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Minneapolis
April 1, 1939

FOR THE SECRETARY:

Since yesterday's conversations indicated an overwhelming interest in Europe and since there was much discussion of Hitler's reply to Chamberlain today, I tried especially to find out what the business men and bankers thought we ought to do in the event of a European war. The opinion was almost unanimous that the United States should stay out of the war, but should sell anything any country wants to buy. In addition, most of the people expressed a fatalistic belief that, try as we might to avoid it, we would eventually be dragged into a war abroad. Other outstanding bits of the day's conversations were:

Several people expressed amazement at reports that the President is planning to appoint former Governor Elmer Benson to the ICC or the Federal Reserve Board. They say two of Benson's aides are in jail for graft, that Benson may be in jail himself eventually, and that even politically he has nothing to recommend him.

Local politics, in which the farmers seem to have turned very anti-labor union and in which the 32-year-old Republican governor cuts quite a figure, excited more interest than Washington affairs.

The banks all object to the Federal Savings and Loan Associations which they accuse of dishonest practices and bad management.

Many people remember Mr. Hanes' visit of last year and approve his line of action since coming into the Treasury.

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Nash and Finch, wholesale grocers -- Mr. E. L. Nash, one of the younger members of the firm was the only officer in when I called. He said their firm had made less money last year than in 1937. Earnings in the first two months of this year were better than a year ago, but a shade below expectations.

His company is especially interested in the Government's free food distribution. Very often, he said, this distribution might be the deciding factor in pushing a wholesale grocery house from a small profit into a loss. He cited numerous instances of excessive food distribution by the Surplus Commodities Corporation and was of the opinion that, when more than a usable supply of rice or grapefruit was given to relief clients, the excess food found its way onto the tables of the relief clients' friends who otherwise might have bought the goods from stores. Managers of his company's stores had returned home to find crates of oranges left on their doorstep by the Surplus Commodities Corporation, he said. He had no advance opinion on the orange-and-blue-ticket distribution system, but said his company was going to watch it closely and hopefully.

Europe, Mr. Nash thought, was the chief disturbing factor for business, causing people to wonder about future prices and business activity. The president of their company, he said, had been very much upset by a Kiplinger letter outlining the war-time tax proposals pending in the Senate. Farmers and business men in the Northwest would be very irate at any legislation preventing them from selling their wheat or other products to belligerents, Mr. Nash thought.

Another uncertainty in the business men's minds is doubt over what is going to come out of Washington, according to Mr. Nash. One day "appeasement" seems to be the keynote and the next day the left-wing New Dealers seem to be in the saddle, he said.

Wells, Dickey and Company, local investment bankers -- Mr. Purdy, vice president in charge of sales, described himself as a Democrat who went along on almost all of the Administration's program. He said he personally favored a change in the neutrality act to give the President more discretion, but he indicated that most of his friends disagreed. Regardless of what the President actually told the Senate Military Affairs Committee, our frontiers really are "over there", and supporting the democracies is the cheapest way of defending ourselves, Mr. Purdy feels. He hopes America can stay out of a war. He accounts for the isolationist feeling locally, but saying the Swedes and Norwegians are pacifists and afraid of the Germans, but are anxious to sell to anyone who will buy, including belligerents. European news reaches the Middle West slower than it does the East, but has the same depressing effect on business, he said.

Business is pretty good, and the outlook is good in his opinion. On the other hand, he doesn't believe that there will be a great amount of financing by local industries which will result in expanding their plant or equipment. Some such financing is in sight, but not much is needed, he said. One of the Reserve Bank vice presidents had remarked yesterday that many concerns had invested more in plant in 1936-1937 than they now proved to need.

Mr. Purdy believes that business can get all the credit and capital it needs and deserves through existing institutions. His firm has a reputation of being willing to underwrite securities for small local companies, and he says the firm's experience with these small underwritings has been good. He thinks private enterprise could do more in this field and is not disturbed by the competition banks are giving his company through "term-loans".

He was, however, somewhat provoked at a minority opinion written by Federal Power Commissioner Jack Scott on a $1,200,000 bond issue which Wells, Dickey had underwritten for a small North Dakota power company. Commissioner Scott evidently took the position that the price at which the bonds were offered to the public ($98) was too low. Mr. Purdy thought that, if any such view ever became the majority opinion in Washington, the public would never get an attractively-priced issue. He argued that there are two sides to the price question and that an opinion which looked only at the advantages accruing to the issuing company overlooked the public's interest in attractive prices for securities. Mr. Purdy approves of both the SEC and FPC.

Private investors in this area, according to Mr. Purdy, are chiefly interested in tax-exempt securities and secondly in high-grade corporate bonds. For this reason, he looks for very little change in the prices for such bonds if the war scare continues or increases, but second-grade bonds and stocks will drop, he believes. The interest in common stocks "as a hedge against inflation" has died out, Mr. Purdy says, but adds that common stocks are still regarded by his firm as an important part of any proper portfolio.

Northwest Bancorporation and Northwestern National Bank -- Officers of these two companies, about ten in number, invited Sedlacek, who has just arrived from the Coast to become chief national bank examiner here, the head of the local RFC office, and myself to lunch. The officers were an interesting group, disagreeing among themselves on almost every point.

They were unanimous, however, in asserting that, if was broke out in Europe, the United States should sell anything any country wanted to buy. They argued that we are a trading nation and should sell where we can. Mr. Thompson, president of the Bancorporation, said that he thought the Scandanavian farmers in the region were very selfish and, in spite of their pacifism, would insist on selling to belligerents if belligerents offered good prices.

On the other hand, everyone in the group thought we ought not to become involved in a military way. One officer remarked that any such attitude simply meant that America didn't know what it wanted to do because trading with belligerents and staying out of war were incompatible. This remark brought a few admissions that probably the United States would "get dragged into" any general European war. (After the luncheon some other members of the group, evidently much interested, came up to me to express the same fatalistic view.)

Mr. Thompson and Mr. McGregor, both of whom are Canadian-born, criticized England, saying she was calculating and cold-blooded and would persuade us to fight for ideals when no ideals were involved. This brought much loud dissent from the rest of the group who were all American-born.

Mr. Wold, chairman and senior officer, who is a rugged individualism Republican, spoke up to defend foreign lending (incidentally, he also praised the SEC) and said that America should lend to stimulate the international exchange of goods. Healthy trade, he said, was the mutual exchange of goods, not the exchange of goods for gold. In making foreign loans, he said we should not worry too much about the past record of the borrowers, and Mr. Thompson concurred. Mr. McGregor disagreed saying a bad borrower was always a bad borrower. Mr. Wold replied that past defaults of many nations like Brazil could be blamed on American investment bankers who fostered any type of unsound bond issue to get the commission.

When I asked about the lack of interest in the Government spending issue, Mr. Wold replied, "It depends on whose ox is gored," explaining that nobody wanted to see his type of spending cut. No further remarks were made, and the group seemed not to care at all about the spending issue except to agree that Congress would not economize of its own volition. They turned to a discussion of local politics in which the farmers are forcing through stringent anti-union legislation.

One officer took occasion after the luncheon to praise your position on the social security program. Also Mr. Thompson remarked that he expected the Comptroller's Office to be abolished under the reorganization bill and that Senator Glass had assured him there would be no bank holding company bill. Mr. Thompson and another officer, like the First National of St. Paul officers yesterday, spoke bitterly of Giannini because of the disrepute he had brought on group banking.

Mr. Thompson said he had heard that small banks had bad bond portfolios and that they were worse in Wisconsin than anywhere else.

Minnesota Bankers Association -- Mr. Duncan, secretary, agreed that small banks were getting into trouble by buying speculative, high-yield bonds. He had reports from half the state banks showing that they had sustained almost $1 million of losses on bond transactions last year. Special efforts by the state university to help the bankers with their bond portfolios have had little effect. When I asked why some big banks said that the little banks had no bond trouble, he said the big banks never see the bad banks' portfolios.

Mr. Duncan had collected many examples of what he considers dishonest advertising by Federal Savings and Loan Associations and feels that Washington is letting them get away with something. He approves of other types of Federal activities which bankers have criticized such as production credit associations and the CCC. Mr. Duncan says that, in spite of bankers' complaints, he would like to see the PCA work continued because it would be essential in a depression and because in his opinion a wide-awake energetic banker can get his share of the business away from the PCA. The same, he said, is true of the CCC, and Mr. Maynard, head of the RFC office, said that banks were increasingly willing to make commodity loans (with the RFC standing back of them) since the CCC had shown it could be done. This year the local CCC had had to make very few direct loans on corn and expected that next year it would have to make few wheat loans. The banks are anxious to make the loans with assurance that the RFC will take them over when necessary.

ESD

Columbia University
in the City of New York
SCHOOL OF LAW

April 1, 1939

Dear Henry:

In line with our conversation this morning there are comparatively few major changes which it seems to me need to be made in the statement which we discussed with the President on October 29, 1937. The principal changes to be made are the obvious ones of bringing the figures down to date and discussing the balancing of the budget as a matter to be accomplished in a future year (we hope not too distant) rather than an expectation for the current year.

I am listing below the particulars in which changes might well be made in the statement, with references to the pages of the original memorandum.

1. [page 3.] In my judgment the tax revenues ought certainly to be maintained and if possible increased, since it seems reasonably clear that the Federal budget cannot be balanced at any figure under seven billions of dollars. Probably under present circumstances it would be unwise to attempt too sharp an increase, but since changes made this year in the income tax and the estate tax will not produce new revenue for many months to come, I should think you might fairly aim at a revised revenue system that would produce at least a billion dollars more than the present system is producing, on the basis of about the present national income.

2. [page 3, item 1 (a)] Reference should be made to the fact that the recent decision of the Supreme Court in Graves v. O'Keefe now permits taxation of the salaries of Federal officials by state governments and of state officials' salaries by the Federal government. Do you not want to suggest that taxes on the state salaries should now be imposed by the Federal government, but that in the interest of fairness, the tax should not be collected as to years back of say 1938. I would reaffirm the recommendation that the present exemption of the interest on state and municipal bonds should be eliminated as to future issues.

3. [page 4 and page 12] I presume that you cannot very well afford to eliminate any more nuisance taxes at this time. You will recall that we eliminated the most unproductive and administratively undesirable nuisance taxes in 1938.

4. [pages 5, 6] I do not feel quite so strongly about the modification of the deduction provisions as I did in 1937, but the general idea is all right.

5. [page 8] I am not sure that it is desirable to make any considerable change in the earned income credit except possibly an increase in the limitation on earned income from $14,000 to say $20,000.

6. [page 8] The capital stock tax and excess profits tax should be repealed and the lost revenue made up by an increase of around 1% in the corporation income tax rate. If you wish, it is entirely possible to retain lower rates for "small" corporations than for "large" corporations, but I certainly should not advise you to recommend a graduated set of rates for corporations of different sizes, similar to those now in effect for individuals. The lower rate on small corporations and the elimination of the normal tax on corporate dividend distributions will considerably ease the burden on the stockholder with a small income.

7. [page 9] The undistributed profits tax should be repealed. It is so small as to produce little revenue; it is really an undesirable additional tax with respect to the small income stockholder; and the friction it causes is entirely out of proportion to its revenue significance.

8. [page 11] The estate and gift taxes should be coordinated and the rates should be markedly increased if more revenue is to be obtained from the Federal tax system.

I am very glad to know that you think there is some possibility you can issue a statement of this kind. I am sure that our old statement can be drafted to have a greater popular appeal but I think the meat of the statement is almost as good today as it was in 1937. Be sure to call me if I can give you any further assistance and if you want me to come to Washington to talk with you let me know. I have classes on Tuesday and Wednesday of next week but not on Monday. I have a speaking engagement at Columbus, Ohio on Thursday, the 13th.

With warm regards and all good wishes, I am

Sincerely yours,

Roswell Magill

Roswell Magill

Hon. Henry Morgenthau, Jr.
The Cloisters
Sea Island Beach, Ga.

DRAFT

STATEMENT OF THE SECRETARY OF THE TREASURY
BEFORE THE COMMITTEE ON WAYS AND MEANS

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I am pleased to respond to your invitation and discuss with you the question of what changes, if any, in our tax laws are shown by study and experience to be needed at this time. To approach this question intelligently we need to have in mind the background of our present system.

In your capacities as members of this Committee and of Congress, you have during the past few years been largely instrumental in the making of numerous changes in the structure of the Federal tax system. These changes were made primarily to meet revenue needs growing out of the depression.

In the fiscal year 1930, the revenue collections amounted to slightly less than $4,200,000,000. As the depression deepened, the revenue fell off sharply so that by the fiscal year 1932, the yield was only $2,000,000,000, or less than half the 1930 collections. Expenditures meanwhile were rising as the government acted to meet the problems created by the depression.

Confronted with this situation, Congress in 1932 radically revised the tax system, and in most of the years since then has further strengthened the power of the system to produce revenue. As economic conditions improved and the tax changes became effective, revenues increased from the low point of $2,000,000,000 in 1932 to $6,240,000,000 in 1938 under conditions of incomplete recovery.

The increase in the revenue-producing power of the tax system was accomplished principally:

By lowering exemptions and increasing the rates and degree of progression of the individual income tax, and disallowing deductions that reduced the yield;

By increasing the corporation taxes through raising the rates of the income tax, disallowing types of deductions that reduced the yields and providing an inducement for the distribution of profits, and by imposing a capital stock and an excess profits tax;

By imposing an undistributed profits tax to compensate the government for the loss of revenue that results when corporations withhold earnings from their stockholders;

By lowering exemptions and increasing the rates and degree of progression of the estate taxes and enacting a gift tax to make the estate tax more effective;

By enacting liquor taxes following repeal of prohibition;

By enacting various excise taxes and increasing the rates of others; and

By levying payroll taxes to aid in financing the social security program.*

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* Specifically, during this period the personal exemptions under the individual income tax have been lowered from $3,500 to $2,500 for a married couple or head of family and from $1,500 to $1,000 for a single person. The maximum tax rates, normal and surtax combined, have been increased from 25 percent to 79 percent. Not only were the top rates increased, but the increase was general throughout the range of incomes. For example, on the bracket of income immediately over $100,000, the rate has been increased from 25 percent to 62 percent. During the same period income from dividends has for the first time been subjected to the normal rates of the individual income tax.

The corporation income tax has been increased from a flat rate of 12 percent to graduated rates of from 12½ to 16 percent for small corporations and from 16½ to 19 percent for large corporations. Whereas previously the entire amount of dividends received by corporations had been exempt from the corporation income tax, during this period we have made 15 percent of the amount of such dividends taxable at the same rates as corporate income. The privilege of filing consolidated returns has been abolished for all corporations except railroads, each corporation being treated as a separate entity for tax purposes. Personal holding companies have been subjected to additional special taxes, and the administration of the special taxes on other types of corporations improperly accumulating surplus has been greatly strengthened. Further, a capital stock tax of $1 per $1,000 of declared value has been enacted and implemented by an excess profits tax designed to prevent undervaluation of the corporate capital stock.

The role of death taxes in the Federal revenue system has been greatly increased. This was accomplished by lowering the exemption for the estate tax from $100,000 to $40,000, by increasing the rates, and by enacting a gift tax. The maximum rates of the estate tax were increased from 20 percent to 70 percent. The increases were general throughout the scale, These revisions have produced a tax system capable of yielding adequate revenue under conditions of full recovery. Receipts for the fiscal year ending this June will amount to approximately $5,600,000,000, a decline of about $600,000,000 from the last fiscal year due to the business recession. The receipts for this year will thus fall short of expenditures by nearly $4,000,000,000 but, as the President stated in his budget message:

> "Sound progress toward a budget that is formally balanced is not to be made by heavily slashing expenditures or drastically increasing taxes. On the contrary, it is to be sought by

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the bracket rate on the amount of net estate immediately above $1,000,000, for example, being increased from 8 percent to 32 percent.

The repeal of prohibition has added approximately half a billion dollars a year to Federal revenues. New manufacturers' excise and other miscellaneous taxes have been enacted and the rates of certain others increased, which, together, have added approximately another half billion dollars annually.

Finally, during this period we have enacted payroll taxes which in the fiscal year 1938 yielded approximately three-quarters of a billion dollars, in order to help finance our comprehensive social security program.

employing every effective device we may have at our command for promoting a steady recovery, which means steady progress toward the goal of full utilization of our resources. We can contribute very materially toward that end by a wise tax program."

The revenue system now in existence is capable of supplying the revenue requirements of the Federal Government if a reasonable increase in economic activity and national income takes place. For instance, when our national income reaches $80,000,000,000, Federal receipts under the existing tax system will probably amount to $8,000,000,000. The same conditions which will have produced this increase in receipts will also make possible a considerable reduction in Federal expenditures.

An adequate revenue yield is not, however, the only test of a good tax system. Such a system should have the least possible deterring effects on the operation of the economy; it should distribute the tax burden fairly in accordance with the principle of ability to pay; it should be as inexpensive as possible to administer, both for the government and for the taxpayer; it should, insofar as possible, impose its burdens directly on the persons finally expected to pay in order to give them a proper consciousness of the cost of government; and it should be suitable for our Federal system. No tax system can be perfect in all these respects, or, indeed, in any of them, but we can strive to make it approach the best possible.

It was to be expected that the rapid increase in the revenue-producing power of the tax system would be at the expense of some or all of these other considerations. Efforts were made, of course, to adjust the system as defects were disclosed from year to year. The time has now come to examine our tax system in a more comprehensive fashion to see what adjustments can be made, which, while preserving the revenue-yielding power, will remove inequities and deterrents to business recovery.

We in the Treasury are constantly investigating the problem of reducing the burdensomeness of taxation without sacrificing revenue. Our tax studies indicate that in some instances present taxes interfere with the smooth and efficient operation of business and discourage enterprise. Without successful business operation, without business optimism and initiative, recovery and a permanently high level of national income and employment cannot be attained. I believe that our primary aim in revising our tax system at this time should be to promote these objectives. Moreover, I believe that these objectives are fully compatible with a further enhancement of the equity of the tax system.

A number of features of our taxes are both inequitable and discouraging to the healthy development of business.

Business is now taxed on an annual basis. The profits of one year are treated without regard for the losses of another. The result is inequitable since business concerns with fluctuating incomes and losses must pay higher taxes than do concerns with stable incomes. Some business incomes fluctuate more than others because they are more susceptible to changes in the general business situation, others more from causes peculiar to the particular industry.

In the interest of fairness, it would be desirable to base the tax on a firm's average income over several years instead of on its income in a single year. Administrative difficulties have prevented the averaging of income. The effect of averaging can be largely achieved, however, by allowing net losses of one year to reduce incomes of future years. This was the practice before the depression.

Failure to provide for the carry-over of losses tends to discourage persons from developing new enterprises, since such enterprises usually suffer losses in their early years. The allowance of a loss carry-over would be particularly beneficial to the depressed capital goods industries. Concerns engaged in these industries suffer heavy losses in some years and enjoy large profits in others. Since a large proportion of the unemployment is traceable to these industries, removal of inequitable elements in the tax structure which tend to depress them is especially important.

There are other features of business taxation in need of revision. Among these are the inter-dependent corporation capital stock and excess profits taxes. These are really taxes on the amount of profits and the businessman's ability to predict them rather than on the actual value of capital stock and excess profits. To minimize combined capital stock and excess profits taxes, the taxpayer must estimate his business profits accurately. Since, however, profits are highly unpredictable, most businessmen are likely to make errors in declaring the value of their capital stock -- errors which may result in disproportionate tax burdens. New enterprises as well as other concerns with widely fluctuating earnings are particularly vulnerable in this guessing contest. For these reasons, I believe it would be desirable to repeal the capital stock and excess profits taxes and replace the revenues thus lost by other forms of corporation taxation.

The capital losses of corporations are now deductible from other sources of corporate income only to the extent of $2,000. Under this provision a corporation with a deficit may be required to pay a tax. Such a situation would arise when the capital losses exceeded the income from other sources. While this limitation does not impose a serious hardship on most corporations, it may nevertheless be detrimental to financial corporations. These corporations in years of severe depression may suffer serious capital losses. The limitation on the deduction of such losses may radically interfere with their proper function in the investment market. I recommend, therefore, that the limitation upon the capital losses of corporations be removed and that the deduction be allowed in full against other sources of income as was the practice before the depression.

There is general agreement that the tax burden should be distributed equitably in accordance with individual tax-paying ability. That principle found effective application in the selection of income as a major basis for taxation a quarter of a century ago. Despite almost universal acceptance of the individual income tax as the most generally satisfactory source of Federal revenue, it still plays an inadequate role in the Federal tax system. In the fiscal year 1938 it yielded only $1,300,000,000. Although this amount exceeded 1930 collections by almost

$150 million, the proportion of total revenues which it represented declined from 27 percent in 1930 to 20 percent in 1938.

The present Federal individual income tax reaches comparatively few individuals. For the calendar year 1936 scarcely more than two million individuals paid Federal income taxes. In other words, substantially more than 90 percent of the gainfully employed had no liability under the major progressive element in the Federal tax structure. This circumstance, coupled with the quantitative importance of consumption taxes, has produced an anomalous situation. Those in the very lowest income groups are heavily burdened by consumption taxes; those in the highest income groups pay relatively high income taxes; while a large middle income group is lightly taxed in comparison.

To make the tax system more equitable and to pave the way for the future elimination of less acceptable revenue sources, the role of the individual income tax should be increased. Those with middle-sized incomes should be brought within its scope. With this objective in mind, I recommend that the personal exemptions for both single and married individuals be reduced and that the rates upon the middle income tax brackets be increased. In this manner, and in this manner alone, can the principle of ability to pay be extended to a substantial segment of our people.

In addition to the need for broadening the individual income tax, I call your attention to the upper rates of the individual income tax. The present rate of 79 percent exceeds the maximum rate during the War period. The incentive remaining to high income classes to utilize their savings by investing them in new business or risking them in the expansion of old business has been unduly impaired by these high rates. These rates of tax naturally encourage the upper income classes to resort to ultra-safe investments or to cruder forms of hoarding. The time has probably arrived when we must reexamine the repercussions of these very high rates upon business incentives and the growth of the national income.

Taxes upon property transfers from generation to generation present another opportunity for the application of ability to pay and the advancement of equity in taxation. Although the rates of estate taxation were increased during the past few years, its yield today is not as great as it might well be. This is due in part to a lack of coordination between the estate tax and the gift tax. Individuals of substantial wealth can reduce their prospective death tax liability markedly through the transfer of property during life. The gift taxes applicable on such transfers result in sufficient savings to make that course extremely profitable. I believe that the solution to the problem lies in combining the estate and gift taxes so that gifts will be treated simply as an early partial distribution of the estate. I recommend that Congress examine the possibilities of such a combination. If this were accompanied by a lowering of exemption and an increase in the rates applicable to the middle estate brackets, the role of the estate tax in the Federal tax system could be substantially increased.

While the national government has been obliged to strengthen its revenue system, the states have been faced with a similar problem. They too have experienced drastic declines in revenue and increasing demands for expenditure. To meet their revenue needs, they have reached out for new tax sources. The simultaneous expansion in the revenue system of both the states and the Federal Government has enlarged greatly the conflicts between national and State taxes. The results are increasingly unsatisfactory to everyone. The governments find their revenues adversely affected by competing taxes of other governments. The costs of collecting duplicate taxes have increased. The taxpayer is often subject to several taxes on the same income or the same transaction. He must prepare numerous reports which must be compiled differently to satisfy the many requirements of the different taxing authorities.

Although in a Federal system the tax structure must inevitably be complex, there is every reason to believe that existing confusion and conflict can be diminished. It is high time to consider seriously how the national and State governments can coordinate their taxes in such a manner as to minimize duplications and conflicts, to reduce the taxpayer's cost in complying with the tax laws and to assure adequate revenues to all governments. The existence and seriousness of the problem has been widely recognized and there has been a good deal of talk about it. To date, however, little has been accomplished. A commission, composed of highly qualified representatives of the Federal, State and local units of government, as well as those of the public, holds promise of contributing to a solution. I recommend that Congress provide for a commission with Federal, State and local representation to investigate the problem of conflicting taxation and to make recommendations to the Congress.

TRIPLICATE Strictly CONFIDENTIAL

No. 166

Rangoon, Burma, April 1, 1939.

STRICTLY CONFIDENTIAL

SUBJECT: American petroleum products for China.

THE HONORABLE

THE SECRETARY OF STATE,

WASHINGTON, D.C.

SIR:

I have the honor to refer to my despatch no. 157 of March 2, 1939, on the subject of "American petroleum products for China", and to report that a situation has developed here which may prevent the shipment of any of these products through Burma. It involves the possible assessment of the full import duty without the anticipated remission of at least fifteen-sixteenths of that duty on re-exportation from Burma to China.

As the matter now stands, motor spirit (gasoline) and kerosene produced in Burma are exempt from the excise duty when bought by the Southwest Transportation Company and exported overland to China. The excise duty on domestic motor spirit is exactly the same as the import duty on foreign gasoline, or 11 annas (about $0.24 at present exchange) an imperial gallon. The excise duty on kerosene is 2 annas 9¼ pies (about $0.066) an imperial gallon, and the import duty, 3 annas 9 pies (about $0.075). However, official action is required to give foreign petroleum, motor spirit, and kerosene the benefit of the present remission, or drawback, of

fifteen-

fifteen-sixteenths of the import duties on materials purchased by China and shipped in transit through Burma, but such action has not yet been taken. Political agitation has resulted from the exemption from excise duty of domestic petroleum products bought for China, on the ground that it discriminates against consumers in Burma and is detrimental to the revenue of Burma, and it is said that the Burma Government hesitates, in consequence, to take any further step favoring China in connection with such products.

If the present situation is permitted to continue, it will be possible for the Chinese Government to purchase economically for shipment through Burma only petroleum products from manufactories in Burma. The difference in the cost of every million imperial gallons of gasoline would be, because of the duty on the foreign product, $240,000. It has been expected to ship the greater part of the gasoline and other petroleum products recently purchased by China in the United States through Burma.

Remission of Duties Banned.

In the official BURMA GAZETTE of March 4, 1939, the Department of Lands and Revenue of the Government of Burma published revised provisions governing the remission or drawback of fifteen-sixteenths of the import duties on materials re-exported to China from Burma. The concession formerly in effect was only seven-eighths of the duties. The provisions included a list of commodities on which no remission or drawback may ordinarily be allowed, and in this list there appeared for

CONFIDENTIAL

the first time "motor spirit" and "kerosene". For years "petroleum" has been one of the commodities excluded from the benefit of the provisions for remission or drawback, and when Chinese interests here, in view of the proposed importation into and shipment through Burma of large quantities of American products, inquired concerning the reqsons for the inclusion in the list of "motor spirit" and "kerosene", it is said that they were told that apparently in the revision of the provisions in the department it wqs considered by the person in charge of the work that as long as "petroleum" was listed the principal petroleum products should also be specified. It is also said that the Chinese were given to understand that official action would be taken to remedy the matter, and that it was indicated that if the Burmese Ministry did not act the Governor of Burma would. It is reported that on the strength of the assurances received, the Chinese Vice Minister for Foreign Affairs, now in Rangoon, telegraphed his department in Chungking that shipments from New York to Rangoon could be commenced.

Chinese Asked Excise Exemption.

On March 11, 1939, before any official action was taken to extend the provisions for the remission or drawback of import duties to petroleum products for China, the BURMA GAZETTE published an order exempting from excise duties motor spirit and kerosene bought from manufactories in Burma by the Southwest Transportation Company and exported overland to China. The application for this exemption was made in July, 1938, by C. M. Chen, the Chinese railroad official who came to Rangoon last year to make preliminary arrangements for shipments over the Yunnan-Burma highway, and who was later in local charge of the activities of the Southwest Transportation Company; he believed that it would be good policy to buy gasoline and kerosene from the British producing companies in Burma, and he sought the exemption for the saving that would result. His application was passed for consideration to several departments of the Burma Government, and it was held up because of differences of opinion on the part of some of the Ministers, apparently in connection with the question of resulting loss of revenue. After the fall of the Ba Maw Coalition Government in February and the formation of the U Pu Ministry the matter was taken up by the present Minister of Lands and Revenue, who in the course of a debate in the House of Representatives on March 16th asserted that he found the Defense Department had notified the Chinese Government in January that the exemption would be granted, and that when he saw the Governor concerning the matter he was told that as an agreement had been reached with the Chinese Government, the decision arrived at could not be countermanded.

Criticism in House and by Press.

Following the publication of the order by the BURMA GAZETTE the matter was discussed in the House of Representatives, and the Burmese press became violently critical. The present Ministry declared that the decision for the exemption of excise duties was a

legacy

legacy from the former Government, and this was denied by Ministers of the Coalition Government, who said that they had opposed it. In writing of the debate in the House, BANDOOLA, the organ of Doctor Ba Maw, former Premier of Burma, asserted that speeches made by Ba Maw and the former Commerce Minister had "touched the European vested interests to the quick", and said:

> "As a matter of fact, petroleum is the life blood of Burma, and the European capitalists have been sucking it. Now it will not be wrong to say that with this life blood U Pu's Government has been prolonging its span of life, because the Government has pleased the European capitalists by way of the exemption given to petroleum transported to China, while retaining the duty in Burma, the producing country. In short, by such an order Burma's revenue will suffer to the extent of about nine lakhs (900,000) of rupees, whereas the European capitalists will gain more than that. We suggest that an inquiry should be made to see which Government is responsible for that exemption order."

<u>New Road Called a Menace.</u>

NEW BURMA told its readers that because oil has become "one of the most essential factors in the Imperial scheme of things", the oil companies "both in Burma and in other countries" are taking great pains to bring pressure on Governments to make important concessions to them. It added:

> "The Burma-Yunnan road, instead of opening new avenues for the people of Burma toward progress and prosperity, has become a menace to the country. If the road is the link between Burma and China, it is also the life belt of the capitalists and imperialists. The road throws open to them new fields to explore and exploit. The indigenous people will suffer all the more as their exploitation becomes more intensified and ruthless. The Exploiters Group has now brought pressure to bear on the weak-kneed U Pu Government to make concessions to the incessant demands of the greedy and exploiting oil magnates."

The DEEDOK said that it could not protest too strongly against the exemption order, and that the country should demand that the order be rescinded. The transport of petroleum to China free of duty, it declared, must be stopped at once.

Property of Chinese Government.

While it is explained that any American petroleum products shipped to Rangoon for transit to China would be the property of the Chinese Government when they left the United States, storage arrangements have been made here by the Standard-Vacuum Oil Company, and the shipments would be handled at this port by the local organization of that company. It was expected that the products would be imported here in bond, and that when they were delivered to the Southwest Transportation Company for re-exportation to China one-sixteenth of the full duty would be paid and the bond required under provisions for the remission of the other fifteen-sixteenths of the duty would be executed by the Chinese concern. While it is possible that the products could still be entered in bond, under present circumstances the full duty, instead of one-sixteenth of it, would be payable on delivery out of bond.

Unless there is a change in the local situation, China may attempt to ship all of the American petroleum products obtained under the credit granted by the Export-Import Bank to the Universal Trading Corporation of New York by way of Haiphong, Indochina, and the French railway from that port to Yunnanfu. It was originally intended, according to information received here, to send about 60 percent of the products to Rangoon and 40 per-

Strictly CONFIDENTIAL

cent to Haiphong. There is a great accumulation of freight for China now at Haiphong, and the capacity of the French railway to Yunnanfu is very limited.

Attitude of Domestic Companies.

American petroleum interests here express the opinion that the Burmah Oil Company and the other British producing companies in Burma are not as deeply interested as might be supposed in the trade advantage which the present situation gives their products compared with foreign oils generally, and, under the circumstances, with American oils particularly. They point out that the Burma companies now have an established market in India for practically all they produce in excess of the domestic demands, and that while production might be increased, this would require time and considerable expenditure. In order to meet the Chinese demand, which might last only a short time, exportation to India, a permanent market, would have to be curtailed, and trade lost there might not be readily regained.

Matter May Be Taken to London.

The Chinese Vice Minister for Foreign Affairs, T. K. Tseng, has asked the Government of Burma for a definite answer to the question of the remission of import duties on foreign petroleum products brought to Rangoon for shipment through Burma to China. He has stated that in the event of an unfavorable answer he will fly to London to consult the Chinese Ambassador

there

Strictly CONFIDENTIAL

there and the British Foreign Office. The advisability of bringing the matter to the attention of the American Ambassador in London has also been considered, it is said.

Respectfully yours,

Austin C. Brady
American Consul

Distribution:

1. Original and four copies to Department.
2. Copy to American Embassy, London.
3. Copy to American Consulate General, Calcutta.

800
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RECEIVED

1944 MAY 1

TREASURY DEPARTMENT

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 1, 1939.

TO Mr. White

FROM Mr. Gass

Two French studies of gold and prices

Ch. Rist, Some Observations on the Relation Between the Rate of Increase in the Production of Gold and the Movements of Prices

L. Baudin, Some Observations Relative to the Influence of the Variations in the Production of Gold and the Long Period Movements of Prices

(Both in the Revue d'Economie Politique, September-October 1938.)

Significance of these studies.

Neither of these studies contributes to the economic analysis of any issue relating to gold or prices.

Their significance is: (1) They recall the exaggerated and misplaced importance assigned to gold by large sections of French opinion. (2) They remind us again of the abysmally low state of understanding of all economic questions which prevails in France.

Mr. Rist's article.

Mr. Rist's statements are of special interest because he is widely regarded as the dean of French economists and since he served as adviser to the Bank of France. In these circumstances, it is particularly unfortunate that his article defends many fallacies and that it never advocates a good cause except for bad reasons.

His key contention is that long period prosperity is impossible unless there is, (1) a steadily increasing production of gold and, (2) the new gold is allowed to have its full "natural" effect on the quantity of money. All efforts to limit gold production are bad, and gold "sterilization" is particularly pernicious. Society needs an increasing quantity of hard money so that there may be an increase in credit and an "increase in the rapidity of exchanges." Neither bank deposits nor paper money can be substituted for gold; these others are only auxiliaries to gold.

Mr. Rist does not distinguish between an increase in the quantity of money and an increase in expenditure, but he assigns to the former consequences which can only result from the latter. He would no doubt be shocked by the contention that the greatest advantage of gold production is the same as that derived from the building of pyramids. His article is a characteristic production of the school which passes popularly for financially sound - reckless in its handling of facts and puerile in its causal analysis.

Mr. Baudin's article.

There is no point in giving an extended analysis of Mr. Baudin's article. It is longer, less dogmatic and has a greater display of learning, but it comes to much the same conclusions as Mr. Rist's. Two quotations will serve to indicate its tone.

"Man tends to intervene more and more between gold and prices."

"Man alone is guilty: it is he who has deliberately falsified the regulatory mechanism constituted by the metal. Gold is not dying; it is being assassinated."

REB

TELEGRAM SENT

GRAY

April 1, 1939.

1 p. m.

AMEMBASSY

PARIS (FRANCE)

221

FOR COCHRAN FROM TREASURY.

Reference Butterworth's cable to Secretary 428. Ascertain from French Treasury what steps they contemplate in similar circumstances and cable not later than Monday evening.

HULL
(HF)

EA:HF:LWW

RFP

GRAY

London

Dated April 1, 1939

Rec'd 11:07 a.m.

Secretary of State

Washington

432, April 1, 1 p.m.

FOR TREASURY FROM BUTTERWORTH

One. The British Treasury referred to its note on the despatching of gold bars by parcel post reported in my 402, March 27, 11 a.m. and stated it would most appreciate an early reply.

Two. The British national account for the fiscal year which ended yesterday closed with a surplus of ordinary revenue over ordinary expenditure of pounds 505,000 before allowing for sinking fund provision. After providing pounds 13.2 million for sinking funds there is a realized deficit of pounds 12.7 million. When the expenditure of borrowed funds under the National Defense Loans Act of 1937 of pounds 128 million is included, the "true deficit" is pounds 127.5 million, or if sinking fund provision is included in expenditure, pounds 141 million.

The ordinary revenue totaled pounds 927.3 million, which was pounds 54.7 million more than the total in 1937-38.

1937-38. The principal changes in receipts as compared with the previous year were an increase of pounds 37.9 million from income tax and an increase of pounds 20.5 million from the national defense contribution, a decrease of pounds 11.5 million in receipts from estate duties and a decrease of pounds 3.5 million from stamps, while customs receipts were up by pounds 4.7 million. What is more significant is that most of the receipt items were smaller than the estimates: income tax by pounds 5.3 million, estate duties by pounds 10.6 million, stamps by pounds 3 million, customs and excise by pounds 3.5 million. On the other hand, the national defence contribution yielded nearly pounds 2 million more than the estimate and surtax brought in pounds 530,000 more than the estimates. In all, revenue fell short of estimates by pounds 17.4 million.

Total ordinary expenditure, excluding sinking fund, amounted to pounds 936.8 or 93.4 million more than in 1937-38. The principal increases in expenditure were for civil supply services which rose by pounds 33.5 million as compared with last year and army, navy and air force which were up by pounds 57.2 million. The total for "defence" at pounds 254.5 million does not include pounds 128.1 million met from borrowed funds

under

RFP -3- #432, April 1, 1 p.m. from London

under the Defence Loans Act so that the total expenditure for the fighting forces was pounds 382.5 million as compared with pounds 262.1 million in the previous year.

The achievement of a small "surplus" in the ordinary budget apart from sinking fund provision was due to the fact that estimates for civil expenditure were evidently liberal when the year's budget was made up and to the fact that much of the increase in defence expenditure arising out of the September crisis and the accelerated arms program was met by borrowed funds, the expenditure of which at pounds 128 million was some pounds 38 million more than originally anticipated.

Three. The city anxiously awaits Hitler's speech pending which the foreign exchange market has not been very active. Again the forward dollar had a tendency to move out. Of the 130 bars sold at gold fixing 68 were married and the British fund supplied about 50.

KENNEDY

PEG:RGC

EG

GRAY

Berlin

Dated April 1, 1939

Rec'd 9:55 a.m.

Secretary of State,

Washington.

220, April 1, 11 a.m.

The German financial and daily press have featured Funk's speech before the Reichsbank directorate Thursday.

Funk started his speech by declaring - apparently forgetting the United States - that Germany was now the "greatest industrial country of the world" and that the "close political and spiritual union" between Italy and Germany must lead also to an economic union (verbund-wirtschaft). He defended the German-Rumanian Trade Agreement as being of mutual benefit to both countries. He admitted that it conferred a "privileged status" on Germany but asserted that Germany had no intention of endeavoring to obtain a "monopoly position". He followed with an attack on foreign credits and loans stating that "the nations poor in capital" would not allow themselves to be dependent through foreign loans at oppressive interest rates.

He

-2- #220, April 1, 11 a.m. from Berlin

He further asserted that the principles in world economy had changed and the "nationalistic strengthened states would not again be involved in the shackles of an automatic international gold standard or international debt entanglements". He insisted that the stopping of the economic conversations with England and France following the taking over of Bohemia and Moravia was only an interruption because after "the creation of a new order of things in the Central Europe area the necessity for the continuation of these conversations had become not less but greater". He said that if England in the last few days had proceeded to a "temporary sequestration of private credits" of a "protectorate of the German Reich" that he regarded this only as a temporary measure which had occurred under the influence of a general uncertainty and a misapprehension of the "real conditions" and felt sure that "with a calming of spirits and clarification of facts" this measure would automatically be ended. He followed this statement with a reference to the forthcoming standstill credit negotiations stating that German proposals had contemplated a new basis which had been extremely well received by the English side.

(END SECTION ONE)

GEIST

HPD

AC

GRAY

Berlin

Dated April 1, 1939

Rec'd 9:30 a.m.

