor Federal associations; and if State-chartered institutions are now given special tax treatment, Federal associations automatically receive the same treatment. In the final analysis, therefore, it seems to me that this proposal would conflict with the intention implied in the legislative history with respect to Federal savings and loan associations, that the competitive situation with respect to State-chartered institutions should not be disturbed.

This section also contains the language to which I have expressed objection contained in Section 11, respecting the exemptions from taxation accorded Federal Home Loan Banks. The same objections apply in this case.

Section 20 would also make shares in Federal savings and loan associations lawful investments for, and acceptable as security for, all fiduciary, trust, and public funds, the investment or deposit of which is under the authority or control of the United States or any officer or officers thereof. Such shares should not be made acceptable investments for any funds with respect to which an important degree of liquidity is desired.

A major anomaly of this provision of the proposed Bill is that it would make shares in Federal savings and loan associations eligible as <u>security</u> for deposits of public funds in national and other banks. (In connection with Section 25, I express my disapproval of the proposal to allow national banks to invest in shares of Federal associations.) Deposits in these banks are roughly analogous to shares in savings and loan associations, except that deposits in commercial banks have the added protection of the stockholders' equity and are much more liquid. The implication of the subject provision that shares in Federal savings and loan associations are safer than deposits in national and other banks, and so may be not only acceptable in their own right without further security for the investment of public funds but should also be eligible as collateral to secure deposits in national and other banks, seems to me to be unsupported by the facts.

Section 24 of the proposed Bill would amend paragraph (b) of Section 14 of the Federal Reserve Act, as amended, to add obligations of the Federal Home Loan Banks (1) to the list of securities having current maturities of not exceeding 6 months which may be bought and sold by the Federal Reserve Banks, and (2) to the list of securities (without regard to maturities) which may be bought and sold by the Federal Reserve Banks but only in the open market. At the present time the only instruments which the Federal Reserve Banks may use for open market operations are Government and Government-guaranteed obligations. My objections to guaranteeing the obligations of the Banks have been stated above in connection with Section 11(b), and if these obligations are not guaranteed it would seem inconsistent to make them eligible for open market operations.

There is an even more fundamental objection to the present proposal, however. The primary function of open market operations of the Federal Reserve Banks is the control of credit conditions. As such, the Federal Reserve Banks are not interested in the particular market conditions of any specific security. The interest of the Federal Home Loan Bank Board, however, in adding obligations of the Federal Home Loan Banks to the list of securities which the Federal Reserve Banks may deal in in their open market operations, is apparently that of strengthening the market position of these obligations.

Section 25 of the proposed Bill would amend the seventh paragraph of Section 5136 of the Revised Statutes, as amended, to liberalize the present restriction prohibiting national banking associations from purchasing stock of corporations, to allow them to invest in shares of Federal savings and loan associations, waiving the restrictions respecting investment securities. In my opinion, this proposal is unsound for two reasons. In the first place, it might result in conflicts between the supervisory authorities of national banks and of Federal associations. Second, it violates the principle of Federal associations that they shall be local mutual cooperative undertakings. The investment of large blocks of funds by national banks in such associations would certainly tend to interfere with the present character of control of these organizations.

Section 26 would amend subsection (b) of Section 401 of the National Housing Act, as amended, to liberalize the term "insured members" to include trusts and fiduciaries holding shares in insured institutions, provided the beneficiaries are disclosed to the institutions. Section 27 would amend subsection (c) of Section 401 of the National Housing Act, as amended, to provide that the term "insured account" should cover any type of investment in an insured institution except nonwithdrawable accounts, up to a maximum of $5,000 for any one person in any one institution, except that the $5,000 limit would not apply to organizations operated primarily for religious, philanthropic, charitable, educational, fraternal, governmental, or similar purposes, or not operated for profit; but the Federal Savings and Loan Insurance Corporation may limit the amount of such accounts an insured institution may accept.

I am opposed to the extension of the insurance granted by the Federal Savings and Loan Insurance Corporation beyond the $5,000 limit in the case of the classes of accounts enumerated. None of these classes of accounts represent primarily savings but consist, for the most part, of accumulations of funds awaiting use in the ordinary affairs of the account holder. This is particularly true of public funds which are among the most volatile class of bank deposits. Accounts of the type singled out for special favor by the subject section are, in fact, quite unsuitable for receipt by a savings and loan association engaged primarily in the making of long-term loans and ought to be discouraged rather than given special encouragement. The difficulty implicit in this situation is magnified because the Federal Deposit Insurance Corporation is authorized to make no such concession with respect to the deposits of these organizations in insured banks. Furthermore, beginning with the Banking Act of 1933, the payment of interest on demand deposits of public bodies has been increasingly restricted by Federal law and regulation, until, beginning August 24, 1937, the payment of interest on such deposits was prohibited with respect to all banks insured by the Federal Deposit Insurance Corporation. In view of these factors, public bodies and other organizations of the type enumerated in Section 27 will be given every encouragement to take their funds out of banks where they properly belong and place them in Federal savings and loan associations where they do not belong.

Section 28 would amend subsection (a) of Section 402 of the National Housing Act, as amended, to change the name of the Federal Savings and Loan Insurance Corporation to Federal Savings Insurance Corporation. Similar objections would apply to this proposal to those I have discussed in connection with the proposal in Section 18 to change the name of Federal savings and loan associations.

Section 29 of the proposed Bill would amend subsection (b) of Section 402 of the National Housing Act, as amended, to provide for repeal of the cumulative feature on dividends of the Federal Savings and Loan Insurance Corporation. Dividends now accumulated but unpaid would be waived and dividends would not be paid in the future until a reserve is accumulated equal to 5 percent of insured accounts and creditor obligations of all insured institutions. The dividend rate would also be changed from the rate being received on the Corporation's Home Owners' Loan Corporation bonds to the rate "paid by the Government on its last issued bonds having a maturity of 10 years or more". Strictly speaking, the Home Owners' Loan Corporation should not be called upon to grant subsidies to the Federal Savings and Loan Insurance Corporation, which is what the waiving of dividends would amount to. As to the dividend rate, I see no reason to make the proposed change, since the rate paid by the Government on its bonds seems to be totally irrelevant in establishing a dividend rate for the Federal Savings and Loan Insurance Corporation. The present arrangement of basing the rate on the interest received on the Home Owners' Loan Corporation bonds held by the Insurance Corporation seems much more logical. In the end this arrangement merely means that the investment of the Home Owners' Loan Corporation in the Insurance Corporation is costless to the former, once the 5 percent reserve has been set up and is currently maintained.

Section 33 of the proposed Bill would amend Section 404 of the National Housing Act, as amended, to provide for a reduction in the insurance premium rate of the Federal Savings and Loan Insurance Corporation from 1/8 of 1 percent to 1/12 of 1 percent, effective as of January 1, 1938. The Federal Savings and Loan Insurance Corporation was organized in 1934, and an analysis of the reserve it has accumulated since organization does not indicate that the present premium rate is excessive. It is true that the Federal Deposit Insurance Corporation levies a premium of 1/12 of 1 percent in connection with its insurance of bank deposits but in my opinion the risk is substantially less than that encountered by the Federal Savings and Loan Insurance Corporation. In the first place, banks are required by law to carry considerably larger reserves than are customarily carried by building and loan associations. Banks in New York City, for example, must carry reserves of 26 percent of demand deposits in the form of a deposit with the Federal Reserve Bank and in addition customarily hold some vault cash and a large portfolio of liquid securities. Building and loan associations, on the other hand, seldom maintain substantial reserves in cash and customarily carry only a small amount of liquid securities. In the second place, the premium base in the case of insured banks is generally higher in relation to the aggregate amount of insurance in force than is the case with building and loan associations. Stated in other words, banks have a relatively greater amount of uninsured funds on which they pay premiums than do building and loan associations. Moreover, if Section 27 is adopted, providing insurance for accounts in excess of $5,000, the amount of uninsured funds upon which building and loan associations pay premiums would be further reduced in comparison with banks.

In the memorandum accompanying the proposed legislation, the Federal Home Loan Bank Board has contended that the Federal Savings and Loan Insurance Corporation has advantages in that its insurance premiums are based on total amounts paid in on shares and deposits plus creditor liabilities, whereas the Federal Deposit Insurance Corporation bases its premium on deposits alone; and that the Federal Savings and Loan Insurance Corporation may levy an additional assessment equivalent to the premium, to cover excess losses, whereas the Federal Deposit Insurance Corporation may not do so. In my opinion, these advantages are not sufficient to offset the disadvantages cited above.

Section 33 would also empower the Insurance Corporation to establish separate reserve funds for different types of insured institutions, each such fund to be free from liability arising out of any other fund, but no restriction being placed with respect to the making up of deficiencies in funds from capital. No evidence has been presented concerning the desirability of setting up such separate funds. Without such evidence, the arguments against the proposal stand out rather strongly. The fact that no fund may be assessed to meet a deficiency in any other fund means that the protection granted by each fund is cut down from that existing under the present system, all other things being equal. The more such funds that are set up, the weaker the insurance protection granted with respect to each fund.

Section 35 of the proposed Bill would amend subsection (b) of Section 405 of the National Housing Act, as amended, to provide that settlement on insured accounts by the Federal Savings and Loan Insurance Corporation shall consist of "at least", instead of "not to exceed", 10 percent in cash, and that debentures shall bear 2 percent interest instead of being noninterest-bearing. The Corporation would also be empowered to pay settlements in full in cash, in its discretion. Investors in building and loan associations receive a relatively high return because of their willingness to invest in institutions making primarily long-term mortgage loans. Consequently, the insurance of building and loan accounts taken the form of insuring their "solvency" rather than their "liquidity". Furthermore, since assets acquired by the Insurance Corporation in the case of insolvency of an insured association are likely to require a considerable time for their liquidation, settlements by the Insurance Corporation take the form of noninterest-bearing debentures except, presumably for convenience, some portion, not to exceed 10 percent, may be paid in cash. The proposal to increase the percentage paid in cash, even to 100 percent in the discretion of the Corporation, and to pay interest on debentures, is in conflict with the character of building and loan association assets.

With the establishment of the Home Loan Bank System, the Federal Government attempted to face, and deal with, the problem of adequate facilities for home financing in the interest of home ownership, and to deal with these problems on a permanent rather than an emergency basis. What has been said here concerning the proposed amendments is not intended to indicate a negative position on the part of the Department toward the original objectives of the system; and the discussion of these amendments serves to raise the underlying problem of a clear definition of those original objectives and of modifications in the system to carry them out.

Very truly yours,

(Signed) Wayne C. Taylor

Acting Secretary of the Treasury

Honorable Daniel W. Bell,

Acting Director of the Budget.

FEDERAL RESERVE BANK
OF NEW YORK

87

OFFICE CORRESPONDENCE

DATE April 21, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE.

FROM L. W. Knoke

I called Cariguel at 10 o'clock this morning. Things were not so good today he said and the franc had been under some pressure, due to rumors that Reynaud, the constant advocate of a lower franc, was at loggerheads with some of the other members of the cabinet and was having his way. The Bank had checked up on these rumors with Government sources but was told that they were without foundation. Nevertheless today's pressure against the franc had cost him about five million dollars after he had gained from the beginning of the present movement a total of two billion francs in gold and foreign exchange. For the time being at least he had the market in hand, Cariguel said.

LWK:KW

REB

GRAY

Paris

Dated April 21, 1938

Rec'd 2:30 p. m.

Secretary of State,

Washington.

RUSH

629, April 21, 5 p. m.

FROM COCHRAN.

French franc began to weaken in late after-bourse trading yesterday evening principally because of fears of strikes in Paris department stores and perhaps in coal mines. While nothing has happened today to warrant such worries over the labor outlook the franc has fluctuated widely. French control is understood to have given considerable amounts of sterling to bring rate down from 160 3/4 which obtained before market opened. At 5:00 p. m. the market was still a buyer of sterling at 159 7/8. Premium on three months sterling moved to 4 today as compared with 2 3/4 yesterday, and was 3 1/2 at closing. The cause for today's pressure on the franc has been gossip, part of which emanated from London to the effect that there was a serious rift in the Daladier Cabinet due to differing

views

REB

2-#269, From Paris,Apr.21,5p.m.

views on the proper rates for the franc. It was reported that Reynaud wanted the franc to move to 175 to the pound while Marchandeau was satisfied with 158 and that Reynaud's views would prevail and that the depreciation would take place over the week-end.

(END SECTION ONE)

WILSON

SMS

SECTION TWO OF TELEGRAM NO. 639 OF APRIL 21, 1938, FROM PARIS

At four thirty this afternoon I saw Rueff at the Ministry of Finance. Rueff told me that there was absolutely no truth in the story that differences on the franc rate had arisen in the Cabinet, that this point had had absolutely no discussion. Rueff said, in answer to my question as to whether any embarrassment was resulting from Marchandeau having as his associates in the Cabinet two former Finance Ministers Bonnet and Reynaud, that neither one of these was making an attempt to take over the duties of Marchandeau and that there had been no official difficulties, irrespective of what views they personally held.

No matter what the actual facts are, it is unfortunate for the new Government that this rumor has spread so much. At the time the new Government came into office, in usually well-informed financial circles there was gossip to the effect that certain very influential business interests had wanted Reynaud - as Finance Minister - and Mandel to be the strong leaders around whom should be build a National Union Government. There was fear that these two men in the Daladier Government might make trouble for this Government and eventually lead to its failure. I am setting this down for your information - it is only financial gossip. In addition, the market has been inclined to interpret the delay in

issuing

issuing new decrees by the Daladier Government as evidence that there is internal dissension.

I was told by Rueff that with regard to flotation of the national defense loan no decision had yet been taken. I understood, and Rueff confirmed this, that for the present the needs of the Treasury are being met by normal receipts, particularly from subscriptions and renewals to Treasury securities. The April 14 statement of the Bank of France showed a further drawing by the State of 580,000,000 francs. This would bring the total under the 20,000,000,000 credit to 18,050,000,000. In Rueff's opinion, no further borrowing by the State would appear on the statement for the period ended today.

As a result of the above factors the tendency on the Paris market today was to buy those French rentes which provide option of foreign exchange but also to invest in international securities such as the Suez.

END MESSAGE.

WILSON.

EA:LWW

REB

PLAIN

London

Dated April 21, 1938

Rec'd 2:35 p. m.

Secretary of State,

Washington.

RUSH

330, April 21, 7 p. m.

FOR TREASURY FROM BUTTERWORTH.

One. Phillips telephoned this afternoon to ask whether I had any information to supplement the newspaper reports on recent financial and monetary developments in Washington. He made his inquiry in such a way as to give the impression that he felt something should be forthcoming. I explained that I had received no such information but that doubtless some would be forthcoming.

Two. Sentiment regarding the franc changed abruptly today due to reports of divergency of views within the French Cabinet; in particular Reynaud is said to be insisting on a further depreciation of the franc to about 175 to the pound. The fact that the two issues of rentes having sterling guarantees improved by about 5% is noteworthy. The French control operated consistently and most dealings

were

REB

2-#330, From London, Apr. 21, 7 p.m.

were done around 159. The French fund is believed to have lost about 4,000,000 pounds.

KENNEDY

SMS

ADDRESS OFFICIAL COMMUNICATIONS TO
THE SECRETARY OF STATE
WASHINGTON, D. C.

DEPARTMENT OF STATE
WASHINGTON

April 21, 1938.

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury, and encloses for his information one copy of telegram No. 164 of April 20, 1938, to the American Embassy, London.

IS ANSWER NECESSARY:
ANSWERED BY:
Distribute to:
Secretary
Mr. Taylor
Mr. Haas
Mr. Harrison

RECEIVED
3:50 P. M.
APR 21 1938
TREASURY DEPARTMENT
Office of the Secretary
Technical Assistant to the Secretary.

REB

TELEGRAM SENT

GRAY

April 20, 1938.

7 p. m.

AMEMBASSY

LONDON (ENGLAND)

164

For the Ambassador. Reference your 298, April 11, 7 p. m., from Butterworth for the Treasury.

The United States has not been represented on the International Relief Bonds Committee inasmuch as the power of disposal of war and relief debts to the United States is in the United States Congress and the debt settlements are regulated by law. In these circumstances, the United States could not usefully participate in the acts of an international creditors' committee.

The United States has already formally notified the German Government that it will look to the German Government for the discharge of the Austrian Relief Debt obligations.

The Austrian Relief Debts are secured by a first lien on the assets and revenues of Austria subject only to the prior lien of the Czechoslovak Conversion Loan associated

with

REB

2-#164, To London, Apr.20,7p.m.

with the now redeemed Austrian guaranteed loan of 1923 and to the lien of the Austrian loan of 1930, and therefore enjoy a clear priority over the two Austrian guaranteed loans, parts of which are guaranteed by the British Government and by several other governments represented on the International Relief Bonds Committee. It would be impossible for the United States Government to submit to the Congress with any prospect of obtaining its approval, any proposal to subordinate the priority enjoyed by the Relief Debt to any loan enjoying an inferior lien on the same Austrian securities.

In these circumstances and as an American observer could not be authorized to participate in the discussions of the International Relief Bonds Committee, it would appear to be of doubtful wisdom for the United States to permit an observer to attend the meeting and thereby make it of record, in connection with any decisions taken by the committee, that the United States was represented by an observer at the meeting.

Please telegraph any comment you may wish to submit on the foregoing.

WELLES
ACTING

EA:FL:EB

GROUP MEETING

April 21, 1938.
9:30 a.m.

Present: Mr. Magill
Mr. Taylor
Mr. Oliphant
Mrs Klotz
Mr. Gaston
Mr. Haas
Mr. Upham
Mr. Lochhead
Mr. McReynolds

H.M.Jr: Good morning, everybody.

Mr. McReynolds?

McR: I talked to Peoples on the telephone this morning. Couldn't reach him yesterday. Never reach Mr. Peoples. But he called this morning, said he was still unable to come in. He was also unable to talk very well.

H.M.Jr: You got an answer? Let me ask you a question which you're going to answer perfectly honestly. Would you be embarrassed to go up there and call on him?

McR: No.

H.M.Jr: And simply say that I am tremendously shocked over this whole thing and that when he is normal again I'd like to ask him what he thinks should be done under the circumstances, seeing that this has been going on now for about two years. I expect him to make the move.

McR: All right, I'll go see him.

H.M.Jr: I mean that I expect him to come in and tell me what he expects to do; that this has been going on now for about two years and it started by his insulting Mrs. Morgenthau and myself by being drunk at my house and that this has been going on now for about two years, and I expect him to come in and make a recommendation what he thinks should be done. See? Mac?

McR: Yes, sir.

H.M.Jr: Is that a fair request?

McR: It's fair.

H.M.Jr: What?

McR: It's fair.

H.M.Jr: I expect him to come in and tell me as a man under these circumstances what he thinks should be done. See? And put it right squarely up to him. What?

McR: All right.

H.M.Jr: Now, if you don't think that's entirely fair.... What?

McR: Oh, I do.

H.M.Jr: Does anybody think that isn't fair, anybody familiar with the circumstances?

Gaston: I think that's wholly fair.

H.M.Jr: What?

Gaston: I think that's entirely fair.

H.M.Jr: I'm putting it up to him - what he thinks he should do under the circumstances. See, I asked him to be back Monday morning.

(On phone) Hello - Thank you. - Hello. - Good morning, Marriner. I got your message from Wayne Taylor and I understood that you'd want to see me some time after one o'clock, and I was making up my schedule and I wanted to do it at a time that was mutually convenient. - Yes. - Uh-huh. - Well, I have - it so happens I have lunch company, so would 2:30 be agreeable to you? - -

(Continuing) Well, here's the way I'm handling the press. I decided to handle it differently. I'm having my regular press conference at 10:30 and I'm then telling the boys that, following a precedent which we have set before, we will have no announcement on the bill situation until five o'clock. See? Because I thought it might frighten people if I postponed my press conference, a thing which I don't think I've ever done before. And why high-light it in that manner? So I'll go through my regular press conference and simply say that at five o'clock the Treasury would announce what their bill program would be for Monday. How's that? In other words, I don't want to attract any more attention to it than is necessary, and do it in as normal a manner as possible. - Yes. - All right. And in any event I'll keep 2:30 open. How's that? - Thank you.

(Further portion of conversation not taken in full, on assumption it was being recorded; portion of further conversation, with loud-speaker turned on, follows:)

Eccles: Duffield said that he would tell you that he had no information of any kind in person from any of the Board, and I merely wanted to clear your mind so the - I haven't the slightest idea where he did get it. I wanted Duffield personally to tell you just that.

H.M.Jr: Well, he hasn't had any opportunity.

Eccles: He said he'd be very glad to do it.

H.M.Jr: Well, I'll talk it over with Gaston.

\- - -

Thank you.

(End of Eccles conversation)

Gaston: Now, the message that Duffield gave to me was that Mr. Eccles had asked him to say to you that he, Eccles, had not talked to Duffield on that subject, and Duffield said that he was very glad to do that. He didn't know why Mr. Eccles should want him to do it, but he was very glad to do it, and it was true: he had not talked to Mr. Eccles on that subject.

H.M.Jr: That was the message you (Taylor) gave me - or have you got one from Duffield too?

Taylor: Mine was the same as....

H.M.Jr: What Eccles said was that neither he or Thurston or any member of the Board ....

Gaston: Duffield did not tell me that. He spoke about Eccles only.

H.M.Jr: Well, I'm just an innocent babe in the woods. I don't know my way around town.

Klotz: Have a cigarette?

H.M.Jr: Sure, it's a good idea. Can you hold it there? Just hold it.

Taylor: Just learning how to smoke.

H.M.Jr: Yes. And I'll have my milk out of the bottle at lunch. Might spill it. It's all right.

McR: Referring once more to Peoples ...

H.M.Jr: Pardon me?

McR: ... I think I better see Peoples later in the day.

H.M.Jr: I'd do it on your way home. Wouldn't do me any good to talk to him now, because if I talked to him now he wouldn't remember tomorrow.

Klotz: Excuse me!

McR: That's true. He was just mumbling. Couldn't talk plainly.

H.M.Jr: Well, Mac, I've thought this thing over a lot. It would upset me terribly to have to call me in an Admiral of the United States Navy and give him a dressing down. I think he's man enough that if I put it up to him on the basis of what does he think should be done under the circumstances .... Gave him the message that he should be back here Monday morning and take care of this cement situation, and today is Thursday. This thing is going on for two years. I'm going to put it up to him squarely to discipline himself.

McR: I'll be delighted to talk to him, but I merely wanted to make sure - that is, I'm satisfied - it hasn't been

15 minutes since I talked to him ...

H.M.Jr: That's all right. You pick the time. He says you're my chief of staff. Not my staff of life. O.K., Mac?

McR: All right.

H.M.Jr: If Mr. Peoples would change his staff of life to a solid food, he'd be a lot better off.

Klotz: He can't.

H.M.Jr: Well, then, he can't be in charge of buying 500 million dollars worth of supplies. At least I'm going to try it the Boy Scout way. If it doesn't work the Boy Scout way, I'll have to give it the other method. But I'm going to try the Boy Scout method once.

What else, Mac? Are you ready to report on the cement thing?

McR: No. But the Army and Navy are both getting the information that we need for definite bids.

H.M.Jr: Well, if you're not ready, let's just move on.

McR: We're not ready, but I have had a report twice a day.

Oliphant: Aren't the analyses of the bids over yet?

McR: No, they haven't ....

H.M.Jr: I guess I left it at the house - this report that came from Upham on Mr. Griswold, Investment Bankers. Now on that my horse sense says - the hint, would we want to pay the $900 and costs to get this thing ....

Upham: Oh, that was, as I indicated, fairly facetious. They're willing to pay it.

H.M.Jr: They should send it out as their own report and not indicate the Treasury asked them to do this. I wish you'd take the report and reduce it to one page. Any report like that can be reduced to one page. Will you, for me, and send it up to the house?

Upham: Surely. I'll get it back.

H.M.Jr: Mrs. Klotz will get it for you.

Upham: We thought it should go to this subcommittee.

H.M.Jr: Well, you fellows take care of it, see? But put it down into one page.

Now - Comptroller? F.D.I.C.?

Upham: Well, of course, they have a number of applications out around there for branches of the Bank of America?

H.M.Jr: Which, now?

Upham: Comptroller. And they're about to the point of either granting or refusing one of them. Now, if you want to leave that to the Acting Comptroller - or do you want to play any part in determining whether ....

H.M.Jr: I would appreciate it if the Acting Comptroller, after he has carefully weighted it, would come in and tell me what he's thinking of doing. See?

Upham: All right.

H.M.Jr: What he's thinking of doing. I'd like to know what he's considering.

Upham: Well, he's considering granting one particular application.

H.M.Jr: Well, I'd like to have him come in.

Upham: When he gets ready.

H.M.Jr: When he's ready, when he's made up his own mind. Not "What do you think?" but when he's made up his own mind, to sit down with Taylor, you, and myself, and let's listen to him. Check, Wayne?

Taylor: (Nods yes)

H.M.Jr: But let him first make up his own mind.

McR: I think that's a good precedent to start with him first.

H.M.Jr: Let him make up his own mind. Let him come in.

Upham: I think that's the only thing, except Mr. Crowley is coming this morning.

H.M.Jr: At 11.

Upham: He'll tell you this. He'd prefer to tell you himself.

H.M.Jr: Well, is he going to tell me about ...

Upham: He's going to bring a letter to you.

H.M.Jr: About this bank?

Upham: And tell you about two things that they have done. No, he won't mention that.

H.M.Jr: When are you and Smythe going to have a recommendation for me as to how the United States Government and its agencies should handle bonds, Government bonds?

Upham: Well, I thought I'd put that in this other memorandum.

H.M.Jr: What other memorandum?

Upham: On bank examination.

H.M.Jr: Oh. On account of the way Governments are acting, I wish you'd give that ....

Upham: All right, we can do that at once.

H.M.Jr: Give that precedence.

Upham: Surely.

H.M.Jr: I wish you'd give that precedence. When you've got that, Mr. Taylor .... Anything else?

Upham: (Nods nothing)

Lochhead: The French franc has dropped this morning from \$.0315 yesterday down to \$.0310. No particular news, of course. The Bank of France - they're borrowing, but I think that's based ....

H.M.Jr: When is Bastille Day? May 14?

Taylor: July 14.

H.M.Jr: July 14. When's May 1? Another week to run yet. All right.

Lochhead: The other ...

H.M.Jr: How's gold?

Lochhead: Gold works out about \$34.81.

H.M.Jr: Pardon me?

Lochhead: \$34.81.

H.M.Jr: (To Mrs Klotz) See, I did speak about an analysis of silver comment. Mr. Taylor mentioned it.

Lochhead: Silver is unchanged in London this morning.

Taylor: (Nods nothing)

Haas: (Hands black book to Secretary) There's one in there that goes ....

H.M.Jr: The right way? Which?

Haas: The first one.

H.M.Jr: United States Steel is on a 42 percent capacity - up. Well, they're going opposite from the rest of industry.

Taylor: Harry Hopkins made a remark last night on that subject at the "little Cabinet" - that inventories at the present time were 28 billion dollars, as compared to 20-odd in 1929. Where would he get that figure?

Haas: The Department of Commerce has an inventory index in which they combine stocks of various materials and so on. I've examined it and found it not to be at all satisfactory in an understanding of the business situation. A more recent study has been made by Dun & Bradstreet ...

H.M.Jr: ... which doesn't check at all. I read that very carefully.

Haas: Yes. Now, where he got that I don't know.

H.M.Jr: And they checked how many concerns?

Haas: 17,000 were actually used in that compilation.

H.M.Jr: And that was December 31; the inventory situation was approximately the same - 47 days, wasn't it?

Haas: That's right.

H.M.Jr: I read that.

Haas: Remarkable how that ....

Oliphant: About the same as '29?

H.M.Jr: No, about the same as '36.

Haas: And '35.

H.M.Jr: And '35. In other words, the people had goods on hand to run them about 47 days.

Haas: I think that's really remarkable when you consider all the talk of inflation and how people were piling up, and so on.

H.M.Jr: Yes, I was surprised.

Get me Jimmy Roosevelt's speech from the Columbus papers, will you (Gaston), please? I don't want to ask the White House for it.

Gaston: Yes. Yes.

H.M.Jr: Also if there was a release on the Farley speech - Farley evidently said something on spending. And also Wallace's speech at Omaha, where he talks about deficits.

All three - will you? And high-light the part where they talk about spending and balance. Any other member of the Administration that you see makes talks on spending - let's have it.

But they all seem to have the same thing. The New York Times answers them. Gives for the last five years what we have spent first nine months of every year, and we have spent increasingly more each year. But there's Wallace that talked on it, Jimmy's talk, and James Farley's talked on it.

Gaston: Yes.

H.M.Jr: Just as a matter of interest, Norman Davis was in here today and - this is all in the room - and he said that when they left - he and Hull and Sumner Welles - as of Friday night, there was no such rumor in the air. It was all fixed. The speech was written largely by them, plus Berle - had nothing in it as of Friday night, but that it was the House action which changed it. But he said when Mr. Hull, Sumner Welles, Berle, and he went to bed Friday night, or rather Thursday night or Friday noon or - there was nothing ... That's what Welles meant when he phoned me. He said, "We're worried. We want you up here. But it can wait until Monday morning. It can wait until Monday morning." But they didn't know the House was going to do that. So I think gradually I'll get the pieces, put them together.

Taylor: Well, that checks absolutely with what we picked up.

H.M.Jr: And on the Potomac Sunday afternoon the thing was settled.

Oliphant: Did you see that draft?

H.M.Jr: Pardon me?

Oliphant: Did you see that draft?

H.M.Jr: Of Hull's? No, did you?

Oliphant: Oh, I heard about one paragraph of it, the first paragraph - all reforms to be abandoned at once.

H.M.Jr: No, I didn't see that.

Oliphant: That was Berle.

Haas: That's all.

H.M.Jr: What reform?

Oliphant: All reforms.

H.M.Jr: Well, what reforms?

Oliphant: I don't know. Wages and hours, I suppose.

H.M.Jr: I said to Norman Davis - I said, "I thought you might be interested in the way I feel. This isn't a question between liberals and non-liberals. That isn't the way the camp is divided. The camp is divided as between spenders and non-spenders. And I won't take second place, in my administration of the Treasury, as to being a liberal, to anybody in Washington." And I said, "I'm still waiting for the Department of Justice to open their first gun against monopoly. I don't know whether the little hair I've got left will be on top of my head when they do start, but I'm still waiting for the first gun. But it isn't a question of left-wingers and right-wingers, it's just a question of spenders and non-spenders. That's not reform."

I like the President's Pittsburgh speech - I'm going to have it put up there (on wall) - that "more liberal governments have been wrecked on the rocks of loose fiscal policy than anything else." And I'd just as leave stick on that - that more liberal governments have been wrecked on loose fiscal policies. Get that exact quotation for me, Herbert, will you?

Gaston: That's the 1932 Pittsburgh speech.

H.M.Jr: Yes.

Klotz: He may like to see it.

H.M.Jr: What? Oh, he knows about it.

Klotz: It's a long time ago.

Haas: I'm driving on that Number One project.

H.M.Jr: O.K.

Herbert?

Gaston: Nothing of importance. Bell, who is ill today, sent down to Mac a telegram from Bundy of the Yale News, asking if he couldn't prevail on Secretary Morgenthau to designate a representative of the Treasury to discuss depression policy at the Yale-Harvard-Princeton conference. Of course the answer is "No."

H.M.Jr: Tell - I want to - Bob's going to be there. I want Bell to take him around and introduce him to some of the people. He's coming around - Bob's coming down to get interviews for his paper.

McR: Dan's sick in bed.

H.M.Jr: Well, if he goes. Is anybody else going?

Oliphant: You asked me, remember. We referred that to White. I assumed White was going on the monetary thing.

H.M.Jr: Well, between Bell and White I want to introduce Bob. Bob won't come to Washington; he doesn't want the boys to say his papa helped him, so he won't come to Washington.

Gaston: Well, I'll just reply to Bundy and say we can't designate anybody.

H.M.Jr: Bob's having a terrible time. He's Number One out of 60 boys, and it's his standing on the paper right now - I mean the last time they posted he was Number One.

Gaston: Mrs. Forbush has a little summary on some letters about the President's speech. She's working - I spoke to her about the other thing.

Klotz: (Words too low to be understood)

H.M.Jr: No, I tried to press a little hard on Mr. Gaston on some of this - a little play - that Mr. Taylor asked Gaston, "What about all this?" and Gaston didn't seem to know, and Taylor said, "Well, you write the letters."

And no one seemed to know except Taylor that all the people are complaining about my silver policy with regard to Mexico.

Klotz: Well then, do I forget about it?

Gaston: She's going to send a - she said she'd send a report down to me.

H.M.Jr: The point is, if you talked with her it isn't necessary for Mrs. Klotz to talk to her. Between you and Mrs. Forbush, I'd like from now on to get a digest once a week of what my mail is.

Gaston: Regular weekly.

H.M.Jr: Including the Baby Bonds. Once a week I'd like to have it, say, as of Monday.

Gaston: Yes, yes.

H.M.Jr: And that might be circulated to the staff here. I think it would be good. And I'll leave that to you and Mrs. Forbush. See?

Gaston: Yes. That will be two digests, one from Bryan and one from Mrs. Forbush.

H.M.Jr: Letters received on President's radio address - seven favorable, five unfavorable; eight letters mention his speech without comment. Favorable nine, unfavorable seven.

Well, I think we ought to know - so between you and Mrs. Forbush.

Gaston: Yes.

H.M.Jr: Anything else, Herbert?

Gaston: No, that's all.

Did you want anything more done on that memorandum about this man?

H.M.Jr: I think that's enough. I don't want it.

Gaston: I can get quite a lot more. For instance, I asked to get his income tax returns for the last four or five years.

H.M.Jr: Get some more.

Gaston: I'll give you another memorandum.

H.M.Jr: Before I - excuse me, is that all?

Gaston: Yes.

H.M.Jr: You two people (Oliphant and someone else) have both spoken to me about this vacancy to be vacant on May 1. I know about it, and I'm going to ask you to be a little patient with me. Because you don't know, who haven't sat in, what we went through yesterday; we're not through it yet today. We have had, not a big battle, but quite an exciting time over the question, should we let a hundred million dollars worth of bills run off or should we renew them, and so forth and so on.

And the whole Federal Reserve crowd - so you will just have the background - took the position we should continue to borrow a hundred million dollars worth a week, notwithstanding the fact that our balance - working balance is about two billion three. Their difficulty is, they have sold down to - they have now got left about 700 million dollars worth of bonds. They want to keep an orderly market, and in order to do that they feel they have to sell bonds, and when they sell bonds they have to replace them with bills. Well, out of a billion 800 million dollars worth of bills outstanding, they already own over 700 million, so there isn't enough ammunition to go around, and they find themselves in the very difficult situation that, by golly, they may have to buy some notes.

And the question was, what did the President want? I mean if we kept on borrowing, why, we would have - a little over 300 million dollars would have been used through deficits between now and the 10th of June. Was that quick enough, or did he want us to let some of the bills run off? I had a long talk with him yesterday morning, and I recommended to him we let

50 million run off a week, and that would put about a hundred million dollars worth of gold to work. But was that what he wanted? And I very carefully pointed out to him, as well as I could, both our sides of the argument, and let him read Duffield's story, which was very intelligently written - Times and Tribune and all the rest - and after having a half hour discussion we decided that we would let 50 million a week run off.

But I told him - I said, "I don't just know how I can defend spending taxpayers' money, even though it is infinitesimal, to borrow one and a half times as much money as I need. And I don't need the money until the fall. And, being 90-day money, I have to go to the market twice between now and the fall - not once, but twice."

Well, the Fed is very much excited about it, particularly Eccles, because they find themselves in the position - they've got two alternatives: either to continue to sell their Governments in order to hold the market down, and then replace them; if they can't replace them, to let their portfolio run off. And I've transferred the responsibility from the Treasury to them. And if they let the portfolio run off, they nullify by that amount what we're trying to do here. And of course the thing that they didn't like was that I remarked several times very quietly that the great trouble was that all of that stuff hadn't been thought of before these people - while these people had been advocating what they had for the last two months, and that the time to think about those difficulties was during the past two months.

So I told them that we were not asking their advice this time for the first time, that this was the policy, but we did want to know what they were going to do. And they're to let us know around the middle of the day what they're going to do and we're holding announcement of our bill program until five o'clock this afternoon. But I just wanted to let you know that it's a very important, very difficult problem, and until I get that off my chest I think the other thing will just have to take its time. But I didn't want you to think I wasn't aware of it; but there's one person involved, and this other thing is a question of the spirit in which the President's message is carried out, and there's a very definite difference between the Federal Reserve and ourselves which I hope will be ironed out today. But I just wanted to let you know what had been going on and I just hadn't been not doing anything.

Mr. Oliphant?

Oliphant: I'll need about ten minutes with you to clear some things.

H.M.Jr: Well, we'll get around to it. It will be after Eccles leaves. He's coming at 2:30, so it will be some time after three. Did you (Klotz) put down Eccles? You have it. And then just write "To follow Eccles will come Oliphant." Some time around three o'clock, depending on how much gas Mr. Eccles has, you'll follow. All right?

Oliphant: Fine.

Magill: A good deal of likelihood that the tax bill deadlock will crack tomorrow.

H.M.Jr: Consolidated Edison is over with a bang. It's a success.

Oliphant: 60 million, wasn't it?

Lochhead: 60 million.

Magill: I said I think there's a good deal of likelihood that the tax bill deadlock will break tomorrow, and as it looks at present the chances are the House will get 20-16. Beyond that I don't think you can tell very much.

H.M.Jr: Well, you think about that thing that I told you about. I'll get a chance to talk to you about it.

Magill: I'd like to talk to you about it if I can.

H.M.Jr: Well, I'll tell you now. Well, I'll put it this way. Crowley comes in at 11, and when he leaves I'll phone you. How's that?

Magill: Fine.

H.M.Jr: I just want to say to you people - I said this to Taylor this morning - that after this thing - because I've been thoroughly satisfied that what I advised the President and what we decided yesterday was the right thing to do, to let 50 million a week run off. I just can't see how I can explain continuing to borrow with a working balance of two billion three. Now, the fact that it's embarrassing to the Federal Reserve is just too bad. But if they owned more bonds or less bills, they wouldn't be so embarrassed. But I just can't help it. I mean we're faced with a situation and I'm satisfied - and I'm very much interested that Professor Williams saw Archie in the hall and said, "Well, there's nothing else that the Secretary could do."

But I just want to let you know that it's fairly tense, and so forth and so on.

All right.

Prepared by: Lawrence H. Seltzer,
Assistant Director of
Research and Statistics;

Assisted by: Sidney G. Tickton, and
Gertrude N. Stanley.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 21, 1938

TO Secretary Morgenthau

FROM Mr. Haas

Subject: Comparative yields on United States and British Treasury obligations

I. U. S. yields below those of U. K. at present time

The market yields of United States Treasury bills, and short- and long-term bonds are significantly lower at this time than the yields of similar British obligations of comparable maturities.

The comparative yields on the latest dates for which the data for both countries are available are shown below*:

Date	Security	Market yield U. S.	Market yield U. K.	Excess of yield on U.K. over U.S.
4/6/38**	3-months' bills	.14	.51	.37
4/6/38	U.S.Tr.3-3/8's of 40-43 U.K.Tr.4½'s of 40-44	.75	2.33	1.58
4/6/38	U.S.Tr.4's of 44-54 U.K.Tr.5's of 44-64	2.07	2.68	.61
4/6/38	U.S.Tr.2-3/4's of 48-51 U.K.Tr.3's of 48-53	2.51	2.83	.32
4/6/38	U.S.Tr.2-3/4's of 56-59 U.K.Tr.2½'s of 56-61	2.70	3.15	.45

* For issues of comparable maturity.
** The British bills were dated April 1, 1938.