Secretary of State

Washington

220, April 1, 11 a.m. (Section two)

These references are locally interpreted as a warning that unless England indicates a renewal of the trade talks and the freeing of Czechoslovak credits Germany may refuse to continue the standstill credits agreements.

Funk stated that under the new status of the Reichsbank the foreign stockholders of the institution would have to sell their stock but insisted that Germany would treat the foreign stockholders "honestly". It is understood that foreign interests mainly in England hold some 21% of the Reich's foreign capital of 150,000,000 marks.

He defended the destruction of the semi-independent status of the Reichsbank and asserted that by Hitler's orders the value of the currency would be maintained and that prices and wages would be held stable. Wages could be increased only as a result of increased individual production. Referring to the new financial plan of which the main feature is the stopping of the long term Government

borrowing

AC - 2 - #220, April 1, 11 a.m. (Section two) from Berlin

borrowing and short term Treasury notes and their replacement by issuance to industry of tax certificates for forty per cent of the amount of all Government orders, he asserted that the unusual tasks devolving on the Reich required "unusual methods". He asserted that a "reasonable relations" would be maintained between "production and consumption goods".

He declared that it was not necessary for the State to cease financing its deficits through public borrowing since the capital market was needed for private industrial replacement and extensions and that the continuance of ordinary borrowing would place an increasing interest burden on the Government which eventually would be intolerable.

While the capital market in the future (*) be reserved for private issues it had recently been so strongly drawn upon by the State that there must be a pause for recovery before it could again function. However he expected that one billion marks of industrial obligations would be floated during 1939 plus increased issues of mortgage bonds as well as a part of the capital needs of the German State Railways which are planning a replacement and extension program of three and one half billion marks for the next four years. In addition to fixed interest securities it was expected that the capital market would also float new stock

issues

AC - 3 - #220, April 1, 11 a.m. (Section two) from Berlin

issues. He pointed out that there had always been a difference in the interest rates between Government and industrial and mortgage bonds. This is interpreted here as an indication of an increase in interest rates on private fixed interest securities which in the last year have been but little above the Government bond interest rate of 4½%.

GEIST

HPD

(*) Apparent omission

RFP

GRAY

Berlin

Dated April 1, 1939

Rec'd 11 a.m.

Secretary of State

Washington

220, April 1, 10 a.m.

(Section Three) Presumably to encourage the flotation of industrial shares he announced that the Anleihestock law which limits dividend payments to 6% (in certain cases to 8%) would be repealed: most stock companies would be exempted from this limitation in 1939 and the remainder 1940. He pointed out that the dividend limitation law no longer had much meaning since dividend payments were now automatically restricted by the obligations of companies to contribute to the welfare of their employees and other social purposes, by the increase last year of the corporation tax to 40% and by the increased efficiency of tax assessment and collection. He did not mention as a further limitation on net earnings the recent surtax of 30% on increase of earnings.

He ended his talk by asserting that the economic "progress" to the Reich would continue stating "the great world around us has its heavy wrecks and financial

cares.

RFP -2- #220, April 1, 10 a.m. from Berlin

cares. Gold is fleeing apparently irresistably into the already over-filled treasury of the United States and the old world denuded of world gold sees the ground disappearing under its gold standard currencies and its payment balances heavily shaken. Is one to sacrifice to the American 'moloch'? The world states stand at the parting of the ways. Either one surrenders to the power of American gold or accepts the new methods of the young, strong, upward striving nations. Our economic and financial methods offer sufficient possibilities of successful cooperation on the world markets for the demand of the world for economic goods is without limit. We have never refused to accept the hand (of cooperation) which is offered to us and we will not refuse it in the future even less so because we are now stronger."

GEIST

RR:KLP

Paraphrase of Section Four, Telegram No. 220
of April 1, 1939, from the American Embassy, Berlin.

The speech which Funk made has not had the effect of dispelling the impression of increased strain on and deterioration of Government finances, and the monetary system arising from certain economic developments and the inauguration of the Reich's new financing plan which these developments brought out. Time limit feature of the new plan is that it discontinues the long-term consolidation loans and the short-term Treasury bills of Schacht's financial plan of a year ago in favor of the issuance of tax certificates to be used in payment of 40 percent of all Government orders, 20 percent of Government orders to be paid in tax certificates of class one which may be used in payment of all Reich taxes 7 months after their issue date and 20 percent of class two usable 37 months after issuance. (See Embassy's telegram 202, March 25, 1 p.m.). In certain respects the certificates of both classes represent a supplementary currency and those of class one are in fact referred to officially as a "means of payment" this character of currency and even though to a limited extent of legal tender attaches to both classes of certificates since subcontractors and subsuppliers are obliged to accept them from firms which have direct dealings with the Government. In order to "sterilize" the inflationary

effect

effect of certification of class one the recipient is entitled to retain them as investments allowing him to write off tax free "depreciatable" equipment in excess of the normal depreciation allowance. This extra write off is directly proportionate to the amount of tax certificates held by the taxpayer irrespective of whether he acquired the certificates directly from the Government or from a bank or private firm.

GEIST.

REB

GRAY

Berlin

Dated April 1, 1939

Rec'd 11:43 a. m.

Secretary of State,

Washington.

220, April 1, 10 a. m. (SECTION FIVE)

The percentage for tax free writing off is fixed at 20% of the amount of certificates held during the first year but is increased to 25, 30 and 35% respectively for each additional year the certificates have been uninterruptedly in the possession of the tax payer. To promote export trade this extra appreciation allowance will be increased by 10% if export business constitutes at least 25% of the turnover.

Class one certificates are non-interest bearing but the class two certificates are usable at maturity at 112% of their face value thus having an effective interest rate of slightly under 4%. The class two certificates are not rediscountable but are "liquidatable" at the Reichsbank at 5%.

Presumably to cover the temporary loss of revenue resulting from the write off privileges above described the law of March 20 providing for the tax certificates also sets

REB

2-#220, From Berlin, April 1, 10a.m.
(Sec. Five)

sets up a surtax of 30 per cent on any increase in income over that of the preceding year. Another object of this surtax is to tax "profiteering" occurring from the arms and industrial boom. There will also be a relatively small increase of revenue under the law of February 17 which raised the rates of income tax on certain unmarried persons and certain other classes of tax payers.

GEIST

HPD

Paraphrase of Section six, Telegram No. 220 of April 1, 1939, from the American Embassy, Berlin.

It is too early to say whether there will be an inflationary effect from the new plan, and how much there might be. It would seem that some inflation of prices cannot be avoided, although control of prices will presumably be successful in keeping the price of workers' necessitous goods from rising too much.

During the fiscal year which ended yesterday, the Government publicly borrowed some 10,000,000,000 marks. Furthermore, reliable reports are to the effect that during the last few months there has been an increase in the normal delay in making payments for Government goods and services, and this extra delay represents an increase in factor(sic.). Certain ministries, it is known, have given certain manufacturers who suffered delay in obtaining payments "debt recognition certificates". The present rate of Government expenditures does not seem to be decreasing; on the contrary, an increase is generally expected. There are substantial inducements to Government suppliers to hold tax certificates for the purpose of gaining greater write-off privileges. However, German industry has so lost its liquidity that it does not seem possible that many of these certificates can be held by it. Expenditures for goods and services by the Government, not counting

salaries

salaries of Government employees which will be paid in cash, will presumably amount at the present rate to between twenty and twenty-five billion marks; therefore it is presumed that tax certificates will be issued in the amount of something like ten billion marks. In addition to financing the deficit of the Government, it is indicated in the speech which Funk gave that during the next 12 months industry and the railroads will be permitted to float two or 3,000,000,000 marks of bond and share issues. Long-term bonds to the amount of only 157,000,000 marks were floated by industry during 1938. It would appear that the present scale of voluntary saving by the German people would be greatly exceeded by the prospective deficit financing of the Government and contemplated industrial investment.

The Government on the other hand has complete authority over a disciplined people, and so far prices and wages have been substantially successfully controlled. It is possible that the Government could put through some increase in savings at the expense of the standard of living. There is furthermore some automatic check in the lack of available labor and materials on the immigrant programs of the Government and the desire to increase plant and production for industry.

Please transmit the foregoing to the Treasury as a telegram from Heath, No. 8.

GEIST.

END MESSAGE.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: April 1, 1939, 4 p.m.

NO.: 324

FOR TREASURY FROM HEATH. No. 9.

It has not been possible for me to get reliable information as to the amount of gold and foreign exchange which the Reich acquired in Moravia and Bohemia. It is estimated locally that the amount ranged from eighty to one hundred million dollars. It is stated at the Reichsbank that only one-third of the Czech National Bank's gold and exchange cover is being taken to Germany. This amount is being taken in order to redeem the Czech crowns which the annexation of the Sudetenland involved. Of course there is no doubt that the Reich will have placed at its disposal the entire resources. At the Economics Ministry no secret is made of the fact that the Czech crown will eventually be withdrawn and within the "protectorate" German marks alone will be circulated; it is also said that a customs union is being elaborated but that unification of customs and currency will take some time. The Czech exchange control at the present time has a nominal autonomy. However, representatives of the Reichsbank and Reichs exchange authority, who brought

a

a staff of employees to Praha, are in fact following and directing its operations.

GEIST.

EA:LWW

REB

TELEGRAM SENT

GRAY

April 3, 1939.

3 p. m.

AMEMBASSY

LONDON (ENGLAND)

230

FOR BUTTERWORTH FROM TREASURY.

Reference your 432.

British Treasury note reported in your 402 has been discussed with Post Office Department and early decision expected. Will keep you informed.

HULL
(HF)

EA:HF:LWW

REB

GRAY

London

Dated April 3, 1939

Rec'd 2:35 p. m.

Secretary of State,

Washington.

435, April 3, 6 p. m.

FOR TREASURY FROM BUTTERWORTH.

The city has found no real comfort in Hitler's speech but as usual has interpreted the absence of an immediate specific threat as a hopeful sign. Consequently, the London stock market was firmer today but the volume of trading remained small. Likewise, there were two-way dealings in the foreign exchange market but the movements in the given circumstances were without particular significance. 180 bars were sold at gold fixing of which 66 were married and less than 20 were supplied by the British fund. There were no substantial dealings after fixing.

KENNEDY

PEG

CSB

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: April 3, 1939, 5 p.m.

NO.: 227

FOR TREASURY FROM HEATH. NO. 10.

Under the "standstill agreement" American bankers are obliged to keep alive open lines of credit previously granted German banks. One Berlin representative of an American bank estimates that such lines of credit are in the order of $10,000,000. Until the announcement of the imposition of countervailing duties German cotton imports were not financed through standstill lines of credit but were made on a basis of compensation. Now, however, these standstill credit lines are being availed of to finance imports of American cotton. The American banks cannot refuse under the standstill agreement to keep open their credit lines. Some fear exists lest when these credits mature Germany will break the standstill agreement, refuse to give exchange for repaying credit lines, and seize the cotton which is in Bremen held in bond.

GEIST.

EA:LWW

Philadelphia Record
April 3, 1939

WASHINGTON MERRY-GO-ROUND

U.S. Ready to Act on Arms Shipments to Third Reich

* * * * * *

Washington, April 2

The State Department at last is doing something about permits issued for arms shipments to Germany in violation of the law.

That there was violation of the law was charged in this column, and subsequently by members of Congress, in May of last year. It was pointed out that Article 170 of the 1921 Treaty of Peace with Germany provides that "importation into Germany of arms, munitions and war materials of every kind shall be strictly prohibited."

Secretary Hull took issue with this charge, and at a press conference suggested to the Merry-Go-Round authors they "study further the legal aspects of the question." He insisted that as Germany was importing the arms, she and not the United States was breaking the law.

NATIONAL ISSUE

A month later, after the matter had become a national issue and was being debated by authorities on international law, this column addressed a letter to Hull, suggesting he ask the Attorney General for an opinion on the legality of licensing arms shipments to Germany.

Hull made no reply. But now--10 months later--comes a complete reversal. The State Department has secretly asked the Attorney General for an opinion.

In the intervening 10 months there have been a number of world-shaking crises in Europe--Sudetenland, the swallowing of Czecho-Slovakia, Memel, and the fall of loyalist Spain. The State Department has issued two seething attacks against Hitler's repacious policies. But on the all-important question of arms shipments to Nazi Germany, the Department said and did nothing.

The Bureau of Munitions Control continued to issue licenses to U.S. manufacturers to export war materials to Germany. Now, with public opinion at high pitch over Nazi aggressions, Secretary Hull has started the ball rolling to end law violation by his department.

CAGEY MURPHY

An old hand at dealing with reporters, Attorney General Frank Murphy always waits for them to start shooting questions at his press conferences. But recently the newsmen decided to wait him out and see what happened.

After they were all seated, they remained silent, looking steadily at Murphy. He stirred uneasily in his chair and cleared his throat. Not a word was spoken. Finally, someone in the rear remarked, "Good morning, Mr. Attorney General."

Murphy grinned genially, replied "Good morning" and then went back to his watchful waiting. Another long silence ensued, broken finally by a reporter inquiring, "Haven't you a question you would like us to ask?"

"Nothing doing," shot back Murphy, laughing, "not me. I'm not putting my neck in the noose that way. If you folks have anything on your minds, you do the talking. This is my press conference."

UNDER THE DOME

Mystery surrounds a lady listed as employed in the office of Representative William P. Lambertson, of Kansas. She is Miss Virginia Cox, who is down on the rolls at $2900 a year, yet never has been seen in Lambertson's office. Last year Lambertson listed a clerk at $2900 who actually worked in a private office downtown. . . Congressman Graham A. Barden, of North Carolina, is a staunch, hard-hitting Democrat, while Congressman Bruce Barton, of New York, is a Republican possibility for President, but according to Barden, "We've just got to be friends. We get too many phone calls meant for the other fellow, and know too much about each other not to get along well." . . . Ed Birmingham, Iowa Democratic State Chairman, is anxious to land the vacant Commissionership of Fisheries, but his chances of getting the plum are zero. Birmingham doesn't rate high in the inner circle, where his support of Senator Guy Gillette in last year's purge campaign is still remembered . . . At a party given by the Dominican Legation, a tipsy out-of-town guest called to genial Ecuadorian Ambassador Alfaro, "Hey, boy, bring me a glass of beer."

THREE VOTES

Administrationites privately claim they have a three-vote majority in the Senate to restore the $50,000,000 slashed from the W.P.A. bill by the House. The White House lost out in the Senate on the original $875,000,000 fund by one vote. Whether the converts are actually sewed up remains to be seen, but there are tell-tale signs that some of the previous antis may flop.

Senator Jim Davis, of Pennsylvania, told a joint session of his State Legislature last week he would vote for $150,000,000, and Senator J. Warren Barbour, of New Jersey, has been worriedly telling colleagues his last ballot against W.P.A. had a very sour kickback.

If the Senate should vote to restore the cut, the House will either have to back down the whole way or compromise on $125,000,000 --which a lot of Representatives privately would like to do.

BUSINESS APPEASEMENT

Tip-off on what Roosevelt thinks of business appeasement is the fact that one decisive influence in making up his mind to name Douglas was the S.E.C. chairman's sizzling retort to the Wall Street moguls, who planned to cut the heart out of the S.E.C.'s regulatory powers. The S.E.C. is one of Roosevelt's prized pets and Douglas' fighting defense of it made a big hit.

He called up Douglas and congratulated him. Then he inquired jocularly, "Bill, what are you doing to appease business?"

"I'm enforcing the law, Mr. President," Douglas replied.

"Thataboy !" approved the President.

--DREW PEARSON and

ROBERT S. ALLEN.

April 3, 1939

FOR THE SECRETARY:

Since this town has a comparatively simple business structure, I have tried to cover it pretty completely, talking to two manufacturers, hardware and furniture dealers, bankers, newspaper editor, printing plant manager and a coal dealer.

Reactions are very different at several points from those I encountered in Minneapolis. Here business is admittedly good and is expected to get better in spite of two temporarily discouraging factors: curtailed state expenditures and low prices for the milk and cheese produced by surrounding farmers. Balancing of the Federal budget by high taxes, if necessary, is suggested with surprising unanimity. Washington is criticized for confusing, contradictory statements of policy which lead to business uncertainty. War scares are considered less of a business factor here than they were in Minneapolis.

At a dinner this evening opening a two-day meeting of the Wisconsin Bankers' Association, I learned from a visiting officer of the Chicago Federal Reserve Bank that the Federal Reserve Board has had the 12 Banks make a check of the bond portfolios of their member banks. In the Chicago area, according to this officer, the survey showed that banks are selling corporate bonds and buying Governments, especially long-term Governments. Their reason for doing so, according to Mr. Young of the Reserve Bank, is that bank examiners have been requiring banks to set up depreciation reserves against corporate bonds, and banks are getting tired of the cost and the trouble. Mr. Young's guess is that banks will be on the buying side of the long-term Government market during the near future although he had just talked to a Detroit banker who had decided he should sell his because the New York banks have recently bought $500,000,000 of long-term Governments which they don't like and which the Detroit banker thought they would sell at the first opportunity, breaking the market.

Farmers have turned very anti-labor after CIO attempts to unionize creameries and canneries.

- - - - -

<u>Gisholt Machine Tool Company</u> -- Mr. George Johnson, a young man who is stepping into the position of operating head of this family-owned company, says business is good and even is above expectations,- a fact which he attributes to the successful introduction of two new products. He expects a good year. His company last year spent more money on plant replacement and enlargement than in any recent year and evidently is now reaping the results of expansion through sales of their new products. In spite of this successful venture, Mr. Johnson believes that there is a psychological resistance among business men against expansion because of uncertainty over the risks involved.

Much of the company's business has begun to fall off slightly, but domestic orders have increased to take up the slack, giving the company a good backlog of unfilled orders. Mr. Johnson says he believes that his company has had exceptional success with domestic orders because of its new products and that other companies have not experienced a similar increase.

Exchange conditions play a big part in the company's trade, Mr. Johnson says, but the availability of exchange is more important than its price. He knows, for instance, that additional Japanese orders are waiting for his company in New York and will be placed when exchange is available. In spite of the large amount of semi-barter trade which his company does, Mr. Johnson feels barter is not the right way to trade.

The wage-hour law is causing this company some inconvenience. To get an order completed by the May 1 deadline, the company is having to work some high-salaried engineers -- who are willing to do the overtime and who are regular employees -- more than 44-hours a week. Mr. Johnson feels that the law was not meant to benefit such employees and that other companies in a similar situation have violated the law. He suggests every regular employee receiving more than $150 a month be exempt.

Mr. Johnson thinks that the Treasury's tax revision suggestions, so far as knows them, are fine. A more generous loss-carryover would greatly help his company which is in a "feast or famine" business, he said. The state income tax law has a three-year loss-carryover which the company found helpful when it was emerging from five years of losses.

The undistributed profits tax hurt his company's business because new machinery, he believes, is bought out of earnings. His salesmen constantly met the argument that, if a customer were to use its earnings to buy machinery, the undistributed profits tax on the earnings made the machine cost up to 30% more than the actual sale price.

Mr. Johnson believes the Government economy is becoming of more public concern. The plant committee of workers recently expressed doubt about continually "living on borrowed money," he says. He personally thinks the budget should be balanced -- by higher taxes if necessary. This view was sufficiently general here to make me suspect that it must have some local origin, perhaps LaFollette preaching.

Mr. Johnson is against Government loans to small business, believing they would be useless or wasteful.

More than anything else, Mr. Johnson believes the Government should have a program, one which is clear and is adhered to. Talk of "appeasement" side-by-side with unappeasing tactics is confusing, he says.

War scares, instead of deterring this company's business, help it.

Ray-o-vac Battery Company - Mr. Cargill, head of the company, announced that he is no New Dealer. He thinks uncertainty about the policy of the Government is a more powerful business deterrent than the threat of war abroad.

instability is the order of the day at home and abroad, and a business man must try to forget Washington with its conflicting statements when he is planning his course, Mr. Cargill says.

Unless the Government balances the budget -- by high taxes if necessary -- we are headed for ruinous inflation, Mr. Cargill asserts and he offers a novel way of bringing about the balance. Unemployment, he believes, is the most pressing industrial and budget problem. A great deal could be done to solve it by the following scheme: Assuming that the Government pays $50 a month to support a man on WPA, Mr. Cargill suggests that the Government offer to reduce any company's income tax by $10 a month (just for example) for each additional employee hired over and above those employed at some base date like the present. The tax reduction would last as long as the employment, but not longer than two years. The result would be a net reduction in the deficit.

His own company's business is good due to radio orders, is better than last year and "is no cause for complaint," Mr. Cargill says.

First National Bank of Madison - Mr. Thomas Hefty, president, and Mr. William Spohn, one of the most active directors, had a good many complaints against the trouble and lack of remuneration on the unemployment insurance account of $1 million carried with them and "will throw it out of the bank" if the complaints are not adjusted.

Business in this region is good and the outlook for the year is good, they say. The leading department store, hardware store and manufacturers all report to the bank that business is above last year's levels. The local Sears Roebuck store has the same to report except in its rural sales. Farmers are angry over the low prices for milk, butter and cheese, and their position may cause trouble eventually. The only other deterrent to retail business is uncertainty among the numerous state employees over their future incomes under the new Republican administration.

Government bonds, Mr. Hefty and Mr. Spohn feel, are too high. The Federal reserve system should and could have intervened to keep the market from going so high by letting its portfolio run off, they think. They regard a break in the market as inevitable. Mr. Spohn as trustee for some trusts recently sold out several thousand dollars worth of Governments which he had bought at par and which had appreciated 6 points. To have done otherwise would have been negligent as a trustee, he feels and he believes others in the same position feel the same way. He is now holding cash instead of investments.

Mr. Hefty, whose bank holds $6 million of Governments, "would be in the market tomorrow morning with $3 million worth" if he saw any signs of a break in prices, and he believes everybody would try to beat everyone else out of the market as they did in March, 1937.

Mr. Spohn believes the Government should try to place more of the debt in private hands -- he doesn't know exactly how -- rather than to continue "borrowing in the commercial money market."

Taxes probably must stay high, but the type of taxation could be improved by changes like loss-carryovers, and business won't mind taxes if it can make money, according to Mr. Hefty. He thinks the Government should adopt a policy and stick to it.

Frautschi Furniture Company - Business is lower than a year ago due to the uncertainty among state employees and to war fears, according to the manager. As a result the store instead of ordering furniture from manufacturers in advance is buying only as it sells to customers.

He regards a sales tax in Wisconsin as inevitable. Economy in government is popular in this region, but no one knows how to achieve it, he thinks. One of the great mistakes of the New Deal has been not to pay its way regardless of the cost, and a payroll tax on workers to pay general expenses and to make them realize that Government must have revenue would not be objectionable if the budget required it, he felt.

Loans to small business he regarded as unnecessary.

Miscellaneous - The hardware company is enjoying good business, is optimistic and is remodeling its stores. The printing firm is having less luck, and the banker spoke of "having to pull in its lines of credit"; the company, which is family-owned, paid out its earnings in the year of the undistributed profits tax, the principal owner bought a new plant site with his share of the money, and now the plant can not be built and the company instead of having a reserve has a fixed asset on which it can not raise the cash it needs. The coal and oil dealer is showing slightly better business than a year ago, but is vehemently of the opinion that Government should leave business alone. The newspaper has a serious advertising slump.

State politics are very absorbing -- more than Washington -- but, unlike Minnesota, Wisconsin is fast turning against the Republican administration because of the personality and actions of the governor.

ESD

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Rio de Janeiro

DATE: April 3, 1939, 10 a.m.

NO.: 101

Reference is made to my telegram No. 82 of March 22.

The order of the Bank of Brazil dated March 22 suspending the purchase of compensation marks for exportation of northern cotton to Germany was canceled by the Bank today.

Inform Commerce.

SCOTTEN

EA:LWW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: April 3, 1939, 7 p.m.

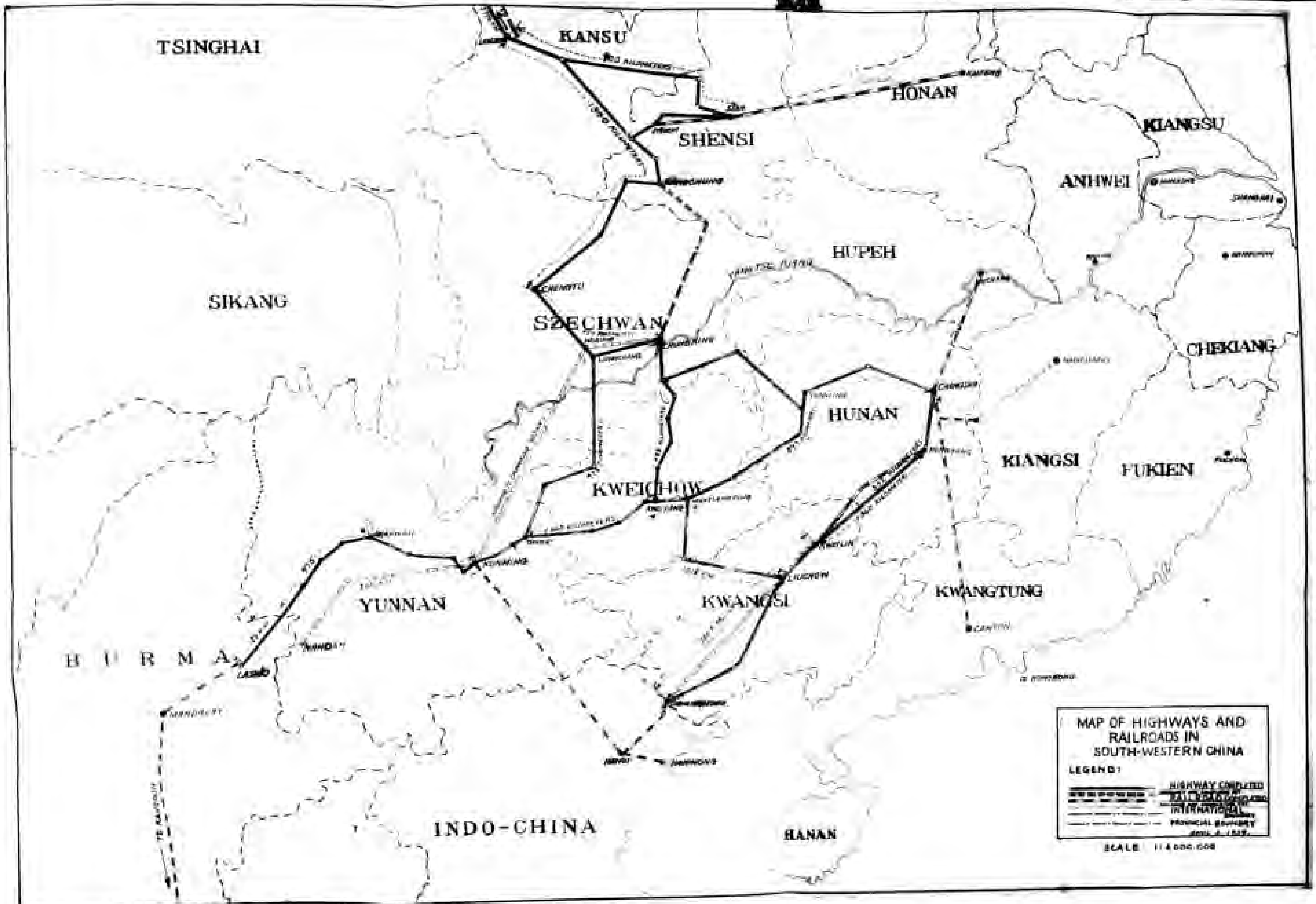
NO.: 229

FOR TREASURY FROM HEATH. No. 11.

With reference to the trip which the Secretary of the Treasury requested Heath to make through three countries, would appreciate indication of the time when he should start.

GEIST.

EA:LWW



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YUNNAN
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KWANGTUNG
B U R M A
INDO-CHINA
HANAN
MAP OF HIGHWAYS AND
RAILROADS IN
SOUTH-WESTERN CHINA
LEGEND:
HIGHWAY COMPLETED
PROVINCIAL BOUNDARY

Chengtu, April 3, 1939

To Secretary Morgenthau from J. Lossing Buck:

Extension of Burma Railway to Chinese Border

Since writing on this topic in my last report I learn from the American Consulate, and also from the director of the Kunming Burma Railway, that an agreement has been reached whereby the Burma Railway people will rapidly extend their line to the Chinese border.

Chengtu, April 3, 1939

To Secretary Morgenthau from J. Lossing Buck:

Bombing Apprehension in West China

Upon my return to Chungking and Chengtu I find people rather upset because of the insistence of the government that people move out of these cities. Chungking is terribly crowded and if indiscriminant bombing did occur considerable loss of life would result, not only from the direct bombing but also from the fires that might be incident there too. In Chungking, therefore, there is a scattering of institutions into the surrounding country. In Chengtu middle schools are beginning to move out. Chengtu does not have the natural conditions for dugout shelters that is found in Chungking, therefore, much of Chengtu is without that type of protection.

Chengtu, April 3, 1939

To Secretary Morgenthau from J. Lossing Buck:

Tsao Ba Reclamation Project, Yunnan

Upon the request of Y.T. Miao I visited the Tsao Ba Reclamation Project, which is being carried out by the Yunnan Economic Council. The area is comparatively level, surrounded by mountains and comprises about 160,000 acres of land, which heretofore has been flooded each summer during the rainy season. The drainage outlet was a sink hole in the limestone rocks, which has gradually become filled up, so during heavy rains the land invariably becomes flooded. A cut has been made between two mountains to carry the water into another stream bed. The area is also irrigated by a new irrigation canal from a lake on the opposite side.

The total investment for irrigation and drainage is about 2,000,000 yuan. Unfortunately the soil is not very good. The original idea was to grow rice entirely and market it at the tin mines near by. Later promoters for growing the mulberry in Yunnan were up against it for land and they asked for 100,000 acres of this reclaimed land. The mulberry industry is a new industry in this section and can only be started with considerable difficulty, but the promoters are enthusiastic and determined. The reclamation project appears to have possibilities of economic success.

I met Mr. Ko, who is in charge of the mulberry work and he is full of enthusiasm for producing high class cocoons and a high grade of raw silk, the latter for the American market, in order to provide foreign exchange and to compete with Japanese raw silk. Silkworm eggs will be supplied by the sericulture station at Kunming, referred to in a previous report. The mulberry project is financed by Bank of China (T.V. Soong) and the New Futien Bank (Y.T. Miao).

FS

GRAY

Paris

Dated April 4,1939

Rec'd 2:53 p.m.

Secretary of State,

Washington.

631, April 4, 5 p.m.

CONFIDENTIAL.

I asked Paul Reynaud in the presence of Daladier today what extraordinary measures if any the French Government would take in the event of the outbreak of general European war. Reynaud replied that at the outset the French Government would take no extraordinary measures whatsoever. He was convinced that the franc in case of war would remain the strongest currency in Europe and that quantities of money would come to France from various European countries. No measures would be decided upon until events should prove the necessity for new decisions. Daladier agreed.

KLP

BULLITT

DEPARTMENT OF STATE
WASHINGTON

April 5, 1939.

My dear Mr. Secretary:

I enclose for your confidential information a copy of a telegram from Ambassador Bullitt, reporting on a conversation he had with Mr. Paul Reynaud, the French Minister of Finance.

Sincerely yours,

Herbert Feis

Herbert Feis,
Adviser on International
Economic Affairs.

Enclosure:

No. 631 of April 4
from Paris.

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury.

AH 77

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 4, 1939, 9 a.m.

NO.: 625

FROM COCHRAN.

This morning I returned from Basel where over the weekend the BIS directors held their meeting.

At the informal meeting on Sunday it was disclosed that before Germany took possession of Czechoslovakia BIS investments in Czechoslovakia had all been repaid with the exception of one item which is scheduled for liquidation on the fifteenth of April. Bachmann tendered his resignation from the BIS Board, which will take effect after the May annual meeting; he retired in March as President of the Board of Management of the Swiss National Bank. His successor on the BIS Board will probably be Weber or Schnorf. I have heard only two names mentioned as successor for Beyen, those of an American private banker in London and a Dutch private banker in the Netherlands; the bankers seem agreed that they should not have a professor as President of the BIS, but that they should continue to have a banker.

At the meeting on Monday an account of his observations in the United States was given by Kano, the Japanese Director, who recently visited there and was much pleased with the reception accorded him in America.

At the Monday meeting the directors decided to recommend to the general shareholders' meeting in May the continuation for the fiscal year ended March 1939 of the regular six percent dividend.

During the recent crisis Switzerland has been particularly nervous. Consideration is being given by the Swiss National Bank to sending Pfenninger to Stockholm shortly for the purpose of studying the financial plans for financial and economic measures in the event of war which the Swedish would follow. I had a talk with Governor Rooth of the Sverigesriks Bank, who said that they had not yet put in final form the details of the plan for submission to Parliament, but he will keep me informed of the progress made.

I talked with Bachmann, who was much perturbed because after he turned over the presidency to Weber in March, the Swiss National Bank permitted the Swiss franc to depreciate to around 30.90 percent as compared to the value before the signing of the Tripartite Agreement. Bachmann mentioned that the Swiss had given the undertaking that their buying and selling prices of gold would not exceed a range covered by a depreciation between 29.25 and 30.75 percent in the document which they signed for me when they adhered to the Tripartite on September 25, 1936. Of course, Bachmann said, the action of the Swiss

might

might be excusable on the ground that other Governments belonging to the Tripartite, particularly the French and lately the British, had permitted their currencies to depreciate much beyond any values anticipated in September 1936 and that the Swiss, who were the only ones to undertake voluntarily the fixing of new gold points, should not be condemned for the present action. However, he expressed concern lest Weber had incurred the ill will of the United States and he wondered whether such annoyance was evidenced by the Federal Reserve Bank of New York purchasing Swiss francs a few days ago without instructions from the Swiss National Bank. It is the expectation of the Swiss Central bankers that there will be launched within the next week or two, if nothing further goes wrong in Europe, the six-year loan to France by which Swiss and Dutch banks will consolidate outstanding French loans on their markets into six-year notes. In my telegram No. 472 of March 14 I announced such a plan, but it was suspended because of the recent crisis.

A few weeks ago a Swiss bank gave a commercial credit to the Burgos Government. The approval of the Swiss authorities was not necessary for this credit,

since

since it was for less than ten million Swiss francs. Consequently the details are not known to the Swiss National Bank.

A first approach to private bankers who usually participate in Swiss-Dutch lending was made by two Franco agents with the view to obtaining a loan for Spain from a syndicate of banks in the Netherlands, Switzerland, Sweden, Great Britain and France. The question of security was raised by the bankers, and last week the agents returned to Burgos to discuss the matter.

I had a talk with Galopin, the Belgian industrialist director, who is also head of the Société Générale. He said that their textile plants in Spain have their machinery left intact, but do not have on hand any wool or cotton at all, and he stressed the fact that raw materials are needed by Spain.

The Belgian National Bank Governor, Janssen, thought there had been an improvement in the outlook for his country in view of the resignation of Maertens from the Academy and because of the results of Sunday's election, all of which made for political peace and a stronger government. He again told me that his Government does not contemplate any changes in monetary policy. Janssen

asked

asked me some general questions about the Johnson law and Export-Import Bank financing, but added that his people did not have anything immediately in mind in regard thereto. He told me about his gold operations with the United States up to the present.

Governor Janssen does not think that Germany will undertake any aggression against Belgium. Several of my friends, including Governor Janssen, think that the general outlook for peace would be much improved in the near future if the French could only be supple enough to meet reasonable claims from the Italians on Suez, Djibouti and Tunisia through diplomatic negotiations. They are all glad to have seen France so strengthened and consolidated internally through the threats from the totalitarian states. However, they think that if Daladier were now a little yielding, in view of his unquestioned position, it would do much to relieve the tenseness of the situation. In the end, they say, it would cost France a comparatively small amount compared to what a war would cost should it eventually come if Italy does not have more space.

My friends from the Bank of Italy were glad that during the recent crisis Mussolini acted with comparative calmness. The growing strength of Germany makes them

genuinely

genuinely unhappy. They look on it as a menace to their own prestige and markets in the Danubian area and there is a possibility of it extending to the Mediterranean. No chance of breaking the axis is foreseen by them, but they would be immensely pleased if the French would be reasonable enough to bring about enough rapprochement between France and Italy to give Germany a cause to worry over and even doubt whether the southern end of the axis would hold. These friends insist that Italy does not want a war and as long as there is any hope of help in improving Italy's economic status, they will keep the peace. However, they do not think the period is indefinite, and Italy cannot wait too long before some move becomes inevitable simply from pressure of population and deterioration of the standard of living in that country.

Observers at the BIS said they would like to see some improvement in the situation in Italy while such conservative financial and economic leaders as Azzolini, Guarneri and Beneduce are still in the Government. They do not believe that these leaders can continue indefinitely to juggle Italian resources sufficiently adeptly so that a balance of payments is achieved.

My

My friends hesitate to contemplate what disorder might result in Italy if the efforts of these leaders fail and more aggressive militarists probably take their place. Mention was made in this connection of the current financial deterioration in Germany that has been quick to follow the ousting of Schacht and his trained assistants, who were replaced by Nazis who are inexperienced. It is becoming somewhat generally understood that new deals, whether totalitarian or liberal, function better with the support of the old hired hands than when their own new-born devotees entirely control their destinies.

END SECTIONS ONE TO SEVEN, INCLUSIVE.

BULLITT.

EA:LWW

Paraphrase of Sections eight to fourteen, inclusive, of telegram No. 625 of April 4, 1939, from Paris

The Netherlands Bank President, Trip, told me that his country had not been so nervous about itself as other countries had been. He does not expect the Germans to make an aggressive move against their country.

Of course if Germany and Great Britain got into a war, the probability would increase, but he feels that even Germany would find it to her advantage now as she did in 1914 to have some neutral neighbors which would act as buffers and provide foodstuffs. During the recent crisis, Trip said, he had lost about $170,000,000 of gold; this was mostly hot money, and belonged to Jews for the most part. Furthermore, large amounts of securities left for safekeeping with Dutch banks by foreigners had been removed; certain securities deposited in Dutch banks by French banks for their nationals have now been transferred to New York where they are held in the name of the Dutch banks.

Trip asked Fournier in my presence whether the Spanish gold which the Bank of France has been holding would now be released. Fournier replied that the litigation had not yet been decided, and of course new factors had come up. There is a growing impression that the French may try to retain some of this gold in payment for taking care of refugees from Spain, and

so

so on.

Fournier objected to Chairman Niemeyer in this connection because recently the BIS permitted the transfer of certain gold which the National Bank of Czechoslovakia had held with it. An international institution like the BIS should not participate in this contentious question of Czechoslovak assets, in Niemeyer's opinion. The BIS would not desire retaliation from Germany, anyway, as it has important investments in that country. Incidentally, now that the British have passed a law to block Czechoslovak holdings, Niemeyer does not know just what they will do with them.

BIS observers did not entirely understand American commercial policy. They did not understand the idea of wheat and cotton export subsidies and possibly import quotas on cotton textiles being developed at the same time that countervailing duties on imports from Germany were imposed. In the Netherlands Premier Colijn is having to countenance an economic program involving increased customs duties and possibly new export subsidies, and in the United States Secretary Hull is facing a dilemma, which affairs are causing concern to European admirers of these two great leaders in liberal trade policies. It would seem much more logical, if cotton planters must be helped by the Government, that exports should not

be

be subsidized, as such subsidy might bring foreign retaliation and would peg the world price of cotton. It would seem better to give benefits to American cotton producers regardless of the destination of their cotton and force the world price down to a level that would put out of business cotton producing countries which have become competitors of the United States since the world price of cotton was raised by the United States.