The most striking spreads exist in the cases of the very short-term obligations. The rate on British Treasury bills, which is some four times the American rate, is believed in some quarters to be the result of an unofficial understanding between the joint stock banks and the British Treasury whereunder the rate is maintained at a level profitable to the banks.

The spread of 1.58 percent between the British 4½'s and the American 3-3/8's, both callable in 1940, and maturing in 1944 and 1943, respectively, can apparently be attributed only to the higher rate structure for short-term money in England than in the United States. Business conditions in Great Britain, despite the recent decline, have held at a relatively high level, and English banks have enjoyed a substantial demand for commercial credit. Further, short-term rates in England are not subject to the special pressure exerted in this country by the possession of large excess reserves by commercial banks.

The two pairs of longer-term issues show the smallest spreads, indicating that the rate structures of the two markets are most nearly akin in this sector.

Part of the spread between the British and American bonds may be conceivably attributed to the fact that the American securities enjoy tax-exemption privileges -- freedom from normal income taxes — which are not possessed by the comparable British obligations. It is our opinion, however, that this factor is not of great practical importance in the present connection.

II. Changes in Spread in Recent Years

On the accompanying chart, the spreads between the yields of the United States and British Treasury bonds are presented at monthly intervals -- for the period beginning with 1933 in the case of four of the bonds, and for that beginning with 1936 for the other four bonds (in the case of the latter issues, comparable pairs did not exist between 1933 and 1936).

For the two pairs of bonds charted from 1933 to 1938, the yields on the United States bonds were in excess of those on the comparable British obligations during most of 1933 and 1934. This condition was reversed during 1935 for the shortest-term bonds and during 1936 for the other pair. The sharply widening spread between the yields of the shortest-term United States and British issues since the spring of 1937 reflects the great difference between the two countries in short-term money rates.

The relatively stable spread of approximately one-half of one percent in the case of the long-term bonds since the middle of 1937 suggests the closer similarity of the interest rate structures of the two countries in the long-term sector -- the American rates, however, being lower than those of the British.

III. Comparative Bill Rates

The accompanying table presents a comparison of the rates on 3-months' Treasury bills in the United States and Great Britain from 1933 to date. This table shows the rate on the first United States Treasury bill issue of 91 days, or of approximately comparable term, offered each month and the rate on the comparable 3-months' British bill issue. In months when the United States did not offer bills of less than 133-day term, no data for either country are shown. Because of the long gaps between periods during which the United States did offer such bills, we have not prepared a chart comparing the rates on the American and British bills.

It is noted that, with the exception of the periods immediately preceding and following the Bank Holiday, the rates on United States Treasury bills have been very substantially lower than the rates on British Treasury bills.

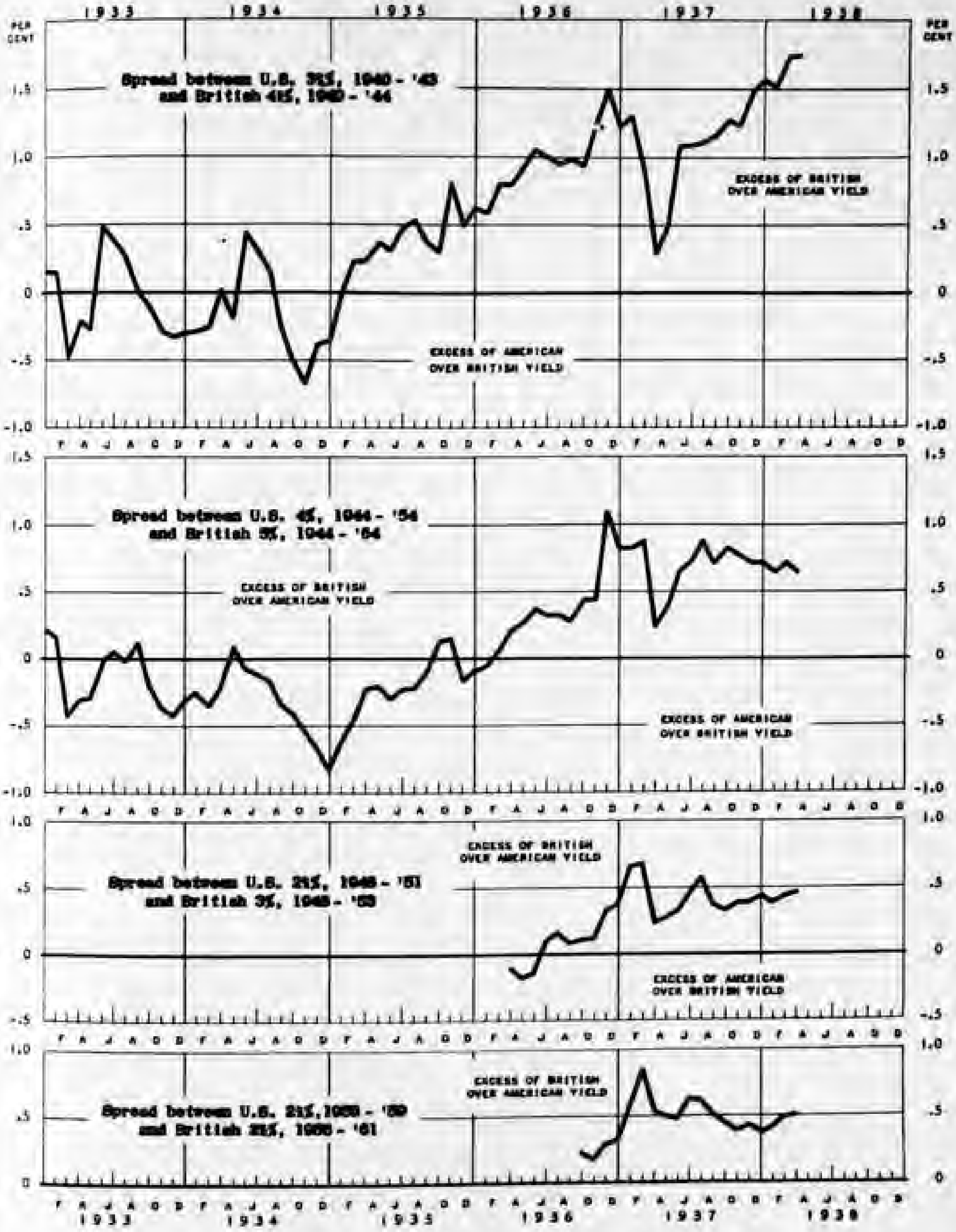
Attachments

Comparison of Rates on 3-Month* Treasury Bills
in the United States and Great Britain, 1933-1938

United States			Great Britain		
Date	Term	Rate	Date	Term	Rate
1938					
Apr. 6	91	.14	Apr. 1	3-mo.	.51
Mar. 2	91	.09	Mar. 4	"	.50
Feb. 2	91	.08	Feb. 4	"	.50
Jan. 5	91	.07	Jan. 7	"	.52
1937					
Dec. 22	91	.10	Dec. 24	"	.60
Nov. 24	114	.12	Nov. 26	"	.75
Sept. 8	104	.48	Sept. 10	"	.51
Aug. 25	117	.33	Aug. 27	"	.51
June 2	108	.38	June 4	"	.70
May 26	115	.43	May 28	"	.53
Apr. 7	72	.51	Apr. 9	"	.54
Mar. 17	92	.17	Mar. 19	"	.50
Jan. 6	71	.20	Jan. 7	"	.52
1936					
Dec. 16	91	.04	Dec. 18	"	.91
1935					
Nov. 27	110	.06	Nov. 29	"	.59
July 3	133	.07	July 5	"	.62
June 5	133	.11	June 7	"	.56
May 22	133	.09	May 24	"	.52
1934					
May 2	91	.07	May 4	"	.86
Apr. 4	90	.08	Apr. 6	"	.89
Mar. 21	91	.09	Mar. 23	"	.70
Feb. 7	91	.66	Feb. 9	"	.87
Jan. 3	91	.62	Jan. 5	"	.95
1933					
Dec. 6	91	.60	Dec. 8	"	1.03
Nov. 1	91	.22	Nov. 3	"	.88
Oct. 4	91	.10	Oct. 6	"	.64
Sept. 6	91	.12	Sept. 8	"	.33
Aug. 2	91	.35	Aug. 4	"	.27
July 5	91	.28	July 7	"	.52
June 7	91	.27	June 9	"	.35
May 3	91	.49	May 5	"	.43
Apr. 5	91	1.35	Apr. 7	"	.55
Mar. 1	91	.99	Mar. 3	"	.57
Feb. 8	91	.18	Feb. 10	"	.84
Jan. 11	91	.20	Jan. 13	"	.80

* This table shows the rate on the first United States Treasury bill issue of 91 days, or of approximately comparable term, offered each month, and the rate on the comparable 3-months' British Treasury bill issue. In months when the United States did not offer bills of less than 133-day term, no data for either country are shown.

SPREAD BETWEEN MARKET YIELDS ON U.S. AND BRITISH BONDS OF COMPARABLE MATURITIES 1933 - 1938



NOTE: YIELDS AS OF THE FIRST WEDNESDAY OF EACH MONTH

Office of the Secretary of the Treasury
Division of Research and Statistics

FD - 113

April 21, 1938

11 a. m.

Present:

Mr. Leo T. Crowley
Mr. Taylor
Mr. Upham

Mr. Crowley: I have been looking for you for a long time and when you were here I was away, but I would like to have you read that, if you will just take a moment. (See attached letter from Mr. Crowley to HM,Jr, dated April 12, 1938.)

HM,Jr: You did not sign this. Did you mean not to?

Mr. Crowley: I will sign it for you.

HM,Jr: (Reading letter) Well, my first reaction is this: in view of the fact that the President in his radio speech, last Thursday, said that we should attempt to -- I don't know the exact wording -- to have a uniform bank examination on the part of the United States Government, I think it would be a great mistake for FDIC to get out anything new and as novel as that, without first consulting with the Comptroller's Office and with the Federal Reserve to try to make it, if possible, uniform.

Mr. Crowley: We don't disagree with you on that at all.

HM,Jr: It seems to me, if you get this thing out, in view of the fact that the President's speech is only one week old and that he more or less laid down this policy and then suddenly FDIC gets this thing out, the immediate reaction would be that the President can't even control his own agencies.

Mr. Crowley: I have no objection in the world to doing anything we possibly can to coordinate all of our policies. I do want to leave this impression with you: that there is no other agency dealing with the 48 State

Banking Commissions that have 7800 State Banks in any fund except FDIC. We did not attempt to dictate to the Comptroller's Office or to the Federal Reserve as to their policy. We do have to work, from time to time, in trying to strengthen these State Bank Commissions' hands and their position. Within the last two or three years we got a lot of State legislation passed and strengthened State laws. We got complete control of chartering with them and many things like that, and we have been trying, since1934, to get some form of coordination between the Federal Reserve, the Comptroller's Office and FDIC.

Now I don't mean that in a critical way, but Marriner rushes over to the White House and absolutely sells the President a bill of merchandise that there is no coordination on bank examination in this Federal system. He has not in his own 12 Federal Reserve Banks. He better find out first what they are doing before he goes out picking on somebody else. All I say is I don't think it's fair that Marriner should go over and get the ear of the President and sell the President a bill of merchandise and leave FDIC and the Comptroller's Office out of the picture without having them represented. I am for any meeting that you would call. I am for coordination of any policy that is fair, but I am not for using a lot of propaganda to try to nationalize the banking system by indirection, that Congress has never permitted. We started out and we have the co-operation of these State Commissions because we have been sympathetic with them. They have done a lot of strengthening of their position and that is FDIC's position with these men. They have come here and worked with us from day to day.

Now, anything that you want to do to bring about coordination, I am for and I will hold up anything until you can do that.

HM,Jr: Here's the point. I have scrupulously withheld any comment as to where I thought bank examination on the part of the Federal Government should land. You know that.

Mr. Crowley: That's right.

HM,Jr: Everybody has tried to find out and I carefully withheld it. I have asked Mr. Upham to write me a memorandum and I think Mr. Taylor is writing me one of your own. Aren't you, Wayne?

Mr. Taylor: Yes.

HM,Jr: On that subject, independent of Upham?

Mr. Taylor: Yes.

HM,Jr: I only asked them to do that this week, in view of the President's speech.

Yesterday -- I think it was yesterday; anyway, within the last 48 hours -- Eccles asked me whether either the President or I wouldn't call a meeting so that we could get started on this question of uniform bank examinations from the standpoint of the Federal Government insofar as our authority goes. I have been turning it over in my mind waiting to see you to see what you had in mind.

Mr. Crowley: Let me say, Mr. Secretary, that it is not a thing we ought to go over and thrash out with the President of the United States. I think you could call a meeting and we could let every fellow air his views. The only thing I say, I am perfectly willing to cooperate and coordinate and carry out the spirit of anything that will bring coordination, but I am not for giving any fellow any edge in this thing.

HM,Jr: What you are saying is you are willing to cooperate, but you won't give up anything.

Mr. Crowley: Let me say this: I came from a State that was reluctant as were all Western States to join FDIC because everyone felt that if we joined FDIC the Government would usurp our State rights. We are cooperating with these State Commissions and we are examining their banks by a permission that we enjoy entirely by their cooperating back with us and they let us go in and hold Board of Directors' meeting and things like that. All I say is I don't believe it was ever the intent of Congress, and if Congress wants to change it, fine! that the National system should take over the State banking system of this country.

HM,Jr: No argument about that.

Mr. Crowley: When you centralize bank examination under an examiner other than State Commissions, then you are usurping their rights.

HM,Jr: If you ask me, in view of the President's message and radio talk, should you send out that letter, you want my answer on that?

Mr. Crowley: I won't do anything if you call a meeting.

HM,Jr: My answer to you is I will see the President within the next 24 hours and I will ask him whether he would like me to call a meeting. I am ready to meet three times a week on this thing with the Fed, with yourself and with the Comptroller's Office, until we get this thing thrashed out so we can go to the President and say: this is the way the thing should be handled.

Mr. Crowley: That's agreeable to me.

HM,Jr: I am willing to start Monday afternoon and work at it until we get something and everybody can air his views.

Mr. Crowley: I don't think you will find any difference of opinion as to what spirit that you are trying to bring about in the way of uniform policies. I think you will find a lot of opposition if anyone is trying to take over something that belongs to somebody else.

HM,Jr: You always do, and I have no axe to grind in this thing.

Mr. Crowley: And the only thing -- I have a memorandum here -- the attempt we have made, at different times, to get the Federal Reserve to cooperate with us on different things. And, just off the record, the trouble with Marriner is that he ought to check up on his 12 banks before he starts coordinating FDIC.

HM,Jr: If we get in this meeting -- and in this room we can call a spade a spade -- Jesse Jones has sounded off on this thing. As a matter of fact, he doesn't himself examine banks. He takes up bank examinations.

Mr. Taylor: He takes other people's bank examinations, but then he goes in there ....

Mr. Crowley: I don't think he has gone into 50 banks.

HM,Jr: I don't think he belongs in there. I will talk to him myself. It would make it that much more complicated. Jesse ought to put his mind on his new authority -- he has all he can do to put that 1½ billions to work.

Mr. Crowley: These fellows all talk about liberalizing bank examination. They are trying to make the bank examiner the goat for this recession. Our bank examiners won't criticize any loan that Jesse Jones or Eccles will make in their own individual banks, but let's not try to encourage them to make any loans that they would not make themselves. You can't make ....

HM,Jr: I am in a very philosopohical mind. I am trying to do the best we can to carry out the spirit of the President's message and I will see him within the next 24 hours and will ask him whether he would like me to get these people together and settle this thing. We have never attempted to do it and if he does, unpleasant as it is, I will do it.

Mr. Crowley: That's all right. You are the most neutral fellow that I know of that we could sit in with.

HM,Jr: Thank you. I try to be neutral. And my mind is entirely open. I am going in on this thing that I would like to listen. There are lots of things that I have not had time to study and this is one of them.

Mr. Crowley: Our job has been to keep FDIC solvent and keep confidence and you can't do that if you give the impression that bank examination is going to be disregarded for the sake of a lot of public spending. It can't be tied up with monetary speculation and spending and all that stuff if you are going to keep any confidence in the banking structure. The banks are, as you know, in good shapre. Right now you have a shift in your Governments. A lot of your bigger banks are shifting out of long-terms into our little banks. The little banks are always the goats in these securities. We always get the worst of it.

HM,Jr: Are you all through?

Mr. Crowley: I have got it all off my chest.

HM,Jr: One thing I would like to do -- before O'Connor left he asked if I had anybody we cared to recommend who would take Diggs' place. Well, I didn't have anybody around, and what I would like to bring to your attention is this fellow, Smythe, who has been very highly recommended by the Vice President. He lives across the street from the Vice President in his home town.

Mr. Crowley: What experience has he had?

HM,Jr: He has been Receiver for the bank in Uvalde.

Mr. Upham: Also Vice President.

HM,Jr: Also Vice President of the bank.

Mr. Crowley: I will be glad to have him come in. Let me say this, as long as we are all making statements. We kept Diggs on at $12,000 as Assistant to O'Connor and he didn't earn $2.10 all the time he was working for us. I have no objection ....

HM,Jr: I have agreed that if you don't take him, I will. I will tell you what he has come up on. I have tried to put him in the place where he will be most use to me.

Mr. Crowley: If this fellow is honest and industrious, we are willing to have such a fellow in my organization, but not at $12,000.

HM,Jr: I told him $7,500.

Mr. Crowley: That's all right if he is good, industrious .....

HM,Jr: He is and the Vice President recommended him higher than anybody in town.

Mr. Crowley: I am going to Lynchburg this afternoon with Carter.

HM,Jr: When would you like to see him?

Mr. Crowley: Tomorrow, any time.

HM,Jr: About ten o'clock?

Mr. Crowley: Yes.

HM,Jr: But the point -- I am trying to be particularly useful at this time -- until the President makes up his mind who he is going to appoint Comptroller, this kind of fellow, to me, would be very useful because he knows banking.

Mr. Crowley: That's all right. We are willing to take him.

HM,Jr: He knows banking, and he would be very useful, and particularly at this junction, and I talked to him yesterday and the thing I want him to work on is this whole question of bank examination. Now the fellow has come up -- he's 45 or 46, maybe a little bit older, and he has made good in Uvalde.

Mr. Crowley: That's all -- I am perfectly satisfied.

HM,Jr: And we checked him and he's clean as a whistle.

Mr. Crowley: That's all we want.

HM,Jr: He's clean as a whistle and I think that kind of fellow could be useful to you, the Comptroller and to me.

Mr. Crowley: That's right.

HM,Jr: We haven't got too many of them.

Mr. Crowley: That's perfectly O. K.

HM,Jr: (To Mr. Upham) Will you see that he goes over to see Mr. Crowley?

Mr. Upham: Surely. He's in my office.

Mr. Crowley: I wanted to see you, but you were away and I was not feeling well.

HM,Jr: Well, I will get word to the President that I want to see him, in the next 24 hours, and I will have an answer by tomorrow.

Mr. Crowley: All right. Good-bye and good luck to you. Carter is going to be Toastmaster at a Chamber of Commerce meeting in Lynchburg and he asked me to go down with him. By the way, he's raising the devil about the bank holding company bill.

HM,Jr: Which way?

Mr. Crowley: He wants to pass it. He said he asked the President when he was going to send his message up and the President said in two or three days.

HM,Jr: (Making memorandum of topics to be discussed with the President. Much obliged.

oOo-oOo

FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON

OFFICE OF THE CHAIRMAN

April
12th
1938

My dear Mr. Morgenthau:

This Corporation is taking certain steps with respect to bank supervision which we believe are of such importance that they should be called to your attention.

1. We are instructing our examiners no longer to classify any loan as "slow." They shall classify a loan as "substandard" if it involves a substantial degree of risk to the bank, but no loan shall be criticized by a bank examiner of this Corporation simply because it has run a long time or because it will not be paid off in the near future. We have long urged this step and intend it to be a permanent policy.

2. We are instructing our examiners to value the securities held by banks on a reasonable basis rather than blindly to follow the market quotations. Securities of high investment quality are to be valued at cost and market price is to be ignored. Securities not of a high investment grade but also not involving great risk of default are to be valued at cost, but the market price is to be noted as a memorandum figure in the examinations. Defaulted bonds, bonds having a high risk of default, and stocks held by the banks are to be valued at market price.

On the other hand, neither unrealized nor realized security profits are to be taken into consideration in bank examinations. As a permanent policy with respect to the banks which we supervise, and insofar as we have power to enforce sound banking standards, we intend to change the practices of banks in rising security markets. Profits from security sales are to be used as a reserve for future losses. Banks will thus no longer be able to profit from security speculation. They must invest simply for interest return. We anticipate that this policy will discourage speculation on the part of the banks and promote stability in the bond market.

The officials of the State Bank Supervisors association have agreed that the members of their organization will go along with us in this program of loan classification and security valuation.

I am very glad to report, incidentally, that the banking system appears to me to be in a very strong position. Its present liquid condition, with more than 50 percent of its assets consisting of cash, interbank deposits and U. S. Government securities, not only makes possible meeting all deposit withdrawals but also permits the banks to meet all demands for loans of a reasonable character. We hope that our change in loan classification will encourage the banks to make all reasonable loans. Loans at present in the portfolios of the banks appear, on the whole, to be sound. In 1934, 7 percent of the loans in national banks and banks not members of the Federal Reserve System were classified as doubtful and loss, and 28 percent as slow. In 1937, the corresponding percentages were 2 percent and 12 percent.

As you can well appreciate, there are, however, certain banks, largely banks which have never regained their strength since 1933, which are in a weakened condition. In the near future it may be necessary and desirable for us to make substantial payments in connection with these situations. However, our present record indicates that where we make such payments there is no substantial loss to depositors. It is my opinion that the banking situation is fundamentally sound and need be no subject of concern.

Sincerely yours,

Leo T. Crowley

Leo T. Crowley
Chairman

The Honorable Henry Morgenthau
Secretary of the Treasury
Washington, D. C.

April 21, 1938

For the Secretary:

Here is the one-page summary of the report of the Investment Bankers Conference, Inc., as requested.

Upm

April 21, 1938

Selected investment bankers in different sections of the country were asked for leads as to industries that needed funds for capital improvements in amounts of $1½ or less. The investment bankers reported that there has been little demand from sound business firms that cannot be handled locally.

The investment bankers reported that inability to secure funds or unwillingness on the part of business concerns to apply for funds have been due principally to the following: (1) The cost and other requirements of the SEC registration; (2) the surtax on undistributed profits, and other taxes; (3) the general condition of business; (4) the difficulty in securing an investment rating for bonds of small companies which would make them eligible for bank investment; (5) labor unrest and other miscellaneous reasons.

A questionnaire was sent to approximately 4,000 small manufacturers in 872 cities throughout the country. Twenty per cent of the companies addressed made replies--regarded as a fair sampling of a broad, cross-section of diversified industrial establishments of from small to medium size and scattered uniformly about the country. These small manufacturers report (1) there is no substantial lack of new capital available for expansion of sound companies; (2) companies entitled to credit for profitable use have been able to obtain it during the past two years; (3) many have been deterred from seeking additional funds because of a lack of confidence in the economical and political outlook engendered by existing laws and the fear of further adverse legislation; by the high level of taxes which have killed incentive to expand; by labor problems and the attitude of the Administration toward labor; by the expense and red tape of SEC registration and by requirements of banking laws with respect to security ratings.

The prevailing thought is to await further development of the Administration's attitude toward business and better business conditions before expanding.

133

Ribbons copies of the attached memo were sent to following on 4/21/38:

The President
Secretary of State
Secretary of War (Attention: Col. Strong - (G-2))

Letters of transmittal signed by Secretary and dated 4/21/38 -

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 21, 1938

TO Secretary Morgenthau

FROM Mr. Haas

Subject: Current Trade with Japan and China, March 1938

A. United States trade with Japan increased markedly in March.

I. Exports to Japan were 22 percent greater in March than in February and 12 percent greater than in January 1938. They were, however, 22 percent less than exports in March 1937. United States exports to Japan usually show a seasonal increase during the month of March.

a. Exports of iron and steel manufactures accounted for 50 percent of the increase and petroleum products for 33 percent. Exports of iron and steel scrap amounted to $2,483,685 or 51 percent of the total iron and steel exports.

b. Raw cotton exports decreased 1 percent as compared with February 1938 and were 53 percent less than March 1937.

c. Exports of aircraft and parts amounted to $525,000, 115 percent more than in February 1938.

II. Imports from Japan were 14 percent greater in March than in February 1938 but were 44 percent less than in March 1937.

a. Imports of raw silk increased 19 percent in March as compared with February 1938. They were, however, 7 percent less than the monthly average for the past six months and were 11 percent less than in March 1937.

b. Imports of cotton manufactures decreased 43 percent in March as compared with February 1938.

B. United States trade with China showed even greater increases in March 1938 than our trade with Japan.

I. United States exports to China and Manchuria increased 41 percent during the month of March 1938 as compared with February 1938. Exports to North China and Manchuria increased 36 percent, and exports to South China, Shanghai

Secretary Morgenthau - 2

and Hong Kong increased 44 percent. Exports to South China, Shanghai and Hong Kong were approximately 61 percent greater in value than those to North China and Manchuria.

II. Imports from China and Manchuria increased 23 percent during the month of March 1938 as compared with February 1938. Imports from North China and Manchuria show a decrease of 2 percent and those from ~~South China~~, Shanghai and Hong Kong increased 32 percent. Imports from North China accounted for 21 percent of the total imports from China in March as compared with 27 percent in February 1938, while imports from South China accounted for 79 percent in March 1938 and 73 percent in February 1938.

Statistics

A. Current trade with Japan

I. United States exports to Japan - total value

	1938	1937
March	$23,459,000	$29,971,000
February	19,266,000	24,745,000
January	20,981,000	22,364,000
	1937	1936
December	$16,532,000	$16,433,000
November	18,133,000	24,100,000
October	20,129,000	26,668,000

Secretary Morgenthau - 3

II. United States exports to Japan by commodities

Commodities showing increases	March 1938	February 1938	January 1938
Iron and steel scrap	$ 2,484,000	$ 1,658,000	$ 534,000
Iron and steel semi-manufactures	1,157,000	586,000	1/
Other iron and steel and manufactures	1,264,000	583,000	1,489,000
Petroleum and products	4,386,000	3,004,000	5,066,000
Industrial machinery	2,979,000	2,609,000	2,853,000
Paper base stocks	840,000	422,000	492,000
Aircraft and parts	525,000	244,000	2/
Fertilizers and fertilizer materials	437,000	362,000	24,000
Ferro-alloys	321,000	24,000	nil
Coal-tar products	301,000	23,000	69,000
Lead and manufactures	228,000	70,000	nil
Rosin	57,000	10,000	11,000
Commodities showing decreases			
Cotton, unmanufactured	5,508,000	5,565,000	5,817,000
Copper and manufactures	1,178,000	1,367,000	1,883,000
Automobiles, parts and accessories	718,000	1,337,000	2/
Hides and skins, raw	224,000	226,000	22,000
Electrical machinery and apparatus	36,000	58,000	252,000
Tobacco and manufactures	1,000	290,000	nil
Total	$22,644,000-97%	$18,438,000-96%	$18,512,000-88%
All other	815,000- 3%	828,000- 4%	2,469,000-12%
Grand total	$23,459,000	$19,266,000	$20,981,000

1/ Included in "other iron and steel and manufactures".
2/ Not shown separately in January 1938.

Secretary Morgenthau - 4

III. United States imports from Japan - total value

	1938	1937
March	$ 9,940,000	$17,660,000
February	8,723,000	18,382,000
January	11,342,000	17,683,000
	1937	**1936**
December	$11,839,000	$16,451,000
November	17,190,000	15,340,000
October	15,420,000	15,930,000

IV. United States imports from Japan by commodities

Commodities showing increases	March 1938	February 1938	January 1938
Silk, unmanufactured	$6,219,000	$5,225,000	$ 5,947,000
Silk manufactures	274,000	198,000	323,000
Pyrethrum flowers	229,000	117,000	295,000
Hats and hat materials	228,000	196,000	115,000
Furs and manufactures	228,000	79,000	19,000
Fish and fish products, edible	202,000	141,000	192,000
Fish scrap and fish meal	153,000	27,000	80,000
Tea	108,000	102,000	185,000
Camphor	97,000	54,000	60,000
Paper and paper manufactures	80,000	66,000	174,000
Commodities showing decreases			
Cotton manufactures	316,000	550,000	738,000
Vegetable foods, other than tea	178,000	212,000	298,000
China and porcelain ware	172,000	189,000	271,000
Menthol	108,000	132,000	148,000
Perilla oil	5,000	149,000	143,000
Total	$8,597,000-86%	$7,437,000-85%	$ 8,988,000-79%
All other	1,343,000-14%	1,286,000-15%	2,354,000-21%
Grand total	$9,940,000	$8,723,000	$11,342,000

Secretary Morgenthau - 5

B. Current trade with China

I. United States exports to China - total value

	1938	1937
March	$8,590,000	$6,483,000
February	6,107,000	5,262,000
January	7,992,000	6,623,000
	1937	**1936**
December	$8,125,000	$5,430,000
November	9,978,000	4,035,000
October	7,152,000	5,421,000

II. United States exports to China by commodities

(a) To North China and Manchuria:

	March 1938	February 1938
Automobiles, parts and accessories	$1,264,000	$ 275,000
Iron and steel manufactures	502,000	648,000
Cotton, unmanufactured	339,000	545,000
Petroleum and products	288,000	275,000
Industrial machinery	270,000	117,000
Tobacco and manufactures	209,000	53,000
Wood and manufactures	137,000	71,000
Total	$3,009,000	$1,984,000
All other	281,000	433,000
Grand total	$3,290,000	$2,417,000

(b) To Shanghai, South China and Hong Kong:

	March 1938	February 1938
Tobacco manufactures	$1,000,000	$ 430,000
Automobiles, parts and accessories	653,000	571,000
Electrical machinery	580,000	79,000
Firearms and ammunition	399,000	384,000
Iron and steel manufactures	336,000	188,000
Copper and manufactures	300,000	269,000
Aircraft and parts	242,000	417,000
Cotton, unmanufactured	238,000	111,000
Vegetable foods, edible	208,000	142,000
Industrial machinery	103,000	72,000
Ginseng	102,000	145,000
Paper and manufactures	102,000	25,000
Petroleum and products	89,000	185,000
Total	$4,352,000-82%	$3,018,000-82%
All other	948,000-18%	672,000-18%
Grand total	$5,300,000	$3,690,000

III. United States imports from China - total value

	1938	1937
March	$4,507,000	$14,103,000
February	3,662,000	11,804,000
January	4,470,000	6,882,000

	1937	1936
December	$5,697,000	$ 5,442,000
November	6,762,000	4,669,000
October	6,914,000	5,498,000

IV. United States imports from China by commodities

(a) From North China and Manchuria:

	March 1938	February 1938
Bristles	$ 213,000	$ 218,000
Furs and manufactures	171,000	56,000
Perilla oil	91,000	182,000
Vegetable products, edible	83,000	22,000
Non-metallic minerals and products	56,000	6,000
Total	$ 614,000-64%	$ 484,000-49%
All other	341,000-36%	494,000-51%
Grand total	$ 955,000	$ 978,000

(b) From Shanghai, South China and Hong Kong:

	March 1938	February 1938
Tung (wood) oil	$1,707,000	$ 689,000
Flax, hemp and ramie and manufactures	293,000	231,000
Tin ore, bars, blocks, pigs, scrap etc.	214,000	622,000
Hats and hat materials	160,000	105,000
Vegetable products, edible	200,000	159,000
Cotton manufactures	151,000	101,000
Bristles	124,000	234,000
Fireworks	110,000	54,000
Silk, unmanufactured	78,000	21,000
Total	$3,037,000-86%	$2,216,000-83%
All other	515,000-14%	468,000-17%
Grand total	$3,552,000	$2,684,000

April 21, 1938

My dear Mr. President:

In response to your memorandum dated April 16, there is submitted the attached table which shows, for tax-exempt obligations reported by individuals with net incomes of $50,000 and over for 1935 (the most recent year for which data are available), the amount owned, interest received, and estimated tax saving at 1936 Act rates, by nature of obligations and by net income classes. In view of the fact that wholly tax-exempt interest does not enter into the taxpayer's gross income nor into his tax computation, the reporting of these data is purely informational, and for this reason they are undoubtedly understated. A comparison of the magnitudes of the interest and the amount owned suggests that the latter data have been incompletely reported, although there is no necessary relationship between these two sets of figures, since the amount owned is reported as at the end of the year whereas the interest comprises amounts received or accrued during the year. It is apparent, however, that individuals do not exercise the same care in reporting their tax-exempt bond holdings as they do in reporting the interest received thereon, and that these latter data with respect to wholly tax-exempt interest are not reported with the same care as is taxable income.

The data with respect to amount owned and interest received on partially tax-exempt obligations are noncomparable. The amount-owned figures include Liberty 4 and 4-$\frac{1}{4}$ percent bonds, United States Savings bonds and Treasury bonds in full, whereas the interest-received data exclude the interest on these bonds on principal amounts not in excess of $5,000, which interest is wholly exempt from income tax. Partially tax-exempt interest also includes amounts reported on the face of the return for which corresponding figures with respect to amount owned in the supporting schedule are not complete.

In estimating the tax saving resulting from the tax exemption of Government interest, it was assumed that such interest would represent an additional increment of taxable income and would, therefore, be subject to the top bracket rates. In order to make the estimate as meaningful as possible, the computation was made using 1936 Act rates rather than the rates actually applicable in 1935.

Faithfully,

(Signed) H. Morgenthau, Jr.

The President,

The White House.

Enclosure.

AFO'D:esh 4/19/38

Wholly and partially tax-exempt obligations reported in 1935 individual income tax returns of net incomes of $50,000 and over, showing amount owned, interest received, and estimated tax-saving at 1936 Act rates, by nature of obligations and by net income classes 1/

(Net income classes and money figures in thousands of dollars)

Net income classes	Amount owned at end of year: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)	Interest received or accrued during year: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt 2/	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)	Estimated tax-saving resulting from the tax-exemption of government interest: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)
50 - 60	182,418	69,252	25,810	43,442	113,166	12,696	3,837	1,504	2,333	8,859	3,978	877	60	817	3,101
60 - 70	175,498	71,075	20,695	50,380	104,423	11,033	3,425	1,053	2,372	7,608	4,333	1,062	42	1,020	3,271
70 - 80	140,653	43,562	10,722	32,840	97,091	9,711	2,635	1,151	1,484	7,076	4,069	743	46	697	3,326
80 - 90	107,797	43,014	11,274	31,740	64,783	6,907	1,973	662	1,311	4,934	3,461	747	26	721	2,714
90 - 100	64,972	24,110	6,759	17,351	40,862	4,350	1,263	490	773	3,087	2,329	508	17	491	1,821
100 - 150	332,070	99,047	16,120	82,927	233,023	18,750	4,107	807	3,300	14,643	11,157	2,078	32	2,046	9,079
150 - 200	132,910	50,644	7,634	43,010	82,266	8,807	2,178	508	1,670	6,629	5,332	1,089	20	1,069	4,243
200 - 250	99,106	40,907	8,614	32,293	58,199	4,980	1,534	458	1,076	3,446	3,002	728	18	710	2,274
250 - 300	149,606	42,952	2,564	40,388	106,654	7,654	1,537	245	1,292	6,117	5,049	889	10	879	4,160
300 - 400	64,339	25,386	2,857	22,529	38,953	3,708	1,060	143	917	2,648	2,502	648	6	642	1,854
400 - 500	97,182	25,873	474	25,399	71,309	5,225	709	15	694	4,516	3,753	501	1	500	3,252
500 - 750	128,671	52,007	4,674	47,333	76,664	7,429	2,118	158	1,960	5,301	5,379	1,456	6	1,450	3,923
750 - 1,000	40,401	20,220	1,035	19,185	20,181	1,730	483	11	472	1,247	1,307	359	3/	359	948
1,000 - 1,500	50,290	33,169	181	32,988	17,121	1,973	1,038	3	1,035	935	1,517	797	3/	797	720
1,500 - 2,000	13,405	6,113	—	6,113	7,292	636	183	19	164	453	476	127	1	126	349
2,000 - 3,000	11,412	1,727	925	802	9,685	458	6	3	3	452	355	2	3/	2	353
3,000 - 4,000	6,463	4,782	10	4,772	1,681	797	260	8	252	537	616	197	3/	197	419
4,000 - 5,000	106,259	76,599	3/	76,599	29,660	3,061	1,729	2	1,727	1,332	2,386	1,347	3/	1,347	1,039
5,000 and over	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Total	1,303,452	730,439	120,348	610,091	1,173,013	109,895	30,075	7,180	22,895	79,820	61,001	14,195	325	13,870	46,846

Treasury Department, Division of Research and Statistics. April 18, 1938

1/ Schedule D, Form 1040, columns 2 and 3, except as explained in footnote 2/ with respect to partially tax-exempt interest received. 1935 is the latest year for which amount held and interest received data are available. However, the estimated tax-saving resulting from the tax-exemption of government interest has been calculated at rates as under present law.

2/ Excludes interest received on 4 and 4-1/4 percent Liberty bonds and Treasury bonds on a principal amount not in excess of $5,000, which interest is wholly exempt from income tax. Includes the partially tax-exempt interest received from partnership and fiduciary sources.

3/ Less than $500.

April 22, 1938.
11:10 a. m.

H.M.Jr: Hello.

Operator: Mr. Frank.

H.M.Jr: Hello.

Jerome Frank: Hello.

H.M.Jr: Morgenthau speaking.

F: Yes sir.

H.M.Jr: Ah, Morris Ernst was in yesterday to see Herman Oliphant, with a story that I was supposed to have opposed your appointment to some judgeship.

F: Well, I never heard of it.

H.M.Jr: Well, Morris Ernst - and I thought I might as well tell you - the first place I never knew there was a vacancy, I never knew you were a candidate, and until Herman Oliphant walked in this office I never heard of it.

F: Well, now, I - ah - Mr. Secretary, ah, this is the first time I ever heard that you ever knew about it or did anything about it.

H.M.Jr: Well.

F: And if Morris so stated it was certainly without my knowledge. I've seen him since and he never mentioned it to me,

H.M.Jr: Yeah.

F: And please don't think that I think so.

H.M.Jr: Well, I just wanted - this is the second time that somebody's planted a story that I've tried to block you in something.

F: I'm sorry you felt it necessary to call me.

H.M.Jr: Well, - I thought you might as well get it, as they say, right from the horse's mouth.

F: Well, will - you will forgive me for any thought that you entertained that I thought so, won't you.

H.M.Jr: Yeah. I certainly will.

F: All right.

H.M.Jr: But, ah ....

F: Thank you for calling.

H.M.Jr: Well the point I'm getting is this - ah, ah, - any time you want to know where I stand on anything as far as you're concerned, or your work, just ask me, and I got a reputation I'll tell you right straight from the shoulder.

F: You have with me. Now - please now, don't ascribe to me the gossip of other people, will you?

H.M.Jr: I won't.

F: All right, sir, thank you.

H.M.Jr: You're welcome.

April 22, 1938.
11:19 a. m.

H.M.Jr: Hello.

Operator:

H.M.Jr: Hello.

Morris Ernst: Hello, Henry.

H.M.Jr: Yeah.

E: Morris Ernst.

H.M.Jr: How are you?

E: Fine, ah - but disturbed. Jerome Frank just told me that somebody has quoted me as saying to you .....

H.M.Jr: What is it?