Eccles' attack on the United States silver policy was commended by my Basel friends. Their only regret was that criticism of this policy by American monetary authorities had not come sooner. These friends marvel at the activity of the United States in foreign affairs, including ~~affairs~~ giving short or medium term Government loans to backward countries to assist in their development. They only wish that such interest were matched by success in restoring the domestic economy of the United States.

Funk did not attend the Basel meeting, being represented by Puhl of the Reichsbank. Pending a decision of mental experts as to whether Vice President Brinkmann may ever be able to resume his post, Puhl is Acting Vice President. Brinkmann is at present in an insane asylum. December 16 was the date of the meeting at which the French press alleges Brinkmann made a speech leading to his ejection from the Bank and being placed in an insane asylum -

or

or about a month before Brinkmann was even given a Reichsbank post.

I had a good visit with Puhl, who asked to see me. Puhl is the last one left of the old group of high ranking officials in the Reichsbank, and apparently will have heavy responsibilities now. He said he would like to have me tell him as an old friend what I thought of the latest move made by Germany. My answer was that the American reaction had been so unanimous and tremendous that everyone must know it. I mentioned that by this action Germany had frightened off trade negotiators from Great Britain and France. I also mentioned that in Great Britain it had aroused sentiment against giving aid to Germany through financial or economic measures in continuing her aggression. It had made it almost impossible for any of us who have genuinely believed that peace through extending trade - and particularly to Germany - could be achieved to say a word in defense of Germany. Puhl assured me that the need for trade was appreciated by the Reichsbank. Even now, he said, any criticism of blocking of Czech balances was being suppressed. The Reichsbank, he said, wants to improve the atmosphere and not contribute to the existing bad feeling. I criticized the Steuergutschein system and told Puhl that by stopping

aggression

aggression and turning to honest trade was the only way to avert a financial debacle; they would have to show an inclination to talk fairly with other trading nations and reestablish faith in the word of Germany. Puhl seemed to appreciate my remarks rather than take offense at them. I repeatedly emphasized that my views were purely personal and unofficial and I made them known to him only because he had questioned me.

I gained the following information or impressions partly from my own conversations with Puhl and Hechler and partly from my Basel friends who also talked with them:

Further direct loans of the German Government could not be absorbed, therefore the Steuergutschein system was resorted to. That this is only a stop-gap is realized by the Reichsbank officials themselves. They know it cannot function for more than a year at the longest without bringing about such an alteration in the percentage of cash payments that German economy would become frozen. Inflation is inevitable if Government military expenditures are not reduced. Sufficient inflation has already come about to involve domestic consumption of more German production than was formerly the case. There is more of a handicap to export trade from German industry's inability

to

to manufacture satisfactory goods for acceptable delivery dates than from foreign barriers to goods from Germany. At present the latest additions to Germany's territory are economic liabilities, and to develop them will require much time and expense.

As for the monetary regime in Prague, Germany has not yet reached any definite decisions. The Reichsbank does not have officials competent in the Czech language, therefore it is difficult for them to supplant the National Bank of Czechoslovakia. Complete German exchange control would be required in order to supplant the crown by the Reichsmark, and such a system could not be entrusted to Czechs. They have not yet settled the question of whether the National Bank of Czechoslovakia will be represented at the BIS shareholders meeting May 8, or whether someone will vote its shares.

It is the opinion of those friends in whose judgment I have most confidence that progress towards a balance of power in Europe has been accelerated by the recent German move. They think that the armaments race should ease once this balance of power is achieved. They do not think that Hitler has yet so lost his sense of touch and timing that he will try anything that will inevitably bring on a world war.

END OF MESSAGE.

BULLITT.

EA:LWW

April 4th 1939
7 P.M. 90

SEA ISLAND
GEORGIA

BK of America

Agrentine

~~Dit~~

Thinks we should get letter from Gianni saying that if either Phelano a F.D.I.C or Federal Reserve or any other angency that has the authority should think in the future that the Bank by paying the ~~[illegible]~~ dividends is imparing its capitol it will agree to withhold the payment of such dividends.

over

In regard to the ~~agr~~ Argentine
I suggested it would be good
time to invite a delegation from
there to come to Wash. similar
to the one that came from the
Brazil. He said it was a
matter he could straighten
out his return with Sec't of Agriculture. He repeated
he could straighten it out.
(If he could why has he not
done so during the last two
years. It is a question of permitting
certain amount of frozen
meat coming in.)

April 4, 1939

Douglas called me up to say to me that in his whole public and private life his association with me stood out above everything else. (This was just after he was confirmed.) And that he wanted to let me know that the understanding that he and I had with regard to Transamerica, he had explained it all to Jerome Frank and Mr. Eichner and that they were ready to carry on. He was only sorry for one thing and that was he had hoped to be able to get out the Court Order against this man, Mahaney, whom they employed in the San Francisco office and who subsequently proved to be an informer or spy for Giannini, and he also had hoped to get out the indictment against Time trust and that those two things were going.

I said that I hoped I would be able to go to him from time to time for advice and he said absolutely, and he hoped our friendship would continue. He repeated several times how much he enjoyed working with me.

April 4, 1939

To: The Secretary

From: Mr. Hanes

I went up to see Mr. Doughton this morning and he told me that he was very much confused about the present status of the tax situation. He asked me whether or not the Secretary had decided not to pursue his recommendations as outlined in his Press conference of February 23d. I told Mr. Doughton that I was somewhat confused myself and that we would have to wait until the return of the Secretary before answering his questions. He then told me that he had called upon the President at the White House not for the purpose of discussing taxes or the tax program but rather to discuss with him some appointments which he was desirous of having made. He told me that just before he left the White House, the President had written in his own handwriting his thought concerning the tax program as follows: (1) renew the excise taxes; (2) delay the step up in payroll tax from 1 to 1½ percent; (3) pass a bill taxing interest from future tax-exempt bonds. Mr. Doughton said that he was not asked whether or not he agreed with this program, but was told by the President that in his opinion this is all that ought to be done at this time. Mr. Doughton told me that he had told the President that he was so out of touch with things, having been away so long that he had not given sufficent study to the situation to be able to talk intelligently about it.

I then went over to see Senator Harrison, having been requested by him to come by his office. He was very pleased about the letter he had received from the President in answer to his letter of March 24th. The letter which Senator Harrison showed me signed by the President was the identical letter which we sent to you to be forwarded to the President with your letter about the Pat Harrison incident.

I then called on Congressman Somers and found out the delay on the Stabilization Fund Act was caused by Congressman Somers not having his report ready to give the Congress. He then told me that it would be a week to ten days before he would have it ready and be sufficiently prepared to present the matter on the floor. At that time he anticipated no trouble in meeting a rule to bring the bill to the floor of the House.

J.W.H.

April 4, 1939

To: The Secretary

From: Mr. Hanes

I went up to see Mr. Doughton this morning and he told me that he was very much confused about the present status of the tax situation. He asked me whether or not the Secretary had decided not to pursue his recommendations as outlined in his Press conference of February 23d. I told Mr. Doughton that I was somewhat confused myself and that we would have to wait until the return of the Secretary before answering his questions. He then told me that he had called upon the President at the White House not for the purpose of discussing taxes or the tax program but rather to discuss with him some appointments which he was desirous of having made. He told me that just before he left the White House, the President had written in his own handwriting his thought concerning the tax program as follows: (1) renew the excise taxes; (2) delay the step up in payroll tax from 1 to 1½ percent; (3) pass a bill taxing interest from future tax-exempt bonds. Mr. Doughton said that he was not asked whether or not he agreed with this program, but was told by the President that in his opinion this is all that ought to be done at this time. Mr. Doughton told me that he had told the President that he was so out of touch with things, having been away so long that he had not given sufficent study to the situation to be able to talk intelligently about it.

I then went over to see Senator Harrison, having been requested by him to come by his office. He was very pleased about the letter he had received from the President in answer to his letter of March 24th. The letter which Senator Harrison showed me signed by the President was the identical letter which we sent to you to be forwarded to the President with your letter about the Pat Harrison incident.

I then called on Congressman Somers and found out the delay on the Stabilization Fund Act was caused by Congressman Somers not having his report ready to give the Congress. He then told me that it would be a week to ten days before he would have it ready and be sufficiently prepared to present the matter on the floor. At that time he anticipated no trouble in getting a rule to bring the bill to the floor of the House.

JWH:ce

orig. to Secretary
in pouch - 4-4-39

93A

Office of the Attorney General
Washington, D.C.

April 4, 1939

The Honorable,
The Acting Secretary of the Treasury.

My dear Mr. Hanes:

I acknowledge receipt of your letter of March 29, 1939, in which you advise that you have designated Mr. E. H. Foley, Acting General Counsel, to represent the Treasury Department on the Advisory Committee in the study of administrative procedure.

I wish to thank you for your cooperation in this important matter and to assure you that I fully appreciate that a successful study of this problem can only be accomplished by the whole-hearted cooperation of the agencies and commissions which are so vitally interested.

Very sincerely yours,

Frank Murphy

Attorney General.

24

April 4, 1939

To: The Files

From: Mr. Hanes

Jimmy Roosevelt came to see me at 3:30 P.M. on April 3rd. He told me that he was on his way to Europe and was stopping to discuss his telephone conversation with me from California. He told me that his only interest in the Giannini matter was that in his opinion Mr. Giannini was an honorable man and wanted to do whatever was necessary in order to adjust his differences with the Comptroller's Office and the Securities and Exchange Commission. More particularly the Securities and Exchange Commission as it was Jimmy's thought that differences with the Comptroller's Office were well on their way to being ironed out. He said that he was advising Giannini to stipulate agreement to certain charges by the Securities and Exchange Commission and that he was on his way to see members of the Securities and Exchange Commission to see if there was not some means by which the present differences could be adjusted.

I repeated to Jimmy practically what I had said to him over the telephone, namely, that a good deal of feeling existed in certain quarters in Washington; that he was interfering with a matter that was none of his business, and I advised him to watch his step and be cautious about being too active in the matter. Jimmy said that he recognized that fact but that since his only interest was in seeing that justice was done to every citizen, he felt that it was his obligation to do whatever he could to get the matter adjusted. I told him that the Comptroller's Office was getting along nicely with Mr. Giannini; that he had agreed to do certain things which were demanded by the Comptroller, and that until he had failed to do these things, which he had agreed to do, the Comptroller's Office had no quarrel with him. Jimmy was very pleasant about the whole matter and said he appreciated our attitude.

Before he left he said there was one other matter he had been asked to mention, and that was the tax situation of one Joseph Schenck. He said that Mr. Schenck had told him that he had a tax difficulty with the Bureau of Internal Revenue, and that he had received a hint to the effect that he might be charged with fraud. Jimmy made the specific request that if we were going to charge Schenck with fraud that we at least give him the opportunity to come in and present his side of the case, before a fraud charge is published against him. I was not familiar with the Schenck case, and therefore called Commissioner Helvering to find out what the status of this case is. I was advised by the Commissioner that we did have a rather important case against Schenck, and that there was a possibility that fraud might be involved although no decision has been reached on this point. I told Jimmy that if it was in keeping with the policy of the Bureau and the Secretary of the Treasury, that we would give Schenck every opportunity to explain his case before charging him with fraud. This seems to me to be perfectly fair, although I do not know if it is in accordance with the policy of the Bureau.

J.W.H.

Woodstock, Illinois
April 4, 1939

FOR THE SECRETARY:

This town of less than 6,000 persons just outside the Chicago commuting fringe is dependent upon its two factories and upon the surrounding dairy farmers. Like the factories in Madison, Wisconsin, the Woodstock plants are enjoying good business, but the dairy farmers are complaining about the price of milk. The situation is well summed up by the local Montgomery, Ward store which, with other lines of business holding up well, is beginning to have trouble with rural sales. One of the factories complained much about the NLRB. The local bank is aggressively interested in the farmers 'round about and has $750,000 of loans compared with $60,000 of Governments. Fear of war is much less talked of here than in Minneapolis or Madison and is said to be of no business importance.

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Alemite Die Casting Company -- Mr. Drummond, general manager, said the company's business is almost double that of a year ago, having recovered nicely from a January lull. It is not yet up to 1937 levels, and no boom is in progress, but Mr. Drummond said the outlook is good and he is very optimistic. When I asked about the possibility of plant expansion, he seemed never to have considered it seriously, saying that the local labor market was already exhausted and that the company "did not want to get too big because, if it did, it would be attacked". He was referring to labor attacks primarily.

Mr. Drummond criticized the NLRB saying that employers feel "they are licked before the case starts". He said outside agitators had been working among the employees who are primarily from local farm families, and the company evidently fears some labor trouble. Mr. Drummond asked about the possibility of amending the labor relations act and said he believed some responsibility should be placed on persons who endanger life and property.

Otherwise Mr. Drummond said he approved of the Administration and what it had done. The WPA, he felt, had prevented a revolution in this country. He is very sure, without seeming to be alarmed, that Government spending will end with a breakdown and a capital tax to pay the debt. He said he works closely with the local employment and relief offices. He also praised the tax exempt security, social security and FHA programs. Because the factories have grown faster than the town, housing is badly needed and the company invited the FHA people to address an employees' mass meeting; 15 or 20 employees undertook houses, but, according to Mr. Drummond, the local landowners choked off development by raising real estate prices. The wage-hour law caused the company no trouble. High taxes he seemed to accept as necessary.

War threats are of no business significance, Mr. Drummond said, although people are worried about war possibilities.

Woodstock Typewriter Company -- This old, small typewriter company is owned by the Sears estate and is run by one of the Sears sons as a minor pastime. His assistant, who was in charge, said the company had recently increased its working week from 3½ to 5 days and that the company couldn't complain about business, although it saw no concrete indication of improvement in the future. The recent pick up was attributable to school buying which recovered after some years of inactivity, but the manager complained that "there is no money in it" because of the special price given schools.

The company does a small export business, shipping about 200 machines abroad each month. To supply some of this business, the company has to buy German-character type from Germany. They had noticed the Treasury's countervailing duties on German imports, but said the duties would not affect their buying because they need the type and can not afford to make such a small amount of it. Blocked balances and similar exchange restrictions did not worry the manager, who had been a foreign representative of Royal Typewriter Company most of his life. He said that he had observed that the pendulum usually swung back in most major countries and that over a period of 10 years an importer could get his money out at full value.

He was very emphatically of the opinion that we should let Hitler swallow what he wanted to and that Europe is none of our business. (Two men coming down on the train expressed the same opinion with many skeptical remarks about Britain and France.) War scares are of minor business importance, he thought.

The Woodstock manager said he approved much that the President has done, especially social security, but that he had bad advisers, particularly Miss Perkins. Federal taxes, he said, are no great trouble and he seemed resigned to high taxes, but he was very critical of the local tax laws.

<u>First National Bank of Woodstock</u> -- The president of this bank demonstrates that an aggressive banker can actually make money on the Government program instead of being hurt by its competition. Out of resources totalling $1,400,000, this bank has loans amounting to $750,000 of which about $400,000 is to local farmers and farm dealers. He makes CCC corn loans, chattel mortgage and real estate mortgage loans, a small amount of automobile financing loans, and commercial loans to local merchants. He has only $60,000 of Government bonds and $230,000 of other bonds of which only three are substandard. Against bond depreciation of $1,300 he has a reserve of $10,500. His cash on hand, at the reserve bank and with correspondents is between $400,000 and $450,000. He pays no attention to the Government bond market.

He likes the CCC corn loan program and makes money on it. He has no complaint against the production credit association, asserting that any active banker can take his share of the business away from the PCA. He says he has his pick of the local farm loans in spite of the PCA. The association advertises a 4½% interest charge, and the bank rate is 7%, but this is on a deferred payment plan which the banker has been able to convince the farmers makes the actual interest charge 3.4%. He thinks the PCA would be bad if, for competitive reasons only and just to maintain itself, it cut interest rates. The PCA should fade out when a local institution is taking care of the farmers' needs; banks might be given the right to discount loans with the Federal Intermediate Credit Banks.

Local farmers, according to the bank president, are complaining about milk and butter prices. He says the only solution is AAA quota control and parity payments on milk; he has made one trip to Washington to urge this solution and has attended local mass meetings in favor of it. (A similar solution was urged by a resolution adopted at a dairy farmers' meeting in Madison, Wisconsin, yesterday.) A part of this farm sentiment is anti-union and is especially directed against the Chicago milk drivers who are getting $48 a week.

In spite of the unsatisfactory milk and butter prices the farmers still are meeting their payments at the bank, which run about $5,000 a month, pretty well, and only a few asked for more time on the March 15 payment date. Also in spite of the farmers' troubles the retail business of the town has held up well because of the two factories' operations. The hardware and clothing stores are doing better than a year ago, and the tendency of chain stores to push in is taken as an indication that they consider the town a good bet. The recent trend in the Montgomery, Ward rural sales is the only sour note.

The bank president complained about the tardiness of Rural Rehabilitation checks which he said do not arrive until 6 weeks after approval. In many instances, he says, the farmers are sitting on the farms with no money to buy seed and equipment although their loan was approved in February. Plowing time is now upon them.

Local, not Federal, taxes worry this banker. He wants all tax exemptions abolished. He is against Federal loans to small business as unnecessary.

ESD

JR

GRAY

Berlin

Dated April 4, 1939

Rec'd 12:55 p.m.

Secretary of State,

Washington.

230, April 4, 3 p.m.

No. 12 FOR TREASURY FROM HEATH.

With a figure of 10,488,000,000 marks total German currency circulation at the end of March reached a record point nearly 100,000,000 marks higher than on December 31 which is normally the high point of year. In part this increase is due to the fact of the end of the quarter falling on Friday a day of great demand for currency for wage payments and in part to increased demand for marks in Bohemia and Moravia where the mark now circulates in fixed relation to the Czech crown. It would seem, however, that the increase is only partly attributable to these causes. The monthend figure is over four hundred million marks higher than at the end of February and nearly three billion /marks higher than on March 31, 1938.

Total investments bills and clerks security loans and securities stood at 8,207,000,000 marks or 1,209,000,000 marks higher than on February 28 and some 63,000,000 marks higher even than on December 31.

The

-2- #230, April 4, 3 p.m., from Berlin.

The Reichsbank statement contains further evidence of the financial stringency of the Reichsbank since it indicates that the operating credit of the Reich Treasury with the Reichsbank is being fully availed of.

There was no indication of open market operations by the Reichsbank during the last three weeks since holdings of eligible securities continue to stand at 677,000,000 marks. During the last three months however these holdings have increased by 120,000,000 marks.

GEIST

CSB

JR

PLAIN

London

Dated April 4, 1939

Rec'd 3:20 p.m.

Secretary of State,

Washington.

442, April 4, 7 p.m.

FOR TREASURY FROM BUTTERWORTH.

1. Apprehension in the city has been revived by the shooting of the King of Iraq, the murder of the British Consul at Mosul and the reports that Italy is preparing to extend its control over Albania. London security markets were consequently weak. Likewise the foreign exchange market in the late afternoon became active and the dollar was fairly heavily bid. Of the 274 bars sold at gold fixing, 146 were married and something less than 20 supplied by the British fund. There were some dealings after fixing.

2. Incidentally the March unemployment figures published today are as of the 13th two days before the Germans marched into Czechoslovakia so that the reduction in unemployment since February of 170,000 which was well spread geographically and over all industries except shipbuilding reflects a continuation up to the day of the count in the general recovery indicated in the February figures.

KENNEDY

KLP

JR

GRAY

London

Dated April 5, 1939

Rec'd 1:56 p.m.

Secretary of State,

Washington.

446, April 5, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

The exchange market was very quiet today with much the same atmosphere as yesterday, the incident of the First Lord of the Admiralty's speech being not taken very seriously in the city. The dollar was slightly bid but the British fund sold a negligible amount. On the 117 gold bars dealt in 95 were married and the market was prorated on a 14% basis. Stock market prices were mostly down but there was little selling.

KENNEDY

RR:CSB

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 5, 1939, 5 p.m.

NO.: 641

I had a talk with Governor Rooth of the Sveriges Riksbank, who said that the Government of Finland had just been granted a thirty million Swedish crown loan jointly by the Stockholm Senskilda Bank, the Bank of Finland and the Sveriges Riksbank. The bonds are to be delivered to the three banks in equal amounts, at 99, and the loan is to run for three years. The foreign exchange holdings of the Bank of Finland will be drawn on for its share. The loan proceeds which are denominated in Swedish crowns will actually be transferred half in dollars and half in sterling. Such action will prevent any great easing on the Swedish money market which a conversion into foreign exchange of 30,000,000 of Swedish exchange on that market might bring about.

The meaning of this operation is that the Swedish Riksbank reduces its dollar and sterling holdings by 10 million crowns, and takes a three year risk with the Finnish Government in Swedish crowns in its place. This loan was decided on by Finland so that it could buy immediately a large part of the material principally for armaments which had been planned for over a three-year program, and tax measures have already been instituted

to

to cover these expenditures.

Yesterday evening Kano of the Yokohama Specie Bank came through Paris. He was on his way to London from Basel. He called on me and we were able to have a longer talk than was possible when we were in Basel. The past few years Kano has regularly talked with me regarding the opportunities for businessmen and particularly bankers to keep their governments informed through their central banks as to the actual state of national sentiment in the countries where they are stationed or with which they are closely related. The military aggression in China on the part of Japan has been consistently opposed by Kano as well as Yanagita of the Central Bank of Japan. I am told that the two officials have repeatedly urged their friends in Japan, particularly former and present governors of the Central Bank, to do what they could to persuade that country to be more conciliatory, especially in dealings with Americans and British.

The friendly reception which Kano received in March in the United States pleased him very much. I think he was influenced partly because of this to talk with the Japanese Ambassador in Washington in line with the above. Kano said that the Japanese people had been much touched by the action of the American Government in using one of its war vessels to take back to Japan the

remains

remains of the former Japanese Ambassador to the United States. This warship is expected to arrive in Japan on the seventeenth of April. Kano said he had recommended to his Ambassador in Washington that this date would be a good time for Japan to make some reciprocal gesture toward the United States and also toward the British, that it was much easier for Japan to deal with some questions in this way than to have compulsion brought to bear to make them admit them. He had recommended to his Ambassador, he said, that with the opening of the Tsingtao port such concrete measures be taken as the opening of the Yangtze River and the factory district of Shanghai, and permitting foreign interests to take back their missions and schools. Kano expressed optimism that at least some of these steps will be undertaken during the next month or so, and that hereafter and effort will be made by Japan to pursue a more agreeable policy toward our country.

BULLITT.

EA:LWW

PARAPHRASE OF SECTION FIVE. Telegram No. 641 of April 5, 1939, from Paris.

There are reports in the press that legislation has been introduced to reduce by 20 percent the value of the Iceland kroner. These reports agree with information I got in Basel. When I was there I was also informed that a visit was made recently to Iceland by one man claiming to represent interests in Manchukuo and another interests in Honduras, behind the front of an Englishman named Wright. An option to extend to the Government a loan of \$2,500,000 ~~\$250,000,000~~ was sought. This offer has not come to anything so far. My informant believes that it will not be successful, since the promoters were suspected of being German agents who were looking for submarine and air bases.

A report comes from Amsterdam that a Dutch combine by the name of Saiopa has been formed, the head office being in Rome with a branch in Addis Ababa. The purpose of the combine is to cultivate in Ethiopia the production of coffee, palm oil, tea and cinchona. It is said that the Dutch supplied most of the capital of 2,000,000 florins with the Italians participating to a small extent.

Very quiet Paris exchange market. A fair amount of sterling has been gained by the Bank of France. Some pressure still on the belga.

END OF MESSAGE.

BULLITT.

EA:LWW

STATEMENT OF THE SECRETARY OF THE TREASURY
BEFORE THE COMMITTEE ON WAYS AND MEANS

April 5, 1939
typed 9:30 a.m.

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I am pleased to respond to your invitation and discuss with you certain changes in our tax laws which, in my opinion, would stimulate economic recovery and bring about a more equitable distribution of tax burdens.

In your capacities as members of this Committee and of Congress, you have during the past few years been largely instrumental in the making of numerous changes in the structure of the Federal tax system. These changes were made primarily to meet revenue needs growing out of the depression. In the fiscal year 1930, the revenue collections amounted to slightly less than $4,200,000,000. As the depression deepened, the revenue fell off sharply so that by the fiscal year 1932 the yield was only $2,000,000,000, or less than half the 1930 collections. Expenditures meanwhile were rising as the government acted to meet the problems created by the depression. Confronted with this situation, Congress in 1932 radically revised the tax system, and in most of the years since then has further strengthened the power of the system to produce revenue. As economic conditions improved and the tax changes became effective, revenues increased from the low point of $2,000,000,000 in 1932 to $6,240,000,000 in 1938 under conditions of incomplete recovery. If the national income should rise to $80,000,000,000, the system would probably produce $8,000,000,000 in revenue.

The increase in the revenue-producing power of the tax system was accomplished principally:

By lowering exemptions and increasing the rates and degree of progression of the individual income tax, and disallowing deductions that reduced the yield;

By increasing the corporation taxes through raising the rates of the income tax, disallowing types of deductions that reduced the yields and providing an inducement for the distribution of profits, and by imposing a capital stock and an excess profits tax;

By imposing an undistributed profits tax to compensate the government for the loss of revenue that results when corporations withhold earnings from their stockholders;

By lowering exemptions and increasing the rates and degree of progression of the estate taxes and enacting a gift tax to make the estate tax more effective;

By enacting liquor taxes following repeal of prohibition;

By enacting various excise taxes and increasing the rates of others; and

By levying payroll taxes to aid in financing the social security program.*

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* Specifically, during this period the personal exemptions under the individual income tax have been lowered from $3,500 to $2,500 for a married couple or head of family and from $1,500 to $1,000 for a single person. The maximum tax rates, normal and surtax combined, have been increased from 25 percent to 79 percent. Not only were

the top rates increased, but the increase was general throughout the range of incomes. For example, on the bracket of income immediately over $100,000, the rate has been increased from 25 percent to 62 percent. During the same period income from dividends has for the first time been subjected to the normal rates of the individual income tax.

The corporation income tax has been increased from a flat rate of 12 percent to graduated rates of from 12½ to 16 percent for small corporations and from 16½ to 19 percent for large corporations. Whereas previously the entire amount of dividends received by corporations had been exempt from the corporation income tax, during this period we have made 15 percent of the amount of such dividends taxable at the same rates as corporate income. The privilege of filing consolidated returns has been abolished for all corporations except railroads, each corporation being treated as a separate entity for tax purposes. Personal holding companies have been subjected to additional special taxes, and the administration of the special taxes on other types of corporations improperly accumulating surplus has been greatly strengthened. Further, a capital stock tax of $1 per $1,000 of declared value has been enacted and implemented by an excess profits tax designed to prevent undervaluation of the corporate capital stock.

The role of death taxes in the Federal revenue system has been greatly increased. This was accomplished by lowering the exemption for the estate tax from $100,000 to $40,000, by increasing the rates, and by enacting a gift tax. The maximum rates of the estate tax were increased from 20 percent to 70 percent. The increases were general throughout the scale, the bracket rate on the amount of net estate immediately above $1,000,000, for example, being increased from 8 percent to 32 percent.

The repeal of prohibition has added approximately half a billion dollars a year to Federal revenues. New manufacturers' excise and other miscellaneous taxes have been enacted and the rates of certain others increased, which, together, have added approximately another half billion dollars annually.

Finally, during this period we have enacted payroll taxes which in the fiscal year 1938 yielded approximately three-quarters of a billion dollars, in order to help finance our comprehensive social security program.

An adequate revenue yield is not, however, the only test of a good tax system. Such a system should have the least possible deterring effects on the operation of the economy; it should distribute the tax burden fairly in accordance with the principle of ability to pay; it should be as inexpensive as possible to administer, both for the government and for the taxpayer; it should, insofar as possible, impose its burdens directly on the persons finally expected to pay in order to give them a proper consciousness of the burden of government; and it should be suitable for our Federal system of government. No tax system can be perfect in all these respects, or indeed, in any of them, but we can strive to make it approach as closely as possible.

It was to be expected that the rapid increase in the revenue-producing power of the tax system would be at the expense of some or all of these other considerations. Efforts were made, of course, to adjust the system as defects were disclosed from year to year. The time has now come to examine our tax system in a more comprehensive fashion to see what adjustments can be made, which, while preserving the revenue-yielding power, will remove inequities and deterrents to business recovery.

The set of circumstances with which we are now confronted indicate that our need today is not for new and heavier taxes, but rather for ways and means of making existing taxes more productive. As the President stated in his annual message of January 3, 1939, the internal revenue system now in existence is believed to be capable of supplying the revenue requirements of the Federal Government if a reasonable increase in economic activity and national income takes place.

We in the Treasury are constantly investigating the problem of increasing revenues without increasing the over-all burdensomeness of taxation. Our tax studies indicate that in some instances present taxes interfere with the smooth and efficient operation of business and discourage enterprise. Without successful business operation, without business optimism and initiative, recovery and a permanently high level of Federal revenues cannot be attained. Government needs additional revenue. This need can be met with the least harmful effects through increased business activity and a larger national income. It is a worthwhile task, then, to promote better business by removing features of currently imposed taxes which interfere with this objective, especially if in this manner the equity of the tax system can be enhanced.

(Continue with business tax proposals and other proposals.)

115

This draft was sent to the Secretary
in Georgia, in the mail pouch - April 5th

DRAFT

STATEMENT OF THE SECRETARY OF THE TREASURY
BEFORE THE COMMITTEE ON WAYS AND MEANS

April 5, 1939
3:30 p. m.

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I am pleased to respond to your invitation and discuss with you the question of what changes, if any, in our tax laws are shown by study and experience to be needed at this time. To approach this question intelligently we need to have in mind the background of our present system.

In your capacities as members of this Committee and of Congress, you have during the past few years been largely instrumental in the making of numerous changes in the structure of the Federal tax system. These changes were made primarily to meet revenue needs growing out of the depression.

In the fiscal year 1930, the revenue collections amounted to slightly less than $4,200,000,000. As the depression deepened, the revenue fell off sharply so that by the fiscal year 1932, the yield was only $2,000,000,000, or less than half the 1930 collections. Expenditures meanwhile were rising as the government acted to meet the problems created by the depression.

Confronted with this situation, Congress in 1932 radically revised the tax system, and in most of the years since then has further strengthened the power of the system to produce revenue. As economic conditions improved and the tax changes became effective, revenues increased from the low point of $2,000,000,000 in 1932 to $6,240,000,000 in 1938 under conditions of incomplete recovery.

The increase in the revenue-producing power of the tax system was accomplished principally:

By lowering exemptions and increasing the rates and degree of progression of the individual income tax, and disallowing deductions that reduced the yield;

By increasing the corporation taxes through raising the rates of the income tax, disallowing types of deductions that reduced the yields and providing an inducement for the distribution of profits, and by imposing a capital stock and an excess profits tax;

By imposing an undistributed profits tax to compensate the government for the loss of revenue that results when corporations withhold earnings from their stockholders;

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The corporation income tax has been increased from a flat rate of 12 percent to graduated rates of from 12½ to 16 percent for small corporations and from 16½ to 19 percent for large corporations. Whereas previously the entire amount of dividends received by corporations had been exempt from the corporation income tax, during this period we have made 15 percent of the amount of such dividends taxable at the same rates as corporate income. The privilege of filing consolidated returns has been abolished for all corporations except railroads, each corporation being treated as a separate entity for tax purposes. Personal holding companies have been subjected to additional special taxes, and the administration of the special taxes on other types of corporations improperly accumulating surplus has been greatly strengthened. Further, a capital stock tax of $1 per $1,000 of declared value has been enacted and implemented by an excess profits tax designed to prevent undervaluation of the corporate capital stock.

The role of death taxes in the Federal revenue system has been greatly increased. This was accomplished by lowering the exemption for the estate tax from $100,000 to $40,000, by increasing the rates, and by enacting a gift tax. The maximum rates of the estate tax were increased from 20 percent to 70 percent. The increases were general throughout the scale.

These revisions have produced a tax system capable of yielding adequate revenue under conditions of full recovery. Receipts for the fiscal year ending this June will amount to approximately $5,600,000,000, a decline of about $600,000,000 from the last fiscal year due to the business recession. The receipts for this year will thus fall short of expenditures by nearly $4,000,000,000 but, as the President stated in his budget message:

> "Sound progress toward a budget that is formally balanced is not to be made by heavily slashing expenditures or drastically increasing taxes. On the contrary, it is to be sought by

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the bracket rate on the amount of net estate immediately above $1,000,000, for example, being increased from 8 percent to 32 percent.

The repeal of prohibition has added approximately half a billion dollars a year to Federal revenues. New manufacturers' excise and other miscellaneous taxes have been enacted and the rates of certain others increased, which, together, have added approximately another half billion dollars annually.

Finally, during this period we have enacted payroll taxes which in the fiscal year 1938 yielded approximately three-quarters of a billion dollars, in order to help finance our comprehensive social security program.

employing every effective device we may have at our command for promoting a steady recovery, which means steady progress toward the goal of full utilization of our resources. We can contribute very materially toward that end by a wise tax program."

The revenue system now in existence is capable of supplying the revenue requirements of the Federal Government if a reasonable increase in economic activity and national income takes place. For instance, when our national income reaches $80,000,000,000, Federal receipts under the existing tax system will probably amount to $8,000,000,000. The same conditions which will have produced this increase in receipts will also make possible a considerable reduction in Federal expenditures.

An adequate revenue yield is not, however, the only test of a good tax system. Such a system should have the least possible deterring effects on the operation of the economy; it should distribute the tax burden fairly in accordance with the principle of ability to pay; it should be as inexpensive as possible to administer, both for the government and for the taxpayer; it should, insofar as possible, impose its burdens directly on the persons finally expected to pay in order to give them a proper consciousness of the cost of government; and it should be suitable for our Federal system. No tax system can be perfect in all these respects, or, indeed, in any of them, but we can strive to make it approach the best possible.

It was to be expected that the rapid increase in the revenue-producing power of the tax system would be at the expense of some or all of these other considerations. Efforts were made, of course, to adjust the system as defects were disclosed from year to year. The time has now come to examine our tax system in a more comprehensive fashion to see what adjustments can be made, which, while preserving the revenue-yielding power, will remove inequities and deterrents to business recovery.

We in the Treasury are constantly investigating the problem of reducing the burdensomeness of taxation without sacrificing revenue. Our tax studies indicate that in some instances present taxes interfere with the smooth and efficient operation of business and discourage enterprise. Without successful business operation, without business optimism and initiative, recovery and a permanently high level of national income and employment cannot be attained. I believe that our primary aim in revising our tax system at this time should be to promote these objectives. Moreover, I believe that these objectives are fully compatible with a further enhancement of the equity of the tax system.

A number of features of our taxes are both inequitable and discouraging to the healthy development of business.

Business is now taxed on an annual basis. The profits of one year are treated without regard for the losses of another. The result is inequitable since business concerns with fluctuating incomes and losses must pay higher taxes than do concerns with stable incomes. Some business incomes fluctuate more than others because they are more susceptible to changes in the general business situation, others more from causes peculiar to the particular industry.

In the interest of fairness, it would be desirable to base the tax on a firm's average income over several years instead of on its income in a single year. Administrative difficulties have prevented the averaging of income. The effect of averaging can be largely achieved, however, by allowing net losses of one year to reduce incomes of future years. This was the practice before the depression.

Failure to provide for the carry-over of losses tends to discourage persons from developing new enterprises, since such enterprises usually suffer losses in their early years. The allowance of a loss carry-over would be particularly beneficial to the depressed capital goods industries. Concerns engaged in these industries suffer heavy losses in some years and enjoy large profits in others. Since a large proportion of the unemployment is traceable to these industries, removal of inequitable elements in the tax structure which tend to depress them is especially important.

There are other features of business taxation in need of revision. Among these are the inter-dependent corporation capital stock and excess profits taxes. These are really taxes on the amount of profits and the businessman's ability to predict them rather than on the actual value of capital stock and excess profits. To minimize combined capital stock and excess profits taxes, the taxpayer must estimate his business profits accurately. Since, however, profits are highly unpredictable, most businessmen are likely to make errors in declaring the value of their capital stock -- errors which may result in disproportionate tax burdens. New enterprises as well as other concerns with widely fluctuating earnings are particularly vulnerable in this guessing contest. For these reasons, I believe it would be desirable to repeal the capital stock and excess profits taxes and replace the revenues thus lost by other forms of corporation taxation.

The capital losses of corporations are now deductible from other sources of corporate income only to the extent of $2,000. Under this provision a corporation with a deficit may be required to pay a tax. Such a situation would arise when the capital losses exceeded the income from other sources. While this limitation does not impose a serious hardship on most corporations, it may nevertheless be detrimental to financial corporations. These corporations in years of severe depression may suffer serious capital losses. The limitation on the deduction of such losses may radically interfere with their proper function in the investment market. I recommend, therefore, that the limitation upon the capital losses of corporations be removed and that the deduction be allowed in full against other sources of income as was the practice before the depression.

There is general agreement that the tax burden should be distributed equitably in accordance with individual tax-paying ability. That principle found effective application in the selection of income as a major basis for taxation a quarter of a century ago. Despite almost universal acceptance of the individual income tax as the most generally satisfactory source of Federal revenue, it still plays an inadequate role in the Federal tax system. In the fiscal year 1938 it yielded only $1,300,000,000. Although this amount exceeded 1930 collections by almost

$150 million, the proportion of total revenues which it represented declined from 27 percent in 1930 to 20 percent in 1938.

The present Federal individual income tax reaches comparatively few individuals. For the calendar year 1936 scarcely more than two million individuals paid Federal income taxes. In other words, substantially more than 90 percent of the gainfully employed had no liability under the major progressive element in the Federal tax structure. This circumstance, coupled with the quantitative importance of consumption taxes, has produced an anomalous situation. Those in the very lowest income groups are heavily burdened by consumption taxes; those in the highest income groups pay relatively high income taxes; while a large middle income group is lightly taxed in comparison.

To make the tax system more equitable and to pave the way for the future elimination of less acceptable revenue sources, the role of the individual income tax should be increased. Those with middle-sized incomes should be brought within its scope. With this objective in mind, I recommend that the personal exemptions for both single and married individuals be reduced and that the rates upon the middle income tax bracket be increased. In this manner, and in this manner alone, can the principle of ability to pay be extended to a substantial segment of our people.

In addition to the need for broadening the individual income tax, I call your attention to the upper rates of the individual income tax. The present rate of 79 percent exceeds the maximum rate during the War period. The incentive remaining to high income classes to utilize their savings by investing them in new business or risking them in the expansion of old business has been unduly impaired by these high rates. These rates of tax naturally encourage the upper income classes to resort to ultra-safe investments or to cruder forms of hoarding. The time has probably arrived when we must reexamine the repercussions of these very high rates upon business incentives and the growth of the national income.

Taxes upon property transfers from generation to generation present another opportunity for the application of ability to pay and the advancement of equity in taxation. Although the rates of estate taxation were increased during the past few years, its yield today is not as great as it might well be. This is due in part to a lack of coordination between the estate tax and the gift tax. Individuals of substantial wealth can reduce their prospective death tax liability markedly through the transfer of property during life. The gift taxes applicable on such transfers result in sufficient savings to make that course extremely profitable. I believe that the solution to the problem lies in combining the estate and gift taxes so that gifts will be treated simply as an early partial distribution of the estate. I recommend that Congress examine the possibilities of such a combination. If this were accompanied by a lowering of exemption and an increase in the rates applicable to the middle estate brackets, the role of the estate tax in the Federal tax system could be substantially increased.

While the national government has been obliged to strengthen its revenue system, the states have been faced with a similar problem. They too have experienced drastic declines in revenue and increasing demands for expenditure. To meet their revenue needs, they have reached out for new tax sources. The simultaneous expansion in the revenue system of both the states and the Federal Government has enlarged greatly the conflicts between national and State taxes. The results are increasingly unsatisfactory to everyone. The governments find their revenues adversely affected by competing taxes of other governments. The costs of collecting duplicate taxes have increased. The taxpayer is often subject to several taxes on the same income or the same transaction. He must prepare numerous reports which must be compiled differently to satisfy the many requirements of the different taxing authorities.

Although in a Federal system the tax structure must inevitably be complex, there is every reason to believe that existing confusion and conflict can be diminished. It is high time to consider seriously how the national and State governments can coordinate their taxes in such a manner as to minimize duplications and conflicts, to reduce the taxpayer's cost in complying with the tax laws and to assure adequate revenues to all governments. The existence and seriousness of the problem has been widely recognized and there has been a good deal of talk about it. To date, however, little has been accomplished. A commission, composed of highly qualified representatives of the Federal, State and local units of government, as well as those of the public, holds promise of contributing to a solution. I recommend that Congress provide for a commission with Federal, State and local representation to investigate the problem of conflicting taxation and to make recommendations to the Congress.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 5, 1939

TO Secretary Morgenthau

FROM Mr. White

Subject: Proposal to Tax Idle Deposits

A plan designed to force idle savings and idle funds into active use has been floating around for some time. (A book entitled "When Capital Goes on Strike" advocating the proposal appeared last year). Should business fail to improve the idea may attract popular attention, so you might be interested in the essence of the plan and its merits.

Proposal

1. A monthly tax to be placed on demand deposits (with some exemptions). Time deposits would be handled differently: the tax would be imposed upon the bank in proportion to its uninvested assets (also with some exemption).

2. The tax would be increased or decreased according as the rate of spending and investing was to be speeded up or retarded.

The advantages claimed for the plan are:

1. By forcing large portions of idle funds into investment or expenditure, full business recovery would very soon be attained.

2. The tax would provide an additional source of revenue for the Federal Government, between $1 to $2 billion a year. The tax would be simple to administer and easy to collect.

3. It would permit the Government to borrow at lower interest rates and would even provide a substantial premium on sale of Treasury bills or notes.

4. The tax would greatly reduce the inflow of foreign balances for deposit. It would also probably discourage further foreign investment in the United States since both fixed interest-bearing securities and equities would be for a time at least worth more to the American than to the foreigner.

Secretary Morgenthau - 2

Comment

Reduction of "hoarding" is much to be desired but the difficulties of successful administration of a tax on idle funds are almost insuperable.

1. To avoid the tax people would transfer the deposits they did not need into cash and place the cash in deposit vaults or elsewhere. To stop that channel of evasion would be a most difficult and troublesome task. It would be essential to have a currency which through one way or another would be subject to a reduction of its value every month to an amount almost equivalent to the tax. Currency that automatically is reduced in value each month obviously would be a severe inconvenience. All sorts of troublesome consequences would ensue in day to day business transactions.

2. A tax of 1/2 percent or 1/4 percent a month on deposits would be a sufficient incentive to drive some funds out of the United States; how much would depend, of course, on the height of the tax and the extent of political disturbance abroad. At the moment, the political insecurity abroad and the exchange risk would doubtless deter some funds from leaving the United States, despite a tax of 1/4 to 1/2 percent a month, but whether it would be enough to prevent a substantial exodus (either into foreign currencies, or gold kept abroad) is uncertain. Funds could so easily be sent abroad, (to Canada for example) that it probably would be necessary to adopt exchange controls in order to keep the flight from the dollar within reasonable limits.

3. There would occur a sharp rise in the market value of all securities, but especially for government obligations and high grade bonds. The value of those securities would be subject to wide swings in response to anticipated changes in the penalty tax rate. Sharp fluctuations in business activity might accompany adjustments in the rate of the tax penalty.

4. The plan attacks only one of the numerous maladjustments which contribute to successive depressions. It is not even remotely certain that a high level of recovery could be sustained by use of that tax even were it administratively and politically feasible -- which is very doubtful.

Newton, Iowa
April 5, 1939

FOR THE SECRETARY:

(The Army's drive as reported in the attached clipping from the front page of the Des Moines Tribune is disturbing people. A broadcast similar to the one mentioned in the clipping caused two women in Madison, Wisconsin, to call the local bank and ask if this meant mobilization. The drive suggests to them that we are getting ready for military activity.)

Newton is a small town almost completely owned by the Maytag family. The Maytag washing machine factory, which netted $7,000,000 in 1929 and $2,800,000 in 1937, dominates the town's economic life. The town is just beginning to recover farm retail business diverted by last year's Maytag strike.
In Newton the outlook is just the opposite of that in Woodstock: here the farmers apparently will do well while the local industry has recently suffered a slump in business. However, there is general agreement that the CCC corn loan price was too high and may cause trouble later. One of the local bankers was much incensed over the Treasury offering securities at a premium and said that he had suggested to a Des Moines banker that all Iowa banks sell their Governments as a gest~~er~~ure of protest. The other banker, whose bank is owned by the Maytags, pays almost no attention to Governments and has an extraordinarily large amount of loans outstanding.

There is criticism of "conflicting" Government statements and actions on business appeasement.

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PLEA TO FORMER SOLDIERS

Urged to Join 'Minute Men'

Ask Recruits For Reserve

WASHINGTON, D. C. (AP)—The war department appealed to former soldiers Wednesday to join its new enlisted reserve, a "minute man" force, for quick service in the event of war.

Officials said the army had begun a series of brief radio broadcasts designed to stimulate recruiting in one or two corps areas which had failed to keep up their quotas.

The army set out last year to build up a force of 75,000 to be recruited in four years from former soldiers under 36 years of age. They are paid $24 a year, but do not drill.

Gen. Malin Craig, chief of staff, reported to congress that enlistments were slow at first but were increasing by "leaps and bounds." In January, 5,100 had been enrolled and General Craig said a total of almost 11,000 recruits was expected by July 1.

Maytag Company -- This company's business has recently dried up after running well ahead of last year throughout the first quarter. Fred L. Maytag II, who is the rising young man in this family company, explains that, having cut prices early in 1938, the company in December announced a partial restoration of the higher prices effective January 15. The result was a large amount of what he called "more or less speculative buying" by dealers in advance of the price increase, and the factory has just finished filling these orders. Now the wholesalers are well stocked up, and retail sales show no evidence of absorbing these stocks rapidly. Consequently new factory orders are small. This is the only heavy inventory situation I have found thus far. Mr. Humbreit, the treasurer and general manager, is inclined to blame the slow retail sales on uncertainty arising out of the European situation. Government spending never has helped his company's sales as far as he can tell, he says.

Mr. Humbreit had several suggestions for tax law changes. He very much favors a loss carry-over provision saying it would help the company's dealers who are not well financed, through lean years like 1938, when "they fell flat on their faces" after two years of profits. He believes companies should be allowed to deduct losses sustained when they junk absolescent machinery and buy new equipment. Inability to do so causes companies to retain outmoded equipment until they can gradually deduct its costs through depreciation allowances. Mr. Higden, the company auditor, says the company has some useless machinery sitting in a shed just so they can continue their depreciation deductions whereas they would have liked to charge off the loss on the machinery in the year they replaced it; the continuing depreciation charge falsifies their profit and loss statement, he says.

Mr. Humbreit also criticized the undistributed profits tax for its effect on machinery purchases, saying that they always figured the tax as an added cost to plant improvement. He favors combining the capital stock, excess profits and corporate income taxes. The company's total taxes last year were 23 cents per man hour.

Although he favors old age benefits, Mr. Humbreit believes they should start now at the maximum amount. His company, he says, is carrying old employees who are keeping young people out of jobs. The company would retire the older workers if they had an adequate pension, and the company would be willing to pay taxes sufficient to finance such a program, he says.

Both Mr. Higden and Mr. Humbreit were disgusted at the way the unemployment benefit payments are working out. Some of the examples they cited were: a girl quits to get married and draws 15 weeks unemployment benefits, the local country club golf professional and his wife are employed only during the summer and live all winter on unemployment benefits, a man who was fired for cause was drawing unemployment benefits and running a filling station at the same time. On the other hand, a worker has to quit because of tuberculosis and gets no unemployment benefits because he can not register for re-employment. Both men thought the unemployment system should be rechecked, and Mr. Higden suggested greater Federal supervision in the interest of uniformity, saying that his company has to fill out 32 unemployments returns for various states and they are all different.

Their relationship with Federal internal revenue men since 1936 have been very good, and the agents are "a high type of man," they say.

Mr. Maytag was very measured but very thorough in his criticism of the Labor Board as a biased group. The Board's employees, he believes, regard themselves as designated to further the cause of unionism and do not give the employers an honestly even break. He was particularly critical of the Board using the large high school assembly hall for its hearing during the height of last year's strike tension and for allowing the audience of 1,100 to boo the company's counsel and cheer the NLRB counsel.

Newton National Bank -- Mr. Karstens, the vice president who runs the bank, was the most outspoken critic of the Treasury March offering that I have met. He referred to the offering at a premium as "a racket" and says the country banks would all be helped if it were stopped. He said that he had suggested to a Des Moines bank that the Iowa banks sell their Government securities as a protest against the premium offering. The Des Moines bank objected to the premium also, Mr. Karstens said.

Mr. Karstens said that he tried to keep to short maturities, preferrably those before 1940 because he did not like to carry Governments over an election year. He has bought the 1947 bonds, however. Banks like his can not keep well enough informed to trade successfully in the Government bond market and should not do so although a big bank like Continental Illinois in Chicago "with Mr. Cummings, a government man, at the head of it" can make a lot of money trading in Governments. Nevertheless, Mr. Karstens is of the opinion that all banks will try to sell out their bonds at once if the prices appear to weaken.

Mr. Karstens is opposed to the Government spending program. He believes farmers in this region are worried about the long-term outcome of the spending although, naturally, they are willing to accept Government money as long as it is being handed out. For instance, E. H. Maytag, a wealthy member of the washing machine family, is joining the soil conservation program this year for the first time although he does not really need the money. Mr. Maytag figures that joining will net him $4,000 annually on his farm, according to Mr. Karstens.

The CCC corn loans are heartily approved by Mr. Karstens who believes that "they help purchasing power and that is what the community needs." The loaning rate was too high this year, however, and has backed up a lot of corn which would otherwise have been used, he said. His bank has made a good many corn loans.

Production credit associations worry Mr. Karstens. A customer of the bank to whom the bank had made a mortgage loan at 4½% and an additional $500 unsecured loan at 6% had recently gone to the PCA to borrow $1,100 on some cattle. Such competition where the local bank is taking care of the credit needs of an old customer should not be allowed in Mr. Karstens' opinion.

Farmers in this area, unlike those in the Northwest dairy belt, are pretty well satisfied, and local retail trade is about up to last year, according to Mr. Karstens. Business, however, is upset, he feels, by contradictory statements and actions from Washington. The local community was much interested in Secretary Hopkins' Des Moines speech, but, according to Mr. Karstens, waited in vain for any concrete demonstration of "appeasement" and then was shocked by the President's statement that more taxes would be needed. (I think Mr. Karstens misunderstood the President's "no taxes" statement.)

Mr. Karstens, like most people, was very emphatic in saying that the United States should stay out of any war in Europe, but he seemed to feel that the President probably had pledged this country's aid to Britain and France; he asked me if the President had not already committed the country. However, Mr. Karstens also thought that we should sell to belligerents at their own risk. He was the only person I met who favored barter trading by the United States, saying that it should be used to hold our world markets against what he appeared to believe was an overwhelming attack by Germany. Spread of the barter system will make our gold useless, he thinks.

Jasper County State Bank -- Mr. Bailey runs the bank for the Maytag family. It ~~has~~ furnished a good example, as did the bank in Woodstock, of how a local banker can serve his community in spite of all the talk about banks refusing to make loans. The bank has total loans and discounts of more than $2,400,000 out of total deposits amounting to slightly less than $4,000,000. These loans include CCC corn loans, real estate mortgage loans, chattel mortgage loans, loans to local merchants, and automobile financing loans. Mr. Bailey is particularly interested in automobile loans of which he has $200,000 because they are good earners with little loss and in corn loans. He is not much interested in Government bonds, saying that he would rather have a five year mortgage than a Government bond, but he has gradually increased the proportion of Governments in the rather small bond portfolio of $500,000, and is gradually working off a $300,000 bond loss which was in the bank when he took over.

Mr. Bailey is not actively critical of the production credit associations, but related the following incident which he thought might be symptomatic of forthcoming trouble between his bank and the local PCA. The bank has loaned $31,000 at 6% to a local cattle feeder who now is angling for another loan. The feeder reported that he could get the loan for 5% and the bank agreed to this interest rate. A few days later the feeder came in to remark that interest rates were still going down and that he could get the loan for 4½%. Mr. Bailey suspects that the PCA is underbidding the bank deliberately and thinks such a practice might lead to trouble. Generally speaking, however, he thinks most of the blame is on the bankers and not on the PCA because the bankers are not trying to make loans.

Incidentally, Mr. Bailey feels that farm interest rates are really not very flexible and can actually only be changed downward, therefore, he questions the outcome when banks in hard times try to raise the rates which they are charging farmers.

CCC corn loans are being made at too high a price, according to Mr. Bailey. Farmers are sealing corn which they normally would feed and are buying corn from their non-complying neighbors who can not get a CCC loan. The result is that a great deal of corn is being backed up on the farms and "When it starts to move, watch out," according to Mr. Bailey.

Local farmers are doing pretty well and their loan repayments to his bank are good, Mr. Bailey says. He anticipates good farm machinery sales in this territory this year if cattle and hog prices stay at their present satisfactory levels. Local retail merchants, however, are just beginning to recover farm business which they lost last year when the farmers went elsewhere to trade during the Maytag Company's strike.

Mr. Bailey, like Mr. Karstens, questioned the wisdom of Government spending, said that he believes benefit payments are higher than they need to be to assure compliance and expressed the opinion that farmers feel that some day in some way they will have to repay the money they are getting now. He himself is going into the soil conservation program with his 240 acre farm because compliance will mean an additional $1,000 annually for him.

Des Moines banks and some country banks are actively trading in the Government bond market, "sitting at the end of the wire all day," and will all try to jump if the market softens, according to Mr. Bailey.

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What this market needs is more speeches. Every time one of the big four - Chamberlain, Daladier, Mussolini and Hitler - start pitching, Governments move upwards anywhere from 3/8 to 1 point, depending on how much they don't say - viz: Hitler's harangue around the end of January put a point on the market, and his latest effort behind rumored shatter-proof glass added another 3/8's. Previous to both his orations the market underwent a bad case of the shakes and didn't act as if it could hold anything.

The past two weeks has seen the four spokesmen for their respective nations toe the rubber, and thanks to them they pretty well managed to hold prices to a 1/2-point range. So Let's hope the boys keep talking - no matter how dull their speeches, because as long as they take the trouble to answer one another there won't be war. We don't want to be around when Hitler refuses to rise to Chamberlain's admonitions.

With all the nervous markets we still don't see any move to shortening maturity. The trend from notes to bonds, while it slowed up perceptibly, still shows for member banks: Notes down $2,000,000 and bonds up $8,000,000. While the current market, especially on the down side, prohibits any wholesale liquidation, the larger institutions - although they may be sitting on a hot seat, and they know it, are kept from selling because (1) they need the income, and (2) they would knock the bottom out of the market if they let go their bonds on weakness.

Cash in June

Rumor has it that because the rise in the Social Security tax from 1% to 1-1/2% will be thrown out by Congress this session, the Treasury will be forced to enter the market sooner than September. It's quite far away to be worrying about that now, what with Europe acting as it is. Tie up Hitler and then let's worry about cash in June. Better yet, let Mr. Morgenthau worry about it for you. He's much more on the spot than you are. All you have to do is to buy the new bonds if you want to. Remember, Mr. Morgenthau has got to sell 'em. He'll dress 'em up plenty if necessary. Which reminds us - why not let Mr. Morgenthau handle our cotton situation? He can't do any worse than the rest who have tried to handle it, and to start with, he's an affluent farmer himself. Mr. Morgenthau has done a first-rate job with the Government market. He's schooled it to a snaffle, whereas before he took the reins it needed a curb and bar bit, and even then he was tossed around. He made institutions bond hungry and has created a demand which seems insatiable. Maybe he can do the same for cotton?

The Quarterly Bank Statements

Always of interest are the institutional quarterly statements. But this time we had more than a good idea what they would show. From the weekly statements of the reporting banks it was well known that the larger banks had been adding heavily to their Governments. Two local institutions show over a $100,000,000 increase in their bond accounts, one of which had been very backward about adding Governments to its portfolio; in fact, this institution had sold on balance during 1938. Most of the banks show an increase in cash and deposits. Whether they care for this situation or not, it has been with them now for the past few years with increasing embarrassment. This quarter, however, the local banks took determined steps to do something about it. If gold hadn't been coming into the banks faster than they could buy Governments, they would have shown a much greater proportional increase in Treasury issues than they now do in relation to their present position.

Home 2-1/4's, 1944/42

Try as the Home 2-1/4's do, they don't seem able to break through 105. There must be plenty for sale at a price just below the even dollar price. Sluggish acting at times, because of the conversion of the Home 3's and Home 2-3/4's into the Home 2-1/4's, they pull themselves together now and then, and work slowly upwards, only to bump their heads against the 105 ceiling, whence they drop down to repeat the performance. They are currently selling around 104-28/32nds.

When the Home 2-3/4's are refunded, as is rumored, it will stop more conversions to the Home 2-1/4's from that source. The market action on these bonds should be relatively strengthened. The Corporation can still, of course, convert the 3's, but these bonds are harder to pry loose from their holders. Since last October 1st only $26,000,000 Home 3's have been converted against approximately $75,000,000 Home 2-3/4's.

What to Buy

Any of the last bonds if the market will move down to a point where you are willing to take a chance on Europe. They will naturally show the greatest improvement of any on the list. But added to that haphazard buying, here's a further idea: Pick a high coupon bond. They will go up as fast as any, depending on the length of maturity chosen, and if by some odd chance the market turns downward, you will be sitting with a high current return. For example, 3's, 1955/51 and 2-7/8's, 1960/55. If you prefer a shorter maturity - 3-1/8's, 1952/49.

If you want to take a few profits in the long bonds but still keep in the market, the shortest bonds, namely, 3-3/8's, 1943/40, 3-3/8's, 1943/41, and 3-1/4's, 1941, present an opportunity for a temporary hedge. During the recent market decline of two weeks ago, the 3-3/8's, 1943/40, lost only a 1/4 of a point to over 3/4's of a point on the longest maturities. The next time the long bonds make new highs don't overlook the possibility of this move.

Telephone or write us. Investigate our reputations and service, if you will. And next time you visit Wall Street, visit our office. Let's talk about this market and your investment problems.

H. D. Swihart & Co.

April 6, 1939.

PARAPHRASE OF TELEGRAM SENT

TO: American Embassy, Berlin, Germany

DATE: April 5, 1939, noon

NO.: 79

FROM THE SECRETARY OF THE TREASURY.

FOR HEATH.

Reference is made to telegram No. 229 of April 3 from the Embassy.

In view of the present circumstances it is believed advisable that you postpone the proposed trip and remain in Berlin for the time being.

HULL.

EA:LWW

April 5, 1939

Over the phone today from Sea Island, HM,Jr told McReynolds that last Friday he sent to the President the draft of a letter that he suggested the President write to Pat Harrison, and that the President signed it and sent it to Pat on Tuesday.

April 4?

Dear Pat:

I appreciate the cordial tone of your letter of March 25th.

I have no desire to confuse the record on the matter of proposals for amendment of the corporate tax structure, which appear to have come from a variety of sources. Of course, I accept wholly your statement that the suggestion for a single corporate tax to replace various existing taxes did not originate with you.

What I did wish to make plain in sending you the Treasury's estimates of the effect of one way of working out this suggestion was that they were merely intended as a basis for study and did not in any sense constitute recommendations.

I still have reservations both as to the practical effect and as to the equity of changes in the corporate tax structure along these lines, but I agree that the whole subject is worth our careful study.

I hope to have the opportunity to discuss the matter further with you.

Sincerely,

The Honorable Pat Harrison,
Chairman,
Senate Finance Committee,
Washington, D. C.

original sent to Secretary as a proposed letter to Harrison from the President - see letter of 3/29/39 to the Secretary from the Under Secretary, which is self-explanatory

My dear Mr. President:

I have received your memorandum of March 25th, accompanying a letter to you from Senator Pat Harrison, dated the 24th.

I am also in doubt as to how you should answer Senator Harrison's letter. It may be helpful to you in preparing a reply if I review the facts as I know them. On February 17th, while you were aboard the special train at Key West, you told the Press in substance that business and industry need not fear any new taxes at this time. At my Press conference on February 23d, the first conference I held after your tax statement was made public, I told the Press that I was pleased by your statement and that for my part I should like to see the committees of Congress look into the tax law for the purpose of discovering whether there were any deterrents to business which could be removed. The following day at Des Moines, Harry Hopkins advocated also the removal of tax deterrents to business. On the same day, the 24th, Bob Doughton issued a statement approving what I had said and offering to cooperate.

I had not discussed the matter with Harrison up to that point, but I had sent him a summary of what I said at the Press conference. He came to see me the following week and he and Doughton on March 3d sent me a joint letter expressing approval of your tax statement, my statement, and that of Hopkins and offering cooperation.

John Hanes and I saw you on March 8th and presented our tax ideas and you arranged for a conference with Harrison and Jere Cooper (Doughton being away) the following day. Our recommendations to you included the substance of the material later furnished to Harrison.

At the conference on March 9th, Harrison referred to a proposal to repeal the excess profits, capital stock, and undistributed profits taxes and to substitute a revised corporate tax schedule, not as his suggestion but as one that he had heard. To your question whether the present revenue could be preserved under such a revision, he said that he thought it could be.

I had been careful not to give out to the newspapers any details whatever as to what I regarded as tax "deterrents." Nevertheless, it was widely known that various business organizations had suggested changes of this character and speculation in the Press after my Press conference of February 23d and Harry Hopkins' speech centered around these particular suggestions. This would certainly offer adequate ground for Harrison's statement that he had heard these things suggested.

In view of this background, I do not think that we can successfully maintain the proposition that these ideas originated with Senator Harrison. I should not myself want to avoid responsibility for initiating the suggestion that the corporate tax structure be revised. It was not done at Pat Harrison's suggestion. It was my own idea.

I am enclosing herewith my idea of a letter in answer to Senator Harrison's letter of March 24th.

Faithfully yours,

The President,

The White House.

JWH:ce-
3-29-39 letter recopied after JWH talked with Sec'y on 3-30-39- Sec'y asked that paragraph 8 of 29th letter be taken out recopied 3-30-39

original given to Dietrich - 1:10 3-30-39 in brown sealed envelope - to be sent in pouch to Secretary -

Returned

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My dear Mr. President:

I have received your memorandum of March 25th, accompanying a letter to you from Senator Pat Harrison, dated the 24th.

I am also in doubt as to how you should answer Senator Harrison's letter. It may be helpful to you in preparing a reply if I review the facts as I know them. On February 17th, while you were aboard the special train at Key West, you told the Press in substance that business and industry need not fear any new taxes at this time. At my Press conference on February 23d, the first conference I held after your tax statement was made public, I told the Press that I was pleased by your statement and that for my part I should like to see the committees of Congress look into the tax law for the purpose of discovering whether there were any deterrents to business which could be removed. The following day at Des Moines, Harry Hopkins advocated also the removal of tax deterrents to business. On the same day, the 24th, Bob Doughton issued a statement approving what I had said and offering to cooperate.

I had not discussed the matter with Harrison up to that point, but I had sent him a summary of what I said at the Press conference. He came to see me the following week and he and Doughton on March 3d sent me a joint letter expressing approval of your tax statement, my statement, and that of Hopkins and offering cooperation.

John Hanes and I saw you on March 8th and presented our tax ideas and you arranged for a conference with Harrison and Jere Cooper (Doughton being away) the following day. Our recommendations to you included the substance of the material later furnished to Harrison.

At the conference on March 9th, Harrison referred to a proposal to repeal the excess profits, capital stock, and undistributed profits taxes and to substitute a revised corporate tax schedule, not as his suggestion but as one that he had heard. To your question whether the present revenue could be preserved under such a revision, he said that he thought it could be.

I had been careful not to give out to the newspapers any details whatever as to what I regarded as tax "deterrents." Nevertheless, it was widely known that various business organizations had suggested changes of this character and speculation in the Press after my Press conference of February 23d and Harry Hopkins' speech centered around these particular suggestions. This would certainly offer adequate ground for Harrison's statement that he had heard these things suggested.

In view of this background, I do not think that we can successfully maintain the proposition that these ideas originated with Senator Harrison. I should not myself want to avoid responsibility for initiating the suggestion that the corporate tax structure be revised. It was not done at Pat Harrison's suggestion. It was my own idea.

As to continuation of the remnant of the undistributed profits tax, I must say frankly that I believe the Senate Finance Committee would be almost, if not quite unanimously, against it. It is argued that the present spread is so small that the tax has lost any value that it may have had as a compensating tax for dividends withheld and that it has little if any value in stimulating dividend distributions. On the other hand, we have a great volume of testimony that its chief importance is that of an irritant. It seems to me that its abandonment would be a gesture that would be genuinely beneficial.

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Faithfully yours,

The President,

The White House.

original sent to Secretary as a proposed reply to the President - see letter Under Secretary sent to Secretary on 3/29/39, which is self-explanatory

Secretary called JWH 3/30/39 A.M. and asked that 8th paragraph of this letter be deleted

JWH:ce
3-29-39

THE UNDER SECRETARY OF THE TREASURY

WASHINGTON

March 29, 1939

Dear Henry:

I have studied the President's letter to Pat Harrison of March 21st, Pat Harrison's letter to the President of the 24th, and the President's memorandum to you dated March 25th, with great care.

The fundamental weakness in the President's position with Senator Harrison is that none of the facts will bear out his contention that this program originated with Senator Harrison. You and I know full well that neither of us ever discussed the tax program with Pat Harrision prior to our meeting at the White House on March 9th. This fact Pat stated emphatically several times to the President, but apparently the President has fixed in his mind the thought that Senator Harrison has set a trap and that these suggestions are his instead of ours. In the first place, there is nothing unusual about the suggestions of repeal of the corporate taxes and the substitution therefor of a flat corporation tax. This recommendation has been unanimously made by every business organization calling on the Treasury during the past eight months. To mention only a few, we have written recommendations from the National Chamber of Commerce, the National Association of Manufacturers, and Harry Hopkins' advisory council, plus any number of individual tax experts, such as former Under Secretary Magill and the unanimous opinion of the Treasury staff. Further, all of these suggestions had been widely discussed in the Press prior to the time of our meeting with the President. So there is nothing unusual in the fact that Pat would have heard of these recommendations.

I quote to you the following from the first paragraph of the President's memorandum to you: "The point of the whole thing is that suggestions for the repeal of 'deterrent taxes' were made by Senator Harrison. These, as I remember, antedated any statement by you that the subject was being studied." So far as I know the facts, this statement is absolutely incorrect. Senator Harrison made no statement about deterrent taxes either publicly, or so far as I know, privately. The sequence of events was as follows: (1) the President's statement to the Press on February 17th at Key West; (2) your statement at your Press conference on February 23d about encouraging business by removing deterrents from the tax structure; followed by (3) Harry Hopkins' statement on February 24th calling for a removal of deterrent taxes; and (4) Bob Doughton's statement on the same day promising cooperation on behalf of the Ways and Means Committee with the Secretary of the Treasury in his objective of removing taxes which were deterrents to business recovery.

You will remember that about this time I came back from the Hill one afternoon and told you that Senator Harrison was upset about the proposal to raise the Government debt limit from 45 to 50 billion dollars. I told you further that Senator Harrison had planned to make a public statement which seemed to me would not do the Administration any good. I told you that I had pleaded with Senator Harrison not to do anything hastily but to discuss the matter with you before going ahead. This Senator Harrison agreed to do and you invited him to luncheon the next day. He first accepted but then said he would be unable to come to luncheon but would like to come to discuss the matter with you at four o'clock in the afternoon. He came and you persuaded him to approach the matter cautiously. He did not say what he was going to do but I certainly got the impression that you had succeeded in getting him to temper the statement he had in mind making. Finally, he did make a statement which I think appeared in the Press on Thursday, February 23d. That was his so-called economy blast, and it is possible that the President may be confusing that statement with the tax matter.

The first word from Senator Harrison on taxes, so far as I know, was made public on March 3d and that was a splendid statement made jointly with Congressman Doughton, in which he offered every cooperation to the Administration in its objective of "raising additional revenues by removing deterrents and encouraging business enterprise."

Right here, at this time, Hell seemed to break loose in the Administration circles, and we found the tax program upon which we had been working conscientiously for more than eight months right in the center of this thing called "appeasement." You and I know that we have been motivated by one purpose, and that has been economic recovery for our country and that we have wanted to do everything possible to help the Administration by advancing recovery. Doubtless the President was told that we were a part of the economy bloc in Congress, and also a party to Harry Hopkins' movement toward business appeasement. Whether we were sympathetic to these movements or not is beside the point, the fact remains that we have consistently maintained our policy of minding our own business and not going outside the Treasury butting into the business of others.

It is, therefore, very clear to me that in all fairness to Senator Harrison and to the facts, you and I should be willing to assume whatever responsibility rests upon us.

I am enclosing herewith a proposed letter drafted by Herbert Gaston and me for you to send to the President. I also enclose Herbert's idea of a possible draft of letter from the President to Senator Harrison.

After you have read these, I will talk to you on the telephone if you wish.

My love to you and Elinor.

Affectionately,

Johnnie -

The Honorable

The Secretary of the Treasury.

March 29, 1939

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After you have read these, I will talk to you on the telephone if you wish.

My love to you and Elinor.

Affectionately,

/s/ Johnnie

The Honorable
The Secretary of the Treasury.

original sent to Sec'y at
Cloister Hotel, Sea Island Beach, Ga.
CE gave to McHugh 3:25 P.M.-3/29/39-
Sec'y's maid was to carry this
material to the Secretary -

Attachments: proposed letter to
Pat Harrison to be
signed by President
proposed letter to
President to be signed
by the Secretary

Secretary called JWH 3/30/39 A.M. and
asked that 8th paragraph of proposed
letter to the President (to be signed
by him) be deleted.

JWH:ee

Carbon copy to Hanes March 27, 1939.

March 27, 1939.
10:20 a.m.

HMJr: This is -- I mean what I'm going to say to you now isn't why I'm calling. I got a terrifically important letter from the President I want to read you.

John Hanes: Right.

HMJr: But before that I just wanted to say that I did talk to Preston Delano just to give him a little pat on the back, you know.

H: Yes.

HMJr: Now, here's a letter from Pat Harrison to the President, and a long memorandum from the President, see?

H: Yes.

HMJr: And I'll read this to you -- this is the quickest way I could get it to you, see?

H: Yes.

HMJr: This is dated the twenty-fourth, received at the White House the twenty-fifth. It is from Pat Harrison:

"My dear Mr. President:

"I am in receipt of your letter of March 21st and the enclosed data prepared by the Treasury Department. Only because inferences might be drawn in certain parts of your letter that the enclosed data prepared by the Treasury Department was based on my suggestion and my reiterating what I told you at our last conference; namely, that I had not seen and had no definite knowledge until our conference of the suggestion and revenue estimates based thereon, both of which were prepared by the Treasury Department for the purpose of discussion and study. I did not know until I received a photostatic copy of the proposals and estimates that the suggestion, 'a ceiling with two thousand dollar limitations on the deduction of net losses for other income' and 'allowing the three-year carry over of net losses' had been made or were under consideration.

"I had read in several of the newspapers rumors that the Treasury Department intended to suggest that the repeal of the capital stock tax, excess-profits tax and the undistributed profits tax, and the substitution therefore of a flat corporate tax. I did not know definitely -- definitely that these suggested changes were Treasury proposals until our conference on March 9th when we exchanged views, at which time we were all agreed that regardless of what might be finally evolved and recommended the smaller corporations would continue to receive the same fair and beneficial treatment that they have received in prior tax laws, and that the total of taxes paid by corporations to the Treasury should be not lowered by any change in the laws.

"At our conference I asked the Treasury's proposals and the revenue estimates based thereon because of my desire to know exactly what they were and in order that I might study the suggestions with a view to cooperating in the formulation for any fair program of tax legislation that might be suggested by the Treasury Department.

"I appreciate your sending me this data and I show you my sincere desire to cooperate wholeheartedly in effectuating the purposes announced by the Secretary of the Treasury to aid business with the modification or elimination of any provisions of our tax laws which act as deterrents to business.

Sincerely yours,

Pat Harrison."

Hello?

[illegible]: Yeah.

[illegible]: Now comes the President's.

[illegible]: Yeah.

[illegible]: It's a memorandum -- it's dated March 25th. Memorandum to the Secretary of the Treasury:

"I don't quite know how this letter from Pat Harrison should be answered.

"The point of the whole thing is that suggestions for the repeal of 'deterrent taxes' were made by Senator Harrison. These, as I remember, antedated any statement by you that the subject was being studied. Thinking back I know you will remember that the repeal of excess-profits and capital stock tax was seriously considered both a year ago and two years ago without any particular objection on the part of either yourself or myself. This was based, of course, on some assurance that the amount of their yield be made up to the Treasury in some other way. Therefore, there can be no serious objection to the statement on your part to the above effect, but I hesitate to have you or Hanes propose a substitute tax for these two because of the difficulty of getting a fair substitute tax without revamping the whole tax structure.

"When we come to the change in the 'spread the tax, I am not ready to take the position because I have no information as to which corporation would be helped or hurt by it, and we must be very certain that any action on this would not merely to the benefit of the very large corporations.

"In regard to the four proposed changes, however, the elimination of what is left of the undistributed earnings tax, I do not see how you and I could forget or bury the fact that two years ago one of the principle reasons for advocating the undistributed profits tax was to prevent very rich people from leaving their earned income in corporations contolled by them, the effect of avoiding both personal and income tax payments.

"This is a matter of fundamental principle.

"For this reason I hate to see you put in the hole of proposing these changes. It seems to me perfectly clear that the origin of the proposed changes was Senator Harrison himself. Frankly, the political mistake made while I was with the fleet was falling into Senator Harrison's trap. Obviously he tried, and tried with some success, to make it appear that the Treasury was listing taxes which he believed to be deterrent or recommending their repeal or recommending a substitute or substitutes for them.

"In regard to these substitutes, it is all very well to say, 'add the necessary amount to the state percentage corporation taxes.' But if you do this you and I know that you will either step on the toes of the hundred and fifty-three thousand small corporations or you will step on the toes of the one thousand very big corporations. Why put your head into that noose?

He doesn't complete that quote. I don't know where he gets that quote from. That quote is left open.

"The mistake made was that in the first instance we did not pin this thing on Senator Harrison. Offer every kind of assistance and in good faith give him our opinion on what would be the result of any change which he had asked us to study.

"The last analysis, the amount involved and the proposed changes is negligible. We are all agreed that the corporations as a whole continue to pay the same amount of money to the Treasury. We cannot allow the Administration to get behind any change which will withdraw old abuses.

(Signed) F.D.R."

Well, now, the first thing is - there she is, and I don't want to do anything for twenty-four hours.

H: No.

HMJr: Hello?

H: Yes.

HMJr: You can get it typed and look at it.

H: Yes.

HMJr: And I'd be terribly careful to show it to a very limited number of people in the Treasury only.

H: Well, I don't we'll show it to anybody for twenty-four hours. I think I'll talk to you again after

I've seen it stretched out.

HMJr: I've got a perfectly good reason I'm down here and -- I -- as I say, I can't remember who said what first. See?

B: Well, Henry, I think -- I honestly think the President is -- is misinformed or is hot -- he is not in possession of all the facts.....

HMJr: Yeah.

B: As I -- as I hear it. I can't see it at the moment, and.....

HMJr: No, you've got to see it and then you can -- when I talk to you tomorrow refresh your memory, and I can't -- my memory is -- I'm just tired out.

B: Yeah. Well......

HMJr: And.....

B: He's -- he's wrong as to the happenings as they came about and -- and, in my opinion, I -- I don't believe Pat Harrison ever made any statement about taxes prior to the time that Harry Hopkins made his speech. I don't think that -- I don't think Harrison made any statement about taxes. You remember he sounded off when he came down here to talk to us about the forty-five billion dollar debt limit.

HMJr: Yeah.

B: He sounded off on economy.

HMJr: Yeah.

B: And that had nothing to do with taxes whatsoever.

HMJr: Yeah.

B: And he didn't say anything about taxes until both the -- both you -- both the President and you and Harry Hopkins had all made statements, and you remember Doughton made his statement and Pat told us the morning he came down here to talk about the forty-five billion dollar debt thing, that he had made no statement, I rather upbraided him for the fact that he hadn't come in line and offered to cooperate with us; so I think the President has got his -- I think he's got his facts a little bit twisted there.

HMJr: Well, I think the thing to do -- for you to do is -- is to sort of jot down, and use your own confidential secretary.....

[illegible]: Yeah.

HMJr: ....and make out a kind of a timetable what did happen.

[illegible]: Well, I've got that, Henry. I've kept it day by day.

HMJr: Well, I.....

[illegible]: And I -- I've got.....

HMJr: I'm glad you have it.

[illegible]: Yeah. Well, I've got that and I can give you -- in chronological order on the dates and the time of day.

HMJr: Well, why don't you put that in the air mail tonight. Find out at what time the air mail leaves for here.

[illegible]: I will.

HMJr: And put it -- I have not got it -- I mean, things are happening so fast that I only dictated once when we came back, you remember.

[illegible]: Yeah.

HMJr: And I have not kept it in chronological order.

[illegible]: Well, I've got it.

HMJr: But, after all, when you get all washed up leaving out the difference between the President and Pat, which I can't remember, the interesting thing is he says here -- he's all right on the -- he doesn't object to the repeal.

[illegible]: He's all right on everything except the undistributed profits tax.

HMJr: That's -- that's what it amounts to.

H: Yeah.

HMJr: See?

H: Yeah. Well.....

HMJr: And.....

H: Henry, we're -- we're awfully fortunate in one thing, and that is that what Pat says about not knowing anything about the program is absolutely true.

HMJr: Yeah.

H: And as I told you....

HMJr: Yeah.

H: ..... I had never discussed with Pat any of the details nor any of the things that we were studying here at all.

HMJr: Yeah.

H: And so Pat is absolutely telling the truth when he says that he knew nothing until he came to the White House conference.

HMJr: Of course, I can't agree with the President that Pat is as deep-dyed villain as he tries to paint him.

H: No. (Laughter) No, I can't myself, because I think, unless Pat is deceiving you, which I don't believe he would do....

HMJr: Yeah.

H: He has been as fair and as open about the thing as anybody could possibly be.

HMJr: Because if he was such a deep-dyed villain, he could have jumped on the President with both feet the other day.

H: Yes. Yes, and he could have made this letter that he has written the President public too....

HMJr: Yeah. Which he hasn't done.

H: Which he's not going to do, I am sure. Pat wouldn't do that because he -- he wouldn't be keeping faith with us if he did.

HMJr: Now, you see, where the President, I think, left himself unnecessarily open was he never gave us a chance to go over the letter he wrote to Pat in advance.

H: No.

HMJr: So we had nothing to do with it.

H: That's right.

HMJr: And now he's got an answer from Pat and he wants me to help him answer it.