E: ....somebody indirectly to you.

H.M.Jr: Yeah.

E: That you are opposed to Jerry's appointment to the bench.

H.M.Jr: Yeah.

E: I haven't mentioned it to a human being; never thought of it, don't believe it - just want to clear back to you.

H.M.Jr: Well, Morris, the person that told me that was Herman Oliphant.

E: Well let me - I tried to reach Herman, is he there?

H.M.Jr: He's sitting right here.

E: Never mentioned it to him.

H.M.Jr: You want to talk to him?

E: Yes. I'd like very much to.

H.M.Jr: Yeah. But, let me - let - let him talk to you.

Herman Oliphant: Ah, ah, - you're right.

E: What?

Oliphant: Hello. This is Oliphant.

E: Yes.

Oliphant: We're both on now.

E: What?

Oliphant: I had a slip - I made a slip.

E: Yeah.

Oliphant: It was Ed Foley.

E: Oh.

Oliphant: He saw me just the minute - a few minutes before you did.

E: Now. Will you do me a favor.

Oliphant: Yeah.

E: Will you call up Jerry.

Oliphant: I certainly will.

E: What? Ah, there's ah, ah - tell Henry that not only did I - did not say it, I didn't even think it.

Oliphant: Naturally.

E: You see.

Oliphant: I'm awfully sorry.

E: Will you?

Oliphant:

E: That's all right.

Oliphant: Ed was in just before you came in.

E: That - that's inept, but ah, I just want to clear myself on it, because I never said a word like it.

Oliphant: That's right.

E: All right. Call Jerry, will you?

Oliphant: Ah, hold on.

E: Yeah.

H.M.Jr: How are you otherwise?

E: Fine, Henry. Swell, and - and I just was awfully lucky it straightened out.

H.M.Jr: Swell.

E: Because ah, - God knows (laughs) it's on the market.

H.M.Jr: The reason I called Frank was because there was a story around that I had opposed his coming down on the S. E. C......

E: That I heard, originally, through Jerry.

H.M.Jr: And I - and I told, ah, Frank that it wasn't so.

E: Well, I'm very - I think you were very wise to call him up today.

H.M.Jr: As far as - in the case of his coming down, I never was consulted, nobody asked my advice, or anything else.

E: Right. Well .....

H.M.Jr: I just thought that ah - when I heard this story it looked to me as though somebody was malicious - out of his way to make a little

E: Well - look. Will you do me a favor. Either you or Herman call back Jerome?

H.M.Jr: I'll let Herman .....

E: Because, ah, God knows I - (laughs)......

H.M.Jr: What else do you know?

E: Fine. Everything's going pretty good, and I've had some chats with Herman he may tell you about.

H.M.Jr: He did. He was ....

E: And I saw Gaston last night.

H.M.Jr: What?

E: I saw Gaston for dinner last night.

H.M.Jr: Gaston?

E: Yeah. I had dinner with him, and Jerry and some other people.

H.M.Jr: Herbert Gaston?

E: Yeah.

H.M.Jr: Oh.

E: And, all told, I think I can be of help around there in the way I mentioned to Herman.

H.M.Jr: Well Herman tells me that, ah, the result of your ....

E: Well, you're going to - I think - I know it's a hell of an improvement. And I know that the cement thing is coming out very nice. You see? And whenever you want me let me know, I .....

H.M.Jr: I don't know - Of course, I suppose I'm the worst man in the world, but I - for publicity - but I don't know how - how you're going to give it to these fellows.

E: Well, let me tell you some day.

H.M.Jr: What?

E: Let me tell you how, some day.

H.M.Jr: I'd like very much to know.

E: Because it's - it's - it's really, it's—it's just a little gap in there that makes all the difference between a picture being painted one way and another.

H.M.Jr: A little what, did you say?

E: A little - a little matter of technique.

H.M.Jr: Well, I guess I ....

E: It's - it's the difference in the - no, it - I don't think it's matter whether you have it or not. I think if I point out a few things to you I think it's fairly simple.

H.M.Jr: All right, sir. If you .....

E: Well swell, Henry. I'm glad to help.

H.M.Jr: Fine.

E: Well - call up Jerry.

Oliphant: I'll take care of that.

E: All right. Will you, thanks, Herman.

April 22, 1938
11:30 a. m.

Present:

Mr. Oliphant
Mr. McReynolds

HM,Jr: Did you get in touch with Peoples?

Mr. McReynolds: I talked to Mrs. Peoples. She said she was very much disturbed. She had heard that it had been said that she did not give the Admiral the word about his being due back here last Monday and she wanted to assure me that she did give him the word. I talked to the Admiral on the 'phone and he said, 'My head is just ringing. I have got vertigo.' I said, 'Have you had the doctor?' and he said 'No.' So I said, 'You had better get him.'

HM,Jr: Between now and Monday morning you see that fellow, whether he's in bed or not.

Mr. McReynolds: I told Mrs. Peoples this morning that I would go to the apartment sometime this afternoon.

HM,Jr: I saw the President at 9:30 and told him about this cement and will you instruct Mr. Collins that that on fixed amounts we want bids f.o.b. mills.

Mr. McReynolds: In other words, you don't want them f.o.b. site.

HM,Jr: F.O.B. Mills. That's what the President wants.

Mr. Oliphant: You are perfectly willing that if it turns out from the President's standpoint that silo is the same as mill, great silos, great storage points, if it turns out it's the same as mills, we are investigating that now ....

Mr. McReynolds: You will get in trouble there because you have a lot of big dealers who maintain concentration points.

HM,Jr: The President said f.o.b. mill.

Mr. McReynolds: It's a very important point, because while there is an advantage to the silo added to the mill, any concentration point of the mill, there are a number of other dealers who maintain concentration points that are comparable and if you ....

HM,Jr: Is the silo owned by the manufacturer?

Mr. McReynolds: In many cases it is.

HM,Jr: If you want to do this thing in a clean-cut way, and the silo is in between, and the next thing is the dealer's store -- from his standpoint, the clean-cut way is f.o.b. mill: You have from now until Monday, but every time I told him about the dealers' organization he said, Let's investigate, and I said that's what is being done. He did not know that Ickes had been trying to break this thing for four years.

oOo-oOo

Offering of Commodity Credit Notes
Study of Uniform Bank Examinations

April 22, 1938

11:50 am

Present:

Mr. Taylor
Mr. Gaston
Mr. Upham
Mr. Harris
Mrs. Klotz

HM,Jr: (Spoke to Dr. Burgess on telephone; record attached.)

Did you (Mr. Taylor) check with Jesse Jones?

Mr. Taylor: All we need is a resolution from his Board, which is to meet tomorrow morning, to fill in amounts and rates.

HM,Jr: Has he talked about how he can use this? Twelve months or 18?

Mr. Taylor: I don't think he cares very much.

HM,Jr: (Spoke to Jesse Jones on telephone; record attached.)

(When he finished his conversation with Mr. Jones, the Secretary again spoke to Dr. Burgess, and copy of the latter conversation is also attached.)

* * *

HM,Jr: I saw the President and he said to go ahead and have a meeting with the bank examination agencies and see if we can do something without the necessity of legislation, so what I thought we would do, that I would see the boys at 10:30 Tuesday morning, but that you fellows could have a dress rehearsal before that. And get Crowley and Diggs and Eccles together and kind of rub off some of the rough edges. Taylor could call it and I would like Upham to be there and I would like Smyth to be there, and then you decide when you want it and get off some of the rough

April 22, 1938.
11:51 a. m.

H.M.Jr: Hello.

Operator: Burgess. Go ahead.

H.M.Jr: Hello.

Randolph Burgess: Hello Henry.

H.M.Jr: Good morning.

B: How are you this morning?

H.M.Jr: Physically? Fine.

B: (Laughs) I feel just the same way.

H.M.Jr: All right. Mentally - still sound.

B: Yeah. Well I'm the same way.

H.M.Jr: O. K.

B: Yeah.

H.M.Jr: I'm calling up about the two hundred million dollar issue R. F. C. ......

B: Uhh ...

H.M.Jr: ...Commodity Credit.

B: Yes.

H.M.Jr: Ah - how does it look to you right now? Wayne Taylor's here with me; so's Harris.

B: Oh - well, I just had a call in for him about the same thing.

H.M.Jr: Well, you can talk here. Your voice .....

B: Well, these, ah, these short rates are changing so fast, and the scarcity of short paper is so great .....

H.M.Jr: Yeah.

B: ..... that it will go beautifully.

H.M.Jr: Yes.

B: And, ah, ah - the rates - a - can be considerably lower than those we first talked about.

H.M.Jr: Well, before you talk rates, would you mind saying, how many months you're talking about?

B: Well, ah, ah - I was going to ask you that.

H.M.Jr: Yeah.

B: Ah, the market would take the eighteen months very nicely. It would take fifteen, it would take twelve. You can - you can take your choice.

H.M.Jr: I see.

B: It would take eighteen months at three quarters of one per cent very easily.

H.M.Jr: Uh-huh. What .....

B: Or even - even slightly under that.

H.M.Jr: Uh-huh. And, uh - three quarters of a per cent for eighteen months - well, what about one month?

B: Oh, uh - one year?

H.M.Jr: One year.

B: Uhh - a half.

H.M.Jr: A half?

B: Yeah.

H.M.Jr: That doesn't seem as though it were comparable, does it?

B: A half - three quarters - it's just a quarter up six months - that's about, ah.....

H.M.Jr: Ah, I see. Now, let me just - when would eighteen months - when would that fall? When would that come - May - uh - well I wonder how that fits in with Jones' program?

B: Well, I don't know. Ah, I haven't talked to him this morning. I wanted to talk to you people first. Ah - you could do fifteen months very nicely.

H.M.Jr: I don't like fifteen months.

B: You don't like that?

H.M.Jr: No.

B: Yeah. Well, you could do either one. Now those rates I've given you are round rates, and it may be we could change those.

H.M.Jr: Well, let me call up Jones a minute and I'll call you right back.

B: All right.

H.M.Jr: Will you do that?

B: Sure.

H.M.Jr: How - how about our own Government?

B: Well, they're strong this morning; they're up, ah, oh, a quarter of a point or more. Ah, they were very strong first thing this morning. There's a little bit of selling come in now .....

H.M.Jr: Yeah.

B: ..but they're still a quarter over last night.

H.M.Jr: You people have stopped selling?

B: No, we haven't done a thing this morning.

H.M.Jr: Is that the policy?

B: No - well, as - for the present, till we look at it.

H.M.Jr: Uh-huh.

B: Ah, what we did yesterday did so little good that I think even if, ah - even without your announcement we would have hesitated to go in this morning.

H.M.Jr: Uh huh.

B: And, ah, - we'll just have to let the market, ah, find a level a little bit right now, I think.

H.M.Jr: Ah, it's a little softer.

B: Well, it's a little softer - not very much though.

H.M.Jr: I see.

B: There's still a lot of good buying going on.

H.M.Jr: Good. I'll call you back within five minutes.

B: Very good, Henry.

H.M.Jr: Thank you.

April 22, 1938.
11:56 a. m.

H.M.Jr: Hello.

Operator: Mr. Jones.

H.M.Jr: Thank you.

Operator: Go ahead.

H.M.Jr: Hello.

Jesse Jones: Good morning.

H.M.Jr: How are you?

J: Fine. How are you?

H.M.Jr: How's my twin?

J: (Laughing) All right.

H.M.Jr: What?

J: All right.

H.M.Jr: You and I.

J: Absolute.

H.M.Jr: Well, what do the Tories wear? I've got to look up what a well-dressed Tory wears.

J: Well, now, you know I hadn't thought about that.

H.M.Jr: Yeah.

J: By George, I was just fixing to call you.

H.M.Jr: I see.

J: About nothing in particular. I was just going to - Wayne said you were going to be out of town tomorrow.

H.M.Jr: Well, I just got through talking to Randolph Burgess.

J: Yeah.

H.M.Jr: And he says that right now he can get you, ah, a hundred million at eighteen months for three quarters of one per cent, and for twelve months at a half of one per cent. See?

J: Yeah.

H.M.Jr: The reason I'm taking this interest is I want to have it go out right, and also my name's on the circular.

J: Absolute.

H.M.Jr: I'm a little fussy about that.

J: And you ought to be.

H.M.Jr: Now, ah, I want - what I want to ask you, can you use the money for eighteen months?

J: Yes.

H.M.Jr: You can?

J: No doubt in the world about it.

H.M.Jr: Well.....

J: I'd rather give it to them eighteen months.

H.M.Jr: Well, I think that eighteen. Of course, he said the thing is changing so fast that he won't know until tomorrow morning.

J: Yes.

H.M.Jr: So I thought what I'd do was to get on the phone about eleven o'clock.

J: Uh-huh.

H.M.Jr: And talk to him and then I'll talk to, ah .....

J: To Wayne?

H.M.Jr: To you and to you -

J: All right.

H.M.Jr: To you and Wayne.

J: Well, that'll be fine. You - you will be out of town tomorrow?

H.M.Jr: I'm on the farm, but I'll be on the phone around eleven o'clock.

J: Well, that'll be fine.

H.M.Jr: And, ah - ah - but you could use it for eighteen months?

J: Oh, absolutely.

H.M.Jr: Well, ah - ....

J: We're ah - we're going to be carrying this cotton and corn loans for a terribly long time.

H.M.Jr: Well - eighteen at three quarters, and twelve months, and a half - I mean, between now and tomorrow they may shave it a little, but even if they can't, that's awfully cheap money.

J: That's awful cheap money and I'll - I would want - you see we're not talking about one hundred, we're talking about two hundred.

H.M.Jr: That's right.

J: And so, I would rather err on giving them a little more rate.

H.M.Jr: For the first time.

J: For the first time, and let them butt it.

H.M.Jr: And that makes - popularizes it.

J: Yes.

H.M.Jr: The best way to popularize it is to make it tasty.

J:

H.M.Jr: Make it taste good.

J: That's right, taste good.

H.M.Jr: That's right. It's cheap enough.

J: Yeah.

H.M.Jr: Well, you and I are together.

J: Fine. Let's ah, ...

H.M.Jr: Now, if I let you know what a well-dressed Tory wears, I - I'll send you the prescription.

J: Find out and let me know, will you?

H.M.Jr: O. K.

J: I - I - I can give you my tailor, so you could just have him fix me up on it.

H.M.Jr: All right.

J: Well now ....

H.M.Jr: Maybe he'll give us a little knockdown for two suits.

J: All right.

H.M.Jr: All right.

J: Thank you for calling.

H.M.Jr: I'll - How many pairs of pants?

J: All right.

H.M.Jr: All right.

J: Thanks.

April 22, 1938.
11:59 a. m.

H.M.Jr: Hello.

Operator; Dr. Burgess. Go ahead.

H.M.Jr: Hello.

Randolph Burgess: Hello, Henry.

H.M.Jr: Ah, Jesse says that he could use a hundred million at eighteen months, and a hundred million at twelve months.

B: Ah - yes.

H.M.Jr: Would you sell the whole thing at eighteen months?

B: I would rather see him do the whole thing at eighteen months.

H.M.Jr: Well, I thought .....

B: That is, because I think that it makes a better issue to trade in, in the market; it makes a fuller issue, and .....

H.M.Jr: Oh, really?

B: ..... and you don't have to divide it this time. The market will take it all at one crack. So that I think there's some advantage in putting it all in one bundle. But that's not necessary; he could do it either way he wants to.

H.M.Jr: Well, ah - ah .....

B: It makes a little better issue to trade in.

H.M.Jr: Would you mind casting your mind eighteen months forward please.

B: (Laughs) Well now, let's see.

H.M.Jr: What - what - what month is that?

B: Well, a year would be - would be May, and six months from May is November, if I'm correct.

H.M.Jr. Uh.

B: November. November, 1939.

H.M.Jr: Yeah.

B: That gets him over the spring. I think - of course, your heaviest demand comes in the spring of next year, probably, doesn't it?

H.M.Jr: Yeah.

B: So that your financing problem is more apt to fall about a year from now.

H.M.Jr: Yeah.

B: Ah, try .....

H.M.Jr: Well, the only thing that I'd rather see with Commodity Credit - I'd rather see him to go to the market more frequently. I think he ought to be in there three or four times a year to get him familiar with this thing.

B: Yes. Well, it's going to go beautifully.

H.M.Jr: Well my - my inclination would be divide it in half.

B: I see.

H.M.Jr: But I'm not - I'm not saying that. See?

B: Yes.

H.M.Jr: Now what I'm going to do is I'm going to call you up about eleven tomorrow.

B: Yeah.

H.M.Jr: Will you be at the office?

B: Yes.

H.M.Jr: 'Cause my name's on this thing and I want the thing to go right.

B: Yes.

H.M.Jr: So I'll call you about eleven tomorrow, and by that time you ought to know.

B: All right.

H.M.Jr: Is that right?

B: I'll - I'll - I'd better, ah, call Mr. Jones sometime - see who he talked with about rates.

H.M.Jr: All right. But I - I'd much rather divide it in half and have him go to the market three or four times a year.

B: I see, ah ....

H.M.Jr: This means he wouldn't be in again maybe for eighteen months; they'll forget about it.

B: Yes. Well, there's something in that.

H.M.Jr: Hundred million dollars, after all .....

B: On the other hand, the issue will - the issue will be traded in more, and.....

H.M.Jr: I know. I know, but I - my hunch is that I'd rather divide it in half.

B: Yeah. Well, that's all right.

H.M.Jr: Very much rather.

B:

H.M.Jr: Pardon me.

B: He's sure not to be embarrassed on refunding then.

H.M.Jr: Yes. Ah - I - I don't want two hundred million coming due.

B: Yeah.

H.M.Jr: I'd much rather have it in two bites.

B: I see. Well, that's - that's easy to do.

H.M.Jr: All right; I'll be on the phone tomorrow.

B: Very good.

H.M.Jr: And in the meantime if you want to talk to anybody Wayne's here.

B: All right.

H.M.Jr: O. K.?

B: Very good, yes. Is Wayne right there now?

H.M.Jr: Yes he is.

B: Ah, on the question of policing this thing we'll handle it just like a Government issue, and .....

H.M.Jr: That's right.

B: ..... then we'll stop on it.

H.M.Jr: That's right.

B: Yeah. Now, ah, I think we probably ought to have an additional note from you people about the reimbursement. That wasn't included in the letter - just so there's no misunderstanding.

H.M.Jr: Fine. I'll tell Wayne.

B: All right.

H.M.Jr: Anything else?

B: That's all, I guess. Thanks much, Henry.

H.M.Jr: Ah - Harris tells me that the corporates are improving a little bit.

B: Ah - I think this thing is beginning to go over into the corporates some.

H.M.Jr: Yeah. Listen, ah, is there going to be any more private issues? Have you heard anything around town?

B: There's ah, very little.

H.M.Jr: What - I mean - I saw - some one - that some issue was called off.

B: Ah, - well, there was one called off about three weeks ago. I've forgot which it was.

H.M.Jr: But nothing - but I answered this commercial thing one, ah - the Edison I should think the boys would get in - get in, get some money.

B: Well, ah, there's ah, San Antonio Public Service is coming in for about nineteen and a half million ....

H.M.Jr: Yeah.

B: .... and Puget Sound, Peoria Power and Light, and seven million of General Foods preferred. Those are the ones they're talking about.

H.M.Jr: What's Edison selling at today?

B: It's at a premium, 102 and a quarter - something like that.

H.M.Jr: That's fine.

B: It'll be running out at a hundred and one and three quarters, I think.

H.M.Jr: Yeah.

B: It's a nice premium.

H.M.Jr: All right.

B: For it is a short bond - it's only ten years.

H.M.Jr: O. K. Cheerio.

B: Oh, o. k., Henry.

H.M.Jr: Goodbye.

B: Goodbye.

edges and then I meet with them 10:30 Tuesday. No necessity for Jones to sit in on this. Will you handle that for me?

Mr. Taylor: Yes, sir.

Mr. Gaston: That's on bond portfolio?

HM,Jr: No. The whole question of trying to get these agencies together for uniform bank examinations. There are certain definite things ....

Mr. Taylor: This is not who should do it?

HM,Jr: No. What we can do without legislation, at once.

Mr. Taylor: That's examination policy only.

HM,Jr: Yes. I think if we start that, we will ease this thing into it subsequently who should do it. But get this thing started. There is so much talk since the President's message and the President can say I asked Morgenthau to get those people together and look into the thing.

Mr. Upham: You just want those heads?

HM,Jr: Yes.

Mr. Gaston: There are already stories out as a result of something Crowley said that agencies are considering a policy of more lenient attitude in bond portfolios.

HM,Jr: I thought what you might do, Herbert -- tell the boys that the President has asked me to do this thing and we will start in Monday and do this thing.

Why do you (Upham) wrinkle your forehead. You wouldn't tell them in advance?

Mr. Upham: (Nodding no.)

Mr. Gaston: I don't think I would. I am afraid they might assume too much from what we are going to do.

HM,Jr: Why not?

Mr. Gaston: Well, suppose we tell them Monday.

HM,Jr: All right by me. I will tell them Monday afternoon.

Mr. Upham: If you are going to give the impression we are going to liberalize, I think it would be bad.

HM,Jr: Cy, Pat Boland wants me to come up and talk to the Pennsylvania State Bankers and I am thinking of doing it. I told him I would give him an answer Monday.

Mr. Upham: When do they want you?

HM,Jr: The 19th. And Pat Boland is a nice fellow and I thought we might do it. And, Cy, on this thing of securities in banks, I read it hastily and I have just got one suggestion and I would like you to restudy it between now and Monday. I think you go too far in telling the -- for instance, if you think a bank is weak, you should tell them, so forth and so on. I would like to approach it that we will put down rules and regulations that if a man buys a bond at 103, he has to amortize it down to par. Now if he makes a profit on a bond, I just raise the question that from now on should the United States Government tell this fellow just how to run his bank? If he has a profit and he makes a sale, I think it's up to the president of the bank and his Board of Directors to decide what to do with that. In other words, I am thinking more in terms we will make these rules, but when it comes to tell them how to do it, I think we are taking on much too much.

Mr. Upham: I understand what you mean.

HM,Jr: I think when you get into this thing and then when something goes wrong-- 'Well, the Comptroller of the Currency told me to do that and I did it that way.' How do we know whether the bank is going to be weak? If we think a bank is going to be weak, let's shut it down or strengthen it. My criticism, in this room, and I would like you to think about it, is that we go too far in being teacher. I think we should have rules and regulations about the bonds they buy above or below par, but when we tell them how they should handle the profits on it and so forth, my approach on it is not to tell them quite so much as we have.

Mr. Upham: Glad to think about that.

HM,Jr: Get the idea?

Mr. Upham: Yes, I understand.

HM,Jr: Get it, Wayne?

Mr. Taylor: Yes.

HM,Jr: If a fellow buys a bond at 103, he should amortize it down to par. If it goes up, the profit is his and I don't think the United States Government should tell him what to do with the profit. If he wants to pay it out in dividends, that's his business or put it in his reserves, that's his business.

Mr. Upham: Of course, we have been objecting to the heavy dividends of Transamerica and the reason we objected was because they have a lot of frozen assets because we don't think they are worth what Transamerica shows on their books.

HM,Jr: I think we are getting to be too much teacher telling a bank how to run its business and I think the tendency of this Committee would be to let a bank run their business with more and more responsibility on them; hold them strictly to account, but not try to tell them what each individual item and each bond, how they should treat that.

Mr. Upham: I think you are thinking all right.

HM,Jr: The Bank of America -- my impression is that they have a lot of frozen assets which are written up on their books which are not worth anything like they say it is.

Mr. Taylor: And if you make them charge off the stuff they should charge off, they wouldn't have had the money to pay out dividends.

HM,Jr: When we get into it, I wish you (Upham) would talk to Gus Folger, would he when we get into this thing like to bring in one of the National examiners from the field, to get somebody fresh from the field to sit in with us. Get the idea?

Mr. Upham: Sure.

HM,Jr: And when you have this meeting, Wayne, will you have someone make a record. But you (Upham) get my approach on this thing?

Mr. Upham: Right!

HM,Jr: And I think it's -- you don't have a retail store and go in and tell them what their mark-up should be and how they should value their inventory.

Mr. Upham: I think you are thinking right.

HM,Jr: As I say, it is a new field for me, but just as a matter of horse sense. Do you want anything (Taylor)?

Mr. Taylor: No. The approach that you have just indicated of seeing if we can standardize examination policies, etc., I think it is bound to lead you into the other field.

HM,Jr: Correct! And I am now for the first time ready to go into the final field -- where should final examination be. I am ready for that.

Mr. Taylor: Also, when you start in that field that leads you into a couple of others.

HM,Jr: Well, whatever it is, I am ready. Anything else, Wayne?

Mr. Taylor: That's all right. I am ready now. I am ready for it.

HM,Jr: Have you anything, Cy?

Mr. Upham: You want Smyth put on the payroll as of last Monday. Leo said he would put him to work next Monday. Well, I think he ought to make it last Monday.

HM,Jr: Last Monday, effective the 18th.

Mr. Upham: We are going to have some trouble, I am afraid.

HM,Jr: Where?

Mr. Upham: We went over there this morning and Leo took me aside in the board room and said, I want it definitely understood that if this man comes over he is not to run to the Hill the way Diggs did. I said, I am sure the Secretary had no idea he was to be legislative contact man for the Treasury. He was to be here to work for Diggs and for the Secretary. That seemed to be agreed. He went through a long 'who struck John' with Smyth; you must be loyal; he is working for the corporation. And Smyth comes back. Now, he's O.K., but he just does not want to get in a position where he's between cross fires and where somebody thinks he's double-crossing him.

HM,Jr; Tell Smyth not to worry.

Mr. Upham: I did.

HM,Jr: And maybe Mr. Crowley will tell us who he's working for!

Mr. Taylor: I can tell you that.

HM,Jr: Does his first name begin with Leo?

oOo-oOo

April 21, 1938

For the Secretary:

Attached is the statement which Mr. Smythe and I have prepared on how to treat Government securities in banks. We consulted the Office of the Comptroller and copies have been sent to the Federal Reserve and the FDIC for their critical comment.

This statement represents substantially current practice on the part of national bank examiners.

Upm

Enclosure

April 21, 1938

TREATMENT BY BANK SUPERVISORY AUTHORITIES OF GOVERNMENT BONDS IN BANK PORTFOLIOS

(1) When a bank buys Government securities and the market quotations rise, the increase in asset value represented by the market rise must not be shown on the books of the bank. In other words, there should be no writing up of Government bonds on the balance sheet of the bank by reason of an unrealized appreciation resulting from increased market price.

(2) When a bank buys Government securities and the market quotations rise, and the bank by sale realizes the appreciation in the securities, the resulting profit should be treated just as is any other profit accruing to the bank. The disposition permitted of such profit should depend upon the general condition of the institution. If losses exist at the time the profit is taken, the profit should be utilized to write off or write down those losses. If, in the opinion of the supervisory authorities, the condition of the bank is weak and losses are pretty surely to be expected soon, the profit should be paid into a reserve account (or valuation allowance). If the condition of the bank is satisfactory, the profit should be available for dividends just as are other profits.

(3) When a bank buys Government securities above par, it should amortize the premium over the life of the security.

(4) When a bank buys Government securities at a price of par or above and they later fall below par and when a bank buys Government securities below par and they later fall below the purchase price, there should be no requirement that the bank write off or amortize the decline below par, or in the case of those that are purchased below par, below the purchase price. Those that are purchased at par should be allowed to be carried at par even in the event of a market quotation below par. Those purchased above par will be cared for by amortizing the premium over the life of the security, as above. Those that are purchased below par should be allowed to be carried at the purchase price even though later quotations are lower than the purchase price.

(5) If a bond which is purchased below par goes lower but subsequently rises above the purchase price, it is then a bond upon which there is an appreciation and the rule to apply is as stated in (1) if unrealized or (2) if realized. Similarly, if a bond is purchased at par or above and sinks below par but subsequently rises above the purchase price, it is then a bond upon which there is an appreciation and the rule stated in (1) if unrealized, or (2) if realized, applies.

(6) In any event, the market price of Government securities as of the date of examination, should be shown on the report.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE APR 22 1938

TO Secretary Morgenthau

FROM Herman Oliphant

For your information

In order to establish the eligibility of bonds of local housing authorities for purchase by national banks, Mr. Nathan Straus of the USHA has asked the Comptroller of the Currency whether or not such securities constitute "marketable obligations" within the meaning of Section 5136 of the Revised Statutes. The attached ruling of the Comptroller of the Currency holds, in effect, that 10 per cent of the bond issue of a local housing authority (which under the United States Housing Authority Act must be purchased by others than the Federal Government) constitutes "marketable obligations" and may be purchased for their own account by national banks. Because of the peculiar characteristics of local housing authority bonds, the Comptroller takes the position that the prerequisites for determining marketable obligations contained in the Regulations of the Comptroller of the Currency of February 15, 1936, are not applicable. I understand that bonds of local housing authorities are the only ones singled out for special treatment by the Comptroller of the Currency. In all other cases the standards provided in the Regulations of February 15, 1936, are applied by the bank examiners to the securities included in the banks' portfolios.

In most instances bonds of local housing authorities would be payable from a pledge of project rentals. In addition, an annual subsidy limited to 3½% of the cost of the project will be paid by the USHA so long as certain standards as to tenant selection and low rentals are maintained by the local housing authority. In view of the subsidy, the bonds would appear to be reasonably safe investments. The public housing laws of most of the states provide that local housing authority obligations are legal investments for state banks, insurance companies, public officers and fiduciaries.

The ruling makes no mention of the eligibility of the balance of the issue. As a matter of fact, 90% of the issue ordinarily would be purchased by the USHA and offered eventually for sale to the public. If these bonds are to enjoy the same market advantages as the 10% of the issue included in the Comptroller's ruling, it would appear necessary for the Comptroller to broaden his ruling when such an offering is made.

The language of the ruling is quite loose and in some particulars is inaccurate. For instance, reference is made to the exemption of a project from local real estate taxes. At the present time 33 states have laws providing for the organization of public housing authorities. However, the laws of Illinois, Massachusetts and Montana, for example, do not exempt projects of local housing authorities from real property taxation.

I am told that the USHA is satisfied with the adequacy of the ruling for present purposes.

Herman Oliphant

Attachments - 2

to ... for review ... about ... Please ... comment

HO

TREASURY DEPARTMENT
Office of the Comptroller of the
Currency

April 15, 1938.

TO THE BANK ADDRESSED:

A question has arisen as to whether bonds, notes or debentures issued by public housing agencies under the provisions of the United States Housing Act of 1937, and representing the 10% local participation in the cost of low-rent housing or slum-clearance projects provided by the public housing agency, are "marketable obligations" within the meaning of that term as used in the seventh paragraph of Section 5136 of the Revised Statutes, as amended. A public housing agency is defined in the United States Housing Act of 1937 as any state, county, municipality or other governmental entity or public body (excluding the United States Housing Authority) which is authorized to engage in the development or administration of low-rent housing or slum-clearance projects.

In the Comptroller's regulations covering the purchase of investment securities, promulgated February 15, 1936, certain prerequisites are established for determining whether a given security is marketable. The bonds, notes, or debentures of the public housing agencies referred to in the United States Housing Act of 1937, differ from the usual type of investment securities provided for in the regulations, because of certain special features attaching thereto under the provisions of the said act.

The United States Housing Authority makes an annual contribution to the public housing agency to assist in maintaining the low-rent character of such project substantially adequate to assure the servicing and retiring of the bonds, notes and debentures issued by the said agency, which are held by local private interests. The United States Housing Authority purchases the notes, bonds or debentures issued in each such project in amounts up to 90% of the cost of acquisition and development of the project. The project is tax exempt under local law. The faith of the United States is pledged to the payment of all annual contributions contracted for pursuant to law, and there is authorized to be appropriated in each fiscal year out of any money in the Treasury not otherwise appropriated, the amounts necessary to provide for such payment.

In view of the above, it is the opinion of this office that the bonds, notes or debentures issued by public housing agencies, and representing the 10% local participation in the cost of such projects, are, by reason of the special features attaching thereto under the provisions of the United States Housing Act of 1937, "marketable obligations" within the meaning of that term as used in the seventh paragraph of Section 5136 of the Revised Statutes, as amended, and that the provisions of the Comptroller's regulations covering the purchase of investment securities, providing certain prerequisites for determining whether a given security is marketable, are not applicable to such bonds, notes or debentures.

Respectfully,

J. F. T. O'CONNOR,

Comptroller of the Currency.

TREASURY DEPARTMENT

COMPTROLLER OF THE CURRENCY

WASHINGTON

REGULATIONS GOVERNING THE PURCHASE OF INVESTMENT SECURITIES, AND FURTHER DEFINING THE TERM "INVESTMENT SECURITIES" AS USED IN SECTION 5136 OF THE REVISED STATUTES AS AMENDED BY THE "BANKING ACT OF 1935"

The business of buying and selling investment securities by national banks is governed by Paragraph Seventh of Section 5136 of the Revised Statutes of the United States, as amended by Section 308 of the "Banking Act of 1935", approved August 23, 1935, which paragraph now reads as follows:

"Seventh. To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this title. The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock: *Provided, That the association may purchase for its own account investment securities under such limitations and restrictions as the Comptroller of the Currency may by regulation prescribe.* In no event shall the total amount of the investment securities of any one obligor or maker, held by the association for its own account, exceed at any time 10 per centum of its capital stock actually paid in and unimpaired and 10 per centum of its unimpaired surplus fund, except that this limitation shall not require any association to dispose of any securities lawfully held by it on the date of the enactment of the Banking Act of 1935. *As used in this section the term 'investment securities' shall mean marketable obligations evidencing indebtedness of any person, copartnership, association, or corporation in the form of bonds, notes, and/or debentures, commonly known as investment securities, under such further definition of the term 'investment securities' as may by regulation be prescribed by the Comptroller of the Currency.* Except as hereinafter provided or otherwise permitted by law, nothing herein contained shall authorize the purchase by the association for its own account of any shares of stock of any corporation. The limitations and restrictions herein contained as to dealing in, underwriting and purchasing for its own account, investment securities shall not apply to obligations of the United States, or general obligations of any State or of any political subdivision thereof, or obligations issued under authority of the Federal Farm Loan Act, as amended, or issued by the Federal Home Loan Banks or the Home Owners' Loan Corporation, or obligations which are insured by the Federal Housing Administrator, pursuant to section 207 of the National Housing Act, if the debentures to be issued in payment of such insured obligations are guaranteed as to principal and interest by the United States: Provided, That in carrying on the business commonly known as the safe-deposit business the association shall not invest in the capital stock of a corporation organized under the law of any State to conduct a safe-deposit business in an amount in excess of 15 per centum of the capital stock of the association actually paid in and unimpaired and 15 per centum of its unimpaired surplus."

Section 9 of the Federal Reserve Act, as amended, provides in part as follows:

"State member banks shall be subject to the same limitations and conditions with respect to the purchasing, selling, underwriting, and holding of investment securities and stock as are applicable in the case of national banks under paragraph 'Seventh' of Section 5136 of the Revised Statutes, as amended."

SECTION I

By virtue of the authority vested in the Comptroller of the Currency by said Paragraph Seventh of Section 5136 of the Revised Statutes, the following regulation is promulgated, further defining the term "investment securities."

An obligation of indebtedness which may be purchased for its own account by a national bank or a State member bank of the Federal Reserve System, in order to come within the classification of "investment securities" within the meaning of the paragraph of Section 5136 above quoted, must be a marketable security as designated by the express language of said paragraph, and can be purchased for the bank's own account only under the limitations and restrictions provided in said paragraph and the provisions of these regulations.

Under ordinary circumstances the term "marketable" means that the security in question has such a market as to render sales at intrinsic values readily available.

In determining whether a given security is marketable, it must meet the following minimum requirements:

(a) That the issue be of a sufficiently large total to make marketability possible;

(b) (1) That a public distribution of the securities must have been provided for or made in a manner to protect or insure the marketability of the issue, or, in the alternative
(2) other existing securities of the issuer have such a public distribution as to protect or insure the marketability of the issue under consideration, and such issue must be registered under the provisions of the "Securities Act of 1933" as amended, unless it is exempt from registration under Section 3 thereof.

(c) That where the security is issued under a trust agreement, the agreement must provide for a trustee independent of the obligor, and such trustee must be a bank or trust company.

Particular attention is called to the statutory provision that the investment securities which may be purchased, must be "in the *form of bonds, notes, and/or debentures, commonly known as investment securities.*" If an obligation is in the *form of a security*, it must comply with these regulations as to "marketability" as a condition to the bank's right to invest therein.

Any such security which fails to comply with the law and these regulations, will not be deemed legally acquired, even though the bank considers the transaction as being a *loan* rather than a purchase of "investment securities", except where such security evidences real estate loans made pursuant to Section 24 of the Federal *Reserve* Act, (a) where the obligations actually represent an initial loan by the bank, or (b) where the obligations were purchased pursuant to said section, in which case the bank is required thereby to purchase the entire issue.

SECTION II

By virtue of the authority vested in the Comptroller of the Currency by said Paragraph Seventh of Section 5136 of the Revised Statutes, the following regulation is promulgated as to further limitations and restrictions on the purchase and sale of investment securities for the bank's own account, supplemental to the specific limitations and restrictions of the statute.

(1) Although the bank is permitted to purchase "investment securities" for its own account for purposes of investment under the provisions of R. S. 5136 and this regulation, the bank is not permitted otherwise to participate as a principal in the marketing of securities.

(2) The statutory limitation on the amount of the investment securities of any one obligor or maker which may be held by the bank, is to be determined on the basis of the par or face value of the securities, and not on their market value.

(3) The purchase of "investment securities" in which the investment characteristics are distinctly or predominantly speculative, or "investment securities" of a lower designated standard than those which are distinctly or predominantly speculative, is prohibited.* The purchase of securities which are in default, either as to principal or interest, is also prohibited.

(4) Purchase of an "investment security" at a price exceeding par is prohibited, unless the bank shall:

(a) Provide for the regular amortization of the premium paid, so that the premium shall be entirely extinguished at or before the maturity of the security and the security

* The terms employed herein may be found in recognized rating manuals, and where there is doubt as to the eligibility of a security for purchase, such eligibility must be supported by not less than two rating manuals.

(including premium) shall at no intervening date be carried at an amount in excess of that at which the obligor may legally redeem such security; or

(b) Set up a reserve account in order to amortize the premium, said account to be credited periodically with an amount not less than the amount required for amortization under (a) above.

(5) Purchase of securities convertible into stock at the option of the issuer is prohibited.

(6) As to purchases of securities under repurchase agreement, subject to the limitations and restrictions set forth in the law and these regulations:

(a) It is permissible for the bank to purchase "investment securities" from another under an agreement whereby the bank has an option or an absolute right to require the seller of the securities to repurchase them from the bank at a price stated or at a price subject to determination under the terms of the agreement, but in no case less than the market value at the time of repurchase.

(b) It is permissible for the bank to purchase "investment securities" from another under an agreement whereby the seller or a third party guarantees the bank against loss on resale of the securities.

(c) It is not permissible for the bank to purchase "investment securities" from another under an agreement whereby the seller reserves the absolute right or the option to repurchase said securities itself or through its nominee at a price stated or at a price subject to determination under the terms of the agreement, notwithstanding the fact that the bank may also, under such agreement, have the absolute right or option to compel the seller to repurchase the securities at a price stated or at a price subject to determination under the terms of the agreement.

(7) As to sales of securities under repurchase agreement,

(a) It is permissible for the bank to sell securities to another under an agreement whereby the bank has an option or an absolute right to repurchase the securities from the buyer at a price stated or at a price subject to determination under the terms of the agreement, but in no case in excess of the market value at the time of repurchase.