H: Well, I don't see -- at the moment -- well, I'll wait until I see the letter and then -- then I'll get up for you tonight -- in the mail tonight I'll send you the -- the order of events as -- as they are jotted down in my calendar.

HMJr: And send it air mail.

H: I will.

HMJr: Or, I tell you what we'd better do -- just -- I think, we have a way of sending it down by special pouch. Tell McReynolds to send it down by pouch by Seaboard, see?

H: Yes.

HMJr: And to telegraph my customs men here at Brunswick, see? Mac knows how to do it. Just tell him that you want a special pouch to come down on that six-twenty train.

H: Yeah.

HMJr: Oke.

H: Yeah.

HMJr: And that -- because sometimes the airplane doesn't come through....

H: Yeah.

HMJr: And that Mac should telephone my two customs men down there. I have two men standing by -- that they should pick up that pouch in the morning, see?

M: Yeah, right.

HMJr: Because I've had the air mail go through and sometimes not get it. This is important. They had better send it special pouch down on the train.

M: Right.

HMJr: Let -- let McReynolds arrange the details.

M: Right.

HMJr: And I'll get it in the morning then, you see?

M: Right. I'll get it all in the mail to you this afternoon.

HMJr: What's that?

M: I say, I'll get it all in the mail to you this afternoon.

HMJr: You might tell Miss Chauncey a pouch is coming so if she has anything for Mrs. Morgenthau or me, that it could come down. You see?

M: All right.

HMJr: Well, I'm -- I'm going to put this in the drawer. After all, the President took ten days to answer his, I'd be entitled to five days on that basis.

M: I would think so.

HMJr: It doesn't bother me, Johnny.

M: No, I think -- Henry, I think our -- I think our nose is clean. I don't see as anybody can -- anybody can criticize any step we've made. We've been doing our work and doing it honestly and, I think, intelligently, so I'm not going to worry about it, and don't you.

HMJr: I'm not going to worry about it, and I think you were smart this morning when you said you weren't going to have any press conferences and lay low.

H: Yes.

HMJr: This is a dual between the President and Pat Harrison, and I'm not going to get caught in the cross-fire.

H: Right.

HMJr: O. K.

H: Well, thank you, sir. Good bye.

HMJr: Good bye.

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SEA ISLAND
GEORGIA

March 27,
1939

~~May~~
Dear Mr. President:

I received your memorandum of March 25th today with enclosed letter from Senator Harrison.

In order to make any helpful suggestions to you how to answer Senator Harrison I would appreciate your sending me a copy of your letter to him.

I was very sorry not to be ~~able off~~ able to say goodbye to you, I hope by

the time this letter
reaches you, you will
have entirely recovered
from your cold.
Elinor joins me in
sending our best regards
Sincerely yours

THE SECRETARY OF THE TREASURY
WASHINGTON

My dear Mr. President:

I have received your memorandum of March 25th, accompanying a letter to you from Senator Pat Harrison, dated the 24th.

I am also in doubt as to how you should answer Senator Harrison's letter. It may be helpful to you in preparing a reply if I review the facts as I know them. On February 17th, while you were aboard the special train at Key West, you told the Press in substance that business and industry need not fear any new taxes at this time. At my Press conference on February 23d, the first conference I held after your tax statement was made public, I told the Press that I was pleased by your statement and that for my part I should like to see the committees of Congress look into the tax law for the purpose of discovering whether there were any deterrents to business which could be removed. The following day at Des Moines, Harry Hopkins advocated also the removal of tax deterrents to business. On the same day, the 24th, Bob Doughton issued a statement approving what I had said and offering to cooperate.

I had not discussed the matter with Harrison up to that point, but I had sent him a summary of what I said at the Press conference. He came to see me the following week and he and Doughton on March 3d sent me a joint letter expressing approval of your tax statement, my statement, and that of Hopkins and offering cooperation.

John Hanes and I saw you on March 8th and presented our tax ideas and you arranged for a conference with Harrison and Jere Cooper (Doughton being away) the following day. Our recommendations to you included the substance of the material later furnished to Harrison.

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In view of this background, I do not think that we can successfully maintain the proposition that these ideas originated with Senator Harrison. I should not myself want to avoid responsibility for initiating the suggestion that the corporate tax structure be revised. It was not done at Pat Harrison's suggestion. It was my own idea.

As to continuation of the remnant of the undistributed profits tax, I must say frankly that I believe the Senate Finance Committee would be almost, if not quite unanimously, against it. It is argued that the present spread is so small that the tax has lost any value that it may have had as a compensating tax for dividends withheld and that it has little if any value in stimulating dividend distributions. On the other hand, we have a great volume of testimony that its chief importance is that of an irritant. It seems to me that its abandonment would be a gesture that would be genuinely beneficial.

I am enclosing herewith my idea of a letter in answer to Senator Harrison's letter of March 24th.

Faithfully yours,

The President,

The White House.

THE WHITE HOUSE
WASHINGTON

March 25, 1939.

MEMORANDUM FOR

THE SECRETARY OF THE TREASURY

I don't quite know how this letter from Pat Harrison should be answered.

The point of the whole thing is that suggestions for the repeal of "deterrent taxes" were made by Senator Harrison. These, as I remember it, anti-dated any statement by you that the subject was being studied.

Thinking back I know you will remember that the repeal of the excess profits and capital stock tax was seriously considered both a year ago and two years ago without any particular objection on the part of either yourself or myself. This was based, of course, on some assurance that the amount of their yield would be made up to the Treasury in some other way. Therefore, there can be no serious objection to a statement on our part to the above effect. But I hesitate to have you or Hanes propose a substitute tax for these two because of the difficulty of getting a fair substitute tax without revamping the whole tax structure.

When we come to the change in the "spread the loss" tax, I am not ready to take a position because I have no information as to which corporations would be helped or hurt by it -- and we must be very certain that any action on this would not enure merely to the benefit of the very large corporations.

In regard to the fourth proposed change, however -- the elimination of what is left of the undistributed earnings tax, I do not see how you and I can forget or bury the fact that two years ago one of the principal reasons for advocating the undistributed profits tax was to prevent very rich people from leaving their earned income in corporations controlled by them, with the effect of avoiding both personal and corporate income tax payments.

That is a matter of fundamental principle.

For this reason I hate to see you put in the hole of proposing these changes. It seems to me perfectly clear that the origin of the proposed changes was Senator Harrison himself. Frankly, the political mistake,made while I was with the Fleet, was in falling into Senator Harrison's trap. Obviously he tried -- and tried with some success — to make it appear that the Treasury was listing taxes which it believed to be deterrent or recommending their repeal, or recommending a substitute or substitutes for them.

In regard to these substitutes, it is all very well to say "add the necessary amount to the straight percentage corporation taxes. But if you do this, you and I know that you will either step on the toes of the 153,000 small corporations or you will step on the toes of the one thousand very big corporations. Why put your head into that noose?

The mistake made was that in the first instance we did not pin this thing on Senator Harrison, offer every kind of assistance and, in good faith, give him our opinion on what would be the result of any change which he had asked us to study.

In the last analysis the amount involved in the proposed changes is negligible. We are all agreed that the corporations as a whole will continue to pay the same amount of money into the Treasury. We cannot allow the Administration to get behind any change which will restore old abuses.

FDR F. D. R.

Honorable Henry Morgenthau, Jr.,

Secretary of the Treasury,

Cloister Hotel,

Sea Island Beach,

Georgia.

THE WHITE HOUSE
WASHINGTON

March 21, 1939. 172

MEMORANDUM FOR H.M. Jr.

Dear Henry:

Here is a copy of my letter to Pat.

F.D.R.

COPY

March 21, 1939.

Dear Pat:

In pursuance of our two recent conversations, I am sending you, as I promised, a copy of the Treasury Department estimates on what would be the results if certain changes were made in the corporation tax laws.

I think it is only fair to both you and me that the situation should be made definitely clear as follows:

(1) That you and I are in definite agreement that the total of taxes paid by corporations to the Treasury should not be lowered by any change in the laws.

(2) That at your suggestion we have had certain studies made of what would happen if the corporation capital stock and excess profits taxes were repealed.

(3) That if the capital stock and excess profits taxes were repealed, how would the amount of taxes thus lost to the Treasury be made up by an increase in the existing corporation income tax rates?

The enclosed photostat copy received from the Treasury shows what would happen under your suggestions, including an estimate of a new schedule of percentage corporation income tax rates.

These estimates also take into account two other repeal items which you spoke of (a) repealing the $2,000 limitation on the deduction of net capital losses from other income and (b) allowing a three year carry over of net losses.

You will see from these figures that they present an additional problem as I stated to you the other day. If you increase the percentage of the income tax rate on small corporations, a very large number of them will have to pay more in taxes than they pay now. Incidentally, there are 153,000 of these very small corporations, earning less than $10,000 a year.

On the other side of the picture, if you do not raise the percentage of income taxes on the small corporations, you will have to impose practically the whole of the burden on the very large corporations -- and it seems to be a fact that most of the demand for revision comes from the same very large corporations. How will they like that?

Always sincerely yours,

Honorable Pat Harrison,
United States Senate,
Washington, D. C.

Enclosure.

74

Estimated Revenue Effects of Proposed Changes in
Corporation Taxes
(Full year based on estimated calendar year 1939 business levels)

SUPPLEMENTARY STATEMENT

...se estimates are preliminary and tentative approximations. The proposed changes ...e:

(1) Repeal the capital stock and excess profits taxes;
(2) Repeal the $2,000 limitation on the deduction of net capital losses from other income;
(3) Allow a 3-year carryover of net losses (including in net losses the net capital losses);
(4) Repeal the remainder of the present corporation income tax (to be replaced by new rate as in (5));
(5) Impose a flat rate of 21 percent (including changes (2) and (3) above).

(Money amounts in millions of dollars)

Net income classes	Estimated tax liabilities of corporations under existing law			Increase (+) or decrease (-) in tax liabilities, full five-point program	
	Total	Income tax	Capital stock and excess profits tax	Amount	Percent
...der $10,000	51.6	36.6	15.0	+ 1.9	+ 3.7
$10,000-25,000	47.2	39.4	7.8	+ 6.9	+ 14.6
$25,000-50,000	60.3	52.8	7.5	- 2.5	- 4.1
$50,000-250,000	196.0	173.4	22.6	- 5.5	- 2.8
$250,000-1,000,000	209.5	187.7	21.8	- 3.8	- 1.8
$1,000,000 and over	567.6	521.4	46.2	+ 51.9	+ 9.1
Total, net income corporations	1,132.2	1,011.3	120.9	+ 48.9	+ 4.3
All other	- 6.9	- 41.8 1/	34.9 2/	- 34.9	—
Total	1,125.3	969.5	155.8	+ 14.0	+ 1.2

Treasury Department, Division of Research and Statistics. March 15, 1939.

1/ Estimated tax credit for income tax paid to foreign countries and U. S. possessions.
2/ Estimated amount paid by net deficit corporations.

C O P Y

THE WHITE HOUSE
Washington

March 21, 1939

MEMORANDUM FOR H.M. JR.

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F.D.R.

original in Diary (copy we)
(made)
cc - McReynolds - Secretary called McReynolds and McHugh 3/31/39 and told them that JWH had promised to send him a copy-has not been received.

COPY

March 21, 1939

176

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Washington

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178

C
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Always sincerely yours,

Hon. Pat Harrison,
United States Senate.

JR

GRAY

Rio de Janeiro

Dated April 5, 1939

Rec'd 2:08 p.m.

Secretary of State,

Washington.

103, April 5, 2 p.m.

My 86, March 24, 1 p.m.

The new Director of the Exchange informs me that the Bank of Brazil will close exchange today for maturities and daily quotas for February 14. He states that he will endeavor to allocate exchange daily pending promulgation of the new exchange legislation. Please inform Department of Commerce.

SCOTTEN

CSB

FUTURE ENGAGEMENTS OF THE PRESIDENT
Revised to April 6, 1939

April 10 - 11:15 a.m. Arrive Union Station, Washington.
12:00 noon, greet Easter egg rollers from South Portico.

April 14 - 11:00 a.m. Pan American Day Speech (national hookup)
2:30 p.m. Mt. Vernon address (national hookup)

15 - Gridiron Dinner

17 - Open ball game, Washington, 3:00 p.m.
6:00 p.m. Address to National Parole Conference,
East Room (national hookup)

20 - 8:30 p.m. American Society of Newspaper Editors.

25 - 10:00 a.m. Address White House Conference on Children in a
Democracy.

26 - Leave for Hyde Park.

28 - At Hyde Park - Receives Norwegian Crown Prince and Princess.

30 - Norwegians leave in a.m. The President motors to Fair - speech -
return to Hyde Park by 6:00 p.m.
6:00 p.m. - Crown Prince & Princess of Denmark at Hyde Park.

May 1 - Danes leave.
Dedicate new Post Office at Rhinebeck.

3 - Return to Washington.

(?) 4 - Chamber of Commerce Dinner.

5 - President of Nicaragua at White House.

6 - " " " leaves White House.

7 - Prime Minister de Valera at White House.

8 - " " " " leaves White House.

10 - 10:00 p.m. Radio broadcast dedicating new building of the
Museum of Modern Art, N. Y.

FUTURE ENGAGEMENTS OF THE PRESIDENT
REVISED TO April 6, 1939

June 8 - King and Queen of England at White House

9 - King and Queen of England leave White House
The President leaves White House for Hyde Park

10 - King and Queen of England at Hyde Park

11 - King and Queen of England leave Hyde Park

12 - West Point, N. Y.

28 - Conference of Governors - luncheon at Hyde Park
(Mrs. Roosevelt to act if the President not there)

Nov.11 - Virginia Military Institute - speech.

April 6, 1939

To: The Secretary

From: Mr. Hanes

Dr. Herbert Feis called me on the telephone to say that the Venezuelan Government is pressing him to have the Treasury send one or two men down there to help them with customs and to advise on monetary problems. The Treasury had suggested to Feis the names of two men, Schmidt and Spiegel, but he thinks that neither one of them has the experience or the background. However, he believes that Schmidt might do as the second man. Dr. Feis said that the Venezuelan Legation had told him that if we could not help them they would probably ask the Germans to do so. Feis also stated that he thought it very important that the Treasury Department develop a Latin-American section and that the State Department would be glad to help us find the right men. I discussed this matter at the 9:30 meeting today and Harry White suggested the name of Dr. Wernette of the Harvard Business School as a possibility to undertake this work. I think Archie Lochhead has been in communication with Mr. Briggs of the State Department on this matter. I have told Dr. Feis that we would try to get an answer for him just as soon as you return.

JWH.

April 6, 1939

Dear Henry:

Jerry Frank just called me asking for a meeting between the agencies who might be concerned with the continued break in the stock market. He is again suggesting the purchase of securities. I again refer to my conversation with you and recommend that we think seriously about two things which would be generally helpful: (1) Announce the foreign buying and selling now taking place in the market. For instance, during the past few days of the breaking market, foreigners have actually been buying on balance; (2) I think it might be advisable for the Federal Reserve to explore the possibility of lowering margin requirements and make such announcement at this time which would alleviate the fears of a great many people who may owe money on securities. It is undoubtedly causing a great deal of sacrifice of securities in the market at the present time. Jerry Frank or somebody from the SEC will get in touch with you on Monday.

Best regards.

Sincerely,

/s/ John Hanes

The Honorable,

The Secretary of the Treasury.

orig. to Sec'y in pouch - 4-6-39

JHW:JH:ce

Carbon copy to Mr. Hanes on April 6, 1939.

April 6, 1939.
10:21 a.m.

John Hanes: Yeah. You want that on?

HMJr: Yeah.

H: All right.

HMJr: All set?

H: All set.

HMJr: You've got -- who is all there?

H: There's McReynolds, Ed Foley, Herbert Gaston, and me.

HMJr: Fine. The reason I asked you to get together is it's easier for me and this is fairly important. I -- can they hear me?

H: Yes.

HMJr: I talked to the President last night and he'd read all four letters. See?

H: Yeah.

HMJr: And he asked me what I thought, and I started to explain to him that under the circumstances that we -- that there wasn't much else for me to do, everybody being in favor of doing the stock in this way; although that -- my understanding was not the regular way it was done. Well, he didn't letme get half through my sentence, see?

H: Yeah.

HMJr: And he said -- well, this is the way -- he kept saying, "It's up to me, isn't it ? Up to the President to decide"? And I said, "Yes." So he said, "Well, this is what I'd like them to do." He said, "I don't care whether twenty-five million or thirty million, or -- or what the figures --" He said -- I tried to explain it to him. He said, "No," he said, "the less I know about it the better. The less I know about the details" But -- and I wrote down afterwards, he said, "I think that we should get a letter from Giannini saying that either if the Comptroller's office or F.D.I.C., or Federal Reserve, or any other agency that has the authority over bank examination, should think in the future that the Bank of America, who are paying out dividends, is impairing its capital, that the Bank will agree to withhold the payment of such dividends."

Now I -- several times I said, "Well now, don't you want to hear why Jones, the Comptroller, and Hanes feel that -- that this is a good thing"? And he said, "No," he said, "won't you please do it my way"? And he said that two or three times. And I said, "Yes, I'd be delighted to do it your way, but don't you want to know why they've come to this conclusion"? And he said, "No." He said, "I want them to write you such a letter so that your request that -- or rather the Comptroller's request of last fall that they do not pay the dividends......" I don't remember what the word was he mentioned -- but -- I don't know whether he used the word "plausible" -- he didn't use that word, but -- oh, "seem reasonable" -- I don't know, he used some other word. At least -- I'll have to put my interpretation that -- that such a letter -- I'll have to put my interpretation on it -- would save faces, you see?

H: Yes.

HMJr: So -- I tried to explain that it would seem -- that it would be difficult to get such a letter and as I say he kept interrupting. He'd say, "Won't you please do it my way"? So I said I'd be glad to and I'd be glad to transmit it to these people and that -- to you, and through you to the Comptroller and the Federal Reserve, R.F.C., and F.D.I.C. He was thoroughly insistent that he wants such a letter.

H: Now, let me see if I......

HMJr: He said, "It's up to the President to decide." And I said, "Yes." He said, "Well, I want such a letter."

H: Let me see if I understand. Now, that letter -- he wants -- he wants Giannini to say in a letter to the Comptroller that if in the future he's about to pay a dividend and the -- and the Comptroller thinks it's an unsafe and unsound practice......

HMJr: Right.

H: ......that he will not pay such a dividend.

HMJr: That's right. And he doesn't want us to put any money into the banks until we get such a letter.

H: Now, another thing -- you mentioned F.D.I.C. and -- and Federal Reserve.

HMJr: Well, he said this. He said, "I don't know the details," but he said, "any Federal agency that would have the right or the authority."

H: I see. Well, that's the Comptroller and the Federal Reserve. Of course, the Federal Reserve coming in under section 30 to -- to try the case after the Comptroller has built the case against them, that's where the Federal Reserve comes in.

HMJr: Well, he said -- he said to me -- he said, "I don't know the details, but" he said, "any agency that would have the right to say that their -- that their capital was impaired through payment of dividends.....

H: Right.

HMJr: ......should be included." Now, would that be the Comptroller......

H: That'll just be the -- that'll just be the Comptroller and the F.D.I.C.

HMJr: Well, he -- he said, "I don't know the details. I don't know the practices, but whatever Federal agency would have the right to say to the Bank of America that through the payment of the dividends your capital was being impaired and that if this agency feels that -- that by either withholding the dividend, or reduction of the dividend, that he, Giannini, would agree to it."

H: Well, I think ~~we~~ can get him to sign such a letter as that.

HMJr: What?

H: I think we can get him to sign such a letter as that.

HMJr: Well......

H: I don't -- I don't see why not, because the Comptroller has got the authority to stop him from paying a dividend theoretically. It's a damn hard thing to accomplish but theoretically he's got the right to stop him and -- and the F.D.I.C. has got the right to refuse to guarantee deposits.

HMJr: Well, the President -- I can't put it too strongly that -- that this is what he wanted and that he wouldn't even -- try -- let me explain.

H: Yeah. Well, Henry, I don't think that's so bad. I think that's all right. I think that we ought to be protected and fortified. I think he's right that way. I -- I agree with him, and I think we can get it.

HMJr: Well, of course, I -- I think it would be wonderful if we could get it.

H: Yes. Well, I.....

HMJr: I think it would be wonderful.

H: I believe we can get it.

HMJr: What?

H: I say, I believe we can get it. I don't see anything bad about that at all.

HMJr: I would say that he was adamant about it.

H: Yes. Well, that's -- that's the answer. We've got to -- we've got to get it if we -- if we want to do the job you've got to get it, that's all. He wants to -- he won't sign it any other.....

HMJr: He said, "Well, that's -- then that makes what you people try to do in the fall consistent." That was what he said.

H: All right. That's true.

HMJr: What?

H: I say, I think that's true.

HMJr: See?

H: That's what we were trying to do in the fall. That's right.

HMJr: That was what he said. I was trying to grope for the word.

H: Yeah. Well, I think that's all right. Of course......

HMJr: As I say, he -- I was trying to give him the viewpoint as I understood it of you people, you see?

H: Sure.

HMJr: To try to be fair.

H: Sure.

HMJr: But he wouldn't even let me do that.

H: Yeah.

HMJr: And he said, "The less I know about the details, the better."

H: Right.

HMJr: Now -- which -- if I was writing a letter I'd say, "Paragraph -- which has happened -- what's happened is just what I prophesy what would happen to you. That by Jimmy Roosevelt sticking his neck into this thing, the President has gotten tough on it.

H: Yeah.

HMJr: You remember my saying that?

H: Yeah. I do, yes.

HMJr: What?

H: I do remember, yes.

HMJr: I said, "If Jimmy puts -- what will happen is," I said, "the President is going to get tough on this thing."

H: Yeah.

HMJr: Remember my saying that?

H: I do, yes.

HMJr: Well that's -- now that's just what's happened.

H: Well now, I -- I understand that all right. And -- wait a minute, let me ask these other people.

(Pause)

H: We've got that all right, Henry.

HMJr: Now what I thought was this. In order to make it so there's no question, I thought that somebody -- that you and Foley ought to draft such a letter and then say, "This is what the President wants." And give it to the Comptroller, and to Crowley to O.K., and then send it out there.

H: Right.

HMJr: Now, I don't think that -- in this case that -- that Jones really gets in on it, although he'd better be informed, of course.

H: Yes, I think we'll -- we ought to inform him and keep him posted on it, because......

HMJr: By all means, he should be informed, but I think that -- if you agree with me, I think it's up to the Comptroller and to Crowley to get the letter. It should be written to them.

H: Do you understand that that letter should be written to either the Comptroller or the -- or the F.D.I.C., or to both?

HMJr: Well, I -- I -- again, of course I'm -- a joint letter to both of them.

H: Uh-huh.

HMJr: Or separate letters.

H: All right. Well, we'll -- we'll figure it out and then we'll read the letter to you, after we get it prepared. We can read it to you the next time we talk to you on the phone.

HMJr: Yeah. Now, Johnnie, to go back -- some week or ten days ago I asked you to have the history of the Bank of America brought up to date for me.

H: Yes, sir.

HMJr: Is that being done?

H: Yes, sir. It's gotten -- I've got it down in chronological order now. It is in pretty much outline form, Henry; it's -- it's a mass of documents.

HMJr: I know.

H: And it's pretty much in outline form. I took it from the point that Herman Oliphant brought it, and took it from that point on in outline form just about as it was given to you.

HMJr: Well, in case I should need it when I get back, will you leave it with McReynolds?

H: I tell you who's got it. Preston Delano has got it, but I'll have a copy in your files. See?

HMJr: Well, I'd give it -- put it into McReynolds' hands.

H: O. K.

HMJr: So if I wanted it Sunday, he'd have it.

H: O. K.

HMJr: What?

H: I'll do that.

HMJr: Now, what was I going to say? (Pause) And then also put into McReynolds' hands, because you'll be gone for a couple of days, a summary of the last Comptroller's report of the Bank which I have never seen.

H: Well, I -- you -- wait a minute -- (talks aside). You mean the -- you mean the report of examination?

HMJr: Yes.

H: O. K. I know it.

HMJr: I mean, the criticism which would -- I take it goes -- I take it the criticism was sent to the directors under our -- the program which you suggested, I think we followed, as I remember.

H: Righto.

HMJr: We now sent the criticism to each director, don't we?

H: Well, I -- the examination itself goes to the Board of Directors. I don't know if it goes to each director. I don't know if they've changed the way of going back there or not. We asked them to send to each director, I remember, but whether they've done it or not, I don't know. But I'll check up and find out.

HMJr: Well, will you find out?

H: Yes, sir.

HMJr: And in any case, a summary of the criticism of the Bank be left with McReynolds so in case the President should ask for it while you're gone I'd have it, and I'd like to read it anyway.

H: Righto. I'll get all that in McReynolds' hands.

HMJr: And you think this is a good suggestion?

H: Yeah, I don't see any objection to it. I think it's all right, and I think it's perfectly logical. I don't -- and I think we can get it.

HMJr: O. K.

H: Now, are you through now with that?

HMJr: Entirely.

H: All right, then can I tell you -- I just want to put this on the record. I won't be here when you get back. Berle called me up -- you know, Adolph Berle?

HMJr: Yeah. A.A.

H: Yeah. And said that the President had asked him to get in touch with me and I went and had lunch with him and Berle said that he had been discussing with the President this matter of financing those projects which were self-liquidating.

HMJr: Yeah.

H: You know the things which we worked on a good deal at -- hello?

HMJr: Yes.

H: And which-Frederic Delano wrote a letter asking the President........

(Noises due to bad connection.)

HMJr: Wait a minute, let me get this wire cleared.

H: All right.

HMJr: Will you wait a minute?

H: Yeah.

HMJr: Hello - can you hear me now?

H: Yeah.

HMJr: All right.

H: You remember, we worked on that thing and drew a bill....

HMJr: Yeah.

H: And then Frederic Delano wrote the President a letter....

HMJr: Yeah.

H: The President wrote you a little memorandum..

HMJr: Yeah.

H: And on that memorandum he said, "I think that we had better proceed along simpler lines in accordance with Delano's suggestion and just prepare a bill, or legislation which would provide for financing of such projects as Boulder Dam and one other"-- the name I've forgotten right now -- Panama Canal, that's right -- and then you said in one of your morning meetings here that you were not going to do anything further about it. Now, how Berle gets into it or why, I don't know, except that he told me that the President had asked him to talk to me and see if he couldn't get the Treasury to act or for him to carry the ball, or something of the kind, I didn't quite get what.

HMJr: For Berle to carry the ball?

H: For Berle, yes.

HMJr: Well, that's ridiculous.

H: (Laughter) Well, it struck me so, but.....

HMJr: Well, I'll tell you how Berle got into it -- I mean, a little information and a little gossip. For some reason or other last year, Berle had somebody down at T.V.A. studying the whole question for himself. I don't know why, see?

H: Yeah.

HMJr: And then, when the President mentioned something about Berle, he said, "Oh yes, you know, Berle made a great success in financing for the city," I don't know whether it was the Holland Tunnel, or -- one of these things.

H: Yeah.

HMJr: And I couldn't help but laugh. I mean, the President seemed to think that Berle made a great success of financing one project and doesn't realize that we are doing it every day in the week, and -- but I never go over and say, "Look, what a smart boy I am. Look what I've done."

H: Yeah.

HMJr: And -- of course, Berle hasn't got much to do over at the State Department, and he's one of these fellows that's always working on the outside. He's a smart fellow.

H: Yeah.

HMJr: And we've worked this whole thing up, and what I would do is that I'd have Foley prepare the bill along the line the President says; have it cleared through the Budget in formal manner, and send it over to the President.

H: Well, the bill is, I think, in pretty good shape. The bill has been prepared and you know we had a hellish long meeting here about it one day in which about 21 people were here.

HMJr: I know.

H: And it's -- they all -- every Department of Government that was represented here except the Army sounded on it, included Mr. Delano. I think the rest of them were all more or less opposed to it, but I think Delano was the one who really -- really unsold the President on the -- the main idea of putting the bill into Congress at that time.

HMJr: Well, I've had Berle before try to get in on Treasury business. I've always been very polite, but I -- I have just kept him out, you see?

H: Yes.

HMJr: And you can do it......

H: Well, I got the -- I got the -- this inference is what I drew from what Berle told me and not by direct word of mouth, but by implication. I drew the impression that the President had told Berle or had -- that Berle had gotten the impression from the President that we had stopped the thing here in the Treasury.

HMJr: Well......

H: Now, I told Berle, I said, "I don't know where you got that impression, but," I said, "I just want to tell you the facts. That as far as we are concerned, we've got a bill drawn, which I think is in substantially good shape, and we are ready to go ahead. We have never stopped it at all. My impression is that it was stopped by somebody on the outside."

HMJr: Well, as a matter of fact, when the President wrote me a letter, sending me the Frederic Delano stuff, I wrote him back a letter saying that I wouldn't -- this is the tenure of it -- I wouldn't take "no" for an answer. It was too important, and before he threw it in the ash can, I wanted to talk to him again. Now, that's the last form/a communication I've had with him on it.

H: I see.

HMJr: You can look up that letter. And I sent him that letter, I don't know -- when he was away on one of his trips. See?

H: Yeah.

HMJr: And then -- because -- Berle for some reason or other, worked his way in on T.V.A. and because he sold some Holland Tunnel bonds, he's a great financial expert. Now, I think the thing to do is to leave it there and -- the bill -- and I think.....

H: Well, Berle has asked me the direct question, if he can have a look at this bill. Now, I......

HMJr: Well, why not?

H: I said, I saw no objection to it as far as I was concerned, but I didn't want to let it go without discussing it with you.

HMJr: Why sure. And then -- but why not give it to the Director of the Budget and ask him to forward it to the President?

H: The bill?

HMJr: Yeah.

H: O. K.

HMJr: What?

H: O. K.

HMJr: Ask Mac if that isn't the formal.....

(Through inadvertency the balance of this conversation was not recorded.)

THE UNDER SECRETARY OF THE TREASURY

WASHINGTON

April 6, 1939

Dear Henry:

Jerry Frank just called me asking for a meeting between the agencies who might be concerned with the continued break in the stock market. He is again suggesting the purchase of securities. I again refer to my conversation with you and recommend that we think seriously about two things which would be generally helpful: (1) Announce the foreign buying and selling now taking place in the market. For instance, during the past few days of the breaking market, foreigners have actually been buying on balance; (2) I think it might be advisable for the Federal Reserve to explore the possibility of lowering margin requirements and make such announcement at this time which would alleviate the fears of a great many people who may owe money on securities. It is undoubtedly causing a great deal of sacrifice of securities in the market at the present time. Jerry Frank or somebody from the SEC will get in touch with you on Monday.

Best regards.

Sincerely,

John W Hanes.

The Honorable,

The Secretary of the Treasury.

GROUP MEETING (CONDUCTED BY UNDER SECRETARY HANES)

April 6, 1939.
9:30 a.m.

Present: Mr. Hanes
Mr. McReynolds
Mr. Gaston
Mr. White
Mr. Lochhead
Mr. Graves
Mr. Bell
Mr. Gibbons
Mr. Foley

McR: Those Merry-Go-Round boys tried to get me on the phone last night. I don't know why. They didn't get me. That is, they called me while I was at dinner. Tried to get me in the afternoon, then called at eight o'clock and I hadn't gotten home from dinner yet. They didn't leave any telephone number, so I didn't call them back; wouldn't have called them back anyhow.

Hanes: Did they have a story this morning?

McR: I don't know.

Hanes: (To Gaston) Did they?

Gaston: I didn't see their column. I read Arthur Krock's column with great interest this morning.

(Gibbons comes in)

Gibbons: Hello, John.

Hanes: Hello, Steve.

With some shock.

Gaston: Huh?

Hanes: With some shock.

Got anything else, any news of any interest?

Gaston: I don't believe so. I can't think of anything.

Hanes: Mac, you got anything off the golf course?

McR: Nothing off the golf course, Johnny.

Hanes: Harold?

Graves: (Nods nothing)

Hanes: Harry?

White: Nothing. The Secretary wanted that Wagner letter and his statement before the Social Security committee....

Gaston: Yes.

White: ... to be sent to the Treasury Bulletin mailing list, if there is a mailing list - about a thousand.

Gaston: Yes.

White: Now, if that's done there will be some duplication. I suggest that we get one of the boys to cross out those that are on both lists, because it'll be kind of ....

Gaston: I don't believe there is much duplication with that list you gave me.

White: Well, if there isn't ....

Gaston: That Treasury Bulletin list is almost wholly banks, research libraries - there may be some colleges on that, but it's mostly financial institutions, bankers, brokers, so on.

White: I know there's a few colleges, but that's only because they've asked to have their names added.

Gaston: We could easily check that; if there are college people on that, we can check them against that list. Those other letters have all gone out.

White: Well, we'll take care of the letter if you think any letter of transmittal is necessary.

Gaston: I don't believe so.

Hanes: Archie, how's the market?

Lochhead: The exchange market is just being held fairly quiet. They didn't lose very much yesterday. France has been gaining on balance this last week, continuously gaining. The war situation seems to have gotten over in a part of the country where there are more S's than Z's on the names - in Central Europe; seems to be getting around Albania.

White: That's where the trouble started last time.

Lochhead: Yes, that's where the trouble started last time. I'm afraid as long as it's Italy that's interested - a good catholic country won't have a war over Easter Sunday. That's a fact. You can't get the population aroused very much over a good holiday.

Gibbons: No, the population won't be. Be a good time to sit it over, though, if they're religious.

Lochhead: With the market up a little bit yesterday the foreigners went on the sale side about a million and a half dollars.

Hanes: About a million and a half on balance.

Bell: Speculator market.

Gibbons: Did the market behave all right yesterday?

Hanes: I didn't notice the market yesterday.

Lochhead: It was up about a half point. Kind of a settling period, with the holidays coming in - a lot of evening up. It wasn't a question of any recovery, just a little stoppage in the selling.

White: John, what do you think of the possibility of examining the daily net movements of foreign purchases and sales with the - as compared with the ups and downs in the market, see what it looks like with a couple curves? If you find there is no relation at all - again to repeat what I said yesterday - I wonder whether that information - a historical study in which we'd find there is no high correlation - might not be useful in minimizing fears, expectations.

Hanes: I suggested that to the Secretary yesterday after we had talked about it here. I suggested to him that it might be advisable to think about the possibility of publishing either weekly or every three or four days or something of the kind accumulated totals of net sales or purchases by foreigners, and he seemed to shy away from it a little bit. He said, "Well, let's think about it a little bit. It might be that it shows nothing material now, but it might at some future time develop to the point where it might be very material. You might not want to show it, for some reason."

Bell: Then you couldn't quit publishing it.

Hanes: Then you couldn't quit publishing it.

White: That would be the advantage of not publishing the data or not even indicating - but making a historical study and letting it get out somewhere if we first see that it shows that.

Hanes: I'd like to see that, because I don't believe that a 7½ percent average of the volume of the New York Stock Exchange - 7½ percent I don't believe will have any very great influence over the volume of the New York Stock Exchange - I mean over the price level; because in - I did 7½ percent of the Stock Exchange business myself in one firm on the average over five years - 7½ percent of the volume I did myself, and I know damn well I had no influence over the market. I mean in my firm. My firm did 7½ percent of the total volume on an average over the five years, we did about 6 percent of the total volume, as a matter of fact.

Gemmell: Of course, we do publish the figure of the foreign purchases and sales - the weekly - in the Bulletin now.

White: It's not quite the same. The thought that sometimes has been expressed and we would like to get information on - this question has been raised several times in the last three years - is whether or not the foreign buying and selling is concentrated in relatively few stocks which are presumably the leaders, or if there are any such things as leaders. Let me raise this question, not for the public but our own information: might it be worth while to pursue that study to find out what starts their buying and selling?

[illegible]: Yes. I don't know whether those figures are ever broken down into individual issues.

[illegible]: No, we've raised that question several times and we've never pushed it further but I think we ought to: a question of getting either more information from the security houses or getting the S.E.C. to get the information, which would be the logical thing to do. I wonder whether you couldn't arrange it.

[illegible]: Sure, I think they might be able to get it. It would be quite a task for the individual house to give every individual issue, but it might ...

[illegible]: Only for a period of a month, let's say. I mean let's see what there is in it, then if we find that they are generally distributed, - think that's interesting information. If, on the other hand, you find that the bulk of the transactions fall in some dozen stocks and if in turn they regard those dozen stocks as having a more important influence on the general stock movement, I think we've got something.

[illegible]: I tell you the way it used to be. My experience with it formerly was that the British, for instance - that's where we did most of our business abroad - the British traded entirely in stocks that were listed in London. In other words, the market - they only came to the New York market when there wasn't a big enough market to handle their transaction in London. For instance, if they wanted to buy 10,000 shares of Chrysler and there wasn't but 5,000 available, 5,000 would be executed in London and the other 5,000 would be executed in New York. But if there was a market big enough to take that sale or purchase in London, they'd do the whole thing on the London Stock Exchange. So my experience was that you never had an order, unless an isolated one, in one of the British stocks listed here, - you never do any business outside of those stocks which are listed in London. So you can take a list of those stocks and be pretty sure ....

White: The British list is pretty long now.

Hanes: Oh, they've been stealing our business right and left, taking everything they could take over there that wasn't nailed down.

White: Well, if you think that somebody in the S.E.C. might make - you know, we get the daily figures from them.

Hanes: I know you do. And they get them from forty houses that have foreign connections.

White: That's right. They might be willing to make a study over a period of a month where they would not like to do it continuously and keep current data.

Hanes: I think it would be very interesting. Who does that over there now? Goodrich used to.

White: Goldschmidt - we worked this up with Goldschmidt.

Hanes: I'll call Goldschmidt on the telephone, see if we can ask them to break that down a little bit, give us some idea of stocks for about thirty days.

White: That would be very helpful.

Cox: A historical study to see if there is any plausible relation.

Hanes: That would be very interesting.

Lochhead: I notice the releases of Lehman Brothers and General Investment Trust this morning; they both lightened their common stock holdings pretty heavily this last quarter, to March 31.

Hanes: I notice they went into Government bonds and cash very largely.

Lochhead: That's right. I think sometimes these investment trusts have more of an effect on the market than the foreign people.

H.M.Jr: Stevie?

Gibbons: I have nothing.

H.M.Jr: Steve, I'm going away on Friday night. You're going to be here Saturday; I told the Secretary.....

Gibbons: Yes.

H.M.Jr: ... that you would be here Saturday. We'll be back Sunday. Isn't that right?

[illegible]: We'll be back Sunday morning.

Gibbons: I won't be here Sunday, but I'll be here until four o'clock Saturday.

[illegible]: There's one further fact in connection with this. You might have seen one of the cables that Cronie had that has information that would be very reassuring to the domestic stock market in the event of hostilities. I'm wondering whether you might consider the possibility of letting that information possibly leak out after you see what it is.

H.M.Jr: That's the one I saw - the cable I saw from London.

Lochhead: You mean about not disposing of any stocks. But on the other hand, that cable came over very confidentially. I think you ought to be careful about letting it leak out. I notified the S.E.C. the very day.

Haas: MacGregor of the Herald Tribune saw me yesterday; wanted to write a Sunday story about what would happen to the finances and stock market in case of hostilities. I couldn't tell him very much; told him he could speculate about as well as I could on the thing. But I told him the Secretary had said that he would no doubt on monetary matters go to Congress for additional instructions in such a situation. But about this thing of the dumping of stocks, I said it seemed to me that it would be plainly in their interest not to have any reckless sale of stocks and I thought it rather foolish to suppose there would be any reckless sale of stocks, because they'd certainly take command of the stock situation as to their holdings by their nationals.