(b) It is not permissible for the bank to sell securities to another under an agreement whereby the purchaser reserves the absolute right or the option to require the bank to repurchase said securities at a price stated or at a price subject to determination under the terms of the agreement, notwithstanding the fact that the bank may also, under such agreement, have the option or absolute right to repurchase the securities from the buyer at a price stated or at a price subject to determination under the terms of the agreement.

In view of the fact that some banks may have bought or sold securities under a form of agreement above indicated as prohibited, the bank should either terminate or modify same so as to conform to these regulations, where such action may lawfully be taken. Existing agreements of the prohibited type must not be renewed.

EXCEPTION

(1) The restrictions and limitations of these regulations do not apply to securities acquired through foreclosure on collateral, or acquired in good faith by way of compromise of a doubtful claim or to avert an apprehended loss in connection with a debt previously contracted.

Signed and promulgated this 15th day of February, 1936.

J. F. T. O'CONNOR,
Comptroller.

MR. MORGENTHAU'S OFFICE TO-

Mr. Gibbons
Miss Roche
Mr. Taylor
Mr. Oliphant
Mr. Gaston
Mr. McReynolds

Mr. Allen
Mr. Anslinger
Mr. Bartelt
Mr. Batchelder
Mr. Bell
Mr. Berkshire
Mr. Birgfeld
Mr. Broughton
Mr. Bryan
Miss Chauncey
Miss Diamond
Mr. Graves
Mr. Greenberg
Mr. Haas
Mr. Hall
Adm. Hamlet
Mr. Hanna
Mr. Harlan
Mr. Harper
Mr. Heffelfinger
Mr. Helvering
Mr. Hester
Mr. Julian
Mr. Kilby
Mr. Lochhead
Miss Lonigan
Mr. Moran
Mr. Murphy
Mr. O'Connor
Miss O'Reilly
Adm. Peoples
Miss Reynolds
Mr. Rose
Mr. Ryan
Mr. Schoeneman
Mr. Sloan
Mr. Smith
Mr. Spangler
Miss Switzer
Mr. Thompson
Mr. Upham

~~Dr Haas~~ [illegible]
Dr White HDW

To read and return to Secretary's office pls.

CONFIDENTIAL

178

April [illegible], 1938.

9735

Dear Mr. Delano:

Thank you very much for your letter of April 12th, which encloses a copy of the confidential statement prepared by the Advisory Committee of the National Resources Committee. This is most interesting material and I am going to give it further careful study. I appreciate your sending it to me and can assure you that it will be held in complete confidence.

Sincerely,

Mr. Frederic A. Delano,
Vice-Chairman, National Resources Committee,
North Interior Building,
Washington, D. C.

GEF/dbs

7/6/38

Note: Two other charts were attached to the original; copies were not available.

April 12, 1938.

The Honorable,

The Secretary of the Treasury.

My dear Mr. Secretary:

During recent months the Advisory Committee of the National Resources Committee has had prepared a statement of practical suggestions regarding the Federal Government's policy toward the business situation in relation to the longer time national resources utilization. Its contents have been worked out through conferences principally with the members of a subcommittee which we set up entitled the Industrial Committee, but other experts in various Government agencies have also been consulted with relation to various individual proposals.

Growing unemployment is giving rise to vital needs which must be met by increased Government spending. The proposals herewith pertain to this necessity and address themselves to the end that this increased spending should be orderly and free as far as possible from small political aims, as effective as may be, and consistent with sound long-time policies and plans.

It is not surprising, in view of the number of persons involved and the wide-spread attempt to think through the problems of the present recession, that, one after another, similar proposals to those contained in our memorandum are appearing from various sources.

In view of your special interest in these matters, Chairman Ickes has authorized me to make available to you a copy of this confidential material. I sincerely hope you may find it useful as a presentation of various current proposals considered as a coordinated whole.

Sincerely yours,

Frederic A. Delano

Frederic A. Delano,
Vice-Chairman.

encl.

NATIONAL RESOURCES COMMITTEE
NORTH INTERIOR BUILDING
WASHINGTON

April 12, 1938.

The Honorable,

The Secretary of the Treasury.

My dear Mr. Secretary:

During recent months the Advisory Committee of the National Resources Committee has had prepared a statement of practical suggestions regarding the Federal Government's policy toward the business situation in relation to the longer time national resources utilization. Its contents have been worked out through conferences principally with the members of a subcommittee which we set up entitled the Industrial Committee, but other experts in various Government agencies have also been consulted with relation to various individual proposals.

Growing unemployment is giving rise to vital needs which must be met by increased Government spending. The proposals herewith pertain to this necessity and address themselves to the end that this increased spending should be orderly and free as far as possible from small political aims, as effective as may be, and consistent with sound long-time policies and plans.

It is not surprising, in view of the number of persons involved and the wide-spread attempt to think through the problems of the present recession, that, one after another, similar proposals to those contained in our memorandum are appearing from various sources.

In view of your special interest in these matters, Chairman Ickes has authorized me to make available to you a copy of this confidential material. I sincerely hope you may find it useful as a presentation of various current proposals considered as a coordinated whole.

Sincerely yours,

Frederic A. Delano,
Vice-Chairman.

Confidential

April 9, 1938

WHERE ARE WE?

I. The Economic Health of the Nation.

A sick national economy is still awaiting effective remedies. During this interim of observation, consultation, diagnosis and prescription the fever chart of the nation continues to be discouraging.

In February, 1938, the national income paid out was approximately $4,850 million. In June 1937 the national income paid out was $5,951 million. The decline was approximately 18.5 per cent. In February 1938 compensation of employees was $3,425 million. In June 1937 it was $3,895 millions. The decline was 12 percent.

Production indexes continue their sideward trend, failing to show the hoped-for seasonal increase. Employment indexes in manufacturing industries show a loss instead of the usual seasonal rise. Of particular significance is the decline of the employment index of durable goods from 75.9 in January to 73.3 in February. Non-durable goods rose from 89.6 in January to 91.8 in February. The combined index shows from January to February a decline from 82.5 to 82.2. Preliminary March estimates as of the 15th show a continuation of these trends with a small rise in non-durable goods and a sharp decrease in durable goods.

The figure of unemployment, though less reliable than the others noted, and the latest indications of numbers on relief confirm this picture. The number of WPA workers rises on account of the effort to care for those in need of work.

The patient's bedside chart is not encouraging. A general condition of anemia is complicated by a serious state of nerves. Antidotes have brought some relief. Other prescriptions long under consideration are still being mixed at the Federal apothecary. But the nervous condition must be attended to while the measures to restore the physical health are being administered.

II. Aromatic Spirits of Ammonia.

The ever-increasing human need and the necessity for correcting maladjustments in the industrial world have fathered several measures.

(1) $250 million for PWA. On April 2 about 2.44 million men were employed, an addition of 49 thousand over the increase of 38 thousand of the previous week. The schedule of expenditures from March 1, follows:

Month	Number of persons	Obligations
March	2.5 million (not reached)	$162 million
April	2.4	156
May	2.3	150
June	2.2	143

It is anticipated that within the next few days a maximum of 2.5 million persons on WPA will be reached.

During the last few weeks expenditures for WPA have fallen below official estimates, but these unused funds will doubtless be required to complete the existing WPA program.

While WPA funds are decreasing each month and will be exhausted by the end of June, it is expected that seasonal employment will care for the reductions until the beginning of the next fiscal year without resorting to forced layoffs. During that period the certification of eligibles will be rigidly regulated.

(2) $30 million have been made available for Rural Rehabilitation loans and grants (from funds previously earmarked for WPA). This money with other funds available was scheduled to be loaned roughly as follows:

February	$ 8-10 million
March	12-15
April	10-12

(About 75 percent of these loans will be recovered)

It should be pointed out that for the program of rural rehabilitation to be effective it is essential that funds be authorized not later than September 1, when applications are received. If that condition had prevailed last year, Farm Security claims that approximately $150 million could have been loaned constructively for rural rehabilitation. Since thousands of small farmers were not able to obtain aid when they needed it most they made other arrangements and were forced to pay unreasonable interest rates. For these reasons rural rehabilitation loans will fall approximately $5 million short of the $37 million available on February 1.

(3) Reopening of lending by RFC. More liberal loans to industry through the medium of the RFC now appear to be approaching reality. Both the House and the Senate have passed S. 3735.

It is hoped that this program may prove tbabe of genuine aid to small business. In view of the fact, however, that loans of this character were not available when needed most before the business break, it is doubtful if they will be an effective aid to business recovery until the tide is definitely on the upgrade once more.

On March 26 it was announced by the RFC that total authorizations to industry since the passage of the Amendment of June 19, 1934, authorizing industrial loans, to date have been about \$197 million to 2,377 industrial borrowers, and that banks participated in these loans to an additional amount of about \$10 million. Of these authorizations about \$67 million were cancelled or withdrawn. Disbursement have been about \$106 million and repayments about \$51 million. Industrial loans granted fall into the following amount classifications:

Size of loans	Percentage of total loans granted
$ 5,000 or less	17 percent
5,000 to $ 10,000	15
10,000 to 25,000	20
25,000 to 50,000	18
50,000 to 100,000	14
100,000 to 200,000	7
200,000 to 500,000	5
500,000 and over	1 (slightly more)

No estimate of the amount that may be loaned to business by the RFC is available, and it is not possible to predict how successful the program may be.

(4) Statement of price policy. Work by the price committee continues toward the objective of isolating the "too high" prices and their strategic significance. The first recommendations of the President's Price Committee were announced by the Secretary of the Treasury on March 31. The first of these concentrated the purchase of cement for the Federal

government in the hands of the Procurement Division, required that all bids be on the basis of f.o.b. plant, and provided for an open Government contract available to contractors on all work financed by any Federal funds, (public roads, etc.). The second provides mechanism for assuring that all construction work done on contract for the government shall be carried out without collusion between suppliers of material or suppliers of labor (subcontractors).

(5) Modification of gold sterilization policy. This was a signal that there was no intention to permit a tightening of the money market.

III. A Hypodermic? How Much?

The continuing need for action by government and business which will increase national production, income and purchasing power is readily admitted.

During 1934, 1935 and 1936 the net Federal government contribution to community expenditures averaged approximately $219 million a month. During 1937 this declined to an average of about $90 million a month and in February, 1938 was actually not over 4 ~~negative by $78~~ million (see chart attached). The size of income tax returns indicates that the contribution will continue to be negative unless increased spending is undertaken. Income tax return figures for the month of March closing as of March 29 were about $718 million, and for the corresponding period last year $695 million.

Any attempt to estimate the amount of money which the government should spend is a guess. However, monthly income paid out to employees declined from $3,895 millions in June (1937) to $3,415 millions in February, 1938 (Robert Nathan, Department of Commerce). This would indicate the need for a minimum increase of $480 million a month in national expenditures by business and government. The amount to be spent by the Federal government in order to produce the governmental share of this volume would depend on the methods used (i.e., direct relief, works program, PWA, etc.).

Extremely important in this consideration is the relationship of the net Federal contirbution to the national income from 1934 through 1937:

(Millions of dollars)

	1934	1935	1936	1937
(1) Increase in national income over previous yr	7.8	5.4	8.8	5.0
(2) Net Federal contribution	3.2	3.1	3.8	1.0
Ratio of (2):(1) percent	41	58	43	20

The average net monthly contribution in 1934 and 1935 was about $260 million a month. It appears fair to indicate that this net expenditure was a substantial factor in turning the tide.

If a monthly increase of only the "amount paid out to employees" ($480 million) is sought, the net Federal contribution would seem to fall some place between 58 percent and 20 percent of $480 million a month, i.e., $278 million and $96 million. The general magnitude of the problem is thus indicated, although this type of statistical inference does not present a strictly accurate picture. Yet it is fairly certain that if care is taken to spend wisely it will be difficult to spend too much.

IV. Professional Consultation.

While first aid has so far been the by-word and bruises have been annointed, the patient's general condition has required numerous consultations and many "cures" are being prescribed. Some of these doses are homeopathic but others are dangerous poison. It should be kept in mind that any emergency actions taken now or in the future should be so framed that they may be used in conjunction with more fundamental remedies.

Among the suggestions which can be taken seriously are found the following possible ways for increasing the needed expansion of purchasing power:

(1) Works Progress. Increase the proposed appropriation available after June 30 by $1,000 million.

(2) CCC. Amounts available for CCC should be increased to restore to its previous strength($10 million a month new funds.)

(3) Public Roads. Continue the expenditures authorized under the public roads program up to June 30, 1938, and in the fiscal year 1938-39.

(State purchases in this field should be coordinated with Federal government purchases to prevent any rise in the price of materials necessary for other public or private construction work. Control in the hands of the Bureau of Public Roads would make this practical. It should be noted that the open contracts provided by the Procurement Division's new regulations for the purchase of cement are the first step in this direction.)

(4) Tax Remission. To produce an expansion of purchasing power certain taxes which burden consumption particularly can be waived. Among these are the Federal taxes on gasoline and oil (roughly $20 million a month) and the taxes for Old Age Benefits (roughtly $30 million a month).

If either of these taxes are remitted the authority should be given to the President for reimposing them at a time when business activity shows definite signs of vitality.

If the Old Age tax is remitted all other administrative action under the Social Security Act should be continued, such as payroll reporting and maintenance of records.

Appropriations to the Old Age Account should also be made. Schedules have been drafted which provide for beginning payments on January 1, 1939 under the Old Age Insurance scheme. However, the Advisory Committee of the Social Security Board is still urging caution in making any change in the Social Security Act until further discussion has clarified necessary modifications. 195

Congressional action required.

(5) PWA. Immediate expansion of PWA should be authorized to stimulate construction activities.

Plans are available which could be put into operation within three months. Expenditures under these plans can be stepped up rapidly from $20 million a month to a peak of about $160 million a month in six months. (About half are Federal projects.) The expenditures drop off then at a rate of $20 million a month for six months and ultimately to zero at the end of two years. The total amount of dollar volume of new construction to be produced by this program is in the neighborhood of $1,600 million divided almost equally between Federal and non-Federal projects, - $800 million Federal, $360 million non-Federal, plus $440 million of local contributions. At present PWA activity has been rising slightly due to delayed contracts released as a result of court decisions.

Congressional action and appropriations necessary.

(Actions in this field could be made a nucleus around which price adjustments of materials can be centered. Also wherever long-time contracts are involved the program of yearly wages for workers on long employment could be tried out. This program needs to be watched carefully since there is some competition between it and a road-building program, as well as a housing program.)

(6) <u>Government Purchases.</u> Continue the program of "off-cycle" purchasing by Government agencies (including the Army)

which has already been stated as Government policy. Special attention should be paid to goods manufactured by industries with large amounts of unemployment. Furthermore, "right" prices should be insisted upon. (Volume of funds per month cannot be stated.)

Executive action only.

(7) Federal Administrative Expenditures. Maintain expenditures of Federal government departments.

(Any increased government program throws heavy demands on regular departments as well as emergency agencies. Cuts in the expenditures for the administrative agencies result in inefficient operation and are false economy. Furthermore, the performance of many activities by the regular agencies gets better work done than an equal expenditure for the same work by special WPA Federal projects.)

(8) Capital for Small Business. (See sec. (3), p. 5 above).

Until other business adjustments affecting prices and costs have taken place, probably not much immediate action can be taken in this field, but the mechanism provided would lay the foundation for future lending activity when an expansion has begun and there is pressure for the use of further capacity. Thus, a source of capital funds would be available which would increase production and tend to prevent price rises of finished goods.

(9) Railroads.

(a) Develop a government-financed equipment trust (100 percent 20-year loan with low interest rate for building of new railway rolling stock, such equipment to be made available to roads on the usual equipment trust basis conditioned on collateral agreements of retiring obsolete cars and keeping up the maintenance of way as well as of the equipment. The financing of these maintenance loans by government purchase of preferred stock of the railroads might be necessary.

(b) Work out more expeditious methods for reorganization and consolidation of railroads, for even if we cannot produce immediate results we should make progress in carrying out needed changes in corporate and physical structure. A government policy of "push and coax" will probably be necessary. Authority and methods to bring about consolidation and reorganization supplemented by Federal financial assistance should be devised. Government guarantee of consolidated bonds with lower interest rates would decrease present fixed overhead charges. Combined with the authority to compel consolidation such devices might prove helpful. Until some such steps are taken, little new investment can be expected.

If the ICC does not wish to assume the responsibility of such problems as are involved in loans for equipment, consolidation, reorganization of financial structure, bankruptcies, etc., a special committee with continuing authority for a period of years will be required with power to order action in these fields.

Further legislation.

(10) Housing.

(a) Waive requirements for local capital contributions to public housing projects for projects approved by U. S. Housing Authority within the first two years of the functioning of the Authority. (On April 7 loans to 13 cities throughout the country and in Hawaii were earmarked in the amount of $79,920,000 by the USHA, raising total commitments of that agency thus far to $255,466,000 for 67 communities in 18 States. This sum is more than half of the $500 million made available by the Wagner-Steagall bill).

(b) If new private home building is to materialize under the revised National Housing Act, effective action to reduce building costs must be taken. The alternative to lowered costs is a rise in rents which present purchasing power will not support. The Price Committee under the Secretary of the Treasury is now working specifically on this program.

An additional method for providing residential building funds will become available with the establishment of the working machinery of the new National Mortgage Association, a corporation formed to buy FHA guaranteed loans from lending agencies. Debentures against the mortgages will be issued and offered for public sale. It is hoped that the Association's activities will free funds of the lending agencies to spur private home building. If the total volume of urban residential construction maintains the pace of 1937, it will provide between 275,000 and 300,000 units with a dollar volume of $1 billion to $1.2 billion for the calendar year 1938. Of this volume large-scale undertakings under FHA guarantee probably will be about $100 million. Present indications are that the National Housing Act will provide some stimulant to private housing activities. (Breaking all previous records, the Federal Housing Administration transacted gross business in March substantially in excess of $100 million it was announced April 7. Included in this sum was $95,161,202 of home mortgages selected for appraisal, an increase of 40 percent over March, 1937. The upsurge of activity in the FHA is attributed by that agency to recent legislation insuring mortgages up to 90 percent of the value of homes costing $6 thousand or less.) The indexes of residential building (permits granted and contracts awarded) to date fail to support the indication of a large volume of residential construction. At present it seems probable that FHA is securing business formerly undertaken without mortgage guarantee.

(11) Public Utilities. Since the Supreme Court's decision in the Electric Bond and Share case, practically all of the utility companies have registered with the SEC. One-hundred percent registration is expected immediately. It is believed that this decision will clear the air for the utilities to go forward with short-time capital expenditures required to care for necessary upkeep and replacements.

(12) Merchant Marine. If the Maritime Commission can get reasonable bids on ships to be built some help is to be expected in this field. (Purchase of materials in this field competes with other proposed government activity in construction. Unless care is taken prices of materials can get badly "out of line".)

(13) Educational Activities. The report of the President's Committee indicates the following possibility of expanded Federal and State expenditures in this field:

Year	Expenditure
1938-39	$ 1,250,000
1939-40	72,000,000
1940-41	112,500,000
1941-42	142,000,000
1942-43	162,000,000
1943-44	182,000,000
1944-45	202,000,000

(14) Public Health. When a report is issued by the President's Interdepartmental Committee definite possibilities in this field will be indicated. Early estimates are that an emergency program in the public health field would require approximately $200 million. Of this, medical care for WPA workers, indigents, etc., would take about $75 million, and a building program of hospitals, water

supply system, sewage disposal plants and projects of that character would use approximately $100 million. The Committee met in Washington recently, but as yet no definite announcements have been made. The next conference of the group is scheduled for the first week in July.

V. The Government's Financial Health.

An examination of the status of the Budget and the National Balance Sheet is in point as concern is expressed continuously over the ability of the government to remain solvent.

(1) Asset Accounting. In studying the last four years an analysis of the government's expenditures and receipts presents ample evidence that the Federal over-all policy has been sound. It is important to note that "operating income" has been fairly close to "operating expense." The average citizen would feel less disturbed if he realized that capital assets offset against liabilities indicate a soundness that he has not been permitted to realize since the daily press has paraded the size of the "national debt."

(2) Continued Asset Accounting. In order that the government's accounts may show their real status, future public works expenditures might well be handled by a National Development Corporation with capital stock held by the government.

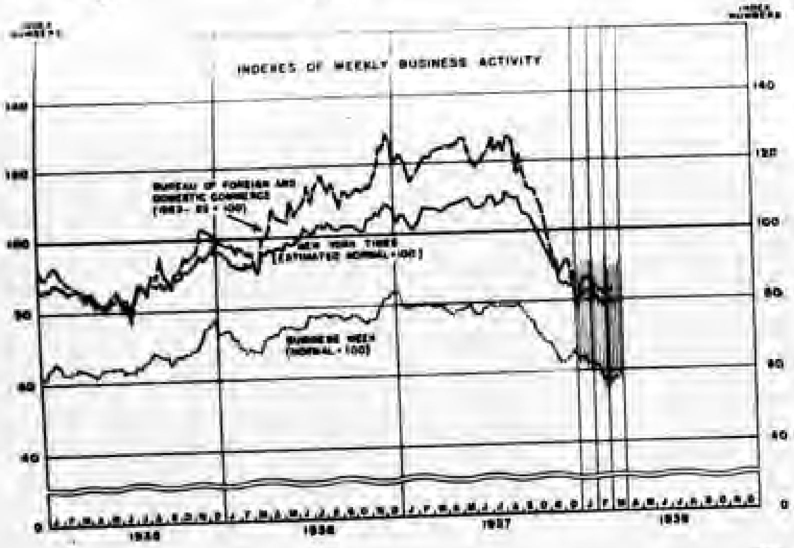
Such a corporation should have authority to develop plans on an engineering basis for long-run development. Congressional authorizations similar to those given for public road development, but with leeway for executive determination of allocation, would make possible proper timing in relation to the state of business. The corporation could have the authority to make loans to states with or without interest.

Such a corporation might well consolidate all funds now used for public works by the Federal government or those carrying authorization to negotiate with states for loan or grant of funds (such as the Flood Control Act of 1936, Housing Acts, public roads authorizations, etc.).

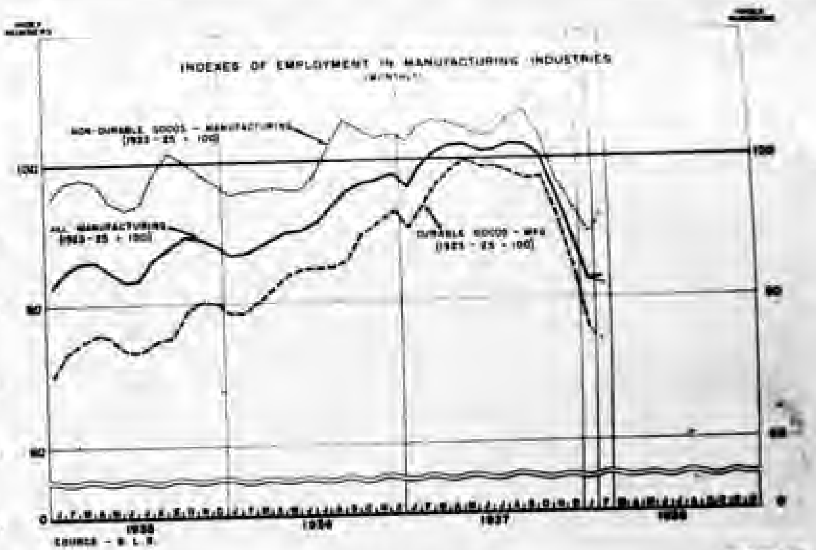
An additional function of such a corporation might be the advance acquisition of land in the states to be used for various public works such as rights-of-way, highways, housing in suburban areas, stream pollution control, flood control, public forests, etc. The principle of excess condemnation can be applied for the financing of this corporation.

Thus we look forward to a situation in which both the patient and the sponsoring government are healthy and look healthy.

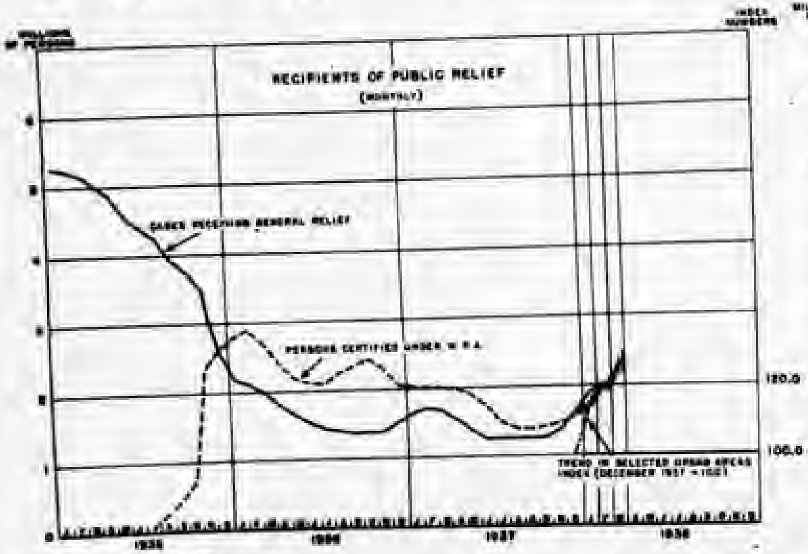
309



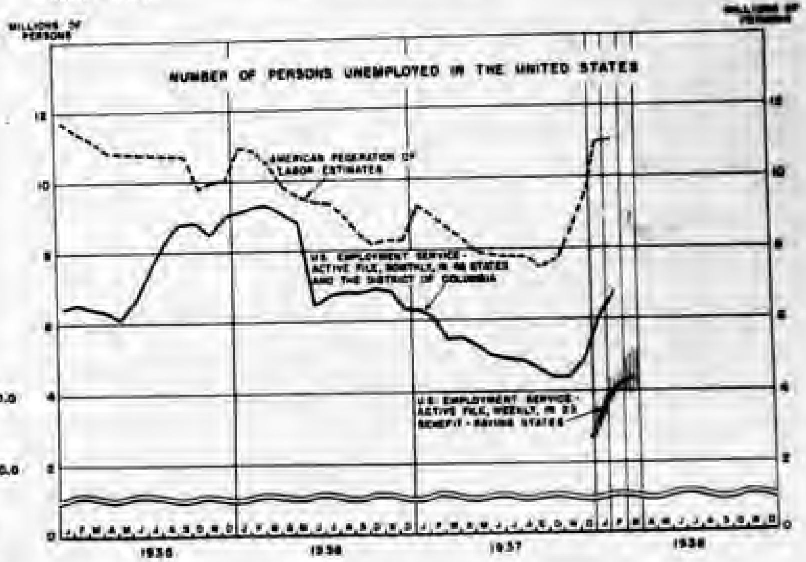
INDEXES OF WEEKLY BUSINESS ACTIVITY
BUREAU OF FOREIGN AND DOMESTIC COMMERCE (1923-25 = 100)
NEW YORK TIMES (ESTIMATED NORMAL = 100)
BUSINESS WEEK (NORMAL = 100)
1935
1936
1937
1938



INDEXES OF EMPLOYMENT IN MANUFACTURING INDUSTRIES
NON-DURABLE GOODS - MANUFACTURING (1923-25 = 100)
ALL MANUFACTURING (1923-25 = 100)
DURABLE GOODS - MFG (1923-25 = 100)
1935
1936
1937
1938
SOURCE - B.L.S.



RECIPIENTS OF PUBLIC RELIEF
(MONTHLY)
CASES RECEIVING GENERAL RELIEF
PERSONS CERTIFIED UNDER W.P.A.
TREND IN SELECTED URBAN AREAS INDEX (DECEMBER 1937 = 100)
120.0
100.0
1935
1936
1937
1938



MILLIONS OF PERSONS
NUMBER OF PERSONS UNEMPLOYED IN THE UNITED STATES
AMERICAN FEDERATION OF LABOR ESTIMATES
U.S. EMPLOYMENT SERVICE - ACTIVE FILE, MONTHLY, IN 48 STATES AND THE DISTRICT OF COLUMBIA
U.S. EMPLOYMENT SERVICE - ACTIVE FILE, WEEKLY, IN 23 BENEFIT-PAYING STATES
1935
1936
1937
1938

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 22, 1938, 11 a.m.

NO.: 631

RUSH.

FROM COCHRAN.

Reference my 629, April 21, 5 p.m., Paris press this morning reported official denials of rumors, (one) that there was a divergence of views within the cabinet and, (two) that France was contemplating borrowing abroad, yesterday's papers having suggested that Daladier and Bonnet were going to take up question of a loan on their London visit. Financial decrees which are now being prepared are expected during first days of May. Bonnet reported to have denied that any change in the tripartite monetary agreement was now envisaged the press having raised this question in connection with rumor of further devaluation of the dollar.

I had a talk with the Bank of France at 11 a.m.; with rate at 160 5/8, the market continues bidding for sterling; up to this time the control had yielded no exchange.

In the opinion of my market contact the movement is entirely speculative and is backed by a group of Paris traders who are very close to Minister Patenotre and Minister Reynaud. My friend told me that this morning it

is

is rumored in London that intimation might be given by Daladier and Bonnet to the British that there must be a further drop in the franc, and that an effort may be made by them to have the gold price in London raised.

WILSON.

EA:LWW

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 22, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE

FROM L. W. Knoke

I called Cariguel at 12:30 in connection with his cable #185 to point out that his buying order for francs against dollars figured out at 302 1/2 whereas his selling price for gold against francs figured out at 304.72. Was this correct? He replied that the figures were in order and that his gold price (under the Tripartite Agreement) was based on the thought that we might want to operate for our own account. I thanked him and made it clear that I had called up solely for the purpose to make sure that the figures had not been mutilated in transit.

He then asked me to hold on for a moment and after a few minutes requested me to consider his limit against dollars good for 10 million francs instead of 4 million as stipulated in his #185; also to note his order to buy unlimited amounts of francs at 165.38 (equivalent to 301 3/8).

I mentioned that I had just spoken to Mr. Beaulieu and understood from him that according to a telephone conversation he had had with Mr. Rueff in Paris all rumors about the further devaluation of the franc, French intentions to borrow abroad, etc., were entirely without foundation and that in all probability the French Government would make a statement to that effect before the day is over. Cariguel replied that that tallied with his understanding.

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 22, 1938.

TO CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE

FROM L. W. Knoke

- 2 -

P. S. I discussed this matter of operating against Cariguel's gold price with Mr. Lochhead and suggested that it would vitalize the Tripartite Agreement if from time to time, when the opportunity presented itself, we operated against these gold prices. I pointed out that as long as the French were carrying about 64 million dollars of gold with us it did not seem particularly risky to me for us to have some gold in Paris. I accordingly recommended that if, for instance, today the New York price for francs should drop below Cariguel's buying limit of 302 1/2 we should step into the market and buy francs for conversion into gold at Cariguel's selling price. Mr. Lochhead indicated that he was in complete accordance with this program.

LWK:KW

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 22, 1938.

TO CONFIDENTIAL FILES

FROM J. W. McKeon

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE

Cariguel called at 1:20 p.m. and asked how the franc was. I told him that we had purchased 1,000,000 francs at 302 3/8 net to him, but that the franc market appeared slightly firmer quoting 302 1/2 wanted, 303 offered. He seemed quite pleased with the firmness of the franc but requested that should the occasion arise during the afternoon that we would be forced to operate on the higher French cross rate, that is 165.38, to immediately call him at his home - telephone No. Carnot 4338.

EG

GRAY

Dated April 22, 1938

Rec'd 1:27 p.m.

Secretary of State,

Washington.

636, April 22, 4 p.m.

FROM COCHRAN

Reference my 631, April 22, 11 a.m.

Paris exchange market has continued nervous throughout the day but with no large turnover. Sterling rate had moved to 161½ by 4 p.m., apparently without any yielding of sterling by the French control to stop the weakening of the franc. Guaranty purchasing belgas for the French control on account of the fifty million belga requirement mentioned my 626, April 20, 5 p.m., and belga stronger today.

Press reports that Swiss and Dutch banks have granted a 3½% loan to the Argentine Government of 40,000,000 Swiss francs and 12,500,000 florins respectively, redeemable within two years in quarterly installments, proceeds destined for public works. (END SECTION ONE)

WILSON

WWC:HPD

PARAPHRASE OF SECTION 2 of telegram No. 636, April 22,
4 p.m. from Cochran at Paris

The above report was confirmed by President Trip of the Netherlands Bank at Amsterdam when I talked with him on the telephone this afternoon. President Trip told me that the head of the Dutch banking group was Mannheimer, and that this group contained the Netherlands Trading Company, the Amsterdam Bank and Pierson and Company, as well as others. He told me that he was glad his market has financed such an operation for twelve and one-half million florins, considering the plethora of gold and credit available on his market. Amsterdam itself was calm, he said, but the sudden turn in the French franc situation had caused the city to become perturbed.

I have received confidential information from Governor Rooth - and please do not repeat this information to New York - that yesterday he wrote to Governor Harrison saying that the Sverigesriks Bank, in view of recent political events, had decided to send some of its gold at present under earmark with the Bank of England to New York for the purpose of having it earmarked in New York for Swedish account. He said he expected that in the near future about five million pounds of such gold would be shipped to New York.

END MESSAGE.

WILSON.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, London, England

DATE: April 22, 1938, 8 p.m.

NO.: 335

RUSH.

FROM BUTTERWORTH.

FOR TREASURY. STRICTLY CONFIDENTIAL.

I saw Phillips today, on his initiative. He brought up the subjects of the developments in French and American affairs.

With respect to the French situation, Phillips said that the present movement bore all the earmarks of a breach of the Tripartite Agreement. He said he of course did not know what Marchandeau intended to do, nor could he say with certainty that there was truth in the rumor which was accepted by the market, i.e., that the French were deliberately depreciating the franc to 170-175 to the pound. However, it was a fact that no serious attempt to stop the movement had been made up to the present.

Phillips said that it was an arbitrary and unwarranted disturbance if the franc were being deliberately depreciated. The United States and Great Britain should in any case have been consulted about such a movement. In his own words, his remark was "we would have expected you to consult us in similar circumstances". His way of saying it reminded me of the impression which I reported in the first paragraph of my telegram No. 330 of the twenty-first of April.

My

My friend told me that prior to the starting of this rumor, the French stabilization fund had gained some £10,000,000. He added that elaborate calculations had been made by Hawtrey, leading him to say that around 155 was the equilibrium rate. Phillips reminded me that even in the pre-Poincaré period the franc had only dropped to 167, and then the market had been buying strongly.

I asked Phillips whether the British were going to do anything just now and whether he was approaching us in this regard. He told me that as yet they had not reached a decision for any action, but that in any contacts which he or Waley might have with the Assistant French Financial Attaché, LeNorcy, they would have this general attitude in mind. Phillips said that if Cochran would do the same it might be useful. He presumed that the British and American treasuries looked on the situation in much the same light, and he asked whether I had any information from Cochran or with regard to the reaction in Washington.

As for the developments in the United States; Phillips asked me again whether I could give him any information, as he did not have a clear idea of our actions or intentions from the sketchy reports he got from the newspapers. [Reference the first paragraph, my No. 330 of April twenty-first.] It seemed to him that decision had been reached

to

to increase excess reserves, which would make the investment problem of the banks difficult; he believed that at the same time Treasury Bills were to be paid off to restrict this outlet for investment.

Inquiry was also made by Phillips as to the truth of the report in the FINANCIAL TIMES of yesterday that Professor Viner had resigned his position as adviser to Secretary Morgenthau.

The franc closed at 164; it had opened at 159 1/2. Trading volume was not as great as would seem to be indicated by the movement. Impression on the market was that no instructions had been given the French stabilization fund with regard to support; the market expects the rate to have reached 175 by Monday.

KENNEDY.

EA:LWW

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 26, 1938.

TO CONFIDENTIAL FILES

FROM L. W. Knoke

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE

Mr. Cariguel called me just before 10 a. m. to inquire as to what was going on this morning. I told him that so far, to our knowledge, no foreign exchange business had been transacted yet, that francs were about 302 and sterling about 498 15/16, both rather on the bid side. I mentioned that so far there seemed to have been no official denial in Paris of the various rumors which had circulated in the last two days. Cariguel replied that he still thought there would be one. Meantime, he continued, they had done their best but had had rather a bad time this morning which had cost them about £300,000. I suggested that a denial would undoubtedly help the franc substantially and Cariguel replied that he would pass that on.

LWK:KW

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 23, 1938.

TO CONFIDENTIAL FILES

FROM L. W. Knoke

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE

Cariguel called again at 10:50. I told him that there was very little new to report except that sterling and francs were possibly a trifle easier, sterling at 498 3/4 and franc at 301 3/4 to 302 1/8. Cariguel thought we were practically through here but I told him that we had an hour and a half to go before closing.

Cariguel called a third time at 11:40 and asked what was going on. I replied that foreign exchange business was practically at a standstill; that I understood that probably not more than 2,000,000 francs had changed hands; and that francs at the moment were quoted at 302 to 302 1/4 and sterling at 498 13/16 and that we had done nothing.

LWK:KW

April 23, 1938.
11:03 a. m.

M. A. Harris: ..... lower but very quiet.

H.M.Jr: Yeah.

H: And the, ah, stock market ....

H.M.Jr: A little louder, Harris.

H: Ah, the stock market has eased off a little from the opening and is now irregular. The corporate bonds continued better this morning.

H.M.Jr: Good. Is that all?

H: Ah, that's all I have, unless you'd like my feeling on that, ah, Commodity Credit.

H.M.Jr: Go ahead.

H: Well, I'd lean toward one issue.

H.M.Jr: What?

H: I'd lean toward one issue.

H.M.Jr: Yeah.

H: And, ah, I think it can be done all right at three-eights and five-eights, but if you want to feel real sure about it maybe three-quarters if you do it all in one year is a better rate.

H.M.Jr: Uh-huh. Well, I'm going to talk to Burgess now and you can all listen.

H: All right, sir.

H.M.Jr: Let me talk to Lochhead a minute first.

A. Lochhead: Lochhead speaking.

H.M.Jr: Archie.

L: Yes.

H.M.Jr: You know, I've been thinking about what you and Taylor told me about all these cables coming in from Butterworth.

L: Yes.

H.M.Jr: And if you don't mind my saying, I think it, ah - you're partly at fault because some time ago I told you it's up to you to service both Butterworth and Cochran, and evidently you haven't been sending him any cables explaining what we've been doing.

L: Well, of course, in regard to this general policy that's why I took it up with you the other day when Butterworth's cable came in.

H.M.Jr: Yeah, but nobody had suggested to me that we should send him this stuff about the bills, the gold, and everything else.

L: Well, I thought that was all in the general line; that's when I brought the cable; I thought you'd decided you didn't want to do anything; you said it was all in the papers.

H.M.Jr: Well, nobody raised it - I mean the great trouble is - I mean, unless I take the initiative, nothing goes to those boys.

L: Well, on a question like that, we have been sending them, of course, just the general information that goes through - not the formal cables but just that general information - servicing them.

H.M.Jr: Well .....

L: Well, now, this particular thing about consultations under the Tripartite, I thought that you wanted to decide on that. That's why, as I said, I .....

H.M.Jr: No, I'm talking about giving them the information about what we've been doing. Evidently they don't get it. See?

L: Well you mean about as far as the, ah, the bill issue?

H.M.Jr: I mean, anything that we've been doing. Evidently we should have sent them a, a sort of a news summary.

L: Yes. Well, of course, the ah - the only other one we had to, ah, correspond with that was when - that last time when we, ah, decided on the desterilization of a hundred million.

H.M.Jr: Well, ah, I'd like to talk to you about it, and Taylor, on Monday .....

L; O.- O. K.

H.M.Jr: Frankly, I - I just can't supply the initiative of all - it - it's a physical impossibility.

L: Well, we'll be there - Mr. Taylor and me, and we'll discuss that fully on Monday then.

H.M.Jr: Yeah. I mean - after all, it's up to you fellows to ask me, and if I don't want to do it, why, then, ah - well, with White and everything there, I mean it's up to us to keep those fellows informed.

L: Yes. Well, as I say, as far as - I feel that we should be more fully informed than we have been. I - I just felt we were holding off on this last one.

H.M.Jr: I'm not talking about the Tripartite. I'm talking about action which we've taken here.

L; I see. Well, I think we'd better get - probably have a fuller understanding on that, and we can do it on Monday.

H.M.Jr: I put in a call for - for Cochran at twelve, and Butterworth at twelve-fifteen.

L: Ah, you've put in a call for Cochran at twelve, and Butterworth at twelve-fifteen.

H.M.Jr: Yeah. I'm going to talk to them from here.

L: I see. O. K. Well, then, in the meantime, Knoke tells me he spoke to Cariguel this morning.

H.M.Jr: Yeah.

L: And, ah, he reminded Cariguel that there was no statement came out in regard to, ah, to the cause for the rumors that have been around. Yesterday Cariguel mentioned that he thought there'd be a statement come out last night, and you remember Beaulieu also said that. Carigeul said that he thought there would be something coming out, but of course there's no word of any official statement denying any of these rumors yet.

H.M.Jr: No.

Lochhead: In the meantime the French franc is strong - a little bit stronger here, about \$.0302.

H.M.Jr: Well, would - I'd like to have Mr. Taylor do the following for me. Is he - is he listening?

Lochhead: Yes, sir. In fact, I'll put him right on.

H.M.Jr: All right. You making a record?

Lochhead: Yes, we're making a record of it.

H.M.Jr: Wayne?

Taylor: Yes.

H.M.Jr: If - if you would check with Mrs. Klotz to see that I'm free at 10:30 Monday, see? - hello?

Taylor: Yes.

H.M.Jr: If I am, about - between 10:30 and 11 I'd like to have a meeting at my office with my own people, plus George Harrison, plus Knoke, plus Professor Williams and Herbert Feis. And you can tell them what it's about; it's to discuss the French situation. Now will you please invite those people down?

T: I will.

H.M.Jr: See? And then we can sit around and talk the thing over.

T: 10:30 Monday.

H.M.Jr: If it's free. But Mrs. Klotz is in her office and you can check with her as to the time.

T: Right.

H.M.Jr: But I'd get word to them today. And then we can sit around and talk about it.

T: All right, fine.

H.M.Jr: And - ah - I'll ask the operator now to give me Burgess and you fellows can listen.

T: Right.

H.M.Jr: (Clicks instrument) Hello. (Clicks again) Hello.

Operator: Operator.

H.M.Jr: Give me Burgess in New York please.

Operator: All right. Just a minute.

H.M.Jr: And - Mrs. Spangler?

Operator: Yes, sir.

H.M.Jr: Let the people in my office listen.

Operator: All right.

(Long pause)

H.M.Jr: Hello. Hello.

(Pause)

I'm talking through the Treasury and Taylor's listening in in my office.

W.R. Burgess: Yes.

H.M.Jr: Can you hear me?

B: Very well, yes.

H.M.Jr: Now, would you like me to - would you give me your recommendations, please?

B: My recommendation is that you do it in one piece.

H.M.Jr: Yes.

B: 18 months, at three-quarters of one percent.

H.M.Jr: Well, why one piece, Randolph?

B: There - there are three reasons. The first is that it's - it's very cheap money, and it's good financing to put it out as long as 18 months. The second place is that an issue of 200 million will stand up much better in the market and be much more popular....

H.M.Jr: Uh-huh.

B: .... and better for future financing than a small issue in which trading is so limited.

H.M.Jr: I see.

B: A third reason is that we have a tremendous problem of allotment. There's going to be a big scramble for these things, and if we have two small issues we'll have to cut it up into such small pieces that there'll be no large lots around.

H.M.Jr: Uh-huh.

B: And that again will hinder future trading and will leave us unsatisfied customers.

H.M.Jr: Uh-huh.

B: But a single issue you can chop up into reasonable size units.

H.M.Jr: Uh-huh.

B: And it makes a better situation.

H.M.Jr: Randolph, three-quarters is not too sweet?

B: Three-quarters is sweet, but I think it's better to have it a little sweet.

H.M.Jr: How much is it too sweet?

B: You could get it out at five-eighths. It isn't more than an eighth too sweet.

H.M.Jr: What's that?

B: Ah - you could get it out at five-eighths.

H.M.Jr: Yes.

B: But I think it's wiser to do it a little generously. When you turn that into price, it doesn't amount to very much, you know.

H.M.Jr: I see.

B: It means only a premium of - of - well, less than a quarter of a point even if it goes very well.

H.M.Jr: Do you think there will be plenty of demand?

B: Oh, there'll be a very good demand, yes.

H.M.Jr: Well now, this time I'm going to take your advice a hundred percent.

B: (Laughs)

H.M.Jr: How's that?

B: That's fine, Henry.

H.M.Jr: Randolph!

B: Yes, sir.

H.M.Jr: I - somebody certainly handled that order for the Panama Pacific Steamship Company in about as crazy a manner as I ever heard.

B: Yes, that was a butchered job.

H.M.Jr: Well, doesn't the Government own Panama Pacific?

B: That's right, yes.

H.M.Jr: Well, I wonder who places their orders.

B: I'm sure I don't know.

H.M.Jr: Well, I'm certainly going to find out.

B: Well, I think that they had the old Government technique of always getting bids, you know.

H.M.Jr: What technique?

B: ...... much about bonds did it.

H.M.Jr: Well, there must be somebody responsible there.

B: There must be, yes.

H.M.Jr: Well now, Randolph, I'm going to talk to Jesse, then my own people, and Wayne will give you the final word.

B: Very good, Henry.

H.M.Jr: And I - I understand our own market is steadying off.

B: Yes. It's off a thirty-second or two and steady this morning.

H.M.Jr: Well, that's all right, isn't it?

B: I think that's splendid, yes.

H.M.Jr: Have you done anything?

B: Not a thing, no.

H.M.Jr: Uh-huh.

B: We did nothing yesterday, you know.

H.M.Jr: I thought, considering everything, the Treasury got a very good press on the announcement on the bills.

B: I thought it did too. I thought it got a very understanding press.

H.M.Jr: I - I was entirely satisfied.

B: Well, that's good.

H.M.Jr: Weren't you?

B:	Very much so, yes.
H.M.Jr:	And aren't you a little bit surprised that - how steady the Governments have been since then?
B:	Yes, I am a good deal. I think that our friends of the Panama Pacific had something to do with that.
H.M.Jr:	Well ....
B:	They helped, as a matter of fact.
H.M.Jr:	What?
B:	They helped us out in keeping the market under wraps.
H.M.Jr:	Yes.
B:	(Laughs)
H.M.Jr:	All right. Well, I'll tell Jesse we'll recommend two hundred at three-quarters.
B:	Very good.
H.M.Jr:	And if he agrees Taylor will give you the word.
B:	Very good.
H.M.Jr:	Thank you.
B:	Good.
H.M.Jr:	Good-bye.
Taylor:	That's his preference, Henry.
H.M.Jr:	Well - it is?
T:	Yes.
H.M.Jr:	Well, I'll just say hello to Jesse.
T:	Good.
H.M.Jr:	And if you have the 11 o'clock averages - would you get them and let me know what they are?

T: I've got them for you right here.

H.M.Jr: 11 o'clock?

T: Yes.

H.M.Jr: All right.

T: Industrials off 33/100.

H.M.Jr: Yes.

T: Rails 5/100. Utilities up 10/100.

H.M.Jr: Yes.

T: Volume, 230,000 shares.

H.M.Jr: And what - what are other bonds?

T: Other bonds, no print.

H.M.Jr: I see. Did you tell me what commodities were?

T: No. They're about as they opened.

H.M.Jr: O.K.

T: And wheat's off a little, corn as it opened, and cotton just about as it opened.

H.M.Jr: Are you leaning towards one issue?

T: Yes.

H.M.Jr: Three-quarters all right with you?

T: Yes, that's my choice definitely.

H.M.Jr: O.K. Now let's have Jesse.

T: All right.

H.M.Jr: (Clicks instrument)

Operator: Operator.

H.M.Jr: Mr. Jones.

Operator: All right.

(Long pause)

Go ahead. Go ahead.

H.M.Jr: Hello.

Jesse Jones: Hello, Henry.

H.M.Jr: Good morning.

J: How are you?

H.M.Jr: Fine. Wayne Taylor's on the phone in my office.

J: Yes.

H.M.Jr: I've just talked to Burgess and our own boys and they're all unanimous: 18 months, 200 million, three-quarters of one percent.

J: O.K.

H.M.Jr: Is that all right with you?

J: Perfect. I think it's fine.

H.M.Jr: Well, they said that it'll go over big.

J: Well ....

H.M.Jr: They could've made it five-eighths, but they don't think the first time it would pay to do that.

J: Well, I agree to that. I think it's better to be - give them - to give them the three-quarters.

H.M.Jr: And ....

J: That's cheap enough.

H.M.Jr: And you can use it for eighteen months?

J: Oh yes.

H.M.Jr: Well then, I'll tell Wayne to give them the high sign that that's all right with you.

J: All right, and we'll have our Board meeting right now - in a little while and authorize it.

H.M.Jr: And - all right, Jesse.

J: Nice and cool down here today.

H.M.Jr: Well, it is up here too.

J: All right. Well, look forward to seeing you soon.

H.M.Jr: I'll be back Monday morning.

J: All right, Henry.

H.M.Jr: Good-bye.

J: Good-bye.

Taylor: O.K.

H.M.Jr: Now, does anybody want to say anything to me?

(Short pause)

T: No. Jolly times.

H.M.Jr: What?

T: They wanted to say "jolly times" to you.

H.M.Jr: Is Gaston there?

T: Yes.

H.M.Jr: May I speak to him a minute?

Gaston: Hello.

H.M.Jr: Herbert.

G: Yes.

H.M.Jr: You might send me a copy of that article also to New York, care of my father.

Gaston: The one that I sent you.

H.M.Jr: This morning.

Gaston: Yes. In care of your father at New York.

H.M.Jr: Yes, with a special delivery.

G: Special delivery.

H.M.Jr: And if I don't get it ~~here~~, I'll get it there tomorrow night.

G: Very good. Yes. That's at the office in New York, or his home?

H.M.Jr: No, 1133 Fifth Avenue.

G: 1133 Fifth.

H.M.Jr: Yes.

G: Yes, all right.

H.M.Jr: And - everything else all right?

G: Everything else is quiet.

H.M.Jr: What are they doing on the Hill on the tax bill?

G: Well, you saw about the - I don't know just definitely what they are doing, but you saw about that conference agreement last night, didn't you?

H.M.Jr: Oh yes.

G: Yes.

H.M.Jr: Yes.

G: I just ...

H.M.Jr: It's a wonderful compromise. Hello?

G: Just a moment. Archie was just telling me that there was an early morning conference with the President by Harrison.

H.M.Jr: What?

G: Harrison saw the President early this morning.

H.M.Jr: I see.

G: Uh-huh.

H.M.Jr: Well, what I want to know - whose face got lifted?

G: (Laughs) Or whose face got saved?

H.M.Jr: Yes.

G: Yes.

H.M.Jr: Yes.

G: Wayne says that they tied for last place.

H.M.Jr: O.K.

G: I asked - I asked Ros this morning, as I saw him just a second in the hall - I asked him if - if he was all buttoned up, and he said no, he had nothing left to button.

H.M.Jr: Well, he's a - he ought to enjoy the Army's fate. They don't have any buttons.

G: Yes. Just a zipper.

H.M.Jr: Yes.

G: Yes.

H.M.Jr: O.K.

G: All right. G'Bye.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 23, 1938, noon

NO.: 641

RUSH

FROM COCHRAN.

This morning at half-past eleven I called at the Bank of France which as usual was closed to general business today although to compensate for the holiday last Monday other Paris banks were open.

To support the franc on Thursday, the French control gave up over 300,000,000 francs of foreign exchange. On the Paris market on Friday the control did not operate except to buy about 35,000,000 francs which were needed by French railways. In strictest confidence I have been told that the control authorities could not even locate Marchandeau, the Finance Minister until after four o'clock in the afternoon; consequently they went through the official market without any instructions from the Minister. The technician who drafted the telegraph order sent to the Federal Reserve Bank at New York did it entirely on his own responsibility; in drafting it he had in mind the French obligations under the Tripartite Agreement to provide a gold price.

This morning by twenty minutes of twelve the French control had yielded 300,000 pounds; the rate had been brought down to 165 3/4 from previous rate of 167. At the

the time I left the Bank of France sterling was still bid. I am told by a private operator that by 12 o'clock, at which time trading stopped, the rate had gone to 166.

I have been told by another market trader that this morning the market had been so demoralized that even a small order would move the rate so far that no operations had been attempted by his bank.

END SECTION ONE.

WILSON.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris

DATE: April 23, noon.

NO.: 641 (Section Two)

RUSH

That there is serious discord in the Cabinet continues to be the market gossip; also that the franc will open at around 175 on Monday and that Reynaud's and Patenotre's views are prevailing. I was told by my official friend that four Paris banks had made the heaviest sales of francs this week; these four banks were Lazard, Dreyfus, Seligmann and Le Hideux. Some of these banks have cabled to their associates on various foreign markets anticipating that the franc sterling rate will drop to 175 early next week.

When instructions were actually being given to sell sterling to the extent which I have indicated for this morning's operations, I was with my friend, who insists that no instructions have been given him with reference to what the franc rate will be on Monday. When I was at the Bank of France, Governor Fournier of that Bank was at the Ministry of Finance. My friend was informed this morning by his London contact that the weakness of the franc was causing certain unhappiness in British official

circles

circles, particularly on the part of Sir Frederick Phillips. Personally, he believes that this official of the Treasury had been anticipating a strong pound against the dollar, perhaps from 5.05 to 5.10 and was disappointed at the extent to which sterling has weakened with the franc instead of being strengthened against the dollar.

It is indicated by the press that preparations for the release next week of an announcement of an agreement between the Treasury and the Bank of France for further borrowing and for issue of the first tranche of national defense loan may be expedited. However, it does not seem probable that while the currency situation is so unsettled an attempt should be made to float a loan. (END MESSAGE)

WILSON

EA:EB

TELEGRAM SENT

MB

GRAY

April 23, 1938

10 a.m.

AMEMBASSY

LONDON (ENGLAND)

168.

FOR BUTTERWORTH.

Reference your No. 335, April 22. Secretary of the Treasury will telephone you on Monday morning, ten o'clock Washington Standard Time.

WELLES

(Acting)

(FL)

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 25, 1938, noon

NO.: 645

RUSH

FROM COCHRAN.

This morning at half-past eleven I called at the Bank of France. The French control by that hour had yielded 100,000 pounds. The rate had been brought from a little beyond 166 to 165.75 to the pound by that time. Therefore there was not as much pressure as there had been the last two days of the past week. Daladier's statement on Saturday, on the other hand, combined with the press report that the Government was speeding up its decisions on financial matters, had not been sufficient influence to bring about a market reverse.

Confidential information was given to me that one of the main features of the plans which are being studied today is that of imposing a 3 or 4 percent tax upon all payments with a view to raising a yearly amount of five or six billion francs. The expection of bank officials is that rather than have a good reaction, such a plan would have a bad effect. Daladier, it is said, is insisting that they should ask the British for a loan when he and Bonnet go to London this week, as an offset for the cooperation which

which it is believed will be requested of France by Great Britain. Attempt is being made by officials of the Bank of France and some Cabinet members to persuade Daladier not to seek assistance from abroad. However, he seems intent to carry out this plan, up to the present. Daladier believes that it would be reasonable for the equalization fund of Great Britain to purchase four or five billion francs and lend them to the French Government rather than take gold for the francs. What the reply of Chamberlain and Simon would be likely to give to such a request is anticipated by my Bank friends.

If the two plans which are outlined above are indicative of the kind of program being launched by the French Government, they do not give much promise as a counter attack against those speculators who anticipate a franc quoted at 175 to the pound and whose theories were very much strengthened by the Treasury's weak policy in the last part of last week in direction of the French control.

WILSON.

EA:LWW

~~243~~

REB

GRAY

Paris

Dated April 25,1938

Rec'd 2:07 p. m.

Secretary of State,

Washington.

RUSH

649, April 25, 6 p. m.

FROM COCHRAN.

When the Cabinet meeting ended at 12:30 today the following communique was issued:

"The meeting was devoted to a discussion of the ensemble of the economic reconstruction plan prepared by the President of the Council and which after an exchange of views between the members of the Government was unanimously approved.

The measures envisaged will be definitively ratified in a Council of Ministers this afternoon.

At the issue of this new government's discussion a detailed communique will make known the decisions taken."

At 1 p. m. Prime Minister Daladier issued a written declaration to the effect that the principal features of the plan involved: increase in French production, tax revision,

REB

2-#649, From Paris, Apr.25,6p.m.

revision, public works, credits for industry and ecommerce, facilities for tourists, et cetera, all to be carried out while maintaining the tripartite agreement and the defense of the franc, indispensable to the return of capital and to dishoarding. It was stated that this plan would be executed through decree laws to be submitted to the Council of Ministers for approval beginning from May 1, the first series whereof would be promulgated in the Journal Official of May 3.

At 6 p. m. there has not yet become available any report of this afternoon's Council meeting.

(END SECTION ONE)

WILSON

CSB

PARAPHRASE OF SECTION TWO, NO. 649 OF APRIL 25

FROM PARIS.

FROM COCHRAN.

I refer to my telegram No. 645 of April 25.

The Treasury, coincident with the above developments, instructed the French control to drive back the franc rate which, when I was at the Bank of France at half-past eleven, had been 165.75. By half-past four when I talked with the Bank, the rate was 160 3/4 to the pound. According to my friend it had not been costly to force the rate to this level, but in order to hold it the control was beginning to have to give sterling rather importantly. Strong rentes and French securities.

Up to the present the announcements which have been made add little to the statement on Saturday by Daladier; the market is therefore showing impatience with the delays in announcing definite measures. It is apparent that the recovery in the franc rate today has come most importantly from the control's intervention, in view of the foregoing. It is my own personal inclination that the Government is temporizing until it finds out whether its representatives succeed in getting financial assistance from the British this week.

END MESSAGE.

WILSON.

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 25, 1938, 3 p.m.

NO.: 647

STRICTLY CONFIDENTIAL.

At luncheon today I had a short talk with Marchandeau, who had just come from the meeting of the Cabinet which this afternoon will be followed a a meeting of the Council of Ministers.

Marchandeau told me that not until after the third of May would they announce the really important decrees. They had found it necessary to go slowly and be sure of the ground in working out these problems, and rumors in the press of dissension in the Cabinet would not stampede them into action which was hasty and ill-considered. Speculators, he said, had initiated these rumors and they were not true, and it was absurd to say that Reynaud with one or two other Cabinet members were demanding that a rate of 175 to the pound be established. Marchandeau remarked that no matter what Reynaud's ideas might have been as to a balanced franc, Reynaud was not the Finance Minister, but he was the Minister of Justice, and that he had accepted the latter post without making any condition as to what the Government's financial program should be. Another absurd rumor, he said, was that with the Government in office only two weeks, there had

had arisen in the Cabinet important divergencies of view among the members. Marchandeau said that he, as Minister of Finance, intended to defend the franc and with that end in view the stabilization fund had been intervening. Nevertheless, he also aimed to protect and build up the stabilization fund, and therefore he was obliged to make careful moves. He did not say anything about his own opinion as to what would be a sound rate for the franc.

The Finance Minister said that the main problem before the Government was to get an increase in production and that in order to bring this about, the Government intends to modify the forty-hour week in important branches of industry.

The denial of the stories concerning differences of opinion in the Cabinet regarding monetary policy does not entirely convince me - "There are too many prima donnas in the Government", as one well-informed person put it to me today.

END MESSAGE.

WILSON.

EA:LWW

April 25, 1938

3:05 pm

Present:

Mr. Bewley
Mr. Lochhead
Mrs. Klotz

HM,Jr: Mr. Bewley, the reason I asked you to come in was this. I will tell you what I know. As near as we can make out, on Friday and Saturday the Minister of Finance of France gave the Bank of France no rate.

Mr. Bewley: No rate?

HM,Jr: Gave no rate at which to buy and sell.

Mr. Bewley: Left them entirely to their own devices?

HM,Jr: Entirely. As a matter of fact, no one could find Mr. Marchandeau. He had gone to places unknown. The Bank of France checked with us three times to see if we knew anything during the day. It is unbelievable. The reason I am telling you this is, Sir Frederic Phillips is after Butterworth to find out. We didn't know anything. The Bank of France did not know anything and, as I say, they telephoned three times. Isn't that right?

Mr. Lochhead: They telephoned three times, Friday and Saturday. Cariguel did. He gave orders, but he seemed to be awfully uncertain of his orders and checked three times to find out if anything was going on in this market.

HM,Jr: Saturday, after Phillips sent for Butterworth to find out whether we knew anything, I got a little interested and I sent Cochran to see Marchandeau and he came out of Cabinet and saw him and my message was this: that under the Tripartite Agreement I at least would like to know what they were going to make the rates.

Mr. Bewley: Yes.

HM,Jr: And this idea that we have no rates is getting just a little bit out of bounds.

Mr. Bewley: Yes.

HM,Jr: But I don't know whether as a result of that or not, but they brought the franc back in terms of the pound.

Mr. Lochhead: 160.

HM,Jr: From 166 to 160.

Mr. Bewley: And it's 160 today?

HM,Jr: And they gave us very narrow points to workbetween.

Mr. Lochhead: Yes. They are supporting the franc at .0311 in this market today and selling at .0311¼, which is very narrow.

HM,Jr: And I imagine -- I don't know -- but pulling him out and saying I was upset and wanted to know where we were at, I imagine had some effect. As a result, they gave the bank a rate. I said, It's just impossible; you can't go on like this. Because you know, they always have given us a rate. Maybe they don't want to say what the range is going to be, but at least they have to give us a rate.

Mr. Bewley: Yes.

Mr. Lochhead: Of course the Bank of France did give us rates, but they did it entirely on their own and not under instructions from the Finance Minister. They did technically give us rates, but they apparently were on their own. The Bank of France had to handle it themselves without any instructions from the Finance Minister.

Mr. Bewley: When they give you a rate, does that mean the rate at which they will hold it or to operate?

HM,Jr: For the day only.

Mr. Bewley: But it would operate for the day. They don't alter it during the day? I did not know what the system was.

Mr. Lochhead: Once or twice, very seldom, they have made a slight alteration, but I would say in the vast majority of instances they give us a rate ....

Mr. Bewley: And it sticks for the day.

Mr. Lochhead: Yes.

Mr. Bewley: Of course, bradly speaking, their market is not open at the same time as yours, so it's a different problem.

HM,Jr: That's the way they do it with us. Today they have gotten out certain decrees which don't mean an awful lot.

Mr. Lochhead: No, it's more or less .....

HM,Jr: So I sent word would they please try and tell us as between -- not from day to day, but what are their objectives.

Mr. Bewley: Yes.

HM,Jr: And I am now putting that up to them tomorrow.

Mr. Bewley: I see.

HM,Jr: That I would like to know what their objectives are.

Mr. Bewley: Yes.

HM,Jr: I don't know whether I will get anything, but I thought we would let you know what little we did know.

Mr. Bewley: Thank you very much. I will pass that along to our people. I suppose they are in the same position.

HM,Jr: I understand they are. If they have anything to return in the way of information, I would be glad to get it.

Mr. Bewley: Yes; I will let them know.

HM,Jr: That's about the whole story.

Mr. Bewley: All right.

HM,Jr: But today the franc has been firm. Do you (Lochhead) think it has cost them much?

Mr. Lochhead: Apparently not an awful lot, but, for instance, in this market I thought we would get some hangover, but there is no interest in this market at all. I think it cost them the most in the first half hour this morning before talk of the decrees came out. As I say, I think they spent a couple of hundred pounds to start off and probably spent some more to bring it up, but not a great amount.

HM,Jr: The unfortunate thing, from their standpoint, up to Thursday night they were doing very well.

Mr. Bewley: Yes.

HM,Jr: And then suddenly something comes over them.

Mr. Bewley: Yes.

HM,Jr: Suddenly something comes over them. They were gaining quite nicely.

Mr. Bewley: Yes.

HM,Jr: But that's the first real thing I have had to tell you -- simply to tell you what we didn't know.

Mr. Bewley: Yes. Well, thank you. I will pass it on to my people and if I get anything I will pass it back to you.

HM,Jr: Would you please? Because until they get this thing settled, I imagine there will be difficulty.

oOo-oOo

HOLD FOR RELEASE HOLD FOR RELEASE HOLD FOR RELEASE

April 25, 1938

CONFIDENTIAL: To be held in STRICT CONFIDENCE and no portion, synopsis, or intimation to be published or given out until the READING of the President's Message has begun in the Senate or the House of Representatives. Extreme care must therefore be exercised to avoid premature publication.

STEPHEN EARLY
Secretary to the President

- -

TO THE CONGRESS OF THE UNITED STATES:

The Sixteenth Amendment to the Constitution of the United States, approved in 1913, expressly authorized the Congress "to lay and collect taxes on incomes, from whatever source derived." That is plain language. Fairly construed this language would seem to authorize taxation of income derived from state and municipal, as well as federal bonds, and also income derived from state and municipal as well as federal offices.

This seemingly obvious construction of the Sixteenth Amendment, however, was not followed in judicial decisions by the courts. Instead a policy of reciprocal tax immunity was read into the Sixteenth Amendment. This resulted in exempting the income from federal bonds from state taxation and exempting the income from State bonds from federal taxation.

Whatever advantages this reciprocal immunity may have had in the early days of this nation have long ago disappeared. Today it has created a vast reservoir of tax exempt securities in the hands of the very persons who equitably should not be relieved of taxes on their income. This reservoir now constitutes a serious menace to the fiscal systems of both the states and the nation because for years both the federal government and the states have come to rely increasingly upon graduated income taxes for their revenues.

Both the states and the nation are deprived of revenues which could be raised from those best able to supply them. Neither the federal government nor the states receive any adequate, compensating advantage for the reciprocal tax-immunity accorded to income derived from their respective obligations and offices.

A similar problem is created by the exemption from state or federal taxation of a great army of state and federal officers and employees. The number of persons on the pay rolls of both state and federal government has increased in recent years. Tax exemptions claimed by such officers and employees -- once an inequity of relatively slight importance -- has become a most serious defect in the fiscal systems of the States and the nation, for they rely increasingly upon graduated income taxes for their revenues.

It is difficult to defend today the continuation of either of these rapidly expanding areas of tax exemption. Fundamentally our tax laws are intended to apply to all citizens equally. That does not mean that the same rate of income tax should apply to the very rich man and to the very poor man. Long ago the United States, through the Congress, accepted the principle that citizens should pay in accordance with their ability to pay, and that identical tax rates on the rich and on the poor actually worked an injustice to the poor. Hence the origin of progressive surtaxes on personal income as the individual personal income increases.

Tax exemptions through the ownership of government securities of many kinds--federal, state and local--have operated against the fair or effective collection of progressive surtaxes. Indeed, I think it is fair to say that these exemptions have violated the spirit of the tax law itself by actually giving a greater advantage to those with large incomes than to those with small incomes.

Men with great means best able to assume business risks have been encouraged to lock up substantial portions of their funds in tax-exempt securities. Men with little means who should be encouraged to hold the secure obligations of the federal and state governments have been obliged to pay a relatively higher price for those securities than the very rich because the tax-immunity is of much less value to them than to those whose incomes fall in the higher brackets.

For more than twenty years Secretaries of the Treasury have reported to the Congress the growing evils of these tax exemptions. Economists generally have regarded them as wholly inconsistent with any rational system of progressive taxation.

Therefore, I lay before the Congress the statement that a fair and effective progressive income tax and a huge perpetual reserve of tax-exempt bonds cannot exist side by side.

The desirability of this recommendation has been apparent for some time but heretofore it has been assumed that the Congress was obliged to wait upon that cumbersome and uncertain remedy—a constitutional amendment--before taking action. Today, however, expressions in recent judicial opinions lead us to hope that the assumptions underlying these doctrines are being questioned by the court itself and that these tax immunities are not inexorable requirements under the Constitution itself but are the result of judicial decision. Therefore, it is not unreasonable to hope that judicial decision may find it possible to correct it. The doctrine was originally evolved out of a totally different set of economic circumstances from those which now exist. It is a familiar principle of law that decisions lose their binding force when the reasons supporting them no longer are pertinent.

I, therefore, recommend to the Congress that effective action be promptly taken to terminate these tax-exemptions for the future. The legislation should confer the same powers on the states with respect to the taxation of federal bonds hereafter issued as is granted to the federal government with respect to state and municipal bonds hereafter issued.

The same principles of just taxation apply to tax exemptions of official salaries. The federal government does not now levy income taxes on the hundreds of thousands of state, county and municipal employees. Nor do the states, under existing decisions, levy income taxes on the salaries of the hundreds of thousands of federal employees. Justice in a great democracy should treat those who earn their livelihood from government in the same way as it treats those who earn their livelihood in private employ.

I recommend, therefore, that the Congress enact legislation ending tax exemption on government salaries of all kinds, conferring powers on the states with respect to federal salaries and powers to the federal government with respect to state and local government salaries.

Such legislation can, I believe, be enacted by a short and simple statute. It would subject all future state and local bonds to existing federal taxes; and it would confer similar powers on states in relation to future federal issues.

At the same time, such a statute would subject state and local employees to existing federal income taxes; and confer on the states the equivalent power to tax the salaries of federal employees.

The ending of tax exemption, be it of government securities or of government salaries, is a matter, not of politics, but of principle.

FRANKLIN D. ROOSEVELT

THE WHITE HOUSE

April 25, 1938

EDA TELEGRAM SENT GRAY

April 25, 1938

6 p.m.

AMEMBASSY

LONDON (ENGLAND)

170.

FOR BUTTERWORTH FROM SECRETARY OF THE TREASURY.

Preliminary figures of subscriptions for $200,000,000 Commodity Credit Corporation 18 months 3/4 percent per annum notes guaranteed by the United States offered today indicate subscriptions at least seven times amount of offer.

WELLES
ACTING
HF

EA:LWW

SAME TO: Amembassy, Paris, France. For Cochran from Secretary of the Treasury as No. 236.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

250

DATE April 25, 1938.

TO Secretary Morgenthau

FROM Mr. Haas

Subject: The next move in the recovery program.

1. The recovery program as outlined by the President.

As we interpret the President's message to Congress, he does not consider legislative action to permit increased Government spending nor the two monetary moves designed to increase bank reserves as isolated measures to benefit business, but as essential parts of a general program for business recovery. Other parts of this program include F.H.A. loans for housing, R.F.C. loans to aid business, and various other measures already taken or to be taken.

In his message to Congress, the President says: "All the energies of Government and business must be directed to increasing the national income; to putting more people into private jobs; to giving security and the feeling of security to all people in all walks of life."

It would therefore seem that the success or failure of these recent measures in stimulating business cannot be considered separately, but that the success of the recovery program in its entirety must be thought of.

2. What will determine whether or not recovery measures are "taking hold"?

In determining whether or not the recovery program is "taking hold", consideration must be given to the usual lag between cause and effect in industrial trends, which may extend to several months. The huge bonus payments made in the summer of 1936, for example, seemed to have no appreciable effect upon industrial production until late in that year, but the upturn in production that eventually occurred was very sharp.

Evidence of its "taking hold" may be seen first in its effect on security prices and on sensitive commodity prices. This does not mean that such prices must rise continuously, however. A typical pattern in a rising market is a succession of strong upturns, each followed by declines of one-third to two-thirds of the previous rise. The action of the markets since it first became known that strong recovery moves were being planned has been within the limits of this pattern.

The next visible evidence of the program's "taking hold" should be seen in its effect on the volume of new orders for goods, materials, and equipment. There may be some lag, however, between the new orders and their actual effect in increasing business activity, since (1) the orders may represent precautionary buying, and call for delivery some time later; and (2) the earlier orders may be filled by reducing accumulated stocks rather than by increasing production.

In the present situation, a favorable reaction to the recovery measures is already evident from the rise in security and commodity prices, and an upturn in textile and steel orders. The trend of business activity, as represented by general business indexes, may not fully reflect these for several months, however, for the reasons above mentioned. The seasonal improvement in business which was in progress at the time of the recovery message may in the meantime be continued.

3. What to do in case recovery measures do not "take hold".

The recovery program, as we see it, is not to be a series of business stimulants, but a continuing program developed on a substantial foundation. The President states in his message to Congress that "I have set my hope, my aim, on stabilized recovery through a steady mounting of our citizens' income and our citizens' wealth."

To achieve this aim, the Administration must necessarily look beyond the short-time reactions of the speculative markets, and concentrate on the fundamentals of the business situation. In comparison with this, the success or failure of individual measures are of minor importance.

Among the fundamentals of the recovery program, the encouragement of private spending and lending is of vital importance. Private spending can accomplish results more quickly and at less cost than Government spending, since private concerns are already in business and each businessman knows where he can put money most profitably to work. Under any recovery program, the Government must eventually retire from the spending field in favor of private spending. The sooner this can be done, the less costly it will be to the Government.

Among the various methods which may be used to encourage private spending, a gradual rising price trend is most effective, and we believe most important in the present situation, where deflation has caused general industrial contraction. Rising prices create confidence in the business outlook, encourage more expansive lending policies, and lead to buying of goods, materials and equipment. All industry spends more freely when convinced that prices are going higher, agricultural incomes are increased, and farmer purchasing is stimulated. The business improvement in 1933 was led by an upturn in purchasing from the South brought on by an improvement in cotton prices.

In view of the importance of keeping prices on a gradually rising trend, we suggest that the President, at a suitable time, reiterate the statement on prices made in February, in which he mentioned that Government policy would be directed toward raising prices, and said: "Government policy must be directed toward reversing this deflationary trend. This does not mean that all prices should advance, nor that the rise should be rapid . . . . Our agricultural, industrial, housing and monetary programs have been and will be directed toward this end." Recent actions taken in furtherance of the price-raising program should be reviewed, and the intention expressed to continue directing Government policy toward bringing about a rising price trend.

A suitable occasion for such a statement might be in connection with any statement on monopolies, or in connection with the announcement of any plan for reducing steel prices.

<u>Opening of special avenues for private spending</u>

In addition to the broad field of encouraging private spending through raising commodity prices, work should be done in a number of special fields toward removing obstacles which now block a substantial volume of private spending and lending. The opening of these avenues for private spending would constitute strong price-raising influences, not only in a psychological way, but through making more effective on prices the increase in excess bank reserves recently created.

Among the special fields which appear promising in this respect, we call attention to the following:

(a) Work is now being done by a sub-committee of the interdepartmental price committee toward increasing the buying of steel products. An obstacle to this is the continued high level of steel prices. A reduction in steel prices, even though temporary, would undoubtedly increase steel buying, which is an important need in the present business situation.

(b) Further improvement in residential building could be brought about by a lowering of construction costs through (a) moving against costly rackets in the building industry; (b) eliminating inefficient labor practices which increase labor costs without adding to labor incomes. A sub-committee is also working on these problems.

(c) A large volume of potential spending exists in the utility field, which represents a continually growing industry now in need of new capital. Before the depression, utility issues made up the largest section of the new capital market. The present low interest rates, combined with accumulated capital needs, would tend to stimulate spending by the utility companies if the outlook for the industry could be clarified.

(d) The railroads provide an important source of private spending that is now largely unavailable, partly because of a fundamental declining trend in railroad transportation. The development of some plan for taking care of current financial problems of the railroads, plus a long-term program leading to an expectation that the railroad problem would eventually be solved in a practical way, would do much to increase spending in this field. This is one of our important problems, and efforts should continue to be directed toward its solution. An improvement in business would itself bring increased spending by the railroads.

(e) In the banking field, despite the existence of ample excess reserves, at least two factors restrict lending and investment policies and tend to nullify recent monetary measures. (1) The banks lack adequate capital funds. Unfortunately, the very low interest rates brought about by the existence of a large amount of excess reserves diminish the profitability of banking capital, and so make it difficult to secure an adequate supply of capital from private sources. A method might be worked out for improving the capital positions of banks. In Treasury financing, a concentration upon short-term securities, which are more readily absorbed by banks, would place less strain upon their capital structure. (2) Rigid bank examining policies tend to restrict loans. Banks would be encouraged to expand their loans to private industry by a uniform and more liberal examining system, in which attention is directed entirely to the real quality of loans, to the exclusion of any consideration as to whether or not they conform to a preconceived notion of the banking process (i.e., particularly the concept that bank loans should be "self-liquidating").

<u>Things to be avoided</u>

To increase the volume of private spending most effectively, certain things should be avoided:

(a) The fear of a revival of serious labor difficulties is an important threat to the full success of the recovery program, not only in restricting private investment in industry at the present time, but as a potential threat to the continuation of business recovery after the pump-priming program has been completed. An increase in strikes recently on a slight improvement in business, most of them unauthorized strikes, is taken as foreshadowing more serious troubles on any real business upturn. In his recent message to Congress, the President said: "Let every labor leader find not how work can be stopped, but how it can be made to proceed smoothly, continuously and fairly." Anything that might be done to lessen the threat of labor disturbances would tend to encourage industrial expansion.

(b) In the allotment of funds for W.P.A. projects, those which would have an anti-pump-priming effect should, if possible, be avoided. The allotment of money for building municipal power plants to duplicate existing facilities is an illustration of spending which might retard a much greater amount of spending by private utilities.

(c) Prices of finished products should be kept from going too high when business improves, since this would tend to curtail private spending. Continued effort should be directed toward setting up a permanent committee, similar to the one used by Great Britain, to bring all available influences to bear in preventing unjustified price increases.

(d) Everything possible should be done to encourage new corporate financing. The volume of new financing is greatly dependent upon the trend of the bond market, in which United States Government issues play an important part. Since a gradually rising trend of bond prices is most desirable for financing purposes, any sharp reaction in the Government bond market which might seriously curtail new financing should be carefully guarded against.

261

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 25, 1938

To Secretary Morgenthau

From M. A. Harris

A short review of the U. S. Government security market during the past week

A broad demand for Treasury bonds during the past week forced prices sharply higher with the entire list moving to new highs for the current year. With the exception of the three shortest issues, which were 6 to 10/32nds higher, individual gains ranged from 19/32nds to 28/32nds. The average price for those issues not due or callable in 8 years advanced to 105.72, which is 1 5/8 points above the level on April 13, the day previous to the President's message to Congress. The market was fairly active the first three days but as the System continued to sell bonds day to day advances were confined to small fractions. On Thursday prices advanced sharply, mainly on the belief that the Treasury would announce at the close of the day a program of retiring at least a part of their weekly bill maturity. Gains for the day ranged to 1/2 of a point. Prices continued to advance sharply in early trading Friday morning but in the afternoon and on Saturday some profit selling came into the market and prices drifted off from their highs in much quieter trading.

Volume of trading in the note market diminished as the week advanced and small price advances the first four days were partly offset by small losses the last two days. Demand was centered in the longer maturities and those issues maturing after 1939 advanced 1 to 7/32nds. The June 1938 notes declined 8/32nds and are now quoted 101 11/32nds bid, which is 30/32nds above a "no yield" basis. The September 1938 notes declined 6/32nds while other 1938 maturities and the 1939 maturities were practically unchanged. The main reason why the short term market last week remained relatively quiet in contrast to the sharp advance in bond prices appears to be because of the extremely low yields. It might be said that investors have been practically "frozen" out of the short term market. A positive yield cannot be obtained on any direct government security maturing within 1 year and 9 months and it is necessary to go beyond 5 years to obtain as much as 1%.