White: Herbert, you're quite right, I agree. Notwithstanding, I remember a meeting a year ago of bankers and men at the Secretary's home when this very question was raised, and I think there were only two or three of us who took that position and several who took the other position; and the men who took the other position had much more practical experience than those who took your position. So to what extent their position reflected the general market's position, I don't know, but if it does then if a statement of this kind could leak out it would prevent any widespread - it would reduce the extent of widespread selling that would take place in the event hostilities broke out.

Gaston: I think it wiser to create the impression that it is our view that there wouldn't be any reckless selling.

White: I think that is also a good idea.

Gaston: Of course, I was thinking of this circumstance: that some of these foreign holders might want to rush to cover from the probable mobilization by the foreign governments - they might want to duck that by a quick sale, and that might have some effect.

Hanes: Well, Harry is right that if you could do anything to offset this vicious feeling that you get in the newspapers in those little squibs - I've seen three of them now, all talking about foreign selling, all talking about foreign selling, and that the market was weak .... As I said before, Wall Street has always got to have an excuse, got to have a reason for everything, and, failing to have a good reason, they just assign two stock reasons; one is short selling and the other is foreign selling - when they can't find anything else.

Gaston: I think Harry might get together some very interesting stuff that the Secretary could use in a press conference.

Haney: be very helpful if he did it, I think. I deny that this kind of stuff here - if those facts are correct, I deny that they can have any effect unless all of those are concentrated at one minute. That doesn't happen. People don't rush out and try to give their assets away like that with a megaphone, advertising what they're doing. They just don't do that. That isn't the way it's done.

White: Well, John, is there such a thing as what you might call half a dozen or ten leaders which set the tone for the market, or is that ....

Haney: That's somewhat exaggerated. In the old days, when short selling was unrestrained and when what we used to call bear raiding was a well-known tactic, a fellow like Ben Smith would just keep pounding, making new lows every minute on stocks like Chrysler and Steel, which would upset the general list. No question about that, they would upset the general list. But unless the tide was going with him he wouldn't do a damn bit of good, because the list would recuperate and catch him in a bag every time. That short selling thing was exaggerated, largely. The concentration of bear raiding was not exaggerated; that was a vicious practice, and the fact that you can't do that any more is a hell of a protection in the market.

[illegible]: That's when they sensed that the market was inherently weak and took advantage of it.

Haney. That's right, and then they used to have an accumulation of stop orders just under the market - maybe ten, twelve thousand shares concentrated in stop orders. In order to get down to that, you might have to sell down to three points - to tap that stop order, and if you got it down to that point, then that became a market order; that ten thousand stop order at that point would become a market order, and the fellow who sold that would take it all back from this stop order. He would be careful not to sell more than what was concentrated on the book. That required the fellow who was running the book to be in cahoots with the fellow trying to wreck the market. That sort of thing was just - it was just highway robbery; he didn't have a gun, that's the only difference.

Gaston: Hammer it down to there, stand under it and pick it up.

Hanes: But you can't do that any more. Can't do it. First place, stop orders are limited, and second place, you can't sell down - you can only sell stocks now after a rally of an eighth of a point. You can't keep making successive new lows.

Eddie?

Foley: I don't have anything, John.

Hanes: Danny?

Bell: The only thing I have is that problem the President threw back in the laps of the Secretary of the Treasury, Secretary of Agriculture, Farm Security, Farm Credit, and the Budget, with respect to the Lee bill - insured mortgages on farms. You remember he said that he'd like to have a unanimous recommendation on Monday the tenth. Well, we can get a unanimous recommendation that the Lee bill isn't exactly right, and we can get a sort of unanimous recommendation that if the President wants to do something along this line, why, we can work out a program; that is, we can say that we'll increase the appropriation under the Farm Tenant Bill - Bankhead-Jones Act - or you can put into active operation the Farmers Home Owners Corporation created under that Act but which has never had any money on which to operate, and let them issue guaranteed obligations, have an appraisal of it every year and let Congress appropriate the deficit. But we all agree, Agriculture reluctantly agreeing, that there ought to be a limit on it, not more than 350 million dollars, and the authority to issue securities ought to end not later than June 30, 1942, and preferably June 30, 1941, so as to tie in with all the other emergency corporations' expiration date.

We'll have a memorandum on it probably tomorrow, and I don't know whether we can sell the Secretary on that or not.

We could also have insurance up to 350 million for a three-year period, and Farm Security has agreed that there ought to be at least a half percent premium charge in order to make it have some semblance of an insurance scheme. But I think if we start that insurance scheme we're lost. But I think if we start the corporation and have Congress take a look at it every year through the deficits and put a limit on the time during which it can borrow, so that they have to take another look at it in '41 or '42, maybe we can stop it then.

[illegible]: The idea is to set it up as a separate corporation, not to appeal to the Treasury for its deficit but to go to Congress and get the appropriation direct from Congress?

Bell: That's right.

HMJr: Issue their own obligations.

Bell: Yes, guaranteed obligations.

HMJr: Have to make up their losses by direct appropriation.

Bell: That's right - just like the Commodity Credit.

Foley: On this extension of emergency powers, do you think there is anything in the fact that if they're all centering around June, as they are, the incoming Congress is going to have a terrific time giving all these powers the appropriate consideration? I wonder whether there might not be something in staggering some of these.

Bell: Well, you had them this year.

Foley: It's been this way in '34, '36, '38, and '40, hasn't it, Dan?

Bell: How's that?

Foley: It's been every two years for the last six.

Bell: Yes, and practically all of them expire June 30, 1939, so they're in process of being extended now - like R.F.C., Commodity Credit. Some of them have been extended through already. They go to different Committees, generally speaking, so it isn't much of a problem. And I don't think it would hurt anything if some of them failed to be extended. Wouldn't hurt the Budget Director's feelings very much, at least the present one; I don't know about the next one.

Jones: You say you're going to have a memorandum ready tomorrow?

Bell: I think we'll have a memorandum, yes. I thought we'd get everybody that's in the picture at the present time agreed to it and then try to sell it to the Secretary on Monday. I don't know whether Wallace will agree to it, but Benny Baldwin, as I say, reluctantly agreed that we could do that. They'll take anything or any scheme under which they can get more money; doesn't make any difference to them how they get it.

[illegible]: That's the only thing as far as they're concerned.

Jones: Who told the Secretary or who heard about this plan for buying common stocks? Did you (Lochhead) hear about that?

Lochhead: Why, yes, when I spoke to Frank on it - let's see, it was last Friday that cable came in - he brought up the question and said, "Well, when we spoke about this once before" that he, Frank, had suggested that in the event of any trouble that the stock market be supported; wondered whether we'd give consideration to that again.

Foley: Well, we have the papers all drawn to create a corporation to support the market.

Lochhead: But the Secretary was not very enthusiastic about the idea.

Jones: The reason I ask is because - were there any of you there at the Secretary's - I've forgotten who was there - Harry, were you there the night we were talking to Wallace and when Wallace was talking about his cotton plan and the cotton export plan?

Bell: I was there. You mean just recently.

Hanes: Yes. You remember Wallace brought up that same thought, as to whether or not we ought to buy common stocks in the event of trouble. I wondered whether or not you'd gotten that from Wallace or where you'd gotten that. The Secretary mentioned that.

Lochhead: A year ago.

Foley: It was all up in September and at that time the draft of the papers to create that corporation, you remember...

Hanes: Yes.

White: I think he probably got it from Ezekiel. I know I was present at one meeting at which Frank was present - some informal meeting in which this question of the wisdom and desirability of coming to the aid of the stock market in the event of any serious amount of selling was taken up, and as a consequence of the numerous informal discussions the legal department prepared papers in the event that something of that sort might be considered. But I imagine that Wallace got it there, because this was a long time ago - oh, six, eight months ago. There was no conclusion or decision made at the time, though I remember that Frank felt that it was a desirable thing to do - to examine and prepare for it.

Bell: Use Federal Reserve Bank's authority as part of the credit operation.

White: Well, they felt they had to utilize - they thought a convenient instrument would be the Stabilization Fund, and the Stabilization Fund does possess the powers, I think there's no doubt of that.

Bell: It does?

White: Yes.

Foley: Well, the capital for this corporation would come out of the Stabilization Fund.

Bell: How do you get authority out of the Stabilization Fund?

Gaston: For the purpose of stabilizing the exchange value of the dollar, you can buy any kind of securities if it's for that purpose, if the Secretary deems it's for that purpose.

Jones: I'd hate like the devil to see the Secretary buying common stocks with the Stabilization Fund.

Bell: And then explain it to a Committee in Congress.

White: Well, of course, there's a distinction between what is politically feasible and what is legally possible.

Lochhead: He said it was one thing to have the powers and another to have the common sense to deal with things.

Jones: If I'm not here, please vote no for me.

Bell: I want to sit back in the corner of the Committee hearing when he explains that operation.

White: I don't know - the legal department in preparing the papers I don't think was commenting on the feasibility or the wisdom. They were merely considering getting ready the legal aspect of it.

Jones: When we go before the Committee, it would be Harry's problem to explain that.

White: I think it could be done so they wouldn't understand. It's the easiest thing in the world.

Jones: I'd take the Clipper ship for the Pacific about that time.

HMJr: I thought somebody up there on the Hill had introduced a proposal to appropriate a hundred thousand dollars to get rid of Ezekiel over there.

White: I didn't see that. Don't pin that on Ezekiel. I don't know whether that's his idea or not.

Gaston: If we've got time, I might give a story about the Pendergast case. Pete Brandt of the Post-Dispatch called me up and was very anxious to see me right away yesterday afternoon. He came over and told me that what he was particularly worried about was the fact that the story was being circulated out in Missouri that Guy Helvering had negotiated with Pendergast and they had fixed up a civil settlement of the Pendergast case, but before it could go through the White House had stopped it.

Well, I got hold of Elmer Irey and he told me that, of course, as I knew - I had told Pete Brandt that of course that was nonsense, and I got hold of Elmer Irey and he told me, in the first place, there's never been any liability assessed, and in the second place Guy has never seen any representative of this fellow, and in the third place Guy has always given the most wholehearted support, has kept his hands completely off any criminal investigations except to encourage them, and specifically he had done that in this case. I told that to Pete Brandt.

He called up his office and assured them that there was nothing in the story. They had believed it and they were going to print it, and they were satisfied and didn't print the story.

But he told me also that he had talked to - he had been at Frank Murphy's press conference last Thursday and some question had been asked of Frank Murphy about this investigation out in Kansas City, and it was common knowledge in the newspapers that there was an investigation of Pendergast going on which would probably lead to an indictment; that they had printed that, and they asked Murphy about that. He said yes, he knew the investigation was going on and the Department of Justice certainly would never be deterred by any political considerations, and they were going right through with it, let the chips fall where they may - the Department of Justice was.

And then he asked Pete Brandt and Sam O'Neal to stay behind and he talked to them confidentially on the case, and among the things he told them was that they were all prepared to go right ahead and nothing was going to hold them back, but there was one other department of the Government that was holding things back. And of course they couldn't understand that to mean anything else except that the Treasury Department was interposing obstacles.

Hanes: I'm glad we've got a record on it. Incidentally, if you ever want that record of the first time we came into it, I've got a minute-by-minute record of everything that took place, so ....

H.M.Jr: We approved of their going ahead whenever they were ready and getting our people ready for the grand jury, even though the investigation hadn't been pressed ...

Hanes: We weren't ready to go ahead, but at least their going ahead ....

Gaston: Then, of course, he told me that everybody was laughing out there about how Frank and J. Edgar flew out there to be on the ground when something happened, obviously to grab the glory, as he saw it, and ....

Hanes: Did they go out there?

Gaston: Oh yes, they flew out there, arrived yesterday - J. Edgar Hoover and Frank Murphy - in Kansas City. And he said he knew what he thought the public generally didn't know: that this case was 99 percent Internal Revenue and that J. Edgar could only get into it on the white slave angle, which was a very insignificant feature of the case.

Well, then I told him something I learned from Elmer Irey, that - this is all confidential - that Elmer had just got a letter from his man out there in which he said that they were laying bets that J. Edgar Hoover would be on the ground as soon as things began to get hot; and this letter was written a couple of days ago, and J. Edgar arrived out there yesterday.

Hanes: Well, there was some - I don't know where they're trying to put the heat, but the implication came from the Governor through the White House that the Department of Justice were the ones that were stalling the case, and they were calling the White House.

Gaston: I told Pete that quite confidentially. I didn't know about the conversation between Stark and the White House before that, but I know what Stark called up here for.

[illegible]: We went to great lengths - I did - to tell Stark that that was an erroneous impression, that he had done a great injury to the Department of Justice; I thought it was not good information that he had. And he said that his informant, whoever that was - I guess his informant was a Department of Justice man, and he said his informant had told him that these Department of Justice men were stalling on the case and were trying to block it. And I told him that I didn't think that was true; we had been in communication with them and they had given every cooperation and ...

Gibbons: Did you get a letter, Herbert, from Winchell?

Gaston: On what?

Gibbons: On the reply to that statement he made that narcotics were coming in from Germany.

Gaston: Oh, Walter Winchell. Yes, I did.

Gibbons: About a doctor ....

Gaston: What he said was that J. Edgar Hoover had given him the same information and he had gone back to the man who told him that he got this information and this man would only tell him that some doctor told him this and couldn't give him any verification, so he was now going to drop this man as an informant.

[illegible]: I saw on the ticker yesterday where I had offered somebody a bribe for something. Did you see that?

Gibbons: You had offered somebody a bribe?

Jones: You know that statement that you - I guess I signed while you were away. I'll get that thing for you. Came out on the ticker that I had issued a statement that the Treasury was going to pay for information from informants.

Gaston: Of course, we do pay for information.

Gibbons: Well, we pay for information.

Gaston: We get appropriations for the purpose.

Jones: I know. I guess this was some formal statement which Steve's department had issued.

Gibbons: Maybe it's [illegible]. Harold's got something on that.

Jones: I just saw it last night.

Gaston: The Post-Dispatch crowd are on the level and they're our friends, and I thought it would be a good idea to let Pete know the whole background. He had most of it anyway, knew about Stark's call. They're thoroughly reliable. Pete is a thoroughly honorable man. I told him confidentially all I knew about the thing.

Jones: Well, what has happened out there in the case?

Gaston: I understand they're going to indict within a few days.

Jones: Did our man appear - Harrigan or whatever his name is?

H.M.Jr: Hartmann.

Gaston: Under the new system, you know, he's furnishing his information direct to Milligan, the District Attorney there, against the recommendations of his own man Morris over there. It's an unusual procedure. And now Murphy and Hoover got out there on the job....

H.M.Jr: I don't know...

Gaston: ... to take charge.

H.M.Jr: I don't know what's going to happen. The last I heard was that the United States Attorney out there was going back - somewhat doubtful.

Hanes: Did this all come out before the grand jury, the whole thing?

H.M.Jr: Last I heard, they hadn't gone before the grand jury. Do you (Graves) know?

Graves: No, I don't.

H.M.Jr: After they got approval on their instruction for our people to appear whenever they called, then they began to get cold feet on it, because they weren't ready.

Gaston: I think what Elmer feared was that this fellow Milligan was going to shoot before he was ready.

H.M.Jr: Elmer said he had been working on the information, getting it, picking the thing up and going over it, and he had shown the last information he had. That was a few days ago when he talked to me. The United States Attorney hadn't made up his mind to go ahead on it, so that maybe ....

Gaston: He told me yesterday that he thought he was going to try to get an indictment within the next few days.

H.M.Jr: Oh, he did?

Gaston: Yes.

Pete Brandt also knew what was the principal count in our case against the man - that insurance transaction that took place in Chicago. He knew about that.

Hanes: No. Who?

Gaston: I say Brandt knew about that. He knew about the thing that is one of our ace cards in the case; he knew all about it.

Hanes: Where did he get that from?

Gaston: Oh, they've been following the thing through, and I think they gave some information to Elmer on the thing. They've been working on it for quite a long while.

Hanes: Here's this ticker thing.

Gaston: "Acting Secretary of the Treasury Hanes today asked Congress to provide a secret 'tip fund' for the Customs officers to purchase information on narcotics rings.

"He asked that the Disbursement Division of the Treasury Department be authorized to extend funds to agents for purchase of information, and that it be made secret. Such a fund is provided for the F.B.I., he pointed out.

"Hanes added that it is frequently impossible to procure information and evidence relating to narcotics smuggling unless the information is paid for."

Hanes: Is that the kind of stuff that you (Gibbons) engage in down in your department?

Gibbons: I'm a lucky guy. I was away that day.

Hanes: Yes, you were away.

White: Well, there must be such a fund now, because that's just what they're doing.

Mack: We do it in Narcotics, we do it in Alcohol Tax.

Hanes: We do it in the Income Tax Bureau, too.

Gaston: More liberal in Customs.

White: Would that come under the classification of a bribe, quid pro quo, and is the payer of a bribe above the man who receives it?

Gaston: Oswald Garrison Villard will write a new series of articles when he reads this. He was greatly excited about the fact that we shook down a woman named Polly Adler in New York, who was keeping brothels, for income tax. "It's filthy money and the United States is a partner in the business."

McR: Partner in business if we collect taxes.

Bell: That's an idea.

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE DATE April 6, 1939.

CONFIDENTIAL FILES SUBJECT: TELEPHONE CONVERSATION WITH

L. W. Knoke BANK OF ENGLAND.

I called Mr. Bolton at 10:30 a.m. I mentioned that things were extremely quiet here in the foreign exchange market, which, in view of the approaching Easter holidays was, of course, likely to continue until Tuesday morning. The only two places to be open tomorrow, Saturday and Monday, it seemed to me, were Tokio and New York. Bolton stated that he had just gotten ready to send me a cable and that he was now requesting us also orally to hold the sterling rate for his account at 4.68 1/8 until our opening on Tuesday morning. There was no limit on the amount we were to purchase. If anything startling developed in the international picture he would ring me up from his home. Would I in such a case also try to get in touch with him by telephone. This, of course, I promised (his private telephone is Popes Grove 2588).

Bolton spoke of the bilateral guarantee of independence to be signed a week hence between Great Britain and Poland announcement of which had been made by the Prime Minister in the House. The only other event of the day concerned the Adriatic. The belief prevailed that the Italians were going to seize Albanian ports as a sort of counter to this Anglo-Polish affair. Personally he did not think that war or any crisis was any nearer today than it had now been for many days. The last and final step, he thought, was going to take a long time. Meanwhile they were living in a sort of atmosphere of war with peace-time activities practically suspended. The

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 8, 1939.

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF ENGLAND.

L. W. Knoke

2

market was under very rigid control and there was no sign of speculation. The drift of capital to New York continued and it was worth mentioning that a great deal of Swiss and Dutch money was going to Canada. A great number of security accounts were being opened by Europeans in that country and Barclay's Bank (Canada), being closely associated with one of the biggest London clearing banks, was at its wits end because of the flood of requests made of it for the opening of such accounts. I ventured the thought that capital movement to Canada had always seemed to me a logical thing to develop and that many months ago I had expressed this opinion to Governor Towers. Now it would be interesting to observe the effect that this would have on Canadian economy.

LWK:KW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 6, 1939, 6 p.m.

NO.: 657

FROM COCHRAN.

The Paris market was quiet, the French control getting a fair amount of sterling. Pressure continues on the belga and on the florin. The Easter holidays begin tomorrow, and in view of the nervousness of the international political atmosphere, the market is hesitant to make commitments.

March 30 statement of the Bank of France showed an increase in circulation of about 4,000,000,000 francs. Coverage was 62.15 versus .50.

BULLITT.

EA:HF:LWW

REB

PLAIN

London

Dated April 6, 1939

Rec'd 3:53 p. m.

Secretary of State,

Washington.

452, April 6, 7 p. m.

FOR TREASURY FROM BUTTERWORTH.

1. The City is now being deserted for the Easter holiday. The bullion market and stock exchange will not reopen until Tuesday. The foreign exchange market will be open Saturday morning but closed tomorrow and Monday.

The foreign exchange market is again very quiet with the dollar bid and the British Fund selling small quantities of dollars. Gold was fixed at parity with 159 bars dealt in. 79 bars were married and the British Fund gave a few. The market was again pro-rated, buyers receiving about 35 per cent. The dollar forward rate was slightly easier, the three months' at 2-3/16. Incidentally, the forward Belga moved out to 30 centimes for the one month and 60 for the three months.

The general atmosphere remains one of nervous waiting for something to happen.

2. The

REB

2-#452, From London, Apr.6, 7p.m.

2. The Bank of England return for this week shows an increase in the note circulation of £ 9.4 million due largely to quarter-end and holiday demand. Public deposits were down £ 5.7 million and bankers' deposits £ 6.5 million. The Treasury bill rate moved up to about £ 1.5.3D. as compared with £ 1.5.6.72D. a week ago.

KENNEDY

ALC

St. Louis, Mo.
April 6-7, 1939

FOR THE SECRETARY:

My primary interest in St. Louis was the "light" industries such as clothing and shoes which are centered here; elsewhere I had not talked to companies in these fields.

St. Louis presented an odd picture of relatively good business side by side with very gloomy business sentiment. For instance, a clothing manufacturer started by saying that business was bad, but later revealed with a smile that his business was 15% above a year ago. War jitters play an important part in conversations here, as they did in Minneapolis. On the other hand, business men here were critical of Government spending whereas those in Minneapolis were apathetic; there is a good deal of pessimism about the necessity for continuing relief indefinitely.

Retailers and persons producing for retail were unanimous in saying that the social security tax can not be passed on to the consumer; they insist that they are having to absorb this tax themselves as an added production cost and have some interesting reasons to support their argument. One of the most successful local business men thought your social security suggestion was exactly the correct one for this "experimental period."

The bond man at the First National Bank (very Republican) praised the way in which you have handled the

Government financing, even agreeing with the premium offering in March. He was critical of the Federal Reserve for the way in which it has insisted on replacing bill maturities with bills or notes when the market is so high.

While I was in Tom Smith's bank on April 6, Ronald Ransom called him from Washington and talked with him a half hour arguing that the way for the national bankers to beat the Brown Bill is to support the Federal Reserve's general banking and monetary study. Tom's reply was that Congress will never agree to a general rewriting of the banking laws as long as the Congressional feeling against Mr. Eccles is as strong as it is. Mr. Ransom said Mr. Eccles is only one of the six board members. Tom said the public does not look at it that way.

The following day Tom told me some unnamed national bankers had asked him to call Mr. Delano and urge him not to jeopardize the Comptroller's Office by complaining to Senator Glass about a lack of independence. Tom had called Mr. Delano to convey the bankers' feeling and had been told that Mr. Delano would see Senator Glass the following day.

- - - - - - - - - - -

Edison Brothers Store, Incorporated -- This company has had a phenomenal growth with its worst year being 1929 and each subsequent year showing an improvement. During this period the company's net sales had increased from less than 4 million dollars in 1929 to more than $24,200,000 in 1938.

Their sales are continuing to rise this year, but the company is following a conservative inventory policy. The company operates four chains of shoe stores. It is continuing to expand in spite of what Mr. Harry Edison, the president, describes as "boggy" business conditions. New stores are being opened at this time in at least two cities. Mr. Edison says the company "must keep its capital employed" by continuing its expansion. He is relying on what he describes as an aggressive organization to continue to overcome adverse business conditions. In other words, his company is an example of a business expanding in spite of business uncertainties. Mr. Harry Edison said that he really should not complain about the Government or its activities since he and his four brothers have enjoyed steadily increasing business. However, he went on to say that he would rather have less Government spending and smaller profits if the country could thereby be put on a more sound basis. He regrets that people are learning to look to the Government for support. He says he is willing to pay high taxes if necessary to care for the unemployed provided they are required to do an honest day's work and are encouraged to return to private employment. He does not believe that Government spending has ever influenced the sales of his company. The sort of purchasing power which helps comes from heavy industry payrolls and good farm crops, he says. Low prices have built this company's business and the social security tax has proved to be an added cost to the company because it can not raise the prices which it has so long advertised to the public, Mr. Edison says. However, he approves of the social security objectives. He thinks the only answer is to "go slow during this experimental stage." Therefore, he approves very much of your suggestion to the Ways and Means Committee. His only real objection to the Administration's program was against the wages and hours law and the labor policy.

Marx, Haas, Korrekt Clothing Company -- Mr. Irving Bettmann, president of the company, started out by saying that business is bad, but then disclosed that his company's sales are 15% over last year in dollar volume and even higher in physical volume. He then justified this discrepancy by saying that business was nervous and uncertain about many things, of which war and Government policy were only two. He told of a radio jobber who was worried over his inventory and over sets sold on an installment basis because television would soon make them obsolete. Salesmen for the company report that business is especially slow in small towns (10,000 or less), especially in the south where in some places sales are running 25% under last year. Mr. Bettmann attributes this small town situation to invasion by chain stores, a shift in consumer buying from small towns to nearby big cities, and to a hangover in the small towns of the high priced inventories left in the stores at the end of 1937. Inventories generally, he says, are well worked down but this has been true more of the big cities where there is better advertising and selling than in the small country towns.

Mr. Bettmann said that social security taxes had been an added cost to him and that he has found them impossible to pass on to consumers. He objects to the basis on which the tax is levied and insists that all taxes should be on ability to pay, that is, on profits. He also believes that social security benefits should be on the basis of need only and was somewhat surprised to learn that he is going to get a $280 old age pension which he does not need.

Government spending was criticised by Mr. Bettmann but he was very pessimistic about any decrease in unemployment and believes that the Government must take care of the unemployed through a well-planned public works program. Some new industrial development is necessary to pull the country out of its present condition, in his opinion. War will take up the unemployed and keep his company busy turning out war clothes, Mr. Bettmann says, but he very much would rather have present conditions than involvement in war. However, he has a fatalistic feeling that the United States will get into a war in Europe. Meanwhile, he thinks we should sell belligerents what they can come and get and pay for.

<u>Copper Refining Company</u> -- In Tom Smith's bank I talked briefly with the head of a copper refining company which, like the Edison Brothers Company, has had a very successful history and which is now spending half a million dollars to build a new rolling mill for the manufacture of copper pipe. Incidentally, this expansion is being financed by a term bank loan.

The president of the company is an interesting person because contrary to my expectations he was very pessimistic over the effect of war on the copper industry and his company. He said the war scare made him indifferent to whether he ever finished his new rolling mill. War, of course, would mean that his company operated furiously and either made a lot of money or was taken over by the Government. But, in the end, the plant would be worn out and would be facing an upset economy. Therefore, he said that he would rather make less money turning out copper pipes for cottages than ~~to~~ make more money temporarily in a war.

He has not increased his buying of raw copper because of the war scares and is hedging every purchase he does make. Only speculators will buy copper on the war scares. He said he would be willing to see copper go to five cents, although it would cost him $250,000 on his inventory if at the present time he could see the end of the war scares. He does not object to the Treasury's method of valuing inventories for tax purposes.

Harris Langendorf Hat Company -- Mr. J. W. Harris, president of the company was the most optimistic business man I met in St. Louis. He said his business is good, is running 'way ahead of last year, and that a small recent decline was no more than normal seasonal reaction. He agreed with the generally expressed view that social security taxes have proven to be an added production cost. They are not passed on to the consumer. He recently had a good many negotiations with the Internal Revenue service over a corporate reorganization and says that his contacts with the service have been uniformly good.

Ely and Walker Dry Goods Company -- Mr. Walter Lorch, vice president, was both pessimistic and highly critical of the Administration. He said there is too much Government meddling with business, so much that the business man has decided that he will do as little as possible in an effort to ~~reward~~ avoid Government meddling. He was particularly disturbed over the Wage-Hour Act because he had asked for an exemption of certain workers on October 22 and never received a reply. The result is that the workers have been laid off. He also criticized the cotton loan plan, saying that with 11 million bales of Government cotton hanging over the market his company is uncertain and conservative in its textile buying program. Generally speaking, he believes that business men are not buying but are waiting to see which way prices will move. They are delaying buying because of fear that war may force them to close down temporarily.

The payroll tax costs his company $200,000 a year, according to Mr. Lorch. He also criticized the undistributed profits tax, saying that American business had always grown by plowing back its profits. For instance, he cited ~~the~~ a Philadelphia Hosiery Mill, established by his company in 1922, with $100,000 capital of which $40,000 was invested in machinery. During the next ten years the mill bought $450,000 of new machinery out of its earnings which it could not have retained if an undistributed profits tax had been in effect.

Mr. Lorch said Government spending is undermining the national virtues of thrift, liberty, and honesty, on which he places a great deal of stress.

The business of his company is about equal with that of last year -- which, he says, was bad.

Boatmen's National Bank -- The officers of this bank think business is in an uncertain period, out of which it could move in either direction. Although the officers of the bank said they believe most banks are trading in Governments and will try to get out in a hurry if the price weakens, Tom Smith says that the bank's own bond portfolio has been set up in such a way that the bank will hold its Governments for the income on them regardless of what happens in the market.

The bank is actively making CCC corn and cotton loans and business loans whenever the opportunity presents itself. Ranking officers were very emphatically of the opinion that there is no need for Government loans to business. They knew of an interesting case in which a company with a good standing needed $100,000 which, in view of the company's position, should have been raised by sale of equity securities. The company had an opportunity to obtain such financing, but did not wish to do so because the present owner would then have to share future profits with the new security holders. Instead, the company arranged to borrow the money for five years at a low rate of interest.

First National Bank -- Most of the conversation here with Mr. Smith, the president, and Mr. Chase, the bond man, concerned Government financing plus criticism of Chairman Eccles of whom Mr. Smith has a very low opinion. The bond man was very complimentary about the manner in which you have handled Government financing. The bank has an unrealized profit of $4 million on a Government bond account of $90 million and has amortized most of its premiums on Government securities. The bond man said he is under constant pressure from some directors to sell out the Governments and realize the profit, but has so far successfully argued that the resultant loss of income would more than offset the profit. He has kept most of his portfolio in short and intermediate term maturities and is very critical of the Federal Reserve System for insisting on ~~the~~ replacing ~~of~~ its ~~bond~~ bill maturities with either ~~bonds~~ bills or notes. Both Mr. Chase and Mr. Smith were disturbed over a story in the Wall Street Journal this morning, saying that the Administration supports the Brown Bill to eliminate the Comptroller's Office.

ESD

April 7, 1939

To: The Secretary

From: Mr. Hanes

I have jotted down a few thoughts for your consideration. They may be greatly expanded. I will discuss them with you, if you like, when I return on Wednesday.

orig Miss Chauncey 4/8/39-12:45 PM
for Sec'y

JWH:ce

I am pleased to respond to your invitation to discuss with you the question of changes in our tax structure which study and experience convinces me are desirable at this time. On February 23, 1939, I stated at a Press conference "that business should lay aside the attitude of 'what's the use' and in view of the President's statement of no new tax should again assume normal business risks, and that we should take a careful look at the tax laws to see if there are any deterrents which are holding back business and business men from making future commitments."

On February 24th, at Des Moines, Secretary Hopkins stated that he was in sympathy with the viewpoint of removing tax deterrents to business. On February 24th, Chairman Doughton of the Ways and Means Committee issued a statement that he was in sympathy with the views of the Secretary of the Treasury and invited the Treasury to cooperate with the Ways and Means Committee in a complete study of the tax structure. On March 3d, Senator Harrison and Chairman Doughton in a joint statement offered the full cooperation of the Finance Committee and the Ways and Means Committee in such a program.

It is my belief that economic recovery is the outstanding objective before us today. I believe further that new conditions demand new remedies and that the removal of what the majority of business men consider today "business deterrents" within the tax structure will go far in bringing about reemployment and economic recovery.

The sum total of Federal revenues to be collected can never be fully determined by the imposition of tax meters, or tax measures designed to gather the highest possible tax yield. When equitable adjustments in Federal taxes are proposed, there seems to arise fears that to lessen the rate of taxes will have the effect of reducing the total volume of taxes. I do not subscribe to this theory. It is my belief that the Treasury of the United States will collect a larger total of tax dollars with a tax bill that takes into broad consideration the effect of the dollars it will leave the taxpayer for expansion and development rather than to concentrate on the highest possible yield it can extract from the business, occupation, or profession of the taxpayer. In other words, the dollar that is left for the taxpayer is of extreme importance to the economy of the country.

It is reported that the plant account of our industrial companies declined from $41,000,000,000 in 1929 to about $32,000,000,000 in 1937. Under more normal circumstances plant account should have grown by at least $1,000,000,000 per annum during that period or to a total of, roughly, $50,000,000,000.

Under our economic system the sum of approximately $7,000 of capital assets, such as land, building, equipment, etc., is required to put a man to work. We have approximately 600,000 employables coming into our employment stream yearly. Thus, to put these 600,000 people to work, we require new investment in capital goods at a minimum of $4,200,000,000 annually. It is this type of enterprise capital which we have failed to attract to the capital market during the past ten years.

The economic history of our country points clearly to the only sound solution for unbalanced budgets, for weak capital markets, and for unemployment and that solution is the creation of a healthy, prosperous economy whose maximum powers can be generated only under profitable private enterprise. History proves further that whenever business profits were substantial, farm and labor incomes were correspondingly high and Government revenues consistently increasing. When the profit system was functioning smoothly, we made lasting gains in security and in the building of what we recognize as our material civilization.

When our profit accounts have been depleted by excessive taxation or by higher wages and lower volume of business, or by paying excessive prices for raw materials, purchasing power has been merely shifted from one group to another. When, however, profits are accumulated by business, these funds have customarily been spent on producers goods, that is, land, buildings, and machinery. Profits thus plowed back into business form the basis for attracting additional credit resources and investment by the public. Because such earnings can be capitalized at ten to twenty times their amount in new capital issues, one hundred thousand dollars of profits will make possiblethe purchase by industry up to $2,000,000 worth of capital goods. This capacity of earnings to generate a multiple of dollars in spending power for every dollar of profits is a quality which has been generally ignored.

We have, therefore, directed our tax studies toward providing a real increase in Federal revenue by means of encouraging business enterprise rather than by the continuous raising of the tax rates.

It is partially because we have had little or no profits during the last decade that we have experienced terrifying idleness of deposits, low production, unemployment, lack of investment in venturesome enterprise, and reduced national income. I repeat that it is only by increasing industrial production through the maintenance of conditions under which private enterprise may make reasonable profits, and keep them, that our existing ills may be cured. What other economic changes besides profits has the almost miraculous quality of making a dollar of earnings do the work of many times its number?

I submit for your earnest consideration the following proposals, which I feel are entitled to serious study in order to accomplish in part at least some of the objectives outlined above.

JWH:ce

April 7, 1939.

Secretary Morgenthau

E. H. Foley, Jr.

For your information

Attached is a copy of Mr. Bernstein's memorandum for the file in regard to the Munitions Board annual report for 1938. On page 2 is contained the reference by Mr. Green to his alleged conference with Solicitor General Jackson concerning the legality of the issuance of licenses for arms exports to Germany.

My recollection is that Mr. Taylor subsequently informed me that Mr. Green's explanation was that he had talked with Judge Townsend in Solicitor General Jackson's office and was wrong when he said that he had talked to Solicitor General Jackson personally.

(Initialed) E. H. F., Jr.

Attachment

EHF/akm 4-7-39

original to Mr. Reynolds

at EHF Jr's request.

For original see

p. 237

C O P Y

Jan. 3, 1939

Re: Munitions Board Annual Report for 1938

State Dept.

Within a few days after the receipt of the/letter of December 17, 1938 and the draft of part of the Munitions Board's Annual Report, the Munitions Board called the Treasury to ascertain whether the Treasury approved the report. The report had been sent to me and I felt there were several points on which the Treasury should consider the position that it should take. I advised Mr. Foley of the entire situation and on Friday, December 23, in response to a phone call from the Munitions Board, he called Mr. Yost of the Munitions Board and said we were studying the matter; that we could not complete our study until we had received completed copies of the Annual Report; the copy that had been furnished to us did not have the schedule of the statistical information which we desired to see. Mr. Yost repeatedly stated in his telephone conversation that the Board would not be able to have the report completed until shortly before the meeting on January 5 and that he would like to have the Treasury's okeh of the report before then. He also seemed quite unwilling to show us the schedules, etc., that would go into the report. Very soon thereafter, Foley and I were called to Mr. Taylor's office, Mr. Taylor having received ~~the~~ a call from Green of the Munitions Board. I again explained our position in the matter. Mr. Taylor asked why we could not approve the report as submitted, subject to final check when we received the schedules and other information. I pointed out the difficulties involved. Mr. Taylor then called Green and said that Bernstein would get in touch with him on Tuesday to be shown the additional information which Bernstein wished to see. On Tuesday, I telephoned Mr. Green and was referred to Mr. Allen. I went over to see Allen and he showed me the completed schedules. I asked who had prepared the chapters on pending litigation and he said that the chapters were prepared by the Munitions Board, the cases are handled entirely by Justice and that the files of the Munitions Board on the pending cases are not complete.

The next morning Mr. Barnes of the National Munitions Control Board brought over to me the copies of the completed chapter containing all the schedules, etc., and asked that I let the Munitions Board know that day what the Treasury's position was on the matter. That afternoon I telephoned Allen and advised him I was unable to conclude the examination of the matter. During the following day I prepared a memorandum from Foley to the Secretary, setting out three points to be considered. Foley signed the memorandum and agreed with my suggestion that it clear through Messrs. White and Taylor.

On Tuesday, December 27, Foley told me that Mr. Taylor was to see Green at 11 o'clock and I was to be present at the conference.

I discussed with Foley what should be the Treasury's attitude on the matter and the desirability of discussing it with Mr. Taylor before speaking to Green. Foley and I went in to see Mr. Taylor. Mr. Taylor called Green in immediately thereafter and read to him points 1 and 2 of the memorandum which I had prepared from Foley to the Secretary. In response to point 1, Green said that this point had been fully considered, that the exports to Germany were entirely legal and that he had discussed the matter with Solicitor General Jackson who said that the argument that the exports were not legal were "legal rubbish". Mr. Taylor said in view of that he would not press the point further. With respect to point 2 I was asked to point out some of the objectionable statements which I did. Mr. Taylor said that, we having made such suggestions to Mr. Green, we would leave it up to Mr. Green to decide whether or not to eliminate the statement. Mr. Taylor asked Green whether the chapter on pending litigation, etc. had been taken up with the Department of Justice and Green said that every word in the chapter except a few words had been written by the Department of Justice. Mr. Taylor also asked Green whether he thought the chapter on helium should be shown to Secretary Ickes and Green said that the chapter had been boiled down to its bear essentials, that there was nothing controversial in it and that there was no point in showing it to Interior lest the matter be stirred up again.

The conference ended around 12 o'clock. Mr. Taylor told Green that he would let Green know by one o'clock what the Treasury's position was in the matter. After Mr. Green left, I suggested to Foley that he call Jackson and he agreed as did Mr. Taylor. Foley tried to get Jackson who was out of town. Jackson couldn't be reached until after [illegible] o'clock. Foley told me that Jackson said he had not had any conferences with Green, that the only time he had met Green was once, socially that he had never told Green that the exports were legal; that Jackson was acquainted with the problem that on such an important problem he could not have given a snap answer, and that his inclinations were in the direction of holding the exports to have been illegal. Foley told me that he had also advised Mr. Taylor of his conversation with Mr. Jackson and that Mr. Taylor had told Green of the same. Around 2:30 Foley and I went in to see Mr. Taylor and again we discussed the matter and I pointed out a number of reasons why I thought that before the Treasury okehed the report some changes should be made in the chapters on pending litigation and we should inquire of the State Department as to whether it had an opinion on the legality of exports to Germany. Mr. Taylor then telephoned Mr. Green that the report was okeh.