Corporate Bond Market

During the first three days of the past week industrial and public utility bonds were in fair demand while rails continued to lag. However, the warm reception accorded the $60,000,000 offering of Consolidated Edison Company 3 1/2% debentures on Thursday stimulated the market and brought a good demand into all sections of the market the latter part of the week. The net result was fairly substantial gains for the week. The changes in the various Moody bond averages for the period April 14 - 22 are given below:

Moody's AAA Bond Price Average

	Industrials	Rails	Utilities	Combined
Change from Apr. 14 through Apr. 22	+ 1.80	+ 1.29	+ 0.87	+ 1.43

Moody's BAA Bond Price Average

	Industrials	Rails	Utilities	Combined
Change from Apr. 14 through Apr. 22	+ 2.83	+ 0.89	+ 2.08	+ 1.66

Dealers' Portfolio

Holdings of direct government securities and guaranteed issues by dealers increased by $43,400,000 last week, as shown below. The day to day holding of bonds and notes is also shown.

(in millions of dollars)

	Holdings Apr. 16	Holdings Apr. 23	Change
Treasury bonds	37.8	49.3	+ 11.5
" notes (1 year)	34.4	36.3	+ 1.9
" " (1-5 years)	29.3	60.8	+ 31.5
" bills	18.4	3.9	- 14.5
H. O. L. C. bonds	6.3	14.5	+ 8.2
F. F. M. C. bonds	1.3	6.1	+ 4.8
	127.5	170.9	+ 43.4

Trend of dealers' position in bonds and notes during the past week:

	Bonds	Notes 1 yr.	Notes 1-5 yrs.
April 18	33.6	42.2	50.9
" 19	39.9	39.6	55.0
" 20	39.3	37.9	55.9
" 21	47.3	36.7	54.4
" 22	53.9	35.8	55.2
" 23	49.3	33.3	60.8

Treasury Accounts

The following transactions were executed in the New York market during the past week:

Purchases

$ 1,000,000 2 7/8% Treas. bonds of 1955/60 a/c Gov't. Life Insurance Fund

20,000 2 7/8% " " " a/c Secy. of Interior - Individual Indian Moneys

Sales

$ 1,000,000 3 1/4% Treas. bonds of 1943/45 a/c Civil Service Retirement & Disability Fund *

* Balance to be sold under authorization dated Jan. 11,1938- $13,695,050.

System Account

In the past calendar week, the System sold $63,638,000 various issues of Treasury bonds, replacing these sales with purchases of $28,714,000 Treasury notes and $34,924,000 Treasury bills. However, $43,060,000 of the total amount was reflected in the statement week ended last Wednesday, so that so far during the current statement week only $20,578,000 bonds have been sold and $12,734,000 Treasury notes and $7,844,000 Treasury bills have been purchased.

The only other transaction was the purchase of $35,816,000 various Treasury bills in replacement of a like par amount of bills maturing last Wednesday.

The various transactions since the President's message to Congress have resulted in the following changes in the total holdings of bills, notes and bonds by the System account:

	Present Holding	Increase (+) or decrease (-) in holdings from April 13th
Treasury Bills	$ 714,857,000	+ $ 97,121,000
" Notes	1,191,905,000	+ 31,214,000
" Bonds	657,253,000	- 128,335,000
	$2,564,015,000	

GROUP MEETING

April 25, 1938.
9:30 A. M.

Present: Mr. Oliphant
Mr. Gaston
Mr. Haas
Mr. Taylor
Mr. Lochhead
Mr. White
Mr. Bell
Mr. Upham
Mr. McReynolds
Mrs. Klotz

(Mr. Dietrich comes in, hands Mr. Lochhead an envelope, which Mr. Lochhead gives to Secretary.)

H.M.Jr: (To Mr. Dietrich) I recognize the fact that the hat is on means you just came in.

Dietrich: I just got here.

H.M.Jr: Otherwise, I wouldn't have guessed it.

Dietrich: (Leaves.)

H.M.Jr: I thought you people would be interested to know that I've invited Harry White to become a regular member of the 9:30 staff.

Klotz: Glad to meet you.

Oliphant: Going to make a speech?

H.M.Jr: Want to make a speech, Harry?

White: I think I've made so many, probably the best thing I can do is keep quiet.

H.M.Jr: Don't get many chances - better make it now.

Archie, read this, will you.

Lochhead: (Inaudible.)

H.M.Jr: Huh? Well, let me see. Yeah, I've read that. Let the boys see it's coming in.

(Nods to Mr. Oliphant.)

Oliphant: Nothing.

H.M.Jr: Somebody did a good job on the Pearson item - it must have been you.

Oliphant: It wasn't me.

McReynolds: His wife came home - he's been out of circulation.

H.M.Jr: Whose wife?

McReynolds: Herman's.

Oliphant: She's been down at the farm.

Upham: The sty was quite recognizable.

Oliphant: What?

H.M.Jr: Anyway, the Pearson item was very nice.

Klotz: (Inaudible question to H.M.Jr.)

H.M.Jr: Are you (Oliphant) following this Neblett case in Los Angeles? I'm giving this (clipping) to Irey at ten o'clock. I mean, are you having anybody follow it?

Oliphant: I'm not having anybody follow it; I've been noticing it along.

H.M.Jr: Will you have somebody follow it? I'm having Irey look into the income tax end of it. Why did they spend forty thousand dollars? Why was it necessary to spend forty thousand dollars for that purpose? See? That has nothing to do with the income tax, Herman.

Oliphant: Yes.

H.M.Jr: I'd like it fairly prompt. Here's the headlines. "Elliott tells Pustau ..." Pustau - isn't that a nice name? "..Talk of forty thousand dollars new Federal building 'deal.' Sent five thousand dollar note back." I'd get the original minutes - huh? This, I am going to give to Irey. But the fact that - I mean, they spent that much - Anything else, Herman?

Oliphant: House will consider the Independent Offices bill conference report today. And the Senate is still on Navy Construction.

H.M.Jr: Can you tell me, in what form the new Ickes Public Works bill is?

Oliphant: I'll ask this morning and ......

H.M.Jr: I'd like to know before I go to lunch, because at Cabinet the President said that he did not want it with Ickes making the grants and R. F. C. making the loans - I mean he didn't want to divide it entirely.

Bell: I think - I haven't seen it, but I do know that the Appropriation Committee has a copy of it, and it's an extension of the authority now existing, and increasing the amount of funds available to a million for loans and grants, separating it indefinitely into four fifty for grants and five fifty for loans.

H.M.Jr: My interest is this: I think we've demonstrated the correct way to sell securities for independent agencies the way we are doing it today, and if Mr. Ickes sells his bonds to Mr. Jones and Mr. Jones sells to the public - and all that, I think, is all wrong, and I think any agency, from now on, if they are going to be Government guaranteed, they should be done just the way we are doing it today. Give us complete control, and if the other agencies have not done a good job, the Treasury does, and that's where I'd like to see it done.

Oliphant: I can give you a half-page summary of that bill this morning.

H.M.Jr: That's my interest. We should have the sole authority of offering any securities for any agency - for the Government in their behalf.

Taylor: That is fully guaranteed.

H.M.Jr: That is fully guaranteed, yes.

Bell: Well, Ickes' aren't.

H.M.Jr: Are?

Bell: No. The matter of selling Ickes' bonds will be selling municipal and state bonds after he takes them under contract.

H.M.Jr: Are you sure? There was talk of him selling his own.

Bell: I think that is out.

H.M.Jr: If it's out I'm not interested, but as a divided authority between R. F. C. and Mr. Ickes, - doesn't concern me, but if they are going to be fully guaranteed, I wouldn't think about it.

Oliphant: You wouldn't have any large amount of bonds being thrown on the market at the same time.

H.M.Jr: If they don't sell anything in the first three weeks of June - never have any trouble. He never makes an offering without checking.

Oliphant: I'll give you a half-page summary of that.

Bell: After that's straightened out and we decide to put R. F. C. on its own feet in the matter of selling securities, I'd like to see that arrangement outlined in the President's letter, that whenever we sell any of Ickes' obligations, the proceeds come into the Treasury.

H.M.Jr: Dan, I admire you from the bottom of my heart. You still believe in fairness.

Oliphant: Santa Claus.

H.M.Jr: I'll go through it with you - enjoy it - sign the letter with you.

Bell: The letter has already been signed, and next year's budget has been built on that basis - of an understanding with Mr. Jones.

H.M.Jr: We have no budget for next year. I read the funny papers on Sunday.

Bell: I don't get over them until Monday.

H.M.Jr: But I'll go right along with you, travel right along by your side.

Bell: I think we ought to try it.

H.M.Jr: Oh sure, lots of fun.

As long as you have the floor, who knows who's the President of the Panama Pacific Steamship Company and who owns the stock in it?

Bell: (Nods "No.")

H.M.Jr: Lochhead, you get ahold of that?

Taylor: I talked to Jerry Land on Friday, I guess it was, trying to locate where these bonds could have come from.

H.M.Jr: Yeah.

Taylor: And he's putting a fellow on that.

H.M.Jr: I see.

Taylor: Yeah.

H.M.Jr: Well, it oughtn't to take more than a day.

Taylor: Well, it's - they were - apparently they were going to have a deal for construction of one kind of another with Panama Pacific, and that deal is temporarily off.

H.M.Jr: Do you know about this, Dan?

Bell: Yes. I heard about it Saturday.

H.M.Jr: Panama Pacific sold eleven million dollars worth of bonds on Friday. I want to know who gave that order. I want to know today. I want to know before I see the President. Will you tell Jerry Land that? I want to know before one o'clock.

Bell: You think it came from a Governmental agency?

H.M.Jr: Sold eleven million dollars. Do you know? Well, I'd just like to call up whoever the person is and present him with my compliments and tell him what I think of him - the way he handled this thing. Everybody's so free to criticize us. I'm going to tell him it's the first time that's been done since the Russian Government did that. It's only happened twice since I've been here. Once by the Russian Government and once by Panama Pacific. Will you tell Jerry?

Taylor: (Nods "Yes.")

H.M.Jr: Huh? Tell him, please. I'd like to find out. It's a swell way to sell Governments.

Herbert?

Gaston: I have nothing.

H.M.Jr: I haven't seen Saturday's article about one Jake Viner.

Gaston: In the Post?

H.M.Jr: Yeah. Will you shoot it in?

Gaston: Yes.

Taylor: Got an editorial in the Post this morning.

H.M.Jr: You people know I got the letter from Riefler resigning everything, including going to Geneva and everything - whole business. I'll just read a part of it.

"I have been trying to phrase a note to you that would convey at one and the same time a deep sense of that unhappiness together with my reasons therefore, my deep sympathy, affectionate admiration and respect for you, and my desire, under the new circumstances for relief from any official or semi-official responsibilities which I may have. I have decided finally to convey my reaction to the new program in the accompanying separate memorandum and to confine this note to more personal considerations."

He's resigned, everything included - Geneva thing, and everything. And as a result of which he was up at the conference Saturday there and didn't open his mouth. Didn't take any part in the discussion.

Oliphant: Which conference?

H.M.Jr: New Haven. But I would like to have the Viner thing.

Gaston: Yeah.

H.M.Jr: George?

Haas: I have a couple things.

H.M.Jr: I see you changed the position of your sun burn.

McReynolds: George and Herbert and I played golf Saturday and Sunday both.

Haas: I got the sun burn because the white sand reflects the sun more.

H.M.Jr: Being in the bunker most of the time?

(To Mrs. Klotz:) Say, where are all those nickels I won?

Klotz: They're in the safe.

Oliphant: She thinks we've gone too far in desterilizing now.

H.M.Jr: Ah, ...

Haas: I'll have that business statement in.

H.M.Jr: Anything else?

Haas: That's all.

H.M.Jr: (Nods to Mr. Taylor.)

Taylor: (Nods "No.")

H.M.Jr: Now, who makes the announcement about the books being closed, and how long do we give these fellows to turn the stuff in, and all that?

Taylor: We do - give them ....

H.M.Jr: We do? Four o'clock press conference?

Bell: Make it five. I think about four thirty we'll have a notice - about the same as the Governments.

H.M.Jr: I mean, when they ask me at four o'clock whether the books are closed.

Lochhead: Daylight saving time.

Gaston: Yes, and shall we have the Press Conference this afternoon at three o'clock on account of daylight saving time in New York?

H.M.Jr: I'm sorry. No. No, it's most inconvenient for me. I mean, it just spoils the whole afternoon. But just see that - I mean that the R. F. C. doesn't do both. They were all right on this. Check on this; if we are going to do it, let's us do it. I don't want Jones - I want Jones to keep out of this.

Taylor: He's out.

H.M.Jr: O. K. Well, will you see it flows to me, you people.

Gaston: Yes.

H.M.Jr: Burgess would know by now how it was received.

Taylor: I've got some preliminary stuff already.

H.M.Jr: (Over telephone:) Randolph Burgess.

Archie?

Lochhead: The franc has turned quite strong now. It's up to 3.10 from a low of 2.99 and a fraction, this morning.

H.M.Jr: I'm going to this meeting at ten-thirty .....

(Telephone rings. Conversation with Mr. Randolph Burgess at 9:46 a. m. follows:)

April 25, 1938.
9:46 a.m.

H.M.Jr: Hello.

Operator: Burgess. Go ahead.

H.M.Jr: Hello.

W.R. Burgess: Hello, Henry.

H.M.Jr: Can I buy five million of those Commodity notes?

B: Well, you can put in the subscription for them.

H.M.Jr: I see.

B: You probably won't get allotted more than five percent.

H.M.Jr: Well, haven't I any influence around here?

B: Not the slightest.

H.M.Jr: Not the slightest.

B: (Laughs)

H.M.Jr: Are they that good?

B: They're pretty good.

H.M.Jr: I see.

B: Oh yes, they're going to get a great big subscription.

H.M.Jr: The Street likes them.

B: Yes.

H.M.Jr: Uh-huh.

Ah - how are Governments today?

B: About the same as they were Saturday.

H.M.Jr: Uh-huh.

B: There's a lot of underlying strength there. They'll go up again.

H.M.Jr: Uh-huh. It's wonderful the way private business handles an 11 million dollar bond order, isn't it?

B: Yes.

H.M.Jr: What? If either you or I did it, we'd make the front page.

B: (Laughs)

H.M.Jr: What's the matter with those fellows?

B: I don't know, I'm sure. Well, they didn't do so badly, as a matter of fact, I don't think.

H.M.Jr: Well, I mean it's the craziest sort of ....

B: Oh, of course it is; it's perfectly insane.

H.M.Jr: Well, there's nothing like that since the Russian Government sold a million pounds sterling; that's the last time we had an order like that.

B: Yes, I think it was.

H.M.Jr: Yes.

B: Yes.

H.M.Jr: Well, I'm - I'm going to find - I'm finding out who it is, and I'm most likely going to talk to the president of the company.

B: I think that's a good idea.

H.M.Jr: Pay him my respects ...

B: (Laughs)

H.M.Jr: Mr. Franklin.

B: Well, he was a great help to us.

H.M.Jr: Yes.

B: This is the son, isn't it?

H.M.Jr: Excuse me?

B: This isn't the old man, is it? This is the son.

H.M.Jr: I - I - I don't know. We - we're having them find out who handles their money.

B: Yes, I see.

H.M.Jr: And the interesting thing is, as far as I've found out they have no use for it.

B: They just thought prices were high, is that right?

H.M.Jr: I don't know whether or not.

B: Well, that's right interesting.

H.M.Jr: Nothing you want to volunteer?

B: No, not a thing, except we're going to have a hard time keeping these subscriptions down, if that's a problem.

H.M.Jr: Well, you love to do that.

B: I know it; it's kind of fun. Don't you kind of like it?

H.M.Jr: Now ....

B: (Laughs)

H.M.Jr: Well, I mean I'd rather do that than scrape up some orders.

B: Why, sure, it looks like prosperity anyway.

H.M.Jr: That's right.

B: Glad to have something look prosperous.

H.M.Jr: That's right. All right.

B: All right, Henry.

H.M.Jr: Good-bye.

B: Good-bye.

H.M.Jr: Archie?

Lochhead: That's all. Just on the franc - that's the only thing we have so far.

H.M.Jr: Harry? You know we are meeting at ten thirty.

White: I didn't.

H.M.Jr: Well, I want ten-thirty - I want White, Lochhead, Taylor, and are the visitors here?

Lochhead: Mr. Knoke's here.

~~Taylor:~~ John Williams has had some appendix difficulty and he may not be able to be here. If the doctor - he said if the doctor says it's all right he will be.

H.M.Jr: And George ......

Taylor: George Harrison, I think, is coming.

Klotz: They are all coming with the exception .....

Gaston: I heard that Goldenweiser was taken suddenly ill Friday or Saturday.

H.M.Jr: Oh, I'm sorry. Will you (Mrs. Klotz) check on that. I'm very fond of him. And Mac told me today that Reynolds, over in Procurement has been very sick.

I started to talk to Mac about your organization (White's), you see, and within the next day or two you talk to him, and two things when you talk about it, I want you to think about. One: Possibility of bringing that boy back from Brazil, and two, inasmuch as Professor Buck has an office in the Chinese Government, the possibility of wiring him that if he has that he should take it but we will let him come back, report to us, and let him go, you see, as he's just interested in the salary. Now let him come back; we can talk to him. Maybe just send for him to come back, and say, "Well, if you can get a job with the Chinese Government..." - but let him come back.

White: With respect to Schmidt, I think it might be a good thing to move him. I wonder if you'd consider moving him somewhere else after he comes back for a while?

H.M.Jr: Well, how is he ....?

White: He's on the job, and he's improved, and doing well, I should say.

H.M.Jr: Send him down to the Argentine for a while?

White: Either there or Mexico. I think he ought to be moved.

H.M.Jr: Well, of course, the worse spot we've got is Mexico. Well, think it over.

White: Of course, he's been away sometime, and he's a young man, and possibly you might like to let him come back.

H.M.Jr: Think about it, and we'd like to have Buck come back and talk to him, and if he has a job, let him go back.

Dan?

Bell: I have nothing.

H.M.Jr: (Points to Mr. Upham.)

Upham: You want me to say a word now about this letter from the Pennsylvania Bankers Association?

H.M.Jr: Yeah. Yeah. Yeah, I just - I'll just sign it - you write a letter for me. I am not going to do it. I'm not going to talk at this time - very sorry. No, I thought it over; I'm not going to talk until I've got something really important to say. I don't - as much as I'd like to do it for Pat Boland.

Are you fellows getting started on the Comptroller's business - bank examinations?

Taylor: Two-thirty this afternoon.

H.M.Jr: With me tomorrow.

Taylor: Yeah.

H.M.Jr: (To Mrs. Klotz:) I don't sit in on it.

Did you put Smythe out?

Upham: Oh yes, he's over there this morning.

H.M.Jr: Incidentally, who did that Smathers bill? Smathers, is that it?

Upham: Smathers.

H.M.Jr: Who did that bill?

Upham: Well, (hesitatingly) I don't know.

McReynolds: I was wondering if he'd give you the same answer he gave me.

H.M.Jr: I am surprised. Did you go to church yesterday?

Upham: No.

H.M.Jr: Well, you better. (Laughter)

Upham: Well, just so you know when I'm lying it's all right.

H.M.Jr: Well, you want me to tell you who did it?

Upham: No.

H.M.Jr: All right.

Klotz: He's having a swell time.

H.M.Jr: Mac?

Taylor: Maybe Mac will tell us who did that.

McReynolds: I haven't anything to do with that. I've got nothing.

H.M.Jr: Huh?

McReynolds: I have nothing. I want to alibi George and Herbert if they get noisy. They were exposed to Hester playing golf yesterday and it might react. We had lots of fun - a nice day - did us lots of good.

H.M.Jr: All right.

mck
[illegible]

April 25, 1938

MEMORANDUM TO: Secretary Morgenthau

FROM: Herman Oliphant

The Procurement Division on April 14, 1938, issued an invitation to bid for 35,000 barrels of Sulfate-Resisting Portland Cement for the Bureau of Reclamation, Shoshone, Wyoming, project. The bids are to be opened on April 28. Although bids were invited at F.O.B. prices mill, the location of the project at which the cement is to be used is stated in the invitation.

The invitation was not submitted to the Legal Division prior to its issuance.

April 25, 1938

A meeting of the heads of the bank supervisory agencies was held in Mr. Taylor's office at 2:30 p.m. Those present were:

Treasury	Mr. Taylor Mr. Oliphant Mr. Murphy Mr. Upham
FDIC	Mr. Crowley Mr. Nichols Mr. Tucker Mr. Smyth
Federal Reserve	Mr. McKee Mr. Davis Mr. Paulger Mr. Leonard
Comptroller's Office	Mr. Diggs Mr. Folger Mr. Kelly

Mr. Taylor stated that this was a practice session for rubbing off the edges prior to a meeting on uniformity of bank examination with Secretary Morgenthau tomorrow. The immediate incentive for the present discussion is the statement in the message of the President that there should be a coordination of bank supervisory agencies. The purpose of this meeting, he said, is to find out the amount of coordination of examinations that can be accomplished without legislation. He suggested that it might be valuable to list the difficulties and see what might be done about them. He suggested that the situation be explored from the standpoint of credit shortage.

Mr. Crowley said that there were complaints about bank credit at the Roper conference of small business men. He asked to see the letters that came in from the small business men and was given a lot of excuses and when Roper was finally pinned down, only three or four letters out of the 5,000 made any reference to it. Mr. Crowley said that he told Roper the facts didn't warrant the emphasis that was placed on it in the press release, to which Mr. Roper replied that the press played it up unduly.

Mr. Crowley said that bank examination is primarily to protect depositors from loss but that bankers have used the examiners as a whipping post for many years. The credit reluctance grows out of (1) the shock of 1933; (2) the fact that bankers are living on service charges and security profits and are out of practice on loans and other ways of making money; and (3) the fact that bank examiners really were tough in 1934 and 1935 in reorganizing banks and that a lot of liquidation resulted from loans being thrown out of banks.

He expressed his willingness to enter into the spirit of the meeting and do anything possible that would bring about co-ordination but not to lower the standards of bank examination. He referred to the "lousy" examinations that were made prior to the FDIC.

Mr. Taylor referred to the criticisms of the "slow" classification of loans and the feeling that there was less necessity for it now that all bank assets are eligible for rediscount. He also referred to the rules with respect to marketable securities.

Mr. McKee suggested that Mr. Folger should give the background and history of the liberalization of bank examination which began under Comptroller Pole. Mr. Taylor interposed to say that he should proceed upon the assumption that everyone is against lowering standards. Mr. Folger said that by the means of instructions to examiners from time to time, there had been warnings against a too critical atttitude. He said that at the present time depreciation on Governments and high-grade general market obligations is being ignored. Mr. McKee asked what criticism there had been from the public, and Mr. Folger said he knew of very little although there had been some in Congressional hearings. He said that probably those who had lost money in bank failures were inclined to be critical of bank examiners.

Mr. Crowley said that if the general condition of a bank is bad, examiners should look closely at the bonds and slow paper of the bank and should not temporize with bad bank management. Mr. McKee said to give us something to shoot at he would say he thinks that the examinations have never been fair to general business or to the stockholder or in the public interest. There has been a dual type of examination of every institution, the classification of paper has been bad, and the appraisal of bonds has been bad. In depressions the depreciation in bond accounts has caused a deepening of the depression and calling of loans. He asked why bonds should be criticised and not notes. He thinks all assets should be treated alike. Mr. Paulger said that the exceptions in the loan portfolio are treated in the examination but all bonds are listed and their market price given. He feels this is bad. Mr. Crowley said there should be little criticism of a well-managed bank but when a bank is in and out of the market, if you let them have the profit on the up side, you shouldn't excuse depreciation on the down side.

Mr. McKee said that if it is a good bank, he doesn't care what they do with the non-recurring profit. Mr. Nichols referred to a bank with $2½ million of deposits that had had a $33 million turnover in their portfolio in eleven months and having at one time borrowed $600,000 for the purpose. Mr. Folger referred to Arthur Brown of Indianapolis as an illustration of how the Comptroller's Office bears down on bankers who speculate in Government bonds. Mr. Diggs said we were getting into shades of meanings of words and said that he favored sitting down and working out a program on slow classification and a uniform program on bond depreciation, the latter on a basis of "damn the ticker." He thought the whole thing should be handled quietly without any ballyhoo. Mr. Crowley said too that he thinks a public statement would be harmful.

Mr. Diggs asked what the opinion was as to whether there should be a slow column or whether it should have some other name. Mr. Davis said it ought to be done away with. Mr. McKee said the bank should be told about slow loans but they should not be tabulated. There should be no aggregate and no total but should merely be listed for special attention.

Mr. Folger said that whereas in 1934 twenty per cent of the loans made by national banks were listed in the slow column, following the change in instructions to examiners that were sent out after the Morgenthau conference of bank examiners, that percentage had declined by the last half of 1937 to less than ten per cent. At this point Mr. Crowley asked Mr. Tucker to read the attached letter from him to Marriner Eccles with respect to slow classifications.

Mr. McKee expressed the view that time was being wasted over one word. He would stress the type of examination and how to protect the public interest if the type of examination is varied. Mr. Crowley said there was no difference of opinion on that but that good loans ought to be taken out of the slow column. Mr. McKee renewed his suggestion that the slow column be eliminated and data concerning it be included in the confidential section. Mr. Paulger said that bankers object to the recapitulation of slow, doubtful and loss. He said that (no-kidding) examiners put too much in the slow column. He suggested that the three chiefs get together and stated that there is no disagreement in principle. Mr. McKee said it depended on the opinion of the examiners whether a loan is slow or not. Mr. Taylor asked how about changing the name of the column and suggested that the word "slow" is not useful. Mr. Diggs thought it useful and said that it is the examiners who criticize and thus give the impression that it is a bad loan whereas they have other instructions.

Mr. McKee said that every examiner is tougher than the last one in order to make a record and that every examiner is tough because he doesn't want to be shown up by the next examiner. Mr. Folger said for that reason it is well not to change examiners too often. Mr. McKee said that every board of directors is scared to death until they have cleared up all their slow loans. Mr. Taylor said there still seems to be some disagreement on the slow column but since no decisions are to be reached today, we might go on to bond classifications. He asked Mr. Folger to tell about that.

Mr. Folger said that under Section 5136 of the Revised Statutes national banks can buy all marketable securities. There are too many low-grade securities in banks. The national bank examiners have not been charging off depreciation except defaulted issues, and in recent years have not been showing depreciation in first-grade bonds. No write-up of appreciation is permitted. Depreciation on bonds is included in arriving at net sound capital. He has proposed that depreciation on the first three highest rated bonds and all Governments be eliminated in arriving at net sound capital.

Mr. Davis said he could see no reason for treating bonds differently from loans. He said that you might class a company loan as good and yet criticise its bond because of the market price. Mr. Upham advanced the view that since there is a market price on bonds and no market price on loans, perhaps there is some realism to taking the market price on the asset for which there is a market price.

Mr. Crowley remarked that after all securities are a secondary reserve and are supposed to be used before loans are gone into. At this point Mr. Crowley asked Mr. Tucker to read the position taken by the Corporation on treatment of bonds.

Mr. Folger read instructions which he has proposed to be sent to national bank examiners.

Mr. Crowley and Mr. Davis thought profits on sales of securities should be segregated in a special account and not used for dividends. Mr. Crowley said that the bankers have been living on bond profits and service charges and have gotten soft and won't make any loans. Mr. Tucker said that any other rule than segregation of bank profits encourages bank speculation. Mr. Folger said he doesn't see how you can tell a bank what to do with individual profits. He said the in and outers should be dealt with and anything beyond that goes pretty far.

Mr. McKee spoke for the building up of a reserve of 20 per cent of corporate issues. Mr. Crowley said he opposes any liberalization of bank examination because he feels the bank examiners have not been strict enough.

Mr. Folger asked Mr. McKee if the Federal Reserve banks would disregard the market price on bonds when they are offered as collateral.

Mr. Crowley made the point that there really is no duplication of bank examination.

February 9, 1938

Dear Harriman:

From time to time during the past few years members of the staff of the Corporation have urged in conversations with representatives of the other Federal bank supervisory agencies that the "Slow" classification category in bank examinations be renamed. These conversations have revealed a general willingness to make the necessary changes in terminology. The Corporation has postponed altering on its own account the caption of the Slow column and has not, as yet, contacted the several State Banking Authorities, since an agreement on this question between the Board of Governors, the Comptroller's Office and ourselves is greatly to be desired.

The instructions of the three Federal agencies to their examiners as to the type of loan which should be classified as Slow are believed satisfactory, although these instructions should perhaps be reiterated. The real difficulty is that the word "Slow" is neither accurate nor descriptive of the loans which the instructions indicate should be so classified. Somewhat as a result of this ambiguity in terminology, there has been an apparent tendency upon the part of some examiners to criticize, by including in the Slow column, loans sound as to ultimate repayment although not immediately collectible. Such a tendency may have a deflationary effect on the credit structure and therefore is undesirable. Until this inconsistency between the title of the column and its real purpose is finally and unequivocally cleared up, this tendency is likely to persist and confusion to continue in the minds of both examiners and bankers as to the actual significance of the Slow category.

The Slow column originated as a definite classification in national bank examinations during the Comptrollership of John Skelton Williams at which time the theory that commercial banks should make only self-liquidating seasonal loans was widely held. It was probably intended when the column was inaugurated that inclusion of a loan in the Slow column would be determined in large measure by whether the loan conformed to the tenets of that theory. Strict application of that principal, however, has never been feasible, since it would have necessitated the Slow classification of a large percentage of all loans in commercial banks.

Nevertheless, the self-liquidating loan theory, if not applicable to the letter, was until 1934 an important coloring influence in the use of the Slow category. The result of this influence was that prior to 1934 the column served for the inclusion of two rather separate and distinct types of loans: (1) loans which were Slow in a technical sense but which were nonetheless intrinsically sound and collectible, and (2) loans concerning which there was some question as to the ultimate repayment. At the Examiners' Conference of 1934 called by Secretary Morgenthau, the column was defined to exclude loans of the first type and to include only those of the second; that is, only loans which had unfavorable or criticizable characteristics which, unless corrected and the loan placed in proper bankable shape, might lead to an eventual loss. With the findings of this Conference, the Corporation was and is in agreement, and the Corporation's examiners have been instructed accordingly.

The fundamental characteristic, therefore, of loans which should be classified in the Slow column is not their slowness in a literal sense but whether they are of satisfactory quality as credit risks. Resultingly there exists an unfortunate inconsistency between the caption of the column and what it is to include. We believe the work of the Conference should be followed through, and the title of the column changed to "Substandard Quality for Bank Investment" or to "Unsatisfactory for Bank Investment" or to a similar expression.

It also should be mentioned that if the Slow column were appropriately named, its general usefulness would be greatly enhanced. While at present loans of unsatisfactory credit quality and other real estate, not classified as Doubtful or Loss, may be included in the Slow column, there is no place in the examiner's summary of criticized assets for the inclusion of substandard securities. If the emphasis of the caption of the Slow column were upon the quality of assets or upon their general desirability as bank holdings, securities of inferior grade could be included. The present word "Slow" precludes such inclusion, since many issues of a substandard character are marketable under certain circumstances. Altering the caption of the column would, therefore, permit recapitulation in examination reports of all assets, not Doubtful or Loss, which are unsatisfactory for banks.

In any case we believe the word "Slow" should be abandoned and the present confusion eliminated. In our opinion such a step would be in harmony with policies of the Board of Governors with respect to the broad monetary and credit needs of the nation.

Yours sincerely,

LEO T. CROWLEY
Chairman

Marriner S. Eccles, Chairman
Board of Governors of the Federal Reserve System,
Washington, D. C.

POLICY OF SECURITIES VALUATION BY BANK EXAMINERS

Endorsed by the Executive Committee of the National Association of Supervisors of State Banks, April 5, 1938

I. A sound policy for valuing securities held by banks should accomplish the following:

1. Discourage speculative in and out trading;

2. Encourage purchase of only high grade securities for investment purposes;

3. Induce the write-down and gradual disposal of presently held securities of inferior grade;

4. Provide for segregation of all profits on securities sold in a special liability or valuation account;

5. Provide for an amortization program with respect to securities purchased at a premium.

6. Provide a valuation method which is equitable regardless of market fluctuations.

II. A bond valuation policy which places chief reliance on market quotations is unsatisfactory.

1. Speculative trading in bonds is encouraged.

   a. Bankers holding high grade securities as investments are penalized in times of low market prices and by inference are criticized for not having sold their holdings when apparent profits could have been realized.

   b. The banking system as a whole cannot successfully speculate in the bond market since, for the most part, one bank's sales are another bank's purchases.

2. Certain injustices result at present because of different appraisal treatment of bonds as compared with loans and real estate. In times of low bond prices, banks with mediocre loans or large real estate holdings appear in a more favorable light than banks holding relatively large portfolios of high grade bonds. In times of high bond prices, the banks with large bond portfolios appear in an unduly favorable light.

2. The amount of securities held by insured banks is approximately three times their capital. Consequently a rise of 5 percent in the bond market appears to result in a 15 percent increase in net capital. Conversely, a decline of 5 percent appears to decrease net capital by 15 percent. Therefore, the conclusions of bank supervisors as to the net capital of the banks are largely dominated by the state of the bond market. Under present practice, the banks can trade their securities when the market rises 5 percent, giving the impression of a 15 percent profit on capital, while when the market falls 5 percent we attempt to get the banks to take a loss at the rate of 15 percent on capital.

III. It is unanimously recommended by the Executive Committee that, effective immediately and until further notice, the following rules for bond valuation shall apply to examination of banks by examiners of State Supervisory Authorities:

1. Securities of the three highest credit ratings and other securities of equivalent credit status:

   a. Market price is to be ignored;

   b. Valuation is to be at cost. (By "cost", wherever used in this memorandum, is meant "cost less amortization or book, whichever is lower.")

2. Securities of the fourth highest credit rating, unrated securities of equivalent credit status and Group II securities shall be priced at market, but for net balance sheet purposes, shall be valued at cost.

   a. Market price of this class of securities will appear in the report as a memorandum item but will not be taken into consideration in computing net sound capital nor in computing estimated loss.

3. Groups III and IV securities shall be valued at market and any net market depreciation on the total securities of these classes held by banks shall enter into the computation of net sound capital and estimated loss. If there is net unrealized appreciation, it shall be ignored.

4. All profits realized from the sale of securities shall be segregated in a special liability or valuation account.

5. Even though a bank does not place net realized security appreciation (profits from sale) in a valuation account, the examiners shall so treat all net security appreciation realized after June 30, 1938.

6. All banks shall be discouraged from henceforth purchasing securities of a credit quality below that which is generally required of rated bonds which appear in the three highest grades.

THE WHITE HOUSE
WASHINGTON

April 25, 1938

9722

MEMORANDUM FOR THE SECRETARY OF THE TREASURY

Will you and Magill start in right away to get all the necessary information, such as the enclosed, to Chairman Doughton.

F. D. R.

Enclosure

295

THE SECRETARY OF THE TREASURY
WASHINGTON

RECEIVED
APR 2 1 1938

My dear Mr. President:

In response to your memorandum dated April 16, there is submitted the attached table which shows, for tax-exempt obligations reported by individuals with net incomes of $50,000 and over for 1935 (the most recent year for which data are available), the amount owned, interest received, and estimated tax saving at 1936 Act rates, by nature of obligations and by net income classes. In view of the fact that wholly tax-exempt interest does not enter into the taxpayer's gross income nor into his tax computation, the reporting of these data is purely informational, and for this reason they are undoubtedly understated. A comparison of the magnitudes of the interest and the amount owned suggests that the latter data have been incompletely reported, although there is no necessary relationship between these two sets of figures, since the amount owned is reported as at the end of the year whereas the interest comprises amounts received or accrued during the year. It is apparent, however, that individuals do not exercise the same care in reporting their tax-exempt bond holdings as they do in reporting the interest received thereon, and that these latter data with respect to wholly tax-exempt interest are not reported with the same care as is taxable income.

The data with respect to amount owned and interest received on partially tax-exempt obligations are noncomparable. The amount-owned figures include Liberty 4 and 4-1/4 percent bonds, United States Savings bonds and Treasury bonds in full, whereas the interest-received data exclude the interest on these bonds on principal amounts not in excess of $5,000, which interest is wholly exempt from income tax. Partially tax-exempt interest also includes amounts reported on the face of the return for which corresponding figures with respect to amount owned in the supporting schedule are not complete.

In estimating the tax saving resulting from the tax exemption of Government interest, it was assumed that such interest would represent an additional increment of taxable income and would, therefore, be subject to the top bracket rates. In order to make the estimate as meaningful as possible, the computation was made using 1936 Act rates rather than the rates actually applicable in 1935.

Faithfully,

HMorgenthau Jr

The President,

The White House.

Enclosure.

295

Wholly and partially tax-exempt obligations reported in 1935 individual income tax returns of net incomes of $50,000 and over, showing amount owned, interest received, and estimated tax-saving at 1936 Act rates, by nature of obligations and by net income classes 1/

(Net income classes and money figures in thousands of dollars)

Net income classes	Amount owned at end of year: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)	Interest received or accrued during year: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt 2/	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)	Estimated tax-saving resulting from the tax-exemption of government interest: Total	Obligations of the U. S. government, its agencies and instrumentalities: Total	Partially tax-exempt	Wholly tax-exempt	Obligations of state and local governments, territories and insular possessions (wholly tax-exempt)
50 - 60	182,418	69,252	25,810	43,442	113,166	12,696	3,837	1,504	2,333	8,859	3,978	877	60	817	3,101
60 - 70	175,498	71,075	20,695	50,380	104,423	11,033	3,425	1,053	2,372	7,608	4,333	1,062	42	1,020	3,271
70 - 80	140,653	43,562	10,722	32,840	97,091	9,711	2,635	1,151	1,484	7,076	4,069	743	46	697	3,326
80 - 90	107,797	43,014	11,274	31,740	64,783	6,907	1,973	662	1,311	4,934	3,461	747	26	721	2,714
90 - 100	64,972	24,110	6,759	17,351	40,862	4,350	1,263	430	833	3,087	2,329	508	17	491	1,821
100 - 150	332,070	99,047	16,120	82,927	233,023	18,750	4,107	807	3,300	14,643	11,157	2,078	32	2,046	9,079
150 - 200	132,910	50,644	7,634	43,010	82,266	8,807	2,178	508	1,670	6,629	5,332	1,089	20	1,069	4,243
200 - 250	99,106	40,907	8,614	32,293	58,199	4,980	1,534	458	1,076	3,446	3,002	728	18	710	2,274
250 - 300	149,606	42,952	2,564	40,388	106,654	7,654	1,537	245	1,292	6,117	5,049	889	10	879	4,160
300 - 400	64,339	25,386	2,857	22,529	38,953	3,708	1,060	143	917	2,648	2,502	648	6	642	1,854
400 - 500	97,182	25,873	474	25,399	71,309	5,225	709	15	694	4,516	3,753	501	1	500	3,252
500 - 750	128,671	52,007	4,674	47,333	76,664	7,419	2,118	158	1,960	5,301	5,379	1,456	6	1,450	3,923
750 - 1,000	40,401	20,220	1,035	19,185	20,181	1,730	483	11	472	1,247	1,307	359	3/	359	948
000 - 1,500	50,290	33,169	181	32,988	17,121	1,973	1,038	3	1,035	935	1,517	797	3/	797	720
,500 - 2,000	13,405	6,113	—	6,113	7,292	636	183	19	164	453	476	127	1	126	349
2,000 - 3,000	11,412	1,727	925	802	9,685	458	6	3	3	452	355	2	3/	2	353
3,000 - 4,000	6,463	4,782	10	4,772	1,681	797	260	8	252	537	616	197	3/	197	419
4,000 - 5,000	106,259	76,599	3/	76,599	29,660	3,061	1,729	2	1,727	1,332	2,386	1,347	3/	1,347	1,039
5,000 and over	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Total	1,903,452	730,439	120,348	610,091	1,173,013	109,895	30,075	7,180	22,895	79,820	61,001	14,155	285	13,870	46,846

Treasury Department, Division of Research and Statistics.

April 18, 1938

1/ Schedule D, Form 1040, columns 2 and 3, except as explained in footnote 2/ with respect to partially tax-exempt interest received. 1935 is the latest year for which amount held and interest received data are available. However, the estimated tax-saving resulting from the tax-exemption of government interest has been calculated at rates as under present law.

2/ Excludes interest received on 4 and 4-1/4 percent Liberty bonds and Treasury bonds on a principal amount not in excess of $5,000, which interest is wholly exempt from income tax. Includes the partially tax-exempt interest received from partnership and fiduciary sources.

3/ Less than $500.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 25, 1938

TO Secretary Morgenthau

FROM Mr. Haas

Subject: The Business Situation, week ending April 23, 1938

Summary

A brightening of the business horizon has appeared in a number of important developments this week:

(1) An improvement in business sentiment abroad, as reflected in strong upturns in security prices on the London and Paris exchanges following the Anglo-Italian accord and the change of government in France (See Chart 1), has tended to strengthen the background for a business upturn in this country.

(2) The stimulation given to the capital market by recent monetary moves, as reflected in a strengthening of the market for all classes of bonds and in the success of a large utility flotation this week, has improved the outlook for an increased volume of new capital issues.

(3) New steel orders have again increased (Chart 2), with an upturn in railroad buying apparently reflecting some improvement in the outlook for railroad earnings.

(4) An increase in carloadings last week, contrary to the normal seasonal movement, together with the prospect that the usual heavy movement of freight during the summer and fall will be reinforced by a bumper wheat crop, suggests that a base may have been established for an improving trend in railway traffic.

A prominent development on the unfavorable side has been an increasing number of strikes and other labor difficulties, particularly in the automobile industry. These have been a factor in reducing automobile output this week, and have led to apprehension over labor troubles on any revival in business.

While doubt is expressed in various quarters as to the effectiveness of a Government spending program for promoting recovery, there is general agreement that the monetary measures taken by the Administration should have an important influence in that direction.

The current trend

The New York Times adjusted index of business activity declined to 77.1 during the week ending April 16, as compared with 78.2 for the previous week. Lower adjusted figures for steel production, electric power production, lumber production, and cotton mill activity were largely responsible for the drop of 1.1 points in the combined index.

While the index for the current week (ending April 23) will be unfavorably affected by a greater than seasonal decline in automobile production, recently increased orders for steel and textiles suggest the possibility of an improvement in those industries in the near future.

The steel situation

Evidence of improved business sentiment appears in an increase in steel orders, as reported by the U. S. Steel Corporation, during the week ending April 14. (See Chart 2). This raises them again to the equivalent of about 42 per cent of capacity, as compared with a decline in orders to 35 per cent two weeks ago. The industry this week is operating at 32.4 per cent of capacity, practically unchanged from the previous two weeks. This rate, however, is lower than the equivalent rates of shipments and new orders, indicating that orders continue to be filled in part from accumulated stocks.

The week has been featured by an increase in railroad buying, principally for steel rails, although inquiries have come in for bids on freight cars. This apparently reflects some improvement in the outlook for railroad earnings. In this respect the recent increase in freight rates has not been the only factor. A contra-seasonal upturn in carloadings this week, principally in miscellaneous freight, following a greater than seasonal rise in miscellaneous loadings last week, provides some evidence that the low point of railroad earnings has been passed, and that a base may have been established for a general improvement in earnings. The normally heavy summer and fall freight movement will be reinforced by the marketing of this year's huge wheat crop.

Demand for steel from the construction industry, although far below last year, is greater than the demand from either the automobile industry or the railroads. An analysis indicates that in recent weeks about 80 per cent of the construction steel has been for Federal, State, and municipal projects, about 13 per cent for retail stores, office buildings and apartment houses, and only 7 per cent for industrial expansion.

The automobile situation

Automobile output this week declined to 60,563 units from 62,021 units in the previous week, largely because of labor troubles. A temporary closing of the Plymouth and Buick factories by strikes and other difficulties resulted in declines in the total output of General Motors and Chrysler, while the Ford output remained unchanged. Normally the seasonal peak is reached at this time.

The recurrence of labor troubles at the beginning of a business upturn has reacted unfavorably on business sentiment in industrial sections, leading to the fear that last year's experience may be repeated when a business recovery gets under way. At the end of the week 14 factories in the Detroit manufacturing area remained closed, most of them because of unauthorized strikes.

New orders improved

The general improvement in sentiment brought about by recent Administration action has resulted in an increase to a new high for the year in new orders of 8 important companies, for which we tabulate weekly reports. (See Chart 2.) The combined total for the third week of April amounted to $10,630,000, as compared with $9,070,000 for the previous week, when orders had fallen off sharply following the stock market decline. These are companies whose orders are but little affected by the Easter trade.

Department store sales improved markedly during Easter week, though the reported total of $38,351,000 was less than the $39,329,000 in sales for Easter week last year. Sales by the F. W. Woolworth Company, however, showed a substantial gain over last year's Easter sales, probably reflecting in part a diversion of consumer purchases to lower priced merchandise.

Improved sentiment in Europe
favorable to business

The German invasion of Austria last month set in motion a train of developments distinctly weakening to our own economy, which depressed prices in commodity and security markets both here and abroad. Recently this influence has been counteracted, at least in part, by an accord between England and Italy which goes far toward reducing the unsettled war psychology which had tended to depress British industry.

The improvement in sentiment abroad following these developments has been reflected in marked upturns in security prices on the London and Paris exchanges. (See Chart 1). The change of government in France was an important additional factor in the French markets. The recovery measures taken by the Administration in this country doubtless exerted some favorable influence on foreign security markets. The marked improvement in sentiment abroad tends to strengthen the back-ground for business improvement in this country.

Capital markets stimulated by monetary moves

Evidence that the strength in bond prices created by the recent increase in excess bank reserves is being effective in reopening the capital markets is seen in the strong demand for the $60,000,000 consolidated Edison issue put out this week, and in talk of possible revival of long-delayed stock and bond issues.

The strength in the bond market, which started in Government issues, has extended this week to medium and lower grade bonds, with the Dow-Jones index of second grade rails on Friday recording a gain of 2.15 points.

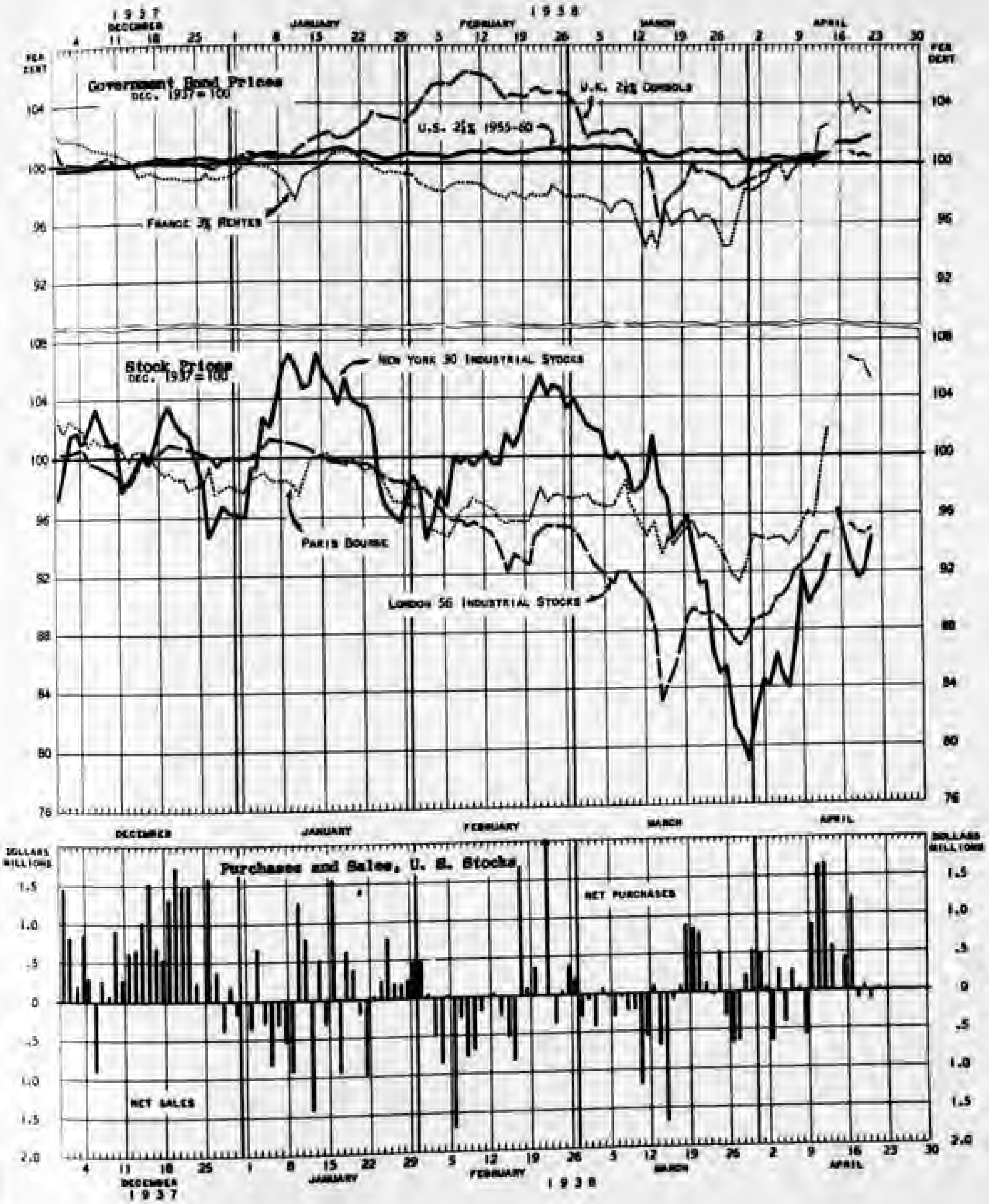
The encouragement to industrial expansion and spending which a strong capital market will provide represents one of the major benefits that may be expected from the recovery program. In the capital market Government issues now occupy a more important place than ever before. In order not to upset the developing market for new corporate issues, it is especially important that sharp reactions in Government bond prices be avoided. A gradual rising trend for Governments would in the long run be most favorable for re-building the market for new capital issues.

Opinions vary on effect of recovery program

While business analysis are in general agreement that the increase in excess reserves will tend to reverse the deflationary tendency in commodity prices and will therefore have a beneficial effect on business sentiment, doubt is expressed that the spending program will have a major influence on business. It is believed by some that any direct influence of the spending program will not be felt before the last quarter of the year, largely because of delay in getting projects under way. The Annalist, however, refers to the definite upturn in recovery and relief expenditures in March, and expresses an opinion that the date of a business upturn resulting from this, if it "takes" at all, woudl be May or June.

As we view the situation, business analysts have been inclined to place too much stress on the possible effect of actual expenditures by the Government, and too little on the important influence of the program in its entirety on public psychology and buying policies.

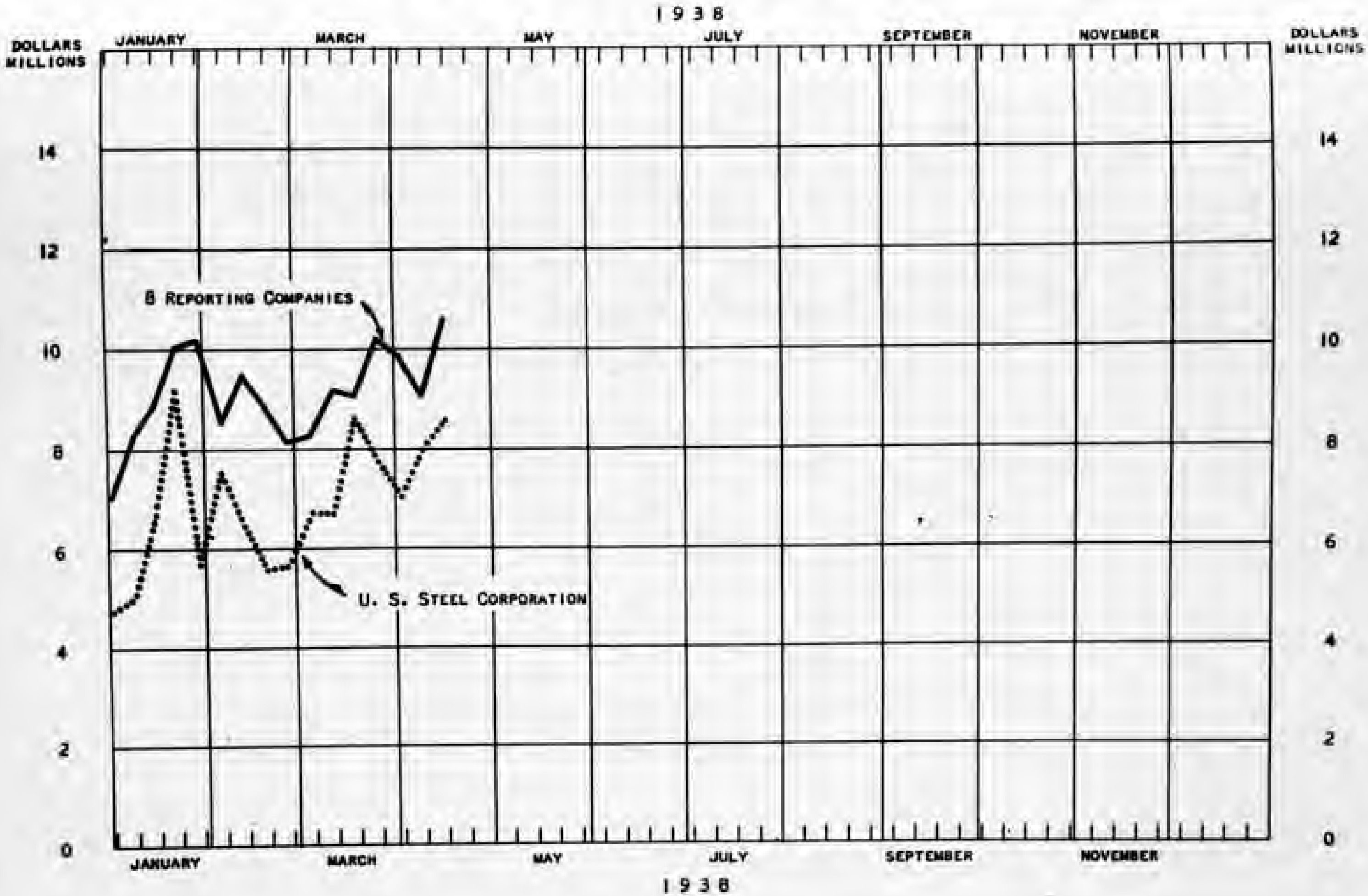
SECURITY PRICES IN U.K., FRANCE AND U.S.
AND FOREIGN TRADING IN AMERICAN STOCKS



Office of the Secretary of the Treasury
Division of Research and Statistics

F - 159

WEEKLY ORDERS OF 8 REPORTING COMPANIES*
AND OF THE U.S. STEEL CORPORATION



* ORDERS, SALES OR SHIPMENTS

Office of the Secretary of the Treasury
Division of Research and Statistics

I - 44

Chart 2

302

TREASURY DEPARTMENT

Washington

FOR RELEASE, MORNING NEWSPAPERS,
Monday, April 25, 1938.
4-23-38

Press Service
No. 13-7

The Secretary of the Treasury, on behalf of the Commodity Credit Corporation, is today offering for subscription, through the Federal Reserve banks, $200,000,000, or thereabouts, of notes of the Commodity Credit Corporation, designated 3/4 percent notes of Series C. Series B Collateral Trust Notes of the Commodity Credit Corporation, maturing May 2, 1938, will be accepted at par in payment for any notes subscribed for and allotted.

The notes will be dated May 2, 1938, and will bear interest from that date at the rate of 3/4 percent per annum. They will mature on November 2, 1939, and will not be subject to call for redemption prior to maturity.

The notes will be fully and unconditionally guaranteed both as to interest and principal by the United States. They will be exempt both as to principal and interest from all Federal, State, municipal, and local taxation (except surtaxes, estate, inheritance, and gift taxes).

The notes will be issued only in bearer form with coupons attached, in denominations of $1,000, $5,000, $10,000 and $100,000.

Subscriptions will be received at the Federal Reserve banks and branches, and at the Treasury Department, Washington. Subscriptions <u>will not be received</u> at the Reconstruction Finance Corporation or at the Commodity Credit Corporation. Banking institutions generally may submit subscriptions for account of customers, but only the Federal Reserve banks and the Treasury Department are authorized to act as official agencies. Cash subscriptions from banks and trust companies for their own account will be received without deposit but will be restricted in each case to an amount not exceeding one-half of the combined capital and surplus of the subscribing bank or trust company. Cash subscriptions from all others must be accompanied by payment of 10 percent of the amount of notes applied for. Subscriptions in payment of which Series B Collateral Trust Notes of the

Commodity Credit Corporation are tendered should be accompanied by the maturing notes.

The right is reserved to close the books as to any or all subscriptions or classes of subscriptions at any time without notice. Subject to the reservations set forth in the official circular, all cash subscriptions will be received subject to allotment and subscriptions in payment of which Series B Collateral Trust Notes of the Commodity Credit Corporation are tendered will be allotted in full.

Payment for any notes allotted on cash subscriptions must be made or completed on or before May 2, 1938, or on later allotment.

The text of the official circular follows:

COMMODITY CREDIT CORPORATION

3/4 PERCENT NOTES OF SERIES C, DUE NOVEMBER 2, 1939

Dated and bearing interest from May 2, 1938

FULLY AND UNCONDITIONALLY GUARANTEED BOTH AS TO INTEREST AND PRINCIPAL BY THE UNITED STATES, WHICH GUARANTY IS EXPRESSED ON THE FACE OF EACH NOTE

Exempt both as to principal and interest from all Federal, State, municipal, and local taxation (except surtaxes, estate, inheritance, and gift taxes).

1938
Department Circular No. 583

TREASURY DEPARTMENT,
Office of the Secretary,
Washington, April 25, 1938.

Public Debt Service

I. OFFERING OF NOTES

1. The Secretary of the Treasury, on behalf of the Commodity Credit Corporation, invites subscriptions, at par and accrued interest, from the people of the United States for notes of the Commodity Credit Corporation, designated 3/4 percent notes of Series C. The amount of the offering is $200,000,000, or thereabouts.

II. DESCRIPTION OF NOTES

1. The notes will be dated May 2, 1938, and will bear interest from that date at the rate of 3/4 percent per annum, payable semiannually on November 2, 1938, and on May 2 and November 2, 1939. They will mature November 2, 1939, and will not be subject to call for redemption prior to maturity.

2. These notes are issued under the authority of the act approved March 8, 1938, (Public No. 442-75th Congress) which provides that these notes shall be fully and unconditionally guaranteed both as to interest and principal by the United States; that they shall be deemed and held to be instrumentalities of the Government of the United States, and as such they and the income derived therefrom

shall be exempt from Federal, State, municipal, and local taxation (except surtaxes, estate, inheritance, and gift taxes); and that the notes shall be lawful investments and may be accepted as security for all fiduciary, trust and public funds the investment or deposit of which shall be under the authority or control of the United States or any officer or officers thereof.

3. The authorizing act further provides that in the event the Commodity Credit Corporation shall be unable to pay upon demand, when due, the principal of, or interest on, such obligations, the Secretary of the Treasury shall pay to the holder the amount thereof which is hereby authorized to be appropriated, out of any money in the Treasury not otherwise appropriated, and thereupon to the extent of the amount so paid the Secretary of the Treasury shall succeed to all the rights of the holders of such obligations.

4. The notes will be acceptable to secure deposits of public moneys, but will not bear the circulation privilege.

5. Bearer notes with interest coupons attached will be issued in denominations of $1,000, $5,000, $10,000 and $100,000. The notes will not be issued in registered form.

III. SUBSCRIPTION AND ALLOTMENT

1. Subscriptions will be received at the Federal Reserve banks and branches and at the Treasury Department, Washington. Banking institutions generally may submit subscriptions for account of customers, but only the Federal Reserve banks and the Treasury Department are authorized to act as official agencies. Others than banking institutions will not be permitted to enter subscriptions except for their own account. Cash subscriptions from banks and trust companies for their own account will be received without deposit but will be restricted in each case to an amount not exceeding one-half of the combined capital and surplus

of the subscribing bank or trust company. Cash subscriptions from all others must be accompanied by payment of 10 percent of the amount of notes applied for. The Secretary of the Treasury reserves the right to close the books as to any or all subscriptions or classes of subscriptions at any time without notice.

2. The Secretary of the Treasury reserves the right to reject any subscriptions, in whole or in part, to allot less than the amount of notes applied for, to make allotments in full upon applications for smaller amounts and to make reduced allotments upon, or to reject, applications for larger amounts, or to adopt any or all of said methods or such other methods of allotment and classification of allotments as shall be deemed by him to be in the public interest; and his action in any or all of these respects shall be final. Subject to these reservations, subscriptions in payment of which Series B Collateral Trust Notes of the Corporation are tendered will be allotted in full. Allotment notices will be sent out promptly upon allotment, and the basis of the allotment will be publicly announced.

IV. PAYMENT

1. Payment at par and accrued interest, if any, for notes allotted on cash subscriptions must be made or completed on or before May 2, 1938, or on later allotment. In every case where payment is not so completed, the payment with application up to 10 percent of the amount of notes applied for shall, upon declaration made by the Secretary of the Treasury in his discretion, be forfeited to the United States. Series B Collateral Trust Notes of the Commodity Credit Corporation, maturing May 2, 1938, will be accepted at par in payment for any notes subscribed for and allotted and should accompany the subscription.

V. GENERAL PROVISIONS

1. As fiscal agents of the United States, Federal Reserve banks are authorized and requested to receive subscriptions, to make allotments on the basis and up to the amounts indicated by the Secretary of the Treasury to the Federal

Reserve banks of the respective districts, to issue allotment notices, to receive payment for notes allotted, to make delivery of notes on full-paid subscriptions allotted, and they may issue interim receipts pending delivery of the definitive notes.

2. The Secretary of the Treasury may at any time, or from time to time, prescribe supplemental or amendatory rules and regulations governing the offering, which will be communicated promptly to the Federal Reserve banks.

HENRY MORGENTHAU, JR.,
Secretary of the Treasury.

—oOo—

April 25, 1938

MEMORANDUM FOR THE PRESIDENT:

You have requested a description of the capital gains provisions of the Revenue Bill of 1938, as agreed upon by the conference committee, in their application to incomes and gains of different sizes.

Not all of the details of the treatment of capital gains and losses have been worked out. The provisions will be quite complicated, since three types of gains (and of losses) are recognized, and optional forms of taxation will be provided with respect to one or more of the three types.

It has been announced, however, that net short-term capital gains, (resulting from sales of property held by the taxpayer less than 19 months), will be treated just as other income and fully subjected to normal tax and surtax rates. Gains resulting from sales of assets held by the taxpayer 19 months or more, but less than 25 months, will, at the option of the taxpayer, be subjected to a flat rate of 20 percent. In the case of gains resulting from sales of property held 25 months or more, the taxpayer may either include half of the gain with his other net income and pay the normal tax and surtax rates on the total; or he may elect the option of paying a flat rate of 15 percent on the full amount of the net gain, irrespective of the rates of tax applicable to his other net income, or of the amount of the gain.

The treatment of losses will evidently be similar to that provided by the Senate bill. In general, short-term losses will only be deductible from the short-term gains of the year of sale, or of the following year. Long-term losses will be deductible from ordinary income, but with limitations.

The lowest surtax rate is 4 percent, applicable to surtax net income in excess of $4000 and not in excess of $6000. The highest surtax rate is 75 percent, applicable to surtax net income in excess of $5,000,000. If a taxpayer with surtax net income of $4000, not counting capital gains, should have a net long term capital gain of $1000, he will obviously be better off to pay the normal tax of 4 percent, plus the surtax of 4 percent on $500 (one-half of the gain), than to pay 15 percent on $1000, the full amount of the net gain. In effect, the bill cuts in half the tax on his capital gain, as compared to the tax on his other income.

At the other extreme is the case of the man with surtax net income of $5,000,000. His surtax rate on amounts of ordinary income over that total is 75 percent, plus the normal tax of 4 percent. If he has a capital gain of $1000 in addition to the $5,000,000, he will obviously choose to pay the 15 percent flat rate on the whole gain, instead of the alternative of 79 percent on one-half the gain. The rate of tax on the capital gain remains 15 percent, if the gain is $1,000,000 rather than $1000. In effect, the bill reduces by more than four-fifths the tax on his capital gain as compared to the tax on his other income.

The reduction thus effected in the tax on capital gains as compared to the tax on ordinary income varies between these two extremes.

increasing as total income increases. To illustrate in a different way, the surtax on a surtax net income of $75,000 is $17,050; the surtax on a surtax net income of $50,000, plus the capital gains tax on a net long-term capital gain of $25,000 is $11,450 or one-third less than the tax in the first case.

(Signed) Roswell Magill

RE FRENCH MONETARY SITUATION

April 25, 1938.
10:30 a.m.

Present: Mr. Taylor
Mr. Lochhead
Mr. White
Mr. Feis
Mr. Harrison
Mr. Knoke

H.M.Jr: Well, I had this conversation with Cochran and Butterworth, as a result of the fact that Sir Frederick Phillips had asked Butterworth to find out just what we knew. And that they knew nothing and, as near as I can make out, that Marchandeau has refused to see anybody Friday and Saturday; nobody could get to him, including the Bank of France. You (Lochhead) check me on this.

Lochhead: Yes, we check on that.

H.M.Jr: I mean I don't know where I get this, but is that right?

Lochhead: Checked in two ways, both by Cochran and secondly Carigeul's calls to the Federal Reserve that day, which we couldn't understand - two or three calls in succession.

H.M.Jr: Then, talking to Butterworth, he said the people in London had the same experience, couldn't reach anybody. And as a matter of fact, for both Friday and Saturday I gather they were under wraps. Is that about right?

Knoke: That's right.

H.M.Jr: So the English said that - they mentioned the man's name - made a computation.

Knoke: Hawtrey.

H.M.Jr: Who?

White: Hawtrey.

H.M.Jr: Made a computation, and it should be 155. And that letting this thing go the way it was, I gathered they felt they were not living up to the spirit of the tripartite, and that they were letting this thing go and they weren't giving it the support which it should receive.

Well, the reason for my asking you gentlemen to come in was that I wanted to talk this over and get your advice, see what you thought. My mind is entirely open. I got a call in quarter of 11 for Cochran and at 11 o'clock for Butterworth to bring ourselves up to date.

But I see according to this morning's papers - what I would gather was that the French were stalling until they went over to London. I mean that's what it looks like. And - did you (Feis) know anything on this?

Feis: Stalling in relation to what, Mr. Secretary?

H.M.Jr: On the announcement - whatever financial decrees they're going to make.

Feis: No, there's been nothing on that, except what's in the Cochran cables. That's absolutely all we've got.

Taylor: Cochran cable says they're going to have an announcement today.

Lochhead: Did make a certain general announcement.

H.M.Jr: Well, you showed me that, which is meaningless.

Lochhead: We have nothing else.

H.M.Jr: Which is meaningless.

Lochhead: Generalities.

H.M.Jr: What?

Lochhead: Generalities.

H.M.Jr: I mean it's just meaningless. And there we are. Of course, I just feel this way - I told Cochran to go in and tell Marchandeau that I didn't like this and that I felt that it was up to them to say something; that they just couldn't act like this, and to be very forceful. And Marchandeau saw him at once; came out of Cabinet and talked to him.

Then my talk to Butterworth - "No, we don't know anything. Tell Sir Frederick Phillips we don't know a thing."

Of course, the way I feel up to now - the French letting their franc go - I can't see that it's hurt us any.

Knoke: See what?

H.M.Jr: I can't see that it's hurt us any. And since Daladier is in they've gained, they say, about 60 million dollars. That was through Thursday. That check?

Knoke: Well, I wouldn't say that.

Lochhead: Two billion francs. Then they lost. Yes, that was right. About two billion francs they gained up to Thursday, then lost about half of it.

H.M.Jr: Half of it?

Lochhead: The last thing we have - reference in here - that they probably lost half of it in Friday's and Saturday's protection.

H.M.Jr: I gathered they didn't protect it.

Lochhead: Oh, they've protected it.

H.M.Jr: You think they lost 30 million dollars Friday and Saturday?

Lochhead: That's one of the references. One item there of 300,000 pounds on Saturday, but then on the day before that it was at least a million pounds. Remember, that was definite.

Knoke: They lost about half of it.

Lochhead: Half may be a little large.

Knoke: Of their gain in the last ten days, last eight days.

H.M.Jr: Well, as I say, this is important, and I thought each fellow - we put what we've got on the table.

White: Hawtrey's calculations, I think, are fairly reasonable from the point of view of the mechanistic one. That is, he can arrive at that figure and be fairly reasonable as to what the movements of prices and the movements of exchange rates over the past have been. I think we might come out a little bit higher, something of that sort, but it is approximately right.

But I think that it avoids a very significant problem which confronts the French, and from our point of view, at any rate, which I take it is definitely toward permitting France to get out of her present situation as best she can .....

H.M.Jr: Well, our record has been that now for four years.

White: Yes, I assume it's continued.

The French are confronted with the - not a franc rate that would reflect the underlying economic conditions, because her more immediate and more acute problem is to protect her gold reserves. And tied up with that is the question as to how long will pressure against the franc continue. And if there has been, as there definitely has been, both rumors and expectation that the franc rate is liable to go to 175, then unless France does something rather spectacular or effective in eliminating the basis of that rumor - I mean in getting the opinion abroad that they are not going to go to that, then the fundamental economic factors have no bearing, it's going to go to that rate, and any attempt on their part to stop it will take place only through the imposition of exchange controls, which he's avoided, or through the loss of gold, which he cannot experience. So it seems to me that the problem is not one of what franc rate is the most economic in the long run, but it's the other problem.

H.M.Jr: Well, I don't want to attempt to - I wouldn't attempt to tell them what their rate should be, but at least as long as they're in the tripartite I want to know what they're thinking of doing.

White: That's different.

Lochhead: By the way, Mr. Feis, ...

H.M.Jr: And after they've told us - I mean if they're just going to let this thing melt and not put on any regulations and not try to do anything - I mean I can't - there may come a time when it doesn't serve a very useful purpose to have them as a partner.

Harrison: I think you've been very liberal in your interpretation of the qualifications of membership in the club so far as the French are concerned. I think you've been right in being liberal, in giving them every break. But if, for instance, you have a new government come in, as you now have, and there are rumors and speculations as to what they're going to do, and the period of those rumors continues more or less indefinitely without their telling you what their plan is, then I think that you have a right to take a very firm position with them.

In other words, if their program is to defend their gold reserve rather than to defend the franc as a policy, then I think you have a right to know, because the spirit of the tripartite agreement was to defend the currency rather than to defend the gold reserve. Now, if they've changed from the left foot to the right foot, or vice versa, I think that the least they can do as a member of the club is to acquaint you with it, and then you to determine if you still want them as partners.

H.M.Jr: I mean when it gets so that neither the British nor the United States Government can talk to anybody for two days in the French Treasury, it isn't very good, is it? Huh?

Feis: No, I agree. But I think the fundamentals are as White has outlined them, so that ...

H.M.Jr: Well, I'm very calm, as I say. After having been through this about four times a year, you get so that you don't get very excited about it. But Butterworth was pushing a little bit hard and he of course was being pushed hard, and I think it's up to us now to have a policy here and then to acquaint our representatives, wherever they are.

Feis: The French have to achieve some measure of redistribution of their productive activity if they're going to carry on their arms effort. They can try that through a system of exchange control and controlled economy, or they can try it through a process of gradual and rather continuous inflation, of which I doubt that 175 will be the bottom myself. And no allegiance to our tripartite monetary agreement is going to make it possible to avoid one or the other thing. Of course, they've made up their mind that they're not going to seriously further reduce their gold reserves, and, while we haven't been formally told that, every Prime Minister since the fellow before Blum has more or less indicated that was a fixed policy of the French Government.

And then, I get - as for the British, I get the idea that they are probably feeling once again a little bit confident and want to make the French feel their dependence upon them in almost any direction that they can bring that feeling home.

H.M.Jr: And you don't want to be used as a cat's-paw.

Feis: No, sir, I don't believe so.

H.M.Jr: What?

Feis: I don't believe so. All of which does not at all affect the thing which you said. Some sketch of their purposes you ought to have.

H.M.Jr: This story, that you may or may not want to comment on, which Pearson and Allen run today as a fact - that the British asked us to get out a note in support ...

Harrison: Asked us to do what?

H.M.Jr: Pearson and Allen run as a factual thing this morning that the British Government asked us to get out a statement complimenting on that British-Italian treaty.

Feis: I ...

H.M.Jr: You can't comment?

Feis: No, I don't know. As far as I know, no, but I might very well just not know.

H.M.Jr: I said you might not want to tell me, because after all we asked them to do that when we came out on our price statement; you remember they came through beautifully.

Feis: My guess would be, with almost complete certainty, no. I mean the British Government and the British Ambassador would say to themselves, "If we were to walk into the State Department with some such request as that, it is the very - the very act of suggestion on our part, is calculated to do something else." So my guess is that there is not one chance in twenty that it is so.

H.M.Jr: Pure matter of curiosity.

Feis: I'll find out, but I don't believe it is possibly so.

White: On economic grounds a pretty good case could be made for France to go to 175, in view of her particular situation, from her own interests. A pretty good case could be made. And another good case could be made that her going to 175 is not very seriously affecting the British situation either. So I think that all comes in substantiation of what Herbert says, that the irritation - that the annoyance, which is justifiable from the point of view of not knowing what they are intending, becomes something different because of the larger political issues involved.

Harrison: Dr. White, what is the cross rate of the franc at 175.

White: I haven't ...

Knoke: $.0285.

Harrison: And at 155?

Knoke: 15 into 45 - about $.0330, something of that kind.

Harrison: I shouldn't think you'd much worry what it is, as far as we're concerned.

White: As far as we're concerned, the effect is very little. We do a very good business with the French.

Harrison: I should think you would worry if they won't give you any indication which way it's going or where they want it to go.

White: I think those are two separate problems indicated, very clearly.

H.M.Jr: Marchandeau saw Cochran within 45 minutes from the time he asked to see him. So it's just a question - I asked Bewley - Bewley hasn't asked to see us in two weeks, has he?

Taylor: Yes.

H.M.Jr: What does that mean - "yes"? He has?

Taylor: Yes.

H.M.Jr: He has asked. Since Saturday?

Taylor: Not since Saturday.

H.M.Jr: No.

Lochhead: Of course, the other interesting thing today is that they spoke about the franc going down to 175 this morning and this morning the franc is up; they've supported it rather vigorously, and the franc has gone up to 160.75; that's a $.0310 rate here.

White: But, Archie, as indicated .....

Lochhead: One of the rumors was that they started off this morning with the French coming in very vigorously to support the franc, and then it went up of its own accord after that.

White: And didn't Marchandeau state in the cable very definitely that they have every intention of supporting the position - I mean so far as the statement is concerned, which apparently is responsible for Monday's action, which indicates that they're going to temporarily at least not give the impression that the franc is going down to 175.

Harrison: Well, my feeling about it is this, that under the terms of the tripartite arrangement, as I remember them, any one of the participants in the arrangement has the right, for purely domestic reasons, to let their currency go if they want to; but I should think it would be implicit in the agreement that if they're going to do that for domestic reasons and reasons wholly satisfactory to them, they would acquaint the other members of the arrangement.

H.M.Jr: Well, it's a little bit different than that, George. That isn't - I would say that that wouldn't quite describe the spirit.

Harrison: You would not?

H.M.Jr: No, I would say they could not let the thing go purely for domestic reasons, because the question is - as I remember, they can not let their currency go, depreciate their currency for competitive reasons, but it doesn't say anything about domestic.

White: It does say that they take into consideration the domestic factors. They all insisted on that.

H.M.Jr: But, after all, if the franc goes to, say, 175 cross rate, it's a question, when does domesticity start and world competition end, or vice versa, you know.

Harrison: Yes, I agree. And that's where I think they're failing, they're not letting .... I should think this paragraph - if they don't go any further than this paragraph in cable 644, you would not be content or satisfied. "The Minister refused to mention any specific level at which he desired the franc. He, the Minister, insisted that Monday's statements should drive back the rate." That's the ones that presumably are in this ticker announcement. "I asked whether 175 or any other limit had been in mind as the proper extent for the franc to sink. The Minister responded emphatically that there was no basis whatever for speculation on the 175 level, and that there was most definitely no intention on this government's part to manipulate a deliberate depreciation of the franc or to accept a franc pushed down to the present level without counter-attack."

Now, in an earlier part of the cable he did say that they were not going to use their gold reserve "as extravagantly as in the past" - I think was the phrase. It's all very vague, rather indicates to me, not that they're being unfrank with us, but rather they don't know themselves what they're going to do.

White: That's right.

H.M.Jr: Oh, I don't think they know.

(On phone) What about Cochran?

Taylor: They've been faced with this series of rumors which are - you notice that part about the four banks who passed word around all over the place; why, probably, that has caused them more trouble than anything, because those banks are supposed to be pretty friendly.

Knoke: Friends to whom? To Reynaud and Patenotre. But that's the difficulty in the whole set-up.

Taylor: And you've got our friend Bonnet, who plays with Lazard pretty hard. I don't know who does the business for the others, but it's .....

Knoke: The whole set-up invites these rumors. You have a Cabinet in which there are two former Ministers of Finance, and yet neither of them has been offered or accepted the portfolio of Finance Ministry. Now, why? Probably because Reynaud thought that the Cabinet was not willing to go - conceivably Reynaud thought the Cabinet was not quite willing to go quite as far as he, Reynaud, has preached for six years now. Now, that lends itself beautifully to these rumors.

Harrison: I hadn't read the last paragraph of this cable. "In our conversation the Minister referred to an interview of Daladier appearing in this evening's press, wherein the Prime Minister said, 'The Government is unanimous in its monetary policy, unanimous in affirming its fidelity to the tripartite agreement.'" The end of the message.

H.M.Jr: Yes, I saw that. It's got to be kind of a formula, like a signature. They always use that, then they say "unquote."

Harrison: I don't see what would be accomplished by firing them from the tripartite agreement - I mean even if they can't formulate their own plans with definiteness.

White: Just put greater pressure on the franc.

Harrison: Put greater pressure on the franc, and if the level of franc is of concern to us, it would only accentuate it, I think.

White: There is also this: from their position, new governments coming in and out, ...

H.M.Jr: (On phone) Hello. - Thank you. (Conversation with Cochran follows:)

April 25, 1938.
10:54 a.m.

Operator: Go ahead.

H.M.Jr: Hello.

H. Merle Cochran: Hello, Mr. Secretary.

H.M.Jr: Good morning.

C: How are you, sir?

H.M.Jr: Ah -

C: I've had a rather interesting day here.

H.M.Jr: Well, let's have it.

C: This morning the franc opened at 165.