(initialed) BB

[illegible]

Carbon copy to Mr. Hanes on April 7, 1939

April 7, 1939.
10:11 a.m.

John Hanes: O. K. Now go ahead.

HMJr: Johnny, last night late I talked to both Delano and Upham to post myself on this bank business, see?

H: Yeah.

HMJr: Now, what I'd like to ask - I haven't got it clear yet - either you or Foley, by giving me some information, could make it very simple for me, I think, to interpret what the President had in mind. When we wrote that letter, was it in September or October, the Bank of America telling them not to pay a dividend?

H: That was a telegram, Henry, that was sent on -- sometime in September.

HMJr: Right. Well now......

H: Around the middle of September.

HMJr: All right. Now, this is what I want either you or Foley to answer me: When we did that, did we have in mind one -- to keep them from impairing their capital stock or, two, did we tell them not to do it because we thought it was an unsafe or unsound banking practice? Which one of those two things did we have in mind?

H: Ed says from an unsafe -- keep them from doing an act that was unsafe and unsound banking practice.

HMJr: That's what we had in mind?

H: Well, but that -- that was because, however, as I understand it, Henry, -- it was because, by paying the dividends they would lower the ratio of capital to deposits, so it was really -- it was really -- the fundamental part about it was that they were reducing their capital, or impairing their capital by paying a dividend, and that became the unsafe and unsound practice.

HMJr: But that was what we had in mind?

H: Now wait a minute. Now, Ed says I'm not right.

HMJr: Could I talk to Ed?

H: Yeah. Yeah, Just a minute.

(Brief pause while Ed Foley takes over conversation.)

Ed Foley: Yes, Mr. Secretary.

HMJr: Would you interpret for me what was the purpose of sending that telegram last September or October -- I mean, as far as the banks were concerned. What -- what did the Comptroller have in mind?

F: Well, the Comptroller had in mind, as I remember it, the declaration of a dividend.....

HMJr: Yes.

F: ......which, in his opinion, would constitute an unsafe and unsound banking practice.

HMJr: I see. Well, then to try to interpret what the President had in mind, because he said he wanted to justify our position of last fall, then I would say that this part of the letter "would constitute unsafe or unsound banking practice" should be included in the letter.

F: Absolutely. I don't think the letter means anything unless you include that, because I understand you want to be consistent with the position which you took last September.

HMJr: That's what the President said.

F: Yes. That's what the President's position is.

HMJr: That we should be consistent with what took place last fall.

F: That was what I understood from the conversation yesterday morning.

HMJr: Well then -- then would you have also -- would it read, "declaration of such dividend would impair the capital stock of the banks, all would constitute an unsafe...." Would you leave that "all" in?

F: No, I would -- I -- I included both things, Mr. Secretary, because I understood both things to be mentioned. In my mind, the two are quite different, and if I were doing it, I would leave out the impairment of the capital and merely say, "the declaration of the dividend, which, in the opinion of the -- any one of the agencies involved, would constitute an unsafe and unsound banking practice."

HMJr: Well, let's leave the question of -- of the agencies for a moment.

F: Yes, sir.

HMJr: But if -- from what you tell me, and -- I am at a considerable disadvantage......

F: Yes.

HMJr: ......at this end. I got what the President had in mind. He wanted to make our position of last fall consistent.

F: That's right.

HMJr: Now, from what you tell me, in order to make it consistent -- hello?

F: Yes.

HMJr: That the best way to cut the dividends -- the letter ought to read, "The best way to cut the dividends, would constitute an unsafe, unsound banking practice."

F: That's right. You see it's -- it's illegal for a bank to impair its capital by the declaration of a dividend. That's against the law.

HMJr: Yeah.

F: So if you merely say that, you're asking them to do what the law requires them to do.

HMJr: Yeah.

F: Now, the Comptroller believes that a ratio of net sound capital to deposits of one to ten is sound banking, and if they declare a dividend that would be in violation of that ratio, it would constitute an unsafe and unsound banking practice in the -- in the judgment of the Comptroller. But it might not be an impairment of capital such as would constitute a violation of criminal law.

HMJr: What I said yesterday -- I mean, thinking back -- I mean, what the President said -- he wanted this thing consistent to what we did last fall......

F: Yes, sir.

HMJr: ......so how would you write the letter with that in mind?

F: Well, if it was -- if it -- with that in mind, I'd say, "That if, in the determination of the Comptroller of the Currency, the declaration of the dividend in the future would constitute an unsafe and unsound banking practice, the Board of Directors should agree that that dividend would not be declared."

HMJr: Well now, say without -- I'll discuss which agencies are involved in a minute.

F: Yes.

HMJr: But that makes sense to me now. Let me see whether that makes sense to Hanes.

F: Yes.

(Brief pause while John Hanes takes over conversation.)

Hanes: Hello.

HMJr: Hello.

H: Henry, my position on that is that I don't think it's of very great importance in the first place, because of the fact that an unsafe and unsound practice could only be unsafe and unsound, in my opinion, if it were -- if, by paying a dividend, it did impair the capital.

HMJr: Yeah.

H: Now, I can't conceive of our entering into the business of any organization to the extent of determining the policy to the extent that we say, "You shan't pay a dividend, even though your capital is perfectly sound, and your ratio is perfectly good." So, an unsafe and unsound practice, to my mind, simple as it is, seems to me to constitute a question of whether or not, by the payment of the dividend, you impair your capital thereby. That's -- that's all my position. I don't think it's of very great importance how you say it in this letter, because I think it's going to -- I think -- I think what Giannini has agreed to in his letter to us, constitutes a contract on his part that he is not going to impair his capital by paying a dividend and if he -- if, by paying a dividend, he would impair his capital, he's going to make arrangements to get new capital in the bank.

HMJr: Well, if you don't mind, I differ with you.

H: Well, I don't mind a bit in the world. I just -- I just don't -- I don't see the difference -- the distinction between unsafe and unsound banking practice. We have no right to tell a man when he can pay a dividend, as I see it, except -- and if he pays the dividend he impairs his capital.

HMJr: Well, don't we have a right to tell a man that he shouldn't pay a dividend if we think it's unsafe and unsound banking practice?

H: Well, what would constitute unsafe and unsound practice about paying a dividend if his capital ratio was perfectly good? What could possibly do it? I just don't see that.

HMJr: Well, of course, I think that that's just what he's been doing.

H: Well, I do too. I do too. I agree with you -- I agree with it, but if I say to you......

HMJr: If I may -- if I may finish a minute.

H: Yeah.

HMJr: I think what he's been practicing is unsafe and unsound banking.

H: Because what?

HMJr: What?

H: I say, because of what? Because, by paying a dividend, he's impairing his capital?

HMJr: Well, by paying -- he's risking the depositors' -- his depositors' money.

H: That's right, because his capital is not -- not at the ratio that we have set down, or one to ten.

HMJr: No, his capital might theoretically be ten to one, but it might be so frozen that he couldn't pay it out.

H: That's -- that's perfectly true. In that case we would classify those assets and move them aside in a classified group and write them out of his capital, so it would reduce his capital.

HMJr: But that's what we've been unable to do, in his case.

H: Well, we -- we've been unable to do up until now, but as it is now -- as it stands now, we are not unable to do it because we've got a good record to go before the Federal Reserve in the section 30 case now.....

HMJr: We have now.

H: We have now, whereas in September we did not have.

HMJr: Well, of course, that's the thing that has always bothered me, you see?

H: Yes.

HMJr: But if you don't think it's important......

H: I don't, and I -- and I'm not -- I'm not arguing against your putting it in there....

HMJr: Well......

H: ......for any other reason except that I -- I want to get -- I want to get him to agree that -- I think the crux of this whole situation is to get Giannini to agree to put capital in the bank which will bring his ratio up to one to ten. I think that's the important thing and I think anything we do which is going to handicap us getting to that goal is just going to make our task about ten times more difficult than -- than is necessary.

HMJr: Well, now Johnny......

H: Yes, sir.

HMJr: You say you don't think it's important.

H: Yes, sir.

HMJr: I haven't raised it. I've never heard the President more insistent, and all I'm trying to do is, as I remember it, he said he wanted to make this thing consistent with what we tried to do last fall.

H: All right.

HMJr: Now, from what Foley tells me, in order to make this thing consistent, I think we ought to put in the words, "would constitute unsafe and unsound banking practice."

H: Well, I -- I think that -- I -- that's perfectly all right with me. I'd like to go on record though as just being opposed to putting it in because I think it will stop him from signing it. That -- that's the reason I'm -- I'm opposed to putting it in, because I don't think he'll sign it on that basis.

HMJr: This is -- this is my position.....

H: Yeah.

HMJr: I want to -- to the best of my ability and intelligence interpret what the President wanted.

H: That's right.

HMJr: And so do you.

H: That's right.

HMJr: Now, let's do it that way. The President will be back Monday.

H: Yes, sir.

HMJr: If, during the week, Mr. Giannini balks and so forth and so on, we can bring it over to the President, put it on his desk and see what he says then.

H: All right.

HMJr: But I don't want to find myself in a position to have the President say, "Well, I told you three times what I wanted; why didn't you do it my way"?

H: Right.

HMJr: And I'm sure you don't want to either.

H: I am sure I do not, no.

HMJr: And this has been going on now for months anyway, and what I was trying to do was -- not having followed the thing, was to make it the word consistent, and that's what he wanted. Now, if we reach the point, and they find that they can't, why all of us can go across the street -- the people involved -- and put the case to the President. I tried my best to put the case to him, but I wasn't given an opportunity.

H: I understand that, yeah.

HMJr: I tried my best to explain the difficulties, and what was involved, and so forth, and I appreciate also that if -- what it means to Preston Delano in order to do this and accomplish it when Mr. O'Connor couldn't, and I want to hold up Preston Delano's hand all I can, you see?

H: Sure.

HMJr: But, I'd much rather have the President recede than have him say, "Well, Henry, you didn't carry out this affair to what I asked you to do."

H: Well, certainly I -- you know I don't want to do that.

HMJr: Now, are you in accord with that? You don't want to protest against that, do you?

H: No, and I don't want to protest against anything. I just want to -- I was just trying to be practical about it.

HMJr: I -- I think that -- I -- I understand fully. I understand what you've been through. I know how difficult this man is and everything else. I -- I was prepared to accept it. I didn't like it, but I was prepared to accept it because I felt that after months that this was the best that you fellows could get. But now we've got something new.

H: Right. Well, Henry, I tell you, I wouldn't feel -- I wouldn't even make a statement about it in one way or the other, because I really don't think it's important and I think we could have gotten yesterday -- we could have gotten Giannini to sign anything, because he was coming good. Today I don't think you can get him to sign anything because he's sore as hell about the S.E.C.'s latest attack on him.

HMJr: Oh!

H: They've attacked him from two fronts now, again, and I think that's made him sore as hell, and I'm not sure he isn't going to back up on us all the way along the line.

HMJr: Well.....

H: And they say -- then -- he's now threatening to take his bank and make a State Bank out of it which would give the Comptroller's office a hell of a black eye.

HMJr: Well, all you'll have to -- I've asked you to handle it with these people. I haven't tried to interfere in the negotiations, have I?

H: Not a bit in the world, no.

HMJr: And I tried my best to explain it and I wasn't given a chance.

H: Right.

HMJr: Now......

H: Well now, you've got -- you've got my support a hundred per cent in trying to get what the President wants, and if this is what he wants, I'll go and try like hell to get it, but.....

HMJr: This -- this is what I would understand what he wanted to make the thing consistent with what we tried to do last fall.

H: Right.

HMJr: Now, you know I've kept him posted right along so the thing -- he has the thing in his mind.

H: Right.

HMJr: And so if you would -- do you have to send it down to me again, or.....

H: No, no. I don't think we'll have to send it. I understand now we'll just -- everything you've decided now -- everything except which one of the agencies you want to put in the letter.

HMJr: Well now, this was my thought. This is again -- I mean, I don't feel -- I'm not at all sure on my ground on this; I was on the other -- trying to interpret what he had, see?

H: Yes.

HMJr: My thought was the Comptroller and F.D.I.C., but I don't feel at all -- I don't know -- I wouldn't know how to interpret what he wants.

H: Well I -- I think -- I don't know how Ed feels about that. I'll abide by his judgment on that, and that -- there again, I don't feel very strongly about it, since -- again the practical side of it is, as I understand it, the Comptroller's office makes the examination. The other two agencies are then furnished a report of the Comptroller.

HMJr: Yes.

H: If they had any complaint to make about the report, either from the guarantee's side or from the Federal Reserve side, they come to the Comptroller and say, "Here's our complaint; here's our trouble. Let's go after this fellow on this point, or that point, or the other point." So it's really, in the last analysis, the Comptroller of the Currency who examines the bank.

HMJr: Yeah, but don't forget, it was the F.D.I.C. that started this whole thing because they were bothered about -- what was it?

H: Well......

HMJr: Half of their capital, or......

H: Oh yes. I guess there's a good deal of it -- is at stake.

HMJr: Was insured.

H: Now, I haven't any feeling about that. If you want to leave the letter just exactly like it is, it suits me perfectly, and I'll try my best to get him to sign it. As I say, I......

HMJr: Well, I don't think -- I don't think the Board of Governors of Federal Reserve should be in it.

H: You don't?

HMJr: No. Because they themselves said when this thing was to come before them that they'd only act after it happened.

H: Ed says he would like to talk with you for just a second.

HMJr: Please.

(Brief pause while Mr. Foley gets on the wire.)

Ed Foley: Mr. Secretary, I -- I'd just as soon leave out the Federal Reserve Board also. I thought maybe you'd like to know why.......

HMJr: Yes.

F: ....we included the Fed.

HMJr: Yes.

F: We included the three agencies that had powers of examination of the Bank.

HMJr: Yes.

F: And if, in the opinion of any one of the three agencies after an examination of the Bank, they found things that they didn't like, they could take disciplinary action. Now, in order for a National Bank to become a member of the Federal Reserve System, the -- the bank has to agree to comply with the National Banking laws, and one of the provisions of the National Banking laws is that the capital of a National Bank may not be impaired by the declaration of dividends.

HMJr: Yes.

F: So, I assume if, after examination of the bank by the Fed, that they found that the dividend policy was impairing the capital of the bank, they could kick them out of the system. And that was the only reason that I included them. Now, I think the two important agencies are F.D.I.C., which can withdraw insurance, and the Comptroller of the Currency.....

HMJr: The President......

F: ......which can close them up.

HMJr: The President mentioned all three.

F: Yeah. Well I -- I just -- just explained the -- the reasoning that I was following in including the three supervisory agencies.

HMJr: Well, under the circumstances, I think your reasoning is good, and I'd leave all three.

F: All right, sir.

HMJr: Well then, if you leave all three, then you'll leave in the words, "declaration of such dividend would impair the capital all would constitute --" you'd leave all that in there, wouldn't you?

F: Well, yes. I'd leave it all in. I think that -- that the important thing is the "unsafe and unsound banking practice."

HMJr: Yes, but if the "declaration of such dividend would impair the capital --," that's the part where the Federal Reserve comes in.

F: That's right.

HMJr: Then I would leave it in.

F: It doesn't do any harm.

HMJr: Well then -- I mean......

F: I mean, that's why I have it in there, you see? -- in the first place, but the important thing is "would constitute unsafe and unsound banking practice." Because that's the -- that -- that deals with the jurisdiction of the agency -- supervisory agencies insofar as taking disciplinary action is concerned. That's the -- that's over and above act u a l compliance with law.

HMJr: Well, I -- what I -- this is my suggestion. I would leave the letter as it was written, taking the brackets out, but in view of the fact that both the Fed. and the Comptroller are mentioned, I think the letter should be shown to them by Mr. Hanes, and that both the Fed. and the Comptroller should be posted as to what -- why the President wants this accepted, and then let them see the letter and let them -- le t their attorneys see the letter and see if they have any suggestions to make.

F: I think that's a good suggestion.

HMJr: What?

F: I think that's a good suggestion.

HMJr: And I'd rather take an extra day and let them see it, and so forth and so on.

F: Yes.

HMJr: Now -- what do you think of that?

F: That -- I think that's the way to do it, sir.

HMJr: All right. Now, may I talk to Hanes again?

F: Yes.

(Hanes takes over the conversation.

John Hanes: Hello.

HMJr: Johnny....

H: Yes, sir.

HMJr: Now, I want to sort of skip from this, you see?

H: Yes, sir.

HMJr: I just wonder whether in suggesting these three agencies, the President doesn't go back to the suggestion which he has in mind that there should be a board composed of these three agencies, with an assistant Secretary of the Treasury sitting on it who would be in charge of bank examination. And that's one of the -- I mean, I was asking the Comptroller last night about this so-called Brown Bill.

H: Yes.

HMJr: I mean, I wondered if he didn't maybe have that in mind.

H: Well I -- I don't know. You remember sometime ago you told me that the President had made some statement to you about his ideas on this subject of -- of consolidating the functions of some of these agencies.

HMJr: Yeah.

H: Now, I don't know whether that's what he's got in mind or whether he's for the Brown Bill or whether he even knows the Brown Bill is in or not. We have no inclination here at all on it, as far as I know.

HMJr: Well, the way that this thing now stands, with the suggestion I made, I wonder whether Gaston or McReynolds have any suggestions.

(Slight Pause)

Herbert Gaston: Hello.

HMJr: Hello.

G: I -- I agree to the form in which the letter is drafted. I think it's an excellent idea to show it to the other agencies, but it seems to me that it's a very desirable thing to -- to get it signed, if it can be done.

HMJr: Yes, I -- I don't -- I don't -- I have no opinion whether he will or won't sign it; all I'm trying to do is to be a good soldier.

G: Yeah. Yeah.

HMJr: And I realize that the Bank of America is important, but I don't feel that this is -- well, I just don't -- well, in this case I -- I want to do what the President wants.

G: Right. Yeah. Well, I -- my feeling is that what the President wants is the right thing to do. I am very much afraid that this man will just slip entirely out of our hands unless something of this sort is -- is incorporated in it.

HMJr: Yeah. Well, I'm -- I'm afraid you're right, but the other people don't think so.

G: Um-hm. Well, that's just a -- that's just a guess. I'm not -- I'm not intimately familiar with it.

HMJr: I'm just going on previous experiences, and maybe I'm wrong.

G: Yeah. Yeah.

HMJr: I say, I've never met the people, so I don't know what...

G: No.

HMJr: ......what they're like.

G: Nor have I.

HMJr: While I have you on the phone -- anything else?

G: No, I -- I don't think of anything else at all.

HMJr: How does Mac feel about it?

McReynolds: Well, I don't -- I haven't got much opinion on this Giannini end of it. I don't know what can be done. I don't know what is practical. On the organization end of it I'm definitely opposed to consolidating, or taking the National Bank examination out of the present Comptroller's office and consolidating it with the F.D.I.C. organization. I think that's illogical; it's a different system; it couldn't -- I don't think there would be any, either economy or advantage, or any sense of it.

HMJr: Well, that's that. Anything you want to tell me?

Mc: No, no. Nothing.

HMJr: O. K. then, Mac. Can I have.......

MC: All right, wait; Herbert's got something else he wants to tell you.

(Slight pause)

Gaston: Off of this subject entirely, did you have any suggestions......

HMJr: Turn off that light, there's no use making a record.

FEDERAL RESERVE BANK

OF NEW YORK

April 7, 1939

Dear Mr. Secretary:

The volume of offerings in the market for new corporate securities increased during the past week, as the first two of the several large issues scheduled to reach the market during April were advertised. On Wednesday $24,000,000 of Commonwealth Edison Company 3 1/2 per cent convertible debentures of 1958 were offered at par. These debentures, the proceeds of which will be used for refunding purposes, were rated A by Moody's. Although the offering is subject to prior sale through the exercise of rights, offered to stockholders as of record March 24, banks were reported to be making commitments, should any of the debentures remain after the subscription rights expire April 28. It is doubtful, however, that there will be any remainder, since the bonds offered at par are identical with outstanding obligations selling between 104 and 107. Later in the week Eastman Kodak Company stockholders, as of record April 6, received rights to subscribe to 225,092 shares of common stock at $127.50 a share. (The common stock of this company is presently selling at about $145.00 per share.) The net proceeds of the issue, rights to which expire April 27, will be used for plant improvement and for additional working capital to be used gradually over an indefinite period. A $505,000 preferred stock issue of a shoe company for new capital purposes brought total corporate financing during the past week to $53,200,000.

Unless the repercussions of European conditions on our markets become so serious as to make advisable postponement of scheduled offerings, new corporate financing should assume even larger proportions during the coming week. The $40,000,000 issue of Texas Corporation 3s of 1959 and the $22,300,000 Consolidated Gas, Electric Light, and Power Company of Baltimore preferred stock should appear early in the week, and should be followed by the $62,500,000 Gatineau Power Company issue of 3 3/4s of 1969. As mentioned previously, corporate issues scheduled for the entire month of April are likely to amount to at least $250,000,000, of which $70,000,000 will represent the raising of new capital.

New municipal bond awards this week totaled about $3,400,000, of which $2,800,000 was for new capital. Next week $17,500,000 Port of New York Authority bonds are expected.

Yours faithfully,

Allan Sproul,
First Vice President.

Hon. Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington, D.C.

April 8, 1939.

Return to Room 285

Dear Mr. Sproul:

As the Secretary is still away from the office, I am acknowledging your weekly letter dated April 7th. We expect Mr. Morgenthau in the office the first of the week, and I am sure he will be most interested in studying your surveys.

Sincerely yours,

H. S. Klotz,
Private Secretary.

Mr. Allan Sproul,
First Vice President,
Federal Reserve Bank of New York,
New York, New York.

GEF/dbs

CHANGES IN COTTON HOLDINGS BY PERIODS

	Commodity Credit Corporation		Cotton Producers' Pool	
	Bales	Amount	Spot	Future
Holdings to June 29, 1936	3,556,921	$240,155,429	155,067	118,100
Changes July through December 1936	- 536,497	- 36,261,626	-155,067	-118,100
Changes January through June 1937	- 1,315,964	- 88,648,898	-	-
Changes July through December 1937	4,068,424	181,235,152	-	-
1938 January	720,116	30,883,663	-	-
February	172,470	7,302,367	-	-
March	43,778	1,891,566	-	-
April	145,087	6,267,108	-	-
May	21,674	878,577	-	-
June	47,428	2,140,382	-	-
July	40,838	1,817,361	-	-
August	- 2,680	2,987,196	-	-
September	13,278	647,598	-	-
Oct. 1	97,771	11,948,545	-	-
8	409,915	19,406,556	-	-
15	429,033	20,019,599	-	-
22	445,359	20,932,238	-	-
29	407,258	18,749,608	-	-
Nov. 5	321,532	14,779,060	-	-
12	211,112	9,735,400	-	-
19	280,616	12,913,940	-	-
26	260,866	12,193,291	-	-
Dec. 3	181,876	8,469,011	-	-
10	176,007	7,957,448	-	-
17	131,472	5,993,824	-	-
23	87,816	3,952,169	-	-
31	171,743	8,155,244	-	-
Jan. 7	101,369	4,674,091	-	-
14	114,014	5,103,770	-	-
21	104,287	4,836,198	-	-
28	74,135	3,470,151	-	-
Feb. 4	156,354	7,385,944	-	-
11	43,130	2,072,533	-	-
18	36,756	1,708,930	-	-
25	29,876	1,497,438	-	-
Mar. 4	22,901	1,044,113	-	-
11	16,330	757,144	-	-
18	12,607	574,647	-	-
25	18,443	817,144	-	-
Apr. 1	8,092	365,501	-	-
Holdings to April 1, 1939	11,325,543	560,809,432	-	-
Held by Commodity Credit Corporation	4,983,239	274,082,338	-	-
Held by banks	6,342,304	286,727,094	-	-

ril 7, 1939.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 7, 1939.

TO Secretary Morgenthau

FROM E. H. Foley, Jr.

For your information

Attached is a copy of Mr. Bernstein's memorandum for the file in regard to the Munitions Board annual report for 1938. On page 2 is contained the reference by Mr. Green to his alleged conference with Solicitor General Jackson concerning the legality of the issuance of licenses for arms exports to Germany.

My recollection is that Mr. Taylor subsequently informed me that Mr. Green's explanation was that he had talked with Judge Townsend in Solicitor General Jackson's office and was wrong when he said that he had talked to Solicitor General Jackson personally.

E.H.F.Jr.

Attachment

January 3, 1939

MEMORANDUM

Re: Munitions Board Annual Report for 1938

Within a few days after the receipt of the State Dept letter of December 17, 1938 and the draft of part of the Munitions Board's Annual Report, the Munitions Board called the Treasury to ascertain whether the Treasury approved the report. The report had been sent to me and I felt there were several points on which the Treasury should consider the position that it should take. I advised Mr. Foley of the entire situation and on Friday, December 23, in response to a phone call from the Munitions Board, he called Mr. Yost of the Munitions Board and said we were studying the matter; that we could not complete our study until we had received completed copies of the Annual Report. The copy that had been furnished to us did not have the schedule of the statistical information which we desired to see. Mr. Yost repeatedly stated in his telephone conversation that the Board would not be able to have the report completed until shortly before the meeting on January 5 and that he would like to have the Treasury's okeh of the report before then. He also seemed quite unwilling to show us the schedules, etc., that would go into the report. Very soon thereafter, Foley and I were called to Mr. Taylor's office, Mr. Taylor having received a call from Green of the Munitions Board. I again explained our position in the matter. Mr. Taylor asked why we could not approve the report as submitted, subject to final check when we received the schedules and other information. I pointed out the difficulties involved. Mr. Taylor then called Green and said that Bernstein would get in touch with him on Tuesday to be shown the additional information which Bernstein wished to see. On Tuesday, I telephoned Mr. Green and was referred to Mr. Allen. I went over to see Allen and he showed me the completed schedules. I asked who had prepared the chapters on pending litigation and he said that the chapters were prepared by the Munitions Board, the cases are handled entirely by Justice and that the files of the Munitions Board on the pending cases are not complete.

The next morning Mr. Barnes of the National Munitions Control Board brought over to me the copies of the completed chapter containing all the schedules, etc., and asked that I let the Munitions Board know that day what the Treasury's position was on the matter. That afternoon I telephoned Allen and advised him I was unable to conclude the examination of the matter. During the following day I prepared a memorandum from Foley to the Secretary, setting out three points to be considered. Foley signed the memorandum and agreed with my suggestion that it clear through Messrs. White and Taylor.

On Tuesday, December 27, Foley told me that Mr. Taylor was to see Green at 11 o'clock and I was to be present at the conference.

I discussed with Foley what should be the Treasury's attitude on the matter and the desirability of discussing it with Mr. Taylor before speaking to Green. Foley and I went in to see Mr. Taylor. Mr. Taylor called Green in immediately thereafter and read to him points 1 and 2 of the memorandum which I had prepared from Foley to the Secretary. In response to point 1, Green said that this point had been fully considered, that the exports to Germany were entirely legal and that he had discussed the matter with Solicitor General Jackson who said that the arguments that the exports were not legal were "legal rubbish". Mr. Taylor said in view of that he would not press the point further. With respect to point 2 I was asked to point out some of the objectionable statements which I did. Mr. Taylor said that, we having made such suggestions to Mr. Green, we would leave it up to Mr. Green to decide whether or not to eliminate the statement. Mr. Taylor asked Green whether the chapter on pending litigation, etc. had been taken up with the Department of Justice and Green said that every word in the chapter except a few words had been written by the Department of Justice. Mr. Taylor also asked Green whether he thought the chapter on helium should be shown to Secretary Ickes and Green said that the chapter had been boiled down to its bear essentials, that there was nothing controversial in it and that there was no point in showing it to Interior lest the matter be stirred up again.

The conference ended around 12 o'clock. Mr. Taylor told Green that he would let Green know by one o'clock what the Treasury's position was in the matter. After Mr. Green left, I suggested to Foley that he call Jackson and he agreed as did Mr. Taylor. Foley tried to get Jackson who was out of town. Jackson couldn't be reached until after 1 o'clock. Foley told me that Jackson said he had not had any conference with Green, that the only time he had met Green was once, socially; that he had never told Green that the exports were legal: that Jackson was acquainted with the problem; that on such an important problem he would not have given a snap answer, and that his inclinations were in the direction of holding the exports to have been illegal. Foley told me that he had also advised Mr. Taylor of his conversation with Mr. Jackson and that Mr. Taylor had told Green of the same. Around 2:30 Foley and I went in to see Mr. Taylor and again we discussed the matter and I pointed out a number of reasons why I thought that before the Treasury okehed the report some changes should be made in the chapters on pending litigation and we should inquire of the State Department as to whether it had an opinion on the legality of exports to Germany. Mr. Taylor then telephoned Mr. Green that the report was okeh.

BB

April 7, 1939.

Secretary Morgenthau

E. H. F ley, Jr.

For your information

Attached is a copy of Mr. Bernstein's memorandum for the file in regard to the Munitions Board annual report for 1938. On page 2 is contained the reference by Mr. Green to his alleged conference with Solicitor Gener 1 Jackson concerning the legality of the issuance of licenses for arms exports to Germany.

My recollection is that Mr. Taylor subsequently informed me that Mr. Green's explanation was that he had talked with Judge Townsend in Solicitor General Jackson's office and was wrong when he said that he had talked to Solicitor Gene l Jackson personally.

Attachment

EHF/akm 4-7-39

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 7, 1939.

TO CONFIDENTIAL FILES

FROM L. W. Knoke

SUBJECT: TELEPHONE CONVERSATION WITH BANK OF FRANCE.

Mr. Cariguel called me from his country home near Paris at 11:15 this morning to find out whether we had bought any francs for him. I replied "No" and added that there was very little going on in our market. Would I phone him if anything special developed (his number is Moret 170)? He would be away from Paris until Monday night.

LWK:KW

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: April 7, 1939, 1 p.m.

NO.: 671

FROM COCHRAN.

This morning unofficial exchange trading here was nervous. A considerable amount of dollars as well as sterling had to be given up by the French control due to reports on the news ticker that Italy had moved against Albania. At noon when word was received that an economic committee was en route from Tirana to Durazzo to consult with the Italians, the pressure tightened.

BULLITT.

EA:LWW

Office of the Postmaster General
Washington, D.C.

April 8, 1939.

The Honorable

The Secretary of the Treasury.

My dear Mr. Secretary:

Reference is made to your letter of March 29, transmitting copy of a cable note received from the British Treasury on the "Despatch of Gold Bars by Post".

Upon careful consideration of the representations made by the British Treasury and of those made by representatives of your Office in conference, I have promulgated a regulation of this Department, prohibiting the transportation in the regular mails or parcel post from any foreign country into the United States of any consignment of gold coin, gold bullion, or gold dust, having a value in excess of $50. A copy of the relative order is enclosed.

This Department will advise the Bureau of Customs of the notices given the foreign countries of the prohibition.

Very truly yours,

Acting Postmaster General.

Enclosure.

IH G-

POST OFFICE DEPARTMENT

Washington

April 8, 1939.

ORDER NO. 12761

Section 2233 of the Postal Laws and Regulations is amended, effective upon the giving of due notice to the respective countries, so as to add paragraph 3, as follows:

"3. The transportation in the regular mails or parcel post from any foreign country into the United States of any consignment of gold coin, gold bullion, or gold dust, having a value in excess of $50, is prohibited."

(Signed) Ambrose O'Connell

Acting Postmaster General.

April 10, 1939.

MEMORANDUM

To: Dr. Feis

From: A. Lochhead

Please forward the following cable to Butterworth from Treasury:

"Refer your 402, March 27th. Advise British Treasury of the following Post Office Order:

'POST OFFICE DEPARTMENT

Washington

April 8, 1939.

ORDER NO. 12761

Section 2233 of the Postal Laws and Regulations is amended, effective upon the giving of due notice to the respective countries, so as to add paragraph 3, as follows:

"3. The transportation in the regular mails or parcel post from any foreign country into the United States of any consignment of gold coin, gold bullion, or gold dust, having a value in excess of $50, is prohibited."

(Signed) Ambrose O'Connell

Acting Postmaster General.'

This subject was treated by the Post Office Department as an internal problem relating to the handling of packages after arrival in this country. Understand the cable notice of this order has been forwarded to French Post Office by United States Post Office."

A. Lochhead

April 12, 1939.

My dear Mr. O'Connell:

On behalf of the Secretary I am acknowledging your letter of April 8th, informing him of the promulgation of a regulation by your Department prohibiting the transportation in the regular mails or parcel post from any foreign country into the United States of any consignment of gold coin, gold bullion, or gold dust, having a value in excess of $50. We appreciate the action you have taken and your promptness in informing us of it.

Sincerely yours,

H. S. Klotz,
Private Secretary.

Honorable Ambrose O'Connell,
Acting Postmaster General,
Washington, D. C.

GEF/dbs

BK176

April 8, 1939

Secretary Morgenthau

Mr. White

Subject: Preliminary report on the possibilities of depriving the aggressor countries of needed strategic war materials.

Summary

What are the possible measures short of complete military blockade which could prevent the countries from obtaining necessary strategic materials?

You have suggested two possibilities for preliminary examination:

1. Purchase and accumulation by leading non-aggressor nations of strategic materials.
2. Prohibition by international agreement of exports of certain of these strategic materials to aggressor nations.

The aggressor countries and their allies (Germany, Austria, Czechoslovakia, Italy, Albania, Japan, Spain, Hungary, Manchoukuo, parts of China) would, in the event of major conflict, need imports of roughly $100 million per month of the following strategic materials:

Manganese	Rubber	Manila fiber
Copper	Petroleum	Tungsten
Tin	Nickel	Cotton

(There are several other items important strategically but not important quantitatively. Some of them will be taken up later.)

None of these commodities could be obtained in adequate amounts for the group as a whole except from countries outside those enumerated above.

In our opinion the measure -- if combined with the principle of the first proposal -- is effective, practicable, and relatively inexpensive. The real issue is whether it is yet politically feasible.

4/10/39 - Original to Secretary - Handed to President by Secretary.
Carbon to Miss Chauncey.

1. The first proposal is for the United States, either alone or together with Great Britain and France, and possibly some smaller countries, to accumulate large stocks of these materials and thereby reduce the world supply available to the aggressor nations.

A survey of the consequence of such a step leads us to the tentative conclusion that if taken alone its efficacy lies far more in its political implications than in its economic or military effects. It does not appear that this method will either prevent the aggressor countries from obtaining adequate materials to conduct a war nor will it raise the cost of the materials to the aggressor countries enough to embarrass them seriously.

The political importance of such a step is that the United States would be taking common measures with the democracies of Western Europe against aggression. Germany fears greatly the industrial and economic might of the United States actively placed on the side of the European democracies.

The proposal taken by itself has the following disadvantages:

(a) The aggressor countries would still be able to obtain enough of the most important strategic materials to carry on a war. The increased demand for those commodities would before long call forth increased supplies and at the same time curtail consumption for industrial uses. The price of those materials, would, it is true, increase substantially, yet not enough to reduce their foreign exchange resources sufficiently to interfere seriously with their purchases.

(b) Several of the aggressor countries doubtless have outstanding contracts which would provide additional stocks at current prices.

(c) The program would be expensive to democratic countries. In order to leave inadequate supplies for the aggressor nations they would probably have to purchase and withhold from the market at least $100 million of material a month and possibly twice that amount.

(d) It would disrupt markets for peacetime consumption of these commodities. In all of these materials the industrial uses are far more important quantitatively than military uses.

Though these disadvantages weigh heavily against the proposal solely as a device to deprive aggressor nations of needed materials serious consideration should be given to the accumulation of strategic materials by the United States on other grounds. In the event of war abroad, exports to the United States of certain vital raw materials from Asia may either be stopped or made subject to the will of Japan. Accumulation of certain vital raw materials should be undertaken not only to insure the amount of materials necessary for adequate defense, but to prevent our economy from being disorganized by the cutting off of the source of supply of needed raw materials as a consequence of a major war.

The materials which we must have and which we must obtain from areas vulnerable to foreign naval interference include tin, rubber, manganese, tungsten, manila sisal, mica and raw silk.

A one or two year supply of these materials could be obtained with an expenditure of about several hundred million dollars. Incidentally, increased purchases of that magnitude would help stimulate our exports. These purchases could be financed in any of several ways which would not involve an increase in the deficit.

2. The second proposal you wished to have examined is an attempt to secure an agreement among as many of the non-aggressor nations as possible to prohibit the exports to aggressor nations either directly or indirectly of as many of the important strategic materials as would be feasible.

A preliminary survey indicates that this proposal is feasible.

(a) The sources of supply of at least eight of the vital strategic materials which the aggressor countries (taken together) must import are almost completely under the control of the United States, the British Empire, France, Russia, Netherlands and Belgium. For several additional major items the inclusion of one or two more countries would make the control complete.

(b) The value of the imports by the aggressor nations of those materials is not so large as to make it impracticable for the leading non-aggressor countries to bear the expense or burden incident to such a program.

Methods of compensation or purchase can be devised which will eliminate opposition by small countries and private corporations based on fears of economic loss.

(c) The aggressor nations would be extremely vulnerable to what would virtually amount to an embargo of vital materials. Those countries must import substantial quantities of those materials not only to maintain their military strength but to prevent a sharp deterioration in their economy.

(d) In the case of nickel, tin and oil (if Russian and Mexican oil could be taken care of) relatively a few corporations control the international market and effective cooperation could be easily obtained.

The difficulties of the plan are:

(a) It would be essential to have the enthusiastic support of the British Empire and of Russia.

(b) England, France and Russia must be willing to give military guarantees to the smaller countries cooperating. This is particularly true of the Netherlands and Rumania.

(c) The great majority of the people of the United States must be in favor of that degree of American participation in foreign affairs involved in the plan.

(d) The principal argument that will be used against this measure is that its adoption would precipitate war.

(e) To be effective, the steps taken must be such as will prevent shipments of strategic materials from non-cooperating countries from reaching the aggressor nations.

(f) The period of negotiations should not be long enough to permit the aggressor nations to accumulate much larger stocks.

Conclusion:

In our opinion the measure -- if combined with the principle of the first proposal -- is effective, practicable, and relatively inexpensive. It is a measure which comes under the "quarantine-the-aggressor" principle of the President's Chicago speech. The real issue is whether it is yet politically feasible.

Any step in the direction of this proposal will have a powerful political effect in raising the morale and encouraging the democratic countries to make firm stand against further aggression. Even discussion -- if official -- of the proposal would be a help in that direction.

The following briefly outlines the situation with respect to the more important commodities:

A preliminary survey of the resources and needs of the aggressor nations indicates that none of them produces adequate amounts of many of the important strategic materials.

Germany, when fully organized for war, must either import, have substitutes for, or have stocks of the following essential raw materials:

95% of natural petroleum	10% of zinc	75% of wool
75% of copper	10% of rubber	70% of phosphates
50% of lead	95% of manganese	100% of tin
25% of sulphur	100% of nickel	100% of antimony
100% of cotton	100% of chromite	100% of mercury
95% of bauxite	95% of tungsten	100% of mica

Italy, Japan (and their allies) can supply Germany only with sulphur, zinc, lead, mercury and some copper.

The situation with respect to Italy is even worse and with Japan, equally bad. Japan must import:

35% of her iron	100% of her bauxite	100% of her wool
55% of her oil	50% of her zinc	75% of her potash
5% of her copper	100% of her rubber	75% of her phosphates
80% of her lead	50% of her manganese	90% of her antimony
80% of her cotton	100% of her nickel	75% of her tin
		90% of her mercury

Of these items her allies could supply Japan with nitrate, potash, zinc, lead and mercury.

These figures indicate that measures which would be ineffective against the British Empire, the United States or Russia are feasible against the present aggressor bloc.