H.M.Jr: Yes.

C: Then went to 166 9/16.

H.M.Jr: Yes.

C: Then it moved back a little bit. I was at the Bank at 11:30 this morning.

H.M.Jr: You were where?

C: At the Bank of France.

H.M.Jr: Yes.

C: At 11:30 this morning. And by that hour they had given 100,000 pounds. They had brought the rate down to 165¾.

H.M.Jr: 165.

C: And ¾. Yes.

H.M.Jr: Yes.

C: And then at one o'clock Daladier, the Prime Minister, gave out a statement following the Cabinet meeting, which was a fairly good statement. It does not give many details. It just gives the general line. But the plan envisages a free defense of the franc and staying within the tripartite agreement, increasing production, adjustment of labor, and so on and so on.

H.M.Jr: Uh-huh

C: And about that time the Control went into the business very seriously of pushing down the franc.

H.M.Jr: Uh-huh.

C: And they got it down to 160¾.

H.M.Jr: Yes.

C: And pushing it down from 164 7/8 to 163¾ took about an hour.

H.M.Jr: I see.

C: And then to get it from 163¾ to 160¾ only required half an hour. So it went down very quickly. And I talked to my friend at 4:30.

H.M.Jr: Yes.

C: And at 4:30 he said that they had knocked it down without much cost, and that after 4:30 there was beginning to be something different, and that they were going to try to get our friends to hold it at that rate.

H.M.Jr: I see.

Well now, our figures are that - something like this: as of Thursday night - during the previous week or ten days they had accumulated about 60 million dollars. Hello?

C: Yes, somewhere between 50 and 60, certainly.

H.M.Jr: Ah - have you any indication where they would stand tonight?

C: No, because that's what I was talking to him - he couldn't get me the figures, although he gave me his 11 o'clock figure. He hasn't finished that yet.

H.M.Jr: Well, we don't know what they spent Friday and Saturday.

C: I've given you Saturday's. Friday they spent nothing.

H.M.Jr: Friday nothing and - Archie's sitting here - we have Saturday's.

C: Thursday, 300 million ....

H.M.Jr: Yes.

C: ... francs. Thursday ...

H.M.Jr: I see.

C: ... I mean Friday nothing, Saturday I gave you the amount up until just before lunch.

H.M.Jr: Yes.

C: So there's no use going over that.

H.M.Jr: Now, you haven't seen Marchandeau.

C: Beg pardon?

H.M.Jr: You have not seen Marchandeau.

C: I saw him that night, Saturday night.

H.M.Jr: Yes, but I mean today.

C: No, but the Ambassador sat next to him at a press luncheon today.

H.M.Jr: Yes.

C: And he said in a telegram at three o'clock today that Marchandeau repeated almost verbatim the statements which he had made to me.

H.M.Jr: Uh-huh.

C: That there was no difference of opinion within the Cabinet, that he intended to hold the franc, and so on.

But the story now is that they're not going to give out any of the important decrees until after May - after a meeting of the Council after May 1; that is, that they'll be published in the Journal Officiel of May 3. See?

H.M.Jr: Yes.

Now, what I would like you to do is this.

C: Yes, sir.

H.M.Jr: I'd like you to ask again to see Marchandeau.

C: Yes.

H.M.Jr: And say that you're doing so at my request.

C: Yes.

H.M.Jr: And that I would like to know what his objectives are in regard to the franc. I mean where is he going to try to hold it?

C: Well, I - I asked him that the other day, you see, and ...

H.M.Jr: I know, I know, Cochran, but since then they've had this meeting, I'd like to ask ... You got nothing; he didn't tell you. I mean at least I wasn't satisfied anyway.

C: No, but he's got busy today and he's forced it back. That in itself is a statement alone.

H.M.Jr: All right. Well, is that his policy or is that only for today?

C: I see.

H.M.Jr: I mean maybe that's the way he feels today; how is he going to feel a week from today? I mean what are their objectives? That's what I'd like to know.

C: The impression that Wilson and I both get about ....

H.M.Jr: What?

C: .. what Marchandeau said - Wilson called me ten minutes ago to tell me about his talk.

H.M.Jr: Yes.

C: Also showed me his telegram. He said that he tried to pull Marchandeau out as I had the other day to get a definite statement and he said he could not. And he said he was convinced that they are not dead sure what their plans will be.

H.M.Jr: Well, I'm going to ask you to please see him again.

C: Surely. Whatever you say.

H.M.Jr: And - I mean I don't lay great stress on it today, but I would definitely like you to see him tomorrow.

C: All right.

H.M.Jr: I mean it isn't that much of an emergency that you have to see him today, but I'd definitely like you to see him tomorrow.

C: I'm - because whatever announcements they're going to make, they would have time to make together after this Council of Ministers is over.

H.M.Jr: Yes.

C: They're sitting now. They assembled at three o'clock to go over the plans discussed this morning at the smaller Cabinet meeting.

H.M.Jr: Yes.

C: So we may have some announcements tonight or in the morning that I could ask him about too.

H.M.Jr: Well, I'd wait until tomorrow, but then I'd see him - I mean, as I say ....

C: I'll see him tomorrow without fail then.

H.M.Jr: Now just wait a minute, please. Herbert Feis is here. Just a moment.

(Pause)

H.M.Jr: Hello.

C: Hello.

H.M.Jr: In seeing him - I mean I'm not - all I want is information.

C: Surely.

H.M.Jr: That's all.

C: Yes. Have you seen the telegram I sent this morning yet?

H.M.Jr: The last one I've seen is 644.

C: No, I sent a 645 this morning.

H.M.Jr: No.

C: About 12:30.

H.M.Jr: No.

C: In which I told about what the Control was doing this morning.

H.M.Jr: No.

All I want is to see him and get from him, if we can, what his objectives are.

C: Yes.

H.M.Jr: And under the tripartite agreement I'm entitled to know that information.

C: Yes.

H.M.Jr: If he knows it himself.

C: Yes.

H.M.Jr: See?

C: Surely.

H.M.Jr: Now, are you keeping Butterworth informed?

C: I sent him that long wire the other night. I haven't sent him anything since then.

H.M.Jr: I see. You sent him 644.

C: Right, I sent him that. Received it by cable.

H.M.Jr: Uh-huh. All right.

C: And may I tell you one Hello?

H.M.Jr: Go ahead.

C: In this morning's wire I told you most confidentially that these two gentlemen who were going from here across the Channel on Wednesday are going to try to get a loan there.

H.M.Jr: Oh, I see.

C: And the thing is in my mind that they're waiting for plans here ...

H.M.Jr: Yes.

C: ... until they see what they can get over there.

H.M.Jr: I see.

C: The head man's advisers don't want him to do this.

H.M.Jr: I see.

C: He's pretty much set on it.

H.M.Jr: Did you put that in your cable?

C: Yes. Yes, I put it in the cable. It's number 645, sent at 12 noon today.

H.M.Jr: Well, send a copy of that to Butterworth, will you?

C: I'd better repeat it by wire then.

H.M.Jr: You can mail it to him and he'll get it in the morning, won't he?

C: Yes, I - I think I can still get this evening's mail.

H.M.Jr: What?

C: I think I can still get this evening's mail.

H.M.Jr: See if you can. If not, repeat it by wire.

C: All right, sir.

H.M.Jr: But I want - I want to work very closely, so that we know.

C: Surely.

H.M.Jr: And what - anything else?

C: No. That's about everything. The general market here is better, of course, with this strengthening in the franc.

H.M.Jr: Uh-huh.

C: are up.

H.M.Jr: Good.

C: There is talk on the market of a British loan. The thing they had in mind is something like that - they put up remember?

H.M.Jr: I - I don't get that.

C: (Words not understandable)

H.M.Jr: I'm sorry, I don't hear you.

C: That is, to buy francs and then loan them back, you see, without buying gold. But I've explained it in the cablegram which you'll get.

H.M.Jr: All right.

C: Fine.

H.M.Jr: Now just a moment.

C: But my - my belief is that they're delaying anything else until they see what the result will be over there.

H.M.Jr: All right, just a moment.

(Aside: Wayne, anything? Anybody?
Oh, I don't think - I'd rather put that in a cable.)

All right, Cochran, then you make the effort to see him tomorrow.

C: I'll see him tomorrow some time.

H.M.Jr: Thank you.

C: There's just one thing, that my market contact talked with London just before I talked with you.

H.M.Jr: Yes.

C: Said they're pretty nervous over there on this Czech situation this afternoon.

H.M.Jr: I see.

C: It's reported that some of the German troops are mobilized on the Czech border now.

H.M.Jr: I see.

C: That's all I know.

H.M.Jr: All right.

C: Fine. Well then, I'll - I'll send you a message after I've talked with him tomorrow.

H.M.Jr: If you please.

C: Good-bye.

H.M.Jr: Good-bye.

H.M.Jr: What he said was that these two fellows who are going over - he always talks in great mystery; nobody would know who was listening in who the two men were that would be there on the first to see "across the channel" - are trying to get a loan. But that's in the 645 cable. But nobody can dream what I'm saying. Instead of saying "the British" Cochran always says "our friends across the channel" - code word.

Harrison: Code word.

H.M.Jr: If you (Feis) get something from Wilson on this, I suppose ....

White: I suspect their coming over to England is one reason why Phillips would like justification for being annoyed at their procedure.

Feis: I think they want to try to .....

H.M.Jr: What?

Feis: I think - I don't say that they've got the direct impulse to, but it doesn't displease them to feel in the position ....

H.M.Jr: To be hurt.

Feis: Hurt or critical, or injured. "We're conferring a favor." It makes it more easy to defend themselves against any French requests for political cooperation.

H.M.Jr: I've got a call in for Butterworth.

Feis: The military people of the two countries are (word not understandable) together all the time now.

Harrison: Who did he say was nervous about the Czechs?

H.M.Jr: English.

White: Who was massing troops?

H.M.Jr: Germans.

Feis: Haven't been over the political cables for today. Just got in. So I don't know whether we've got anything for this. If there's anything special over there, I'll let you know.

H.M.Jr: I would say since Friday and Saturday this thing's improved, because it's improved - what's the cross rate - dropped from 165 to 160, roughly?

Lochhead: That's roughly, right.

H.M.Jr: So they did step in. Maybe my calling up Saturday and being quite firm may have had a little something to do with it.

Harrison: I should think it did.

White: Although that would be their technique - very definitely trying to reproduce a previous rate before letting it go, trying to hold it. I don't think this is the point they're going to do it. But this is the procedure.

Feis: I would say of their procedure that they have sold more pounds and dollars at cheap franc rates which they some time hope to rebuy at dear franc rates than at any time in the world's history. It is perfectly incompetent financial management that goes on - administration both on the budgetary end and every other end.

Knoke: But ....

Feis: Every four or five days it's the same business of fumbling around incoherently.

Knoke: Don't forget that the tripartite agreement made it easier for the French to do this. The tripartite agreement has cost the French 25 million ounces in gold and enabled many of the speculators to get out of France.

Feis: Why? Why do you say the tripartite agreement did that? What do you anticipate would have happened had there been none? Much more of a smash in the franc?

Knoke: Don't misunderstand me, I'm heartily in favor of the tripartite agreement.

Feis: I'm trying to find out what you mean.

Knoke: Nevertheless, I am simply wondering why the French are still ardently in favor of sticking to it.

Feis: Influence of conventional monetary standards.

White: They likewise - not only political - plays a very important role - but they likewise feel that the adherence to that gives them substantial financial strength to the extent that it doesn't greatly increase the pressure of the franc, for the very reason that you yourself give, that if they didn't belong to the tripartite what would have happened would be one of two or both things: namely, the franc would have depreciated much more rapidly and - or they would have imposed exchange control much more quickly. But whether they were convinced by the existence of the tripartite that they couldn't impose exchange control - whether that played a role is, of course, a mute question. But to that extent it has been responsible for a great loss of gold, that's true.

Knoke: Well, that's a difficult thing to say, whether it's been responsible for greater or smaller loss; but the fact is they've lost 25 percent of their holdings in a year and a half.

White: Half of which, at least, they didn't need to lose.

Knoke: Huh?

White: Half of which they could have avoided.

Knoke: Well, you mean through different technique.

White: Yes. I mean through exchange control, more rapid depreciation.

It would be very interesting to compare the discussions at each one of these periodic crises. Find they run very much the same way.

Knoke: Compare what?

White: Compare the periodic crises - the discussions here. Find they run much in the same terms.

Harrison: Knoke, as a matter of operation, isn't there some advantage from the point of view of the French in having some variation in their method of treatment of the day-to-day operations in the franc? I don't mean by that that they ought to stay out entirely on a Friday and then come in with all four feet on Monday necessarily; but unless they have some variations they do open themselves to pretty definite attack by the speculator, who will know just exactly what their position always is.

White: Particularly in view of their closeness.

Lochhead: Of course, it's been felt sometimes that the speculators had just as much knowledge of the variations as they did of the straight program; that's the only trouble.

Knoke: Probably there is no technique that you can't improve upon, but I think generally speaking they have done rather well, and at times they have been up against impossible odds. Now, it has been a known fact for a long while that the French were hesitant about losing too much gold, particularly when the situation in Europe became much more dangerous for them. With Daladier in charge of the defense - I think Daladier has been known to be an ardent supporter of a minimum war chest of - whatever it is, 50 billion francs, and with that in mind they have had to husband their resources and possibly support the currency less than they would have with a full chest.

H.M.Jr: Well, of course, the French, while they have lost how many billions of dollars in gold in the last three or four ....

Knoke: Well, they've lost 25 million ounces in gold since the tripartite agreement, which is 25 percent of their then holdings, which were roughly a hundred million ounces.

H.M.Jr: It may be rather noble of them, but they certainly added to our difficulties, because we got practically all of it.

Knoke: Well, but I think it was harder on them to lose it than on us to get it.

White: Because they won't get back the same thing.

H.M.Jr: True, but it's like - if they hadn't done that, if we hadn't done it, we wouldn't have had a sterilization fund, and all the rest of it.

But to me - I just can't understand why those fellows haven't put on some kind of modified control on export.

Knoke: On what?

H.M.Jr: On export of money.

Knoke: Well, they can't, under the tripartite agreement, can they?

H.M.Jr: Yes, they can. My God, we even sent them a copy of our rules and regulations that you police for us. Can't do any more than that.

Knoke: But, Mr. Secretary, that would have been of no help in a country like France or in any European country where you have the ....

H.M.Jr: We hinted - well, we didn't hint, we told them.

White: You think Marchandeau knows, Mr. Secretary?

H.M.Jr: We certainly saw Blum. I don't know how they work in the Cabinet, and I don't know whether they told Rueff or not; there is no record whether they told. And certainly the English have dropped hints here that they wouldn't object ....

Harrison: ... to some controls.

H.M.Jr: Yes. I mean we did all we could to let them know, as long as it didn't interfere with anything that had to do with the trade treaty ....

Harrison: Mr. Secretary, I don't know whether it's a proper question or not, but did you get any reactions from either the British or the French about our desterilization?

H.M.Jr: The only thing - I got nothing from the French - I thought the British were a little bit childish about it. They said they had seen this and that and the other paper, didn't understand it. In the first place, they've got an Embassy with forty or fifty people in it; if they can't read our newspapers and send the cables over, I don't know .....

And that's one of the things of those three gentlemen (Lochhead, Taylor, and White) - to service Cochran and Butterworth with information. For instance, tonight when we close that Commodity Credit thing, I'd get off a cable to the two boys and say, "We sold 200 million, 18 months, three quarters, 20 times oversubscribed." Let them have it. But it's up to you three fellows to service them. Show it to me; if I don't think it's worth while, all right. But it really ought to kind of originate with White and flow up through - to see that these fellows get information. Butterworth seemed to - but that was all - he kind of hinted around that he said - and that's another thing: that when we did the 300 million dollars we let them know in advance, and we didn't this time. Well, I sent them a cable we didn't let George Harrison know either.

Harrison: I can testify to that.

H.M.Jr: Don't be funny. And it was just one of these times that we .....

Harrison: Well, isn't it true that the British in the past, in the handling of their fund, have desterilized gold by selling it to the Bank and getting pound credit?

White: Yes, without telling us. Quite. Time and again.

H.M.Jr: Not a word.

Harrison: So that - of course, the only difference is that there they have done it as a matter of routine and it doesn't come out in the newspapers, and we do it with a great fanfare of publicity. Seems like a lot more than they did.

H.M.Jr: You're perfectly right.

White: I think they unquestionably have done it. But I venture to predict that when next week's "Economist" comes to us, there will be a very excellent analysis of what desterilization meant and accomplishes, which was probably written 24 or 48 hours after the event. No difficulty in understanding it.

H.M.Jr: I don't think the British Treasury had any real reason - we just couldn't let them know in advance, because we didn't have time to let anybody know in advance. As a matter of fact, if you get right down to it, our own State Department ....

White: Only two hours.

H.M.Jr: I didn't call up Herbert Feis and tell him. I mean if anybody is going to get hurt, Herbert Feis would have the best right. But we didn't let - we didn't do anything ....

Harrison: Glad I'm in such good company, doctor.

Feis: But I think the thing you said makes the main point: that it is really a type of technical banking action that is almost best treated as routine.

Harrison: Well, I think it would have been except for the amount. I think the amount is probably what made them think it was not routine.

Feis: That's right. As you say, they do it week by week over there. We leave it alone for nine months and then ...

Taylor: It's in the way we handle it, too, with quite a lot of publicity.

(H.M.Jr receives charts and ticker clippings from Mrs. Betts)

H.M.Jr: (On phone) Colonel McIntyre, please.

"Roosevelt to see S.E.C. Chairman Douglas at lunch with Sec. Morg." Does that mean that I eat and Douglas doesn't? He sees Douglas and eats with me? Funny wording. Maybe we're having lunch together. Oh my God, Douglas and I eat with the President.

Harrison: Do they give the menu?

H.M.Jr: No.

Feis: They only had enough for two. Have to make it go around for three now.

H.M.Jr: I wonder what's the significance of that? Huh?

Harrison: I hope it's some modification of the S.E.C. rules.

H.M.Jr: That would be ...

(On phone) Hello. - Well, keep after him anyway. Please. Will you? How about London? - Any chance? - - Well, tell them I'm not too fussy on the secrecy; I'll take any old line. But I'm in a hurry, tell her, I'm not too fussy.

Well, at least this kind of clears the atmosphere - I mean we get it off. And it's pretty important; we haven't had a meeting like this in a long time.

If the men don't mind waiting until we hear from Butterworth .....

April 25, 1938
11:24 a.m.

H.M.Jr: Hello.

Operator: Butterworth. Go ahead.

H.M.Jr: Hello.

W. W. Butterworth: Hello.

H.M.Jr: Hello, Butterworth.

B: Yes, Mr. Secretary.

H.M.Jr: How are you?

B: Very well, thank you. And you, sir?

H.M.Jr: I'm all right.

Now, I just got through talking to Cochran.

B: Yes, sir.

H.M.Jr: And he's sending you a copy of a cable he's sending me today.

B: Yes.

H.M.Jr: Did you get his 644?

B: I did indeed, sir.

H.M.Jr: Now, he gave us a review of what happened today, and they got the franc down from about 165 to roughly around 160.

B: Yes, sir.

H.M.Jr: And so evidently they're making an effort.

B: Yes, they are.

H.M.Jr: Now, what they did today - I - it's come out on the ticker. It isn't very clear, but it seems to boil itself down that they're sort of withholding an announcement until these two French gentlemen come over to England.

B:	Uh-huh.
H.M.Jr:	That's what it looks like.
B:	Uh-huh.
H.M.Jr:	Now, in that cable 645 Cochran gives us some of the objectives of the French gentlemen and what they hope to do, you see?
B:	I see.
H.M.Jr:	And I've asked Cochran to go in and see Marchandeau again and ask him what are his objectives in regard to the French franc.
B:	Yes.
H.M.Jr:	That I don't feel that he has yet informed us.
B:	Yes.
H.M.Jr:	Now, that is the whole picture.
B:	Right, sir.
H.M.Jr:	And what I'm telling you - I have no objections that you should pass that along.
B:	Indeed I will, sir.
H.M.Jr:	Now, if they have anything over there that they know as to the objectives of the French in regard to the franc - if the British Treasury knows anything, I'd like to get it.
B:	Right. I certainly will. Well, I had a word with them this morning and they said that they had no specific information at all; that Lenorcy, the Assistant French Financial Attaché, had come to see them here and that he had said that - he had volunteered that the French Government of course could not at this time hold the franc at any particular figure, such as 155 or 160.
H.M.Jr:	Yes.
B:	But the British said to them that they completely

understood that; that - that they never thought they were going to do so.

H.M.Jr: Yes.

B: However, that it was quite a different thing if they had a French Cabinet Minister who was bruiting about stories which were taken up by the market ....

H.M.Jr: Yes.

B: ... and led to a rapid and unnatural depreciation.

H.M.Jr: Yes.

B: And I gather the conversation was left at that.

H.M.Jr: Well, you see, heretofore they've told us what - between what limits they were going to try to hold it.

B: Yes.

H.M.Jr: And when they have told us, they've always made the effort.

B: Yes.

H.M.Jr: Well, up to now they haven't given us those limits.

B: Yes.

H.M.Jr: So we don't know. And what I'm asking for is, I'd like to know. I'm entitled to know.

B: Well, they feel the same way here. They said they thought that all they could do at the moment was to wait in view of this forthcoming visit.

H.M.Jr: Yes. Well, I'm giving you this ....

B: Because the once Finance Minister is coming over here.

H.M.Jr: Yes. I'm giving you this because the scene of action is going to be transferred to London within a couple of days.

B: Yes, sir.

H.M.Jr: And then let's see what you - what luck you have.

B: All right, sir.

H.M.Jr: Now, is there anything - any gossip, anything you can pass along?

B: No - ah - the market at the moment still believes that there is a divergency of view in the Cabinet.

H.M.Jr: In the French Cabinet.

B: Yet the ticker reports that ....

H.M.Jr: Yes.

B: ... that all has been settled at this Council of Ministers.

H.M.Jr: Yes.

B: But whether or not that is correct I don't know.

H.M.Jr: Uh-huh.

B: Naturally the fact that Daladier and Bonnet are coming over here has increased the discussion in the City about the question of a French loan.

H.M.Jr: Uh-huh.

B: But the feeling here is that it would be very difficult to make it upon terms which would be satisfactory to the market.

H.M.Jr: Uh-huh.

B: And there's not much enthusiasm for it.

H.M.Jr: I see.

Now, just a minute, I'll ask Herbert Feis if he has anything. He has not.

Just a moment.

B: Right.

(Pause)

H.M.Jr: (Aside: No. No.)

Hello. Hello?

B: Yes, sir.

H.M.Jr: No, if we get anything we'll let you know.

B: Yes, sir.

H.M.Jr: And - but up to now, all we know is after they've taken the hour-to-hour action - that's all we know.

B: Yes, sir.

May I - may I send a message to Herbert, sir?

H.M.Jr: Yes.

B: Ah -

H.M.Jr: Wait a minute, you can do it direct.

B: Herbert?

Herbert Feis: Hello, Walton.

B: Hello, Herbert.

Feis: How are things over there?

B: all right. Herbert.

F: Yes.

B: Watson just telephoned me.

F: Yes.

B: And asked me to come to dine with him tonight.

F: Yes.

B: To talk over his forthcoming trip to the States. He plans to sail tomorrow.

H: Yes.

B: And I gather this is unexpected. And I don't know what the reason is. But I just thought I'd tip you off.

H: Have you cabled the Department about it?

B: What?

F: Are you cabling the Department about it?

B: He just telephoned me about half an hour ago.

F: All right.

B: So I thought I'd wait until I dined with him tonight and find out what's what.

F: Extremely interesting, Walton.

B: All right. I - I just thought I'd pass that on to you.

F: Thank you.

Walton, are you handling tin?

B: Yes.

F: We're getting you off a cable this afternoon.

B: Well, I just sent you a dispatch which - the final paragraph of it was written by the Ambassador.

F: Written dispatch? Written?

B: That he knows about pools and none of them can work, unless they have the credit of a major country behind them.

F: Uh-huh. Did you say a written dispatch?

B: Yes, a written dispatch on ....

F: All right, if you find anything in the cable instructions that doesn't fit in with the analysis in your dispatch, why, you follow your own judgment, huh?

B: Well, there's not an analysis. The - when this dispatch was shown to the Ambassador he said he'd like to go on record as saying that he didn't believe these pools were workable.

F: I see.

Thank you, Walton. Give my love to Virginia.

B: Mine to Ruth.

F: Right.

B: Good-bye.

F: Wait a minute, I'll find out .. - the Secretary says he's through unless you have something more.

B: No, I haven't.

F: Good-bye, Walton.

B: Good-bye.

April 25, 1938.
11:44 a.m.

H.M.Jr: Hello.

Operator: Mr. Franklin.

H.M.Jr: Hello.

Operator:- Go ahead.

H.M.Jr: Hello.

P. A. S. Franklin: Hello.

H.M.Jr: Mr. Franklin.

F: Yes.

H.M.Jr: Henry Morgenthau, Jr.

F: Oh, Henry Morgenthau, Jr.

H.M.Jr: Yes, sir.

F: All right.

H.M.Jr: Secretary of the Treasury. Mr. Franklin, I'm calling up on a matter which I would like to have your cooperation, but it's purely a volunteer matter. And if you don't feel like giving it, I will not have any hard feelings.

F: Right.

H.M.Jr: And it also is not directly under you, but I felt I'd rather approach you than possibly someone else in your organization.

F: Yes.

H.M.Jr: On Friday the Panama Pacific Railway - Steamship Company - the Panama Pacific Steamship Company ...

F: Yes.

H.M.Jr: ... sold in five minutes $11,000,000 of United States Government bonds.

F: Panama Steamship Company.

H.M.Jr: Yes. And it was such an unusual transaction and it was handled in such an unusual way that I was curious to know what the story was back of it. And we can't find that the Panama Pacific Steamship Company owned $11,000,000 worth of Governments.

F: Oh. What did they do?

H.M.Jr: What they did was - they asked the Government bond dealers to give them bids on $11,000,000 worth of Governments; gave them five minutes, and then - they said, "You've got just five minutes to give us a bid on $11,000,000 worth of Governments." And then they sold them. Well, it so happened that Friday was about the only day in about a year that the market could have absorbed $11,000,000 worth of Governments ....

F: Yes.

H.M.Jr: ... in five minutes. And as I've said jokingly around the office, we haven't had anything like that happen since the Russians sold a million pounds of sterling in thirty seconds.

F: Yes.

H.M.Jr: I mean - and it was an unusual transaction and handled in such an unusual way, plus the fact that we can't find that the Panama Pacific Steamship Company owned any Governments to such an extent.

F: Panama Pacific Steamship Company.

H.M.Jr: Yes.

F: Why, they don't own them.

H.M.Jr: Pardon me?

F: They don't own them.

H.M.Jr: No, we can't find that they own them. So, as I say, I'm asking this purely on a basis of whether you'd care to find out, volunteer it; if you feel that the request is not a reasonable one, why, forget it.

F: I'll see if I can find out about it.

H.M.Jr: If you can, I would appreciate it.

F: I'll telephone you.

H.M.Jr: Yes, sir. Thank you very much.

F: Panama Pacific Steamship Company.

H.M.Jr: Panama Pacific Steamship Company, on Friday.

F: On Friday went into the market for 11 million.

H.M.Jr: Yes. Sold.

F: Sold 11 million.

H.M.Jr: Yes.

F: My goodness, that's astonishing.

H.M.Jr: And - and gave the market just five minutes to take them.

F: Gave the market only five minutes to take them.

H.M.Jr: Yes.

F: All right. Well, I'll look into it and let you know.

H.M.Jr: And - thank you.

F: Let you know if I can find out anything about it.

H.M.Jr: All right. Thank you very much.

F: I've got to go out to luncheon now.

H.M.Jr: Oh, this isn't a matter of minutes. I mean either today or tomorrow. But - but I'd appreciate it.

F: All right, thank you.

H.M.Jr: Good-bye.

April 25, 1938.
2:59 p.m.

H.M.Jr: Hello.

Operator: Mr. Franklin.

H.M.Jr: Hello.

Operator: Go ahead.

H.M.Jr: Hello.

P. A. S. Franklin: Hello.

H.M.Jr: Morgenthau speaking.

F: Good. This is Mr. Franklin.

H.M.Jr: Yes.

F: Ah - there are - I'm very sorry to say I haven't been able to find out a thing about that for you.

H.M.Jr: I see.

F: Now, if you find out anything about it, I'd be very much indebted to you if you'd let me know.

H.M.Jr: Well ...

F: I wish you'd try.

H.M.Jr: Well - ah - we can. I mean we can get - at least, I think we can - but - we can find out about the delivery and all that.

F: I wish we had eleven thousand - eleven millions of the bonds.

H.M.Jr: Yes. Well, you can't find out anything about it?

F: Can't find out a thing about it. I'm very sorry.

H.M.Jr: Well ...

F: And there's no company by that name. Now, please let me hear from you after you've investigated a little further.

H.M.Jr: I'll do that.

F: I'd like to know what was behind it.

H.M.Jr: I would too.

F: There's something behind it.

H.M.Jr: I see.

F: I don't know what it is, I don't know whether somebody's trying to make some impression upon somebody or not.

H.M.Jr: Uh-huh.

F: Or if they're trying to do something against us - I don't know.

H.M.Jr: I see.

F: But I'd appreciate it if you'd let me know.

H.M.Jr: I'll certainly do that, Mr. Franklin.

F: I'm very much obliged to you.

H.M.Jr: We'll - we'll - we'll do the best we can to run it down.

F: How's everything down there now?

H.M.Jr: Oh, I'd say a little quieter.

F: Well, things are awfully quiet with us.

H.M.Jr: I see.

F: We're waiting for a decision from the Shipping Board which we haven't had.

H.M.Jr: Fine. Well, you won't likely know it, but the Treasury is one of your best customers.

F: What?

H.M.Jr: We're one of your best customers.

F: Well, I'm very much obliged to you.

H.M.Jr: That gold and silver we put on your boats.

F: Splendid. I say it's just saved our lives.

H.M.Jr: And we must pay you a tidy sum every year.

F: Yes indeed, and it's been a very great blessing to us.

H.M.Jr: Well, some good out of it anyway.

F: Much obliged to you.

H.M.Jr: All right, Mr. Franklin.

F: I hope you'll let us reciprocate.

H.M.Jr: Well, I'm just - just on the taxpayers' payroll, that's all.

F: All right. Thank you. Very much obliged to you.

H.M.Jr: All right, good-bye.

April 25, 1938.
3:13 p.m.

H.M.Jr: Hello.

L. A. Simon: Yes, Mr. Secretary.

H.M.Jr: Mr. Simon.

S: Yes.

H.M.Jr: The President of the United States is very much disturbed because he hears that the Rhinebeck Post Office - they're not going to use old stone wall, that they're planning to open up some stone quarries. And his instructions are that they should use old stone wall.

S: Well, Mr. Secretary, here's what the situation is. We sent Stanley Brown up there and he found that we could get quite a little stone from the old building, that ....

H.M.Jr: Well, listen, you better write me a memo on it. And the President wants old stone wall.

S: Yes. I see how the thing came about. Mr. Shipley, who is the owner of the place, said that he'd rather not use the old French wall off of his place, but there are plenty of more old stone walls all over Dutchess County.

H.M.Jr: Well, are you going to use old stone walls?

S: Sure we are.

H.M.Jr: Well, for God's sake do, please.

S: Yes, we certainly are.

H.M.Jr: And no new stone.

S: No.

H.M.Jr: Well, the country is saved. O.K.

S: All right.

April 25, 1938.
3:30 p.m.

H.M.Jr: Hello.

Operator: Chairman Douglas is at a meeting at the Capitol. She thought if it's urgent she can ask him to call you, and he'll be back at his office at 5:30 or 6.

H.M.Jr: Uh-huh. Ask him if he would call me - ah - tonight at my house - if he could call me about 7:15.

Operator: 7:15.

H.M.Jr: At my house.

Operator: All right.

H.M.Jr: And if you could get - a good way to do would - if you could find out where he'd be at - well, maybe - ask him to call me.

Operator: All right.

H.M.Jr: Will you please?

Operator: All right.

H.M.Jr: And then - ah - ah - I'll let you know. Do that anyway. Ask him to call me at 7:15.

Operator: All right.

April 25, 1938.
4:23 p.m.

Operator: Operator.

H.M.Jr: Commissioner Hanes, of the S.E.C.

Operator: Right.

(Pause)

H.M.Jr: Hello.

Operator: Commissioner Hanes. Go ahead.

H.M.Jr: Hello.

John W. Hanes: Hello, Mr. Secretary.

H.M.Jr: Can you hear me?,

H: Yes, sir.

H.M.Jr: Are you alone?

H: Yes, sir.

H.M.Jr: Good. Mr. Hanes.

H: Yes, sir.

H.M.Jr: I was at lunch with the President today.

H: Yes, sir.

H.M.Jr: And I asked him whether I could talk to you about coming over to the Treasury as Assistant Secretary, and he said I could. And he said I should talk to Douglas. Well, I've been trying to get hold of Douglas and I can't get him until tonight. But ...

H: He's - he's gone to New York, Mr. Secretary.

H.M.Jr: Has he?

H: You - you - you've knocked me so flat on my back side that I haven't got anything to say.

H.M.Jr: Well, I wanted to have you think about it and I wondered whether you'd care to pick me up at the house tomorrow morning and walk down with me.

H: I'd like to very much, sir. If you'll give me - if you'll give me - if you'll give me the ....

H.M.Jr: Address.

H: ... address where I can pick you up, I'll certainly do it.

H.M.Jr: 2211 30th Street.

H: 22 -

H.M.Jr: 11

H: - 11

H.M.Jr: 30th.

H: 30th Street.

H.M.Jr: Now, that's just off Massachusetts Avenue.

H: Yes, sir.

H.M.Jr: I don't know whether you know where Senator Tydings lives.

H: I do not, no, sir, but I can find this all right. 2211 - that's - I come down Massachusetts Avenue in the morning anyway.

H.M.Jr: Well, it's - it's - we're just opposite House's house.

H: Yes.

H.M.Jr: You know, Ambassador House.

H: Oh yes. Yes.

H.M.Jr: And the reason I'm describing it - lot of people go over into Georgetown, and we don't live over there.

H: I see. It's - it's turn left; if I'm coming from Massachusetts Avenue toward my office, I'd turn left on 30th Street.

H.M.Jr: On 30th.

H: Yes, sir. I'll pick you up. And what time shall I pick you up there?

H.M.Jr: About 8:30.

H: 8:30?

H.M.Jr: Yes.

H: I'll be there, sir, at 8:30.

H.M.Jr: You think this over, because I've been thinking it over and I talked to the President Friday and asked him to think it over.

H: Yes, sir.

H.M.Jr: And we - we could use you over here, and I think can make it interesting.

H: Well, that's awfully kind of you, and very - it's very - I don't know, I think you probably are mistaken in the individual.

H.M.Jr: No.

H: But I'm not going to argue with you about that.

H.M.Jr: No, I'm not. I've taken lots of trouble to find out, and I know I'm not mistaken.

H: Well, you're terribly kind. And I'll pick you up there tomorrow morning at - at 8:30.

H.M.Jr: All right.

H: I do thank you, sir.

H.M.Jr: Good-bye.

H: Good-bye.

April 25, 1938.
4:39 p.m.

H.M.Jr: Randolph.

W.R. Burgess: Yes.

H.M.Jr: I talked to P. A. S. Franklin and ...

B: Yes.

H.M.Jr: ... Governor Harrison was here when I did.

B: Yes.

H.M.Jr: And Franklin called me ~~back and said he~~ was completely mystified. He said he wished to Heavens that they had $11,000,000 worth of Governments. And he said, "Now, Mr. Morgenthau, you asked me to do you a favor; I'm going to ask you to do one."

B: Yes.

H.M.Jr: He said, "Please run that story down." He says, "I'm terribly worried about it."

B: Uh-huh.

H.M.Jr: He says, "We have no record," and he says, "We just don't understand it," and he says, "You've got us worried now."

B: Well, I'll be damned.

H.M.Jr: And he said two or three times, "Now, will you please promise me to run that story down." He says, "Frankly, you've got us worried."

B: Yes.

H.M.Jr: So I promised him that I would.

B: Yes.

H.M.Jr: Now, will you - will you do your best?

B: I will, yes.

H.M.Jr: He said two or three times, "Now, you will promise me to run that story down, won't you?"

B: Yes.

H.M.Jr: He says, "I .." - he says, "I ..." - he says, "We're completely mystified."

B: Well, they didn't sell anything at all, they didn't have anything to sell?

H.M.Jr: They said they don't know, they haven't got it. He said - "Gosh," he said, "we wish we did."

B: Well, I'll be damned.

H.M.Jr: Yep. So I - I think you better call those people in and have a little heart-to-heart talk with them.

B: Yes.

H.M.Jr: What?

B: Yeh. Well, I'll see what I can do, Henry.

H.M.Jr: Yes, because it's - it certainly is worth running down.

B: Yes. There may be - may have some lad in their offices operating as a stooge for somebody else.

H.M.Jr: Yep.

B: Yes.

H.M.Jr: I got my own suspicions, but I - I'm not going to say.

B: Yes. Uh-huh. Uh-huh.

H.M.Jr: So will you run it down?

B: I'll do my best, Henry.

H.M.Jr: Right.

B: See what I can get.

H.M.Jr: Thank you.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 25, 1938, noon

NO.: 645

RUSH

FROM COCHRAN.

This morning at half-past eleven I called at the Bank of France. The French control by that hour had yielded 100,000 pounds. The rate had been brought from a little beyond 166 to 165.75 to the pound by that time. Therefore there was not as much pressure as there had been the last two days of the past week. Daladier's statement on Saturday, on the other hand, combined with the press report that the Government was speeding up its decisions on financial matters, had not been sufficient influence to bring about a market reverse.

Confidential information was given to me that one of the main features of the plans which are being studied today is that of imposing a 3 or 4 percent tax upon all payments with a view to raising a yearly amount of five or six billion francs. The expection of bank officials is that rather than have a good reaction, such a plan would have a bad effect. Daladier, it is said, is insisting that they should ask the British for a loan when he and Bonnet go to London this week, as an offset for the cooperation

which

which it is believed will be requested of France by Great Britain. Attempt is being made by officials of the Bank of France and some Cabinet members to persuade Daladier not to seek assistance from abroad. However, he seems intent to carry out this plan,up to the present. Daladier believes that it would be reasonable for the equalization fund of Great Britain to purchase four or five billion francs and lend them to the French Government rather than take gold for the francs. What the reply of Chamberlain and Simon would be likely to give to such a request is anticipated by my Bank friends.

If the two plans which are outlined above are indicative of the kind of program being launched by the French Government, they ~~xxx~~ do not give much promise as a counter attack against those speculators who anticipate a franc quoted at 175 to the pound and whose theories were very much strengthened by the Treasury's weak policy in the last part of last week in direction of the French control.

WILSON.

London, April 25, 1938.

Dear Henry:

I understand that while Blum was Prime Minister, we told him that, if he considered it desirable to institute a form of limited exchange control in France, we would not object to it and would help to persuade the British that it did not break the Tripartite Agreement. This interests me for two reasons: first, because I am sure that no limited exchange control system can stay limited and still be a control system, and secondly, because in making such a suggestion to Blum we were certainly coming pretty close to playing dirty ball against the British. I grant you the British are usually able to protect themselves, but if we play that kind of game we will get it played on us as well.

Do write me whose idea this was and who harbors such simple faith in limited controls when all of the

The Honorable
Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington, D.C.

countries in Europe that have begun this way have always ended by putting on all the controls they could think of.

Yours sincerely,