Before any conclusions may be finally drawn with respect to the efficacy of any proposal, we need more information with respect to the stocks on hand in the aggressor nations and their needs during the conduct of a major war. We have some information on these points, but not enough.

(a) <u>Nickel</u>

The British Empire produces 95 percent of the total. Japan owns nickel ore mines in New Caledonia, but New Caledonia is under French control. Therefore, it would seem to be relatively easy to prevent the direct export of this metal to the aggressors.

(b) <u>Manganese ore</u>

This (according to the men in the Navy Department with whom I spoke) is one of the three most important of all the strategic materials. The chief sources of manganese are Russia (along the Black Sea), the British Empire, Brazil and Cuba. The best quality manganese comes from Russia. Numerous countries (see Appendix) produce small quantities.

Of these smaller countries, Rumania, Hungary, Bulgaria, produce approximately 80,000 tons, and Japan produces 70,000, Italy 25,000, making a total of approximately 200,000 tons that would be available to the aggressor countries from within their own group. Whether 200,000 tons a year would be enough to keep the aggressor powers adequately supplied is doubtful but we need more information on this point. Judging from the fact that the stock pile recommended for the United States by our military authorities is 1 million tons of ore, and that German imports were around 400,000 tons in 1938, an annual supply of 200,000 tons for all the aggressor nations seems inadequate.

(c) <u>Copper</u>

Leading copper producers are United States, the British Empire, Chile, Belgian Congo, Russia. These five groups together produce 90 percent of total world output. Japan, Yugoslavia, Spain and Germany together produce roughly 200,000 tons a year. Together, Japan, Italy and Germany imported double that amount in 1937.

(d) <u>Oil</u>

The United States, Russia, Venezuela, together produce 75 percent of total oil output. The British Empire, Iran, the Netherlands East Indies, Mexico, Colombia, produce an additional 10 percent. Italy produces virtually none; Germany and Japan together, about 8 million barrels, or less than 1/2 percent of the world output, Poland, 4 million barrels and Argentina, 17 million barrels.

HDW:lrs
4/10/39

Germany, however, produces a high grade synthetic fuel which is reported (by the War Department) to supply two-thirds of her current needs. To judge from the continued increase in petroleum imports from 1935 thru 1938 this is doubtful. Japan and Italy, however, so far produce only negligible quantities of synthetic fuel, though they are increasing their capacities. It appears that Germany cannot supply herself and certainly not the other aggressor countries. Germany is reported to have large stocks on hand.

In order to bar enough exports to the aggressors, the oil from Rumania, Mexico, Venezuela, Colombia and Russia would have to be included in the agreement.

In the case of oil there is another possibility that presents itself. It may be possible to operate through controlling companies. It would probably be found that a few large oil companies control the supply of oil even outside the United States, British Empire and Russia. Therefore the approach might be through the companies in those countries outside of the three mentioned.

(e) Tungsten ore

The bulk of tungsten ore is produced by China, British Empire and the United States. But Portugal produces 2 million tons (almost as much as the United States) and Germany is reported (by the War Department) to have accumulated an enormous stock pile equivalent to 60 percent of the world stock of tungsten ore which she obtained from China. More information would be necessary before you can conclude whether anything can be accomplished by the prohibition of tungsten from export.

(f) Tin

The aggressor nations produce very little tin. The British Empire, Bolivia, and the Dutch East Indies, Siam, China, produce 95 percent of the total tin output. Germany, Italy and Japan imported 20 percent of the 1938 output, and almost that in earlier years. If they do not have adequate stocks on hand and if the enumerated countries would agree to prohibit exports of tin we have here a commodity which might well lend itself to such agreement. According to the War Department it is of first rank importance for numerous uses in military purposes.

(g) Rubber

Germany, Italy and Japan produce no natural rubber. Their imports in 1937 constituted about 18 percent of the total world output of natural rubber. The British Empire, the French Empire and the Netherlands Empire together account for 94 percent of the total world output. The only two countries outside of these three empires that produce substantial quantities of rubber are Siam, which produces 4 percent, and Brazil, which produces 1 percent. It is reported that Germany will be 25 percent self-sufficient by means of synthetic rubber at the end of 1939 and 50 percent self-sufficient at the end of 1941.

(h) Cotton

Cotton linters are essential in the manufacture of powder. For Japan, Germany and Italy cotton would also be essential for their export industries and home consumption. These three countries imported 40 percent of the total world imports in 1937. The United States, the British Empire and Russia produce three-fourths of the world raw cotton. China did produce about 10 percent and a portion of that output is in areas under Japanese control. Brazil produces about 7 percent. It is very doubtful whether Japan or Italy have large stocks of cotton on hand, though it is reported that there were substantial stocks in Germany.

There are numerous other strategic war materials but either they are produced in adequate quantity among the aggressor nations (e.g., raw silk, sulphur, bauxite, optical glass) or they are very unimportant in total value (e.g., quartz crystal, molybdenum, etc.). In a more comprehensive report it would be necessary to study numerous of these minor commodities (for example, quartz crystal, is essential in radio equipment and is found only in Brazil; manila fiber has no substitute, is absolutely essential in merchant marine and is found only in the Philippines and Sumatra; mica has no satisfactory substitute for important electrical uses; only known sources India and Madagascar; hides and wool are essential important and costly items which the aggressor countries import in large amounts.

(Appended are some tables of source of supply and of imports of leading strategic war materials.)

HDW:lra
4/10/39

Rubber

	Present Production	Present Stocks	Apparent Consumption or imports in 1937
	(Long tons)		
Germany	-		115,008
Italy	-		24,820
Japan	-		62,182

Leading producers of rubber in 1937

Netherland Indies	431,646	British Empire	596,463
		Malaya	469,960
French Indo China	43,399	Ceylon	70,359
		Sarivak	25,922
Siam	35,551		
		North Borneo	13,213
Brazil	15,576	India	9,777
		Burma	7,232

JSH:lrs
4/10/39

Copper ore

	Present Production (In metric tons)	Apparent Consumption or Net Imports in 1937
Germany	28,000	263,000
Italy	417	80,000
Japan	100,000	210,000

Leading producers of copper ore in 1937

United States	760,000	British Empire	489,000
Chile	413,000	Canada	249,000
Belgian Congo	150,000	Northern Rhodesia	180,000
U.S.S.R.	93,000	Australia	20,000
Mexico	46,000		
Yugoslavia	42,000	Cyprus	17,000
		Union of S Africa	12,000
Peru	36,000	British India	11,000
Spain	30,000		
Norway	23,000		
Cuba	13,000		
Finland	12,000		
Sweden	8,000		

JSH:lrs
4/10/39

Tin

	Present Production (In long tons)	Apparent Consumption or Imports in 1937
Germany	100	15,800
Italy	443	4,618
Japan	2,210	11,000

Leading producers of tin in 1938

Bolivia	25,371	British Empire	61,773
Netherlands E. Indies	21,001	Malaya	43,247
Siam	13,616	Nigeria	7,305
China	11,250	Burma	3,990
Belgian Congo	7,316	Australia	3,600
		United Kingdom	2,000
Poland	1,819	Union of S.Africa	558
French Indo China	1,575	Uganda	374
Argentina	1,335	Southern Rhodesia	267
Portugal	800	Tanganiyika	263
		S.W.Africa	169

JSH:lrs
4/10/39

Nickel

	Present Production (in metric tons)	Apparent Consumption or Imports in 1937
Germany	300	14,000
Italy	-	2,500
Japan	-	8,000

Leading producers of nickel in 1937:

New Caledonia	6,830	British Empire	103,183
U.S.S.R.	2,000	Canada	101,963
Norway	1,505	British India	1,220
Greece	1,255		

JSH:lrs
4/10/39

Tungsten ore

	Present Production	Apparent consumption or imports
	(In metric tons)	
Germany	-	
Italy	-	
Japan	2,000	

Leading producers of tungsten ore in 1937

China	17,805	British Empire	7,675
United States	3,175	British India	5,300
Portugal	1,948	Malay States	1,200
Bolivia	1,802	Australia	900
Argentina	702	Southern Rhodesia	275

JSH:mh
4/10/39

Manganese ore

	Present Production	Apparent consumption or imports in 1937
	(In metric tons)	
Germany	242	
Italy	25,000	
Japan	70,000	

Leading producers of manganese ore in 1937

(In metric tons)

U.S.S.R.	3,000,000	Chile	5,000
Brazil	253,661	Bulgaria	3,000
Cuba	131,299	British Empire	2,132,881
French Morocco	79,113		
China	51,545	British India	826,498
Rumania	50,749	Union of South Africa	631,194
United States	43,000	Gold Coast	535,838
Hungary	25,000		
Philippines	12,206	Egypt	134,972
Netherland Indies	8,600	Northern Rhodesia	2,379
Sweden	6,000	Australia	2,000
Turkey	5,200		

JSH:mh
4/10/39

Crude petroleum

	Present Production	Apparent consumption or imports in 1937
	(In thousand barrels)	
Germany	4,300	40,000
Italy	109	17,500
Japan	3,614	35,000

Leading producers of crude petroleum in 1938

(In thousand barrels)

United States	1,212,530
U.S.S.R.	217,535
Venezuela	191,593
Iran	74,154
Netherland East Indies	60,165
Rumania	48,800
Mexico	38,861
Colombia	21,315
Argentina	16,900
Peru	16,045
Poland	3,790
British Empire	43,209
Trinidad	17,750
British India	9,648
Bahrein Island	8,361
Canada	7,450

JSH:mh
4/10/39

Raw cotton

	Present Production	Apparent consumption or net imports in 1937
	(In thousand bales)	
Germany	-	1,500
Italy	20	500
Japan	216	4,200

Leading producers of cotton in 1938

United States	18,746
China	3,600
U.S.S.R.	3,482
Brazil	2,205
Peru	424
Mexico	326
Argentine	281
Turkey	157
Iran	156
Belgian Congo	141
British Empire	7,697
British India	4,867
Egypt	2,282
Uganda	314
Egyptian Sudan	234

JSH:mh
4/10/39

585

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE April 8, 1939

TO CONFIDENTIAL FILES

SUBJECT TELEPHONE CONVERSATION WITH BANQUE DE FRANCE 12 F

FROM D. J. Cameron

Mr. Kogan of the Banque de France called at 11 am and inquired about the market. I informed him that the market was quiet with sterling at 468 1/8 and francs quoted at 264 13/16, which is the rate at which we can buy for him, but that no francs had actually been offered in the market. He said the Paris market was very small and that they had done nothing this morning; the feeling in general was a little better than yesterday. He mentioned that his order to buy francs was good for today and Monday, and said he would call us again on Monday at noon. However if something should happen, he would like us to call the Banque de France any time on Monday and speak with him or Mr. Cariguel.

DJC:BOC

DUPLICATE

STRICTLY CONFIDENTIAL

No. 170

286

Rangoon, Burma, April 8, 1939.

STRICTLY CONFIDENTIAL

SUBJECT: Shipments of war materials.

THE HONORABLE

THE SECRETARY OF STATE,

WASHINGTON, D.C.

SIR:

I have the honor to report that about 3,800 tons of war materials for China have now been shipped from Rangoon to Lashio, according to a statement made by an officer of the Southwest Transportation Company.

Freight charges collected by the Burma Railways on war materials transported from Rangoon to Lashio during the month of March amounted to Rupees 183,000 ($64,050 at present exchange).

The movement by motor truck of supplies from Lashio to Chefang, 24 miles across the Chinese frontier, and from Chefang onward, is in progress, but representatives of American motor-vehicle concerns who recently visited Lashio and Chefang assert that much time is being lost at both places through apparent lack of organization and coordination.

Road Transport Arrangements.

The Rangoon haulage contractor who is doing most of the transport work from Lashio to Chefang now has 185 Chevrolet trucks in service. Some of the Dodge trucks received from Hong Kong will probably be placed

on

on the Lashio-Chefang section by the Southwest Transportation Company. Transport onward from Chefang is said to be by Dodge trucks. It is reported that the road from Lashio to Yunnanfu will be divided into three or more sections for the transport of war materials, under the belief that, in the case of trucks, less wear and tear will result from shorter continuous journeys, and that driving efficiency will be increased through drivers becoming familiar with their respective stretches of road.

The Southwest Transportation Company has increased the storage capacity at Lashio to about 6,000 tons, by the erection of sheds for non-dangerous materials. Storage facilities for dangerous materials were provided by the Burma Railways some time ago.

Direct Shipments and Transhipments.

The Swedish steamship HUDIKSVALL, from Gothenburg and Brunshansen, which arrived here on March 27th; the German steamer WILDENFELS, from Hamburg via Amsterdam and Antwerp, which arrived on April 2d, and the German steamer CLAUS RICKMERS, from Hamburg via Antwerp, which arrived on April 6th, all carried some war supplies for China, but not full cargoes. The CLAUS RICKMERS, en route to Singapore and Manila, had a full cargo of arms and ammunition, but only 363 tons of it was for this port, the ship leaving here with 6,300 tons on board.

War materials for China continue to reach Rangoon via Singapore and Colombo, where they are transhipped. These shipments are relatively small, and the ships carrying them from European ports are unwilling to

make

make the journey to Rangoon to discharge them. It is reported that it has been found that transhipment expenses can be reduced nearly 50 percent by using Colombo instead of Singapore, and that future European and any American consignments not routed direct to Rangoon will be transhipped at Colombo. Some supplies from Hong Kong are still reaching Rangoon by way of Singapore.

Demand Shipment of High Explosive.

No further shipments of high explosive have been made from Rangoon to Lashio, and the considerable quantity still stored in the Rangoon River several miles below the port has become a worry to the port authorities, who are eager to get rid of it. They have now notified the Southwest Transportation Company that unless it is shipped any vessel arriving with additional supplies of explosive may be held and refused permission to discharge. The Chinese interests have stated that the principal need in China at present is for machine-guns and ammunition, and that anti-aircraft guns and ammunition are also wanted, and that priority in shipments is being given to such supplies. The high explosive still at this port includes some tetryl as well as TNT.

Secret Service Man in Charge.

The new local manager of the Southwest Transportation Company is a Chinese named Wong-Ping, who is also known as C. P. Chen. It is reliably stated that he is a member of the Chinese Secret Service. He came here from Singapore, where he was stationed for some time.

As previously reported, he has succeeded C. M. Chen, a former railway official, who has gone to Singapore, and who may later go to Colombo, to look after transhipments of war materials.

According to reports from the Southwest Transportation Company, steps are being taken to defend vital points on the Yunnan-Burma road, and shipments passing over the road, against aerial attacks, by the provision of anti-aircraft batteries and bomb shelters.

Respectfully yours,

Austin C. Brady
American Consul

Distribution:

1. Original and four copies to Department.
2. Copy to American Embassy, London.
3. Copy to American Consulate General, Calcutta.
4. Copy to American Consulate, Yunnanfu.

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MAY 12 1940

TREASURY DEPARTMENT
Office of the Secretary

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DUPLICATE

No. 168

Confidential

290

Rangoon, Burma, April 8, 1939.

CONFIDENTIAL

SUBJECT: American motor trucks for China.

THE HONORABLE
THE SECRETARY OF STATE,
WASHINGTON, D.C.

SIR:

I have the honor to report that American motor trucks for China are arriving in Rangoon. Four hundred Dodge truck chassis originally shipped to Hong Kong have been delivered here, and 225 cases of Dodge truck chassis and parts, weighing 726 tons, were discharged at this port by the American steamship WICHITA, which arrived here on March 27, 1939. Additional Dodge and many General Motors (GMC) truck chassis will reach Rangoon from the United States during the present month, on the American steamers PRESIDENT MONROE (April 10th), STEEL TRADER (April 14th), and CITY OF RAYVILLE (April 24th).

The trucks discharged by the S.S. WICHITA and those that will arrive this month are included in the first thousand purchased in the United States under the credit authorized by the Export-Import Bank to the Universal Trading Corporation of New York City. It is stated that they are for the use of the South-west Transportation Company in moving war materials. It is also stated that a second thousand American

trucks

trucks have been purchased, and that it is stipulated that these are to be used for commercial transport purposes, particularly for the movement of Chinese export products. It does not appear to be yet known whether the second thousand American trucks will be delivered at Rangoon or at Haiphong, Indochina, or whether deliveries will be divided between the two ports.

American Suppliers Provide Supervision.

Representatives of the Chrysler Export Corporation, of Detroit, and the General Motors Overseas Operations, of New York City, have arrived in Rangoon to supervise the work of assembling the American trucks purchased for the Chinese Government. The Chrysler representative is H. A. Rhinemiller, a service engineer, and the General Motors representative is C. O. Hogg, who was formerly with that organization in India. Mr. Rhinemiller was accompanied to Rangoon by H. A. Trussell, an engineer of the Indian Division of the Chrysler Corporation, who has now returned to India, and S. Malcolmson, production manager for the General Motors organization at Bombay, India, and H. A. Arshacony, an engineer from the General Motors plant at Bombay, came here with Mr. Hogg.

The Dodge trucks reshipped to Rangoon from Hong Kong were purchased some time ago through Dodwell and Company, a well-known British firm operating in China and Hong Kong, and have been brought to this port by that concern, which now has an office here. As previously reported, the first reshipment consisted of 80 trucks

trucks, and since their arrival Chinese mechanics and carpenters have been assembling them and equipping them with bodies, largely of teak. It is said that all of the trucks from Hong Kong are for the use of the Southwest Transportation Company.

Proposal to Assemble at Lashio.

The question of assembling trucks for China, and building bodies for them, at Lashio, the terminus of the Burma Railways in the Northern Shan States, instead of in Rangoon, has been under consideration for some time by the Chinese interests concerned, and recently instructions were received by the local officers of the Southwest Transportation Company from the head offices of that concern in Hong Kong to provide facilities for assembly and body-building at Lashio. Accordingly, a tract of ten acres of land about half way between the Lashio railway station and the ammunition dump, 2 1/4 miles distant, has been leased and cleared, and arrangements have been made with the Burma Railways to build required sidings. However, the local officers are of the opinion that the work can be done more advantageously in Rangoon, and the representatives of the American companies now here agree with them. All materials required, in addition to the boxed chassis, would have to be transported to Lashio. A final decision has not been reached. T. L. Soong, head of the Southwest Transportation Company, is expected in Rangoon at an early date.

The Burma Railways have made a rate of 65 rupees ($22.75) for the transportation of an assembled truck from

from Rangoon to Lashio, a distance of 561 miles. The rate includes the driver's fare, if a driver is sent from Rangoon.

British Trailers for Tanks.

It is reported that 100 of the GMC chassis to be delivered here will be for operation with armored-tank trailers that will be supplied by a British concern that is furnishing similar trailers to the British Government. The trailers are said to be of the demountable-wheel type onto which tanks can be driven when it is desired to transport them from place to place by road, and to be capable of carrying tanks of 15 tons.

The Dodge equipment shipped to Rangoon on the S.S. WICHITA includes stake bodies and cabs for some of the truck chassis. It appears that cabs and bodies were ordered for about a fifth of the 500 chassis purchased.

It is understood here that the Chrysler Corporation will supply at least half of the second thousand of American trucks purchased for the Chinese Government.

General Motors May Establish Plant.

General Motors interests are again giving consideration to the question of establishing an assembly plant for cars and trucks in Rangoon (despatch no. 124 of November 17, 1938, and despatch no. 129 of December 1, 1938). The Burma market, which is relatively small, is now supplied by shipments from the assembly plant at Bombay, India, but is thought that war-time sales to China might be helped by having a plant here, and that southwestern China might later develop into a market of some importance which could be advantageously

supplied

supplied from Rangoon. Also, the Burma Government is manifesting dissatisfaction over the fact that it now derives no customs revenue from motor vehicles assembled in India and imported into Burma, because of the free-trade agreement with India which became effective on separation, for a period of at least three years, and a readjustment permitting Burma to levy import duties appears likely. The three-year period ends on March 31, 1940, but unless steps for abrogation and revision are taken before that time, the free-trade agreement will continue in effect, subject to termination on twelve months' notice.

Respectfully yours,

Austin C. Brady
American Consul

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Memphis, Tenn.
April 9, 1939

FOR THE SECRETARY:

The cotton shippers, warehousemen and bankers in this city have nothing good to say about the Government's cotton program or about the proposed export subsidy. Although most of them guess that cotton would sell for five cents without the program, they have no alternative. Only a few are willing to admit that they prefer five cent cotton to the program. As to the carryover, most of them would like to see it worked off gradually as the trade requires it in the same way that it was sold in 1935; without some Government sales they foresee a cotton famine before the end of the crop year. They dislike any subsidy plan which would dump all the cotton at once.

The impression the Memphis people would like to leave is that business (which is good) would be very bad if industries were not moving into Memphis and building new plants, such as the $5 million dollar Firestone plant and a new Continental Can plant. These industrial expansions are explained locally on the basis of a cheaper labor supply and good transportation. Cotton, cottonseed, textiles and lumber are very dead, they insist.

The local example of business' ability to go ahead in spite of uncertainty is a local Ford dealer who sold more cars in March than any Ford dealer anywhere in the country. He netted $14,000 in the month through hard,driving salesmanship.

\- - - - - -

Kensinger Motor Company -- Mr. Kensinger has most of the town talking about him because he sold 301 new Fords in March to lead all Ford dealers in the country. He told me that he had also sold 367 used cars during the same month and that he had netted $14,000 for the month. He does not think business generally in Memphis is especially good and ascribes his record to a hard driving sales campaign which gives the customers a good price but -- he admits -- not so good a price as the customers think. He told me, for instance, of a sale closed on the basis of a trade-in value for a used car of $440 and then, by one ruse or another, the salesman worked the trade-in value down to $410. He has three meetings of his salesmen each day (the last one at 9 o'clock at night) and has taught them to learn to trade cars rather than to talk about their mechanical features. He says he believes that his company's selling drive which began in December is making the town generally buying conscious. He was one of the most interesting persons I met on the trip.

C. W. Butler Cotton Brokerage Company -- Mr. Butler is an old cotton broker who knows a great many people in this region, but who has had his troubles with the Government cotton program. He says the compress and warehouse people are making money on Government loan cotton, that the cottonseed oil mills have been hurt by substitutes and that the textile mills are not currently making much money. The soil conservation program he praises very highly for improving the quality of the farms locally, but he points out three by-products:

(1) due to increased fertility farmers are raising almost as much cotton on half their land as they formerly raised on all of it, (2) local planters are learning to raise alfalfa and cattle on the retired portion of their land and will eventually compete with northern farmers, and (3) the big planters are getting large benefit checks ranging up to $30,000, whereas the sharecroppers are being let out so that the program helps the wrong people. Farmers this year are making money on their cattle, which they bought at six cents and ~~they~~ have been selling at ten and a half cents. One large local planter sold $22,000 worth of alfalfa meal last year in addition to getting a soil conservation check of $10,000.

Mr. Butler was very insistent that the cotton loan and proposed cotton subsidy program is unsound. He thinks that with a free market the United States could regain its world outlets and gradually work off its carryover without any trouble. He is very bitter over the loss of foreign markets and points out that one local shipper has sent only 400 bales of cotton to Liverpool this year against 30,000 bales in 1937, which was a bad year. Liverpool is taking only 600,000 bales of American cotton against a normal consumption of 1,000,000 bales, he says. He is very perplexed over Secretary Wallace's refusal to listen to the cotton trade.

First National Bank -- Mr. Turner, executive vice president, lays a great deal of stress on the poor cotton situation compared with the good industrial situation. Without the industrial expansion of the Firestone and Continental Can companies, Memphis would be very badly off, he says. In the cotton trade, only the warehouse people are making money and they are uncertain over the future. ~~since~~ For instance, the Federal Compress Company has spent $800,000 building new sheds to store 1938 CCC cotton, thereby using up all their profits on sheds which may be of use for only a short time. He believes the Government "should let cotton alone", admitting that it might go to five cents. He says he believes it will have to go there sometime anyway to get rid of the surplus. He predicts that cottonseed will go to $15 a ton against the $25 at present, thereby hurting the local sharecroppers who usually are given the seed.

Local business is good and war is no factor in business planning, he says. Considerable home building is going on, but his bank has not been interested in FHA construction loans. His bank is not much interested in Government bonds of which they have only $6,200,000 compared with total deposits of over $43,500,000. He very much believes that the Comptroller's Office should be continued.

National Bank of Commerce -- Mr. William R. King, president of the bank, is also president of the William R. Moore Dry Goods Company, which is the largest wholesale dry goods company in this section. He paints a very gloomy picture of retail business outside of Memphis. Sales, he says, are about equal to those of last year, which were poor. The spurt in the last quarter of 1938 "dropped like a shot" after January 10 for some reason he cannot explain. The business situation would be much worse without the AAA cotton subsidy checks which he admits are the only thing to save the situation in many localities. However, he says he would rather try to do without them if by so doing Government spending could be stopped. Business would be hurt, but people fear that they will be hurt some time anyway and the spending must stop or taxes must increase. Not knowing what the outcome of this situation would be, business men do not want to make commitments in advance, in Mr. King's opinion. Dry goods stores, for instance, are keeping only one month's sales ahead in their inventories.

This bank, unlike the First National, is trying to make FHA loans. Mr. King says that banks "in this country are not much for bonds." They like to keep to short maturities or to buy State and local bonds which yield 7 or 8 per cent. He seemed interested in trying to find out from me what attitude New York banks are taking on long-term Treasury bonds. Mr. Mooney, vice president, criticized the Federal Deposit Insurance Corporation, saying it is unsound and its rates are too high even though he admits that bankers are thankful it has been in existence during this period of nervousness.

ESD

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 8, 1939.

TO Secretary Morgenthau

FROM Mr. White

Subject: Mexican exports of oil.

1. The latest data available on Mexican exports of oil are for July 1938. The appended table gives the monthly exports to various countries of oil from Mexico.

(The Department of Commerce promised to get later figures from their consular agent in Mexico and we have telephoned them several times but they say they have not yet received a reply to their cabled request. In response to our surprise at the delay, the answer was that Mr. Lockett is a "peculiar fellow in answering cabled requests".)

2. The figures available show only that Mexican exports of oil dropped sharply after expropriation measures had been taken.

The figures of total Mexican exports of oil for the months April to July, 1938 -- the first four months after expropriation -- amounted to \$3.6 million, as compared with approximately \$16 million for a comparable period in 1937.

Exports to Germany during those four months were about \$600,000, in contrast with \$1½ million in the same months of 1937. The exports to Italy and Japan were not important enough to be listed separately in the compilations.

Exports to the United States during that four-month period were about \$300,000, as compared with \$3¾ million for the same months in 1937.

The arrangements which involve barter dealings with Germany took place after July 1938 and therefore do not appear in the figures we now have available.

Attachment

Mexico - Exports of Petroleum and Products to Principal Countries, Monthly, January 1937 to Date

(Value in thousands of dollars)

	Total	Germany	United States	Great Britain	Netherlands West Indies	All Other
1937						
Jan.	5,445	148	1,199	1,210	1,163	1,724
Feb.	2,982	208	564	817	957	436
Mar.	5,064	350	1,121	1,424	888	1,281
Apr.	3,736	42	991	435	1,464	805
May	4,894	471	1,051	1,262	1,171	939
June	1,960	408	837	122	161	432
July	5,078	567	569	1,457	1,273	1,211
Aug.	2,791	158	756	696	495	685
Sept.	2,821	251	228	704	940	698
Oct.	2,557	99	531	370	972	586
Nov.	3,852	141	328	1,551	970	862
Dec.	3,872	224	668	1,342	879	759
1938						
Jan.	2,835	137	75	872	768	983
Feb.	3,375	180	314	730	1,022	1,129
Mar.	1,700	23	127	648	610	291
Apr.	306	73	10	67	-	156
May	1,033	279	45	510	-	199
June	1,024	151	175	384	-	314
July	1,317	98	111	582	-	527

TRIPLICATE

No. 169

Strictly Confidential

Rangoon, Burma, April 6, 1939.

STRICTLY CONFIDENTIAL

SUBJECT: Universal Trading interests send representative to Rangoon.

THE HONORABLE

THE SECRETARY OF STATE,

WASHINGTON, D.C.

SIR:

I have the honor to report that a Chinese named C. Chen, who says that he is a Yale graduate, arrived here this week from Singapore to represent the Fooching Trading Corporation of New York City, which, he explains, is operating in connection with the Sino-American Universal Trading Corporation, also of New York City. He called at the Consulate on April 4th, and left with me the following copy of a cablegram which he said he had just received from K. P. Chen, of the Universal Trading Corporation.

> "How about first shipment trucks to South-western Company. Stop. Keep us posted re unloading assembling etc of this shipment. Stop. Contact with American Consul informing him about your mission. Stop. Keep him posted about our general works. Stop. Send report to Tsou and Buck Chungking concerning delivery of trucks to South-western Company. Stop. Has opened Letter of Credit in your favour for U.S. $500.00, 50 for telegraph expenses. Stop. Can we continue ship trucks to Rangoon in view of rainy season. Telegraph reply."

Shipments of Tung Oil.

Mr. Chen told me that he had formerly been with the Foreign Trade Commission of China and its affiliated concern, the Fu Hua Trading Company, and also

from

with the China Travel Association. He said that he had previously worked with Mr. K. P. Chen in China, and that the latter had asked him to come to Rangoon to look after importations from the United States for China, and export shipments of tung oil and other Chinese products to the United States. He described the credit authorized by the Export-Import Bank as a revolving fund to be disbursed as needed, with repayments over a period of five years from the proceeds of sales of Chinese exports.

Mr. Chen said he understood that an effort would be made to ship to the United States during the first year 35,000 tons of tung oil, and to increase the amount each succeeding year during the five-year period. He also said that it was stipulated in the credit agreement that the second thousand American trucks purchased for China should be devoted to commercial shipments, particularly export shipments.

Rolling Stock From Djibouti.

With reference to the French railway from the port of Haiphong to Yunnanfu, Mr. Chen asserted that the management expected to get some additional rolling stock for the line from the Djibouti-Adis Ababa railroad, which is likewise of meter gauge. He estimated the freight awaiting shipment at Haiphong at 60,000 tons, and placed the present capacity of the line at 6,000 tons a month (reference despatch no. 162 of March 24, 1939). He expressed the opinion that the capacity of the Railway could be doubled.

Mr. Chen has taken office space in the quarters

occupied

occupied by the Southwest Transportation Company.

Method of Handling Tung Oil.

In connection with possible shipments of Chinese tung oil through Rangoon, it is authoritatively stated that the Burma Railways were recently asked by Chinese interests if tung oil delivered at Lashio could be transported in petroleum tank cars, and if not, if the Burma Railways would build special tank cars for the tung-oil traffic. The Chinese interests were told by the railway management that petroleum tanks could not be used for tung oil, and that in view of the possible temporary nature of the traffic, special cars would be built only under a financial guarantee. It was suggested by the management as a practicable method of handling tung-oil shipments over roads and railway that steel drums or tanks to fit motor-truck bodies, and which could be lifted from the trucks and placed on railroad cars at Lashio, be constructed by the Chinese. It is said that this method is being considered.

Respectfully yours,

Austin C. Brady
American Consul

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 8, 1939

TO The Secretary

FROM Miss Lonigan E.L.

The total number of WPA workers on April 1, 1939 is 2,976,140.

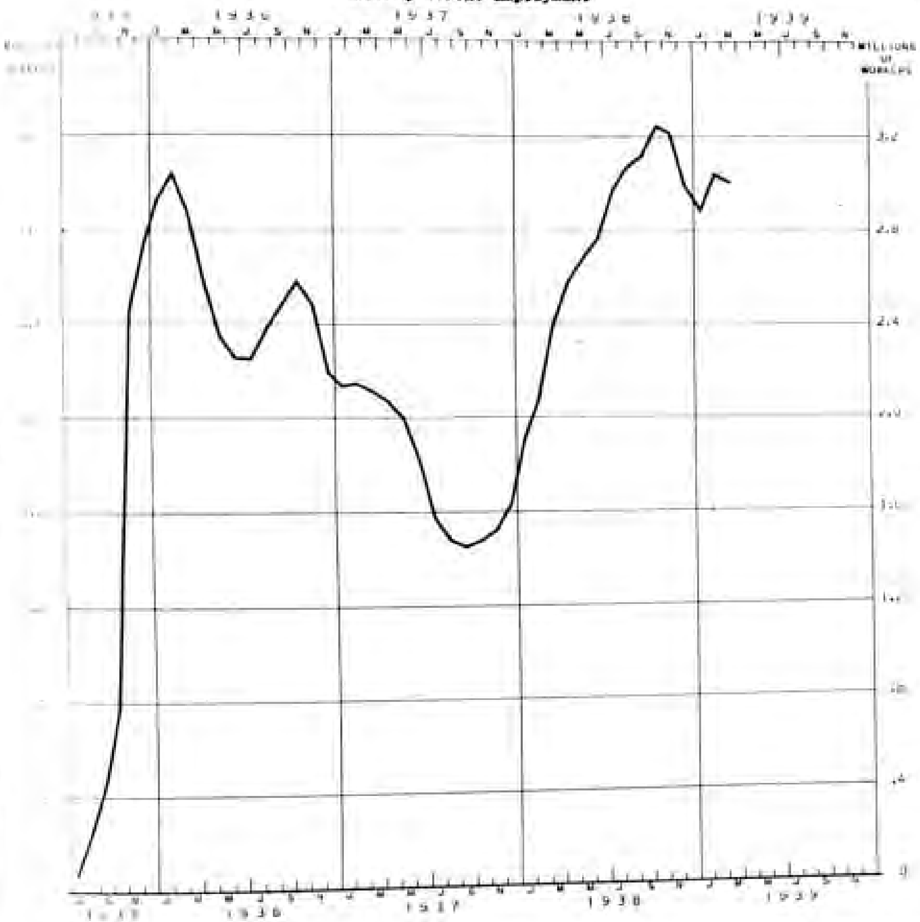
The decrease from March 25 to April 1 was 31,071 workers.

WORKS PROGRESS ADMINISTRATION

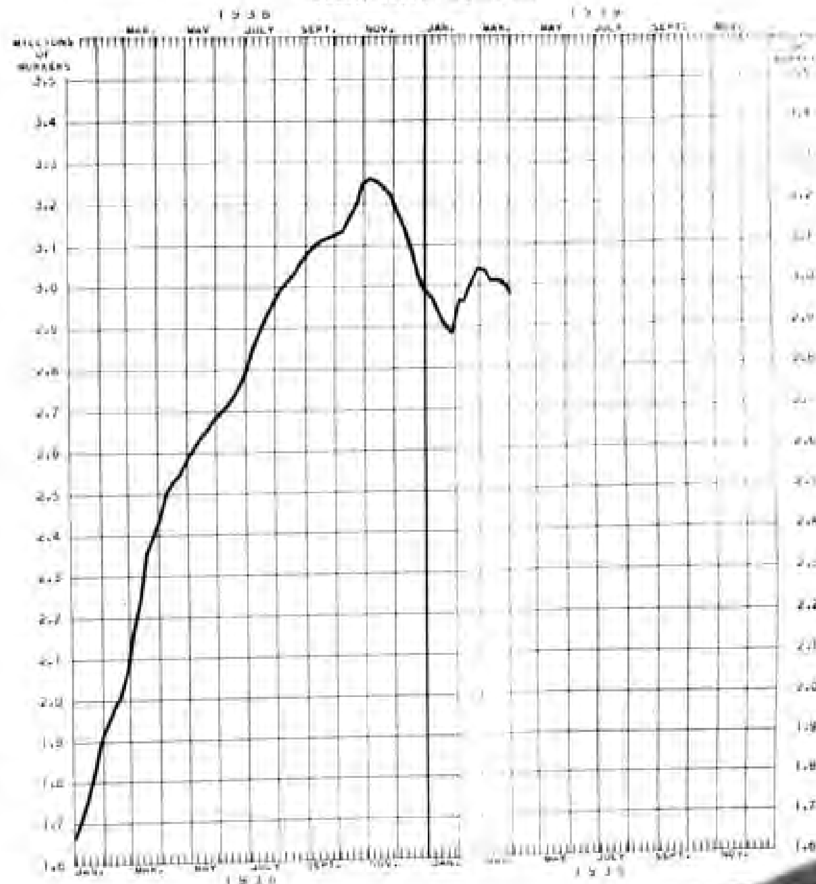
Number of Workers Employed

United States

Monthly W.P.A. Employment



Weekly W.P.A. Employment



SOURCE: WORKS PROGRESS ADMINISTRATION

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

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Weekly
United States

Week ending	Number of Workers (In thousands)
1938	
June 4	2,693
June 11	2,712
June 18	2,736
June 25	2,767
July 2	2,807
July 9	2,8[illegible]3
July 16	2,899
July 23	2,938
July 30	2,967
August 6	2,993
August 13	3,017
August 20	3,039
August 27	3,067
September 3	3,086
September 10	3,102
September 17	3,114
September 24	3,120
October 1	3,129
October 8	3,137
October 15	3,167
October 22	3,201
October 29	3,245
November 5	3,263
November 12	3,258
November 19	3,244
November 26	3,216
December 3	3,185
December 10	3,139
December 17	3,083
December 24	3,021
December 31	2,986
1939	
January 7	2,967
January 14	2,927
January 21	2,898
January 28	2,883
February 4	2,966
February 11	2,964
February 18	3,010
February 25	3,043
March 4	3,034
March 11	3,009
March 18	3,012
March 25	3,007
April 1	2,976 a/

Source: Works Progress Administration.
a/ Confidential.

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Monthly
United States

	Number of Workers (In thousands)
1936	
January	2,926
February	3,036
March	2,872
April	2,570
May	2,340
June	2,256
July	2,249
August	2,377
September	2,482
October	2,581
November	2,483
December	2,192
1937	
January	2,138
February	2,146
March	2,115
April	2,070
May	1,999
June	1,821
July	1,569
August	1,480
September	1,451
October	1,476
November	1,520
December	1,629
1938	
January	1,901
February	2,075
March	2,395
April	2,582
May	2,678
June	2,767
July	2,967
August	3,067
September	3,120
October	3,245
November	3,216
December	2,986
1939	
January	2,883
February	3,043
March	3,007 a/

Source: Works Progress Administration
a/ Confidential
Monthly figures are weekly figures for the latest week of the month.
They include certified and non-certified workers.

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE April 8, 1939.

TO SECRETARY MORGENTHAU

FROM W. R. JOHNSON:

In compliance with your instructions of March 24, 1939, I immediately instituted an investigation to ascertain--

(1) Whether oil is being smuggled into Texas from Mexico, and
(2) The sources of rumors that such smuggling is occurring.

An intensive investigation participated in by the Customs Agency Service, the Customs Border Patrol, and the Coast Guard has failed to develop any basis whatsoever for the smuggling rumors. The investigation covered the border and coastline from Los Angeles, Calif. to Mobile, Ala.

The only basis for any rumor with respect to smuggled oil uncovered by the investigating officers was talk by one Harold John McArdle, alias Jack Kearney, who stated that a German in Mexico City named Gutchrit controls corrupt Mexican officials who are stealing and bootlegging oil. McArdle also stated that he had heard that such oil had been smuggled into the United States by means of barges towed into southern ports by tugs which make off-shore contacts with tankers from Mexico.

McArdle has a bad reputation for veracity and is now under arrest for smuggling jewelry into the United States from Mexico. However, we are continuing the inquiry to see what can be learned about Gutchrit and whether any other leads can be discovered.

American oil interests have complained about importations of Mexican oil at Houston, Texas, by the Eastern States Petroleum Company and at New Orleans, Louisiana, by one W.R. Davis. The imports at Houston are processed for export, and those at New Orleans are stored in bond and exported. These transactions are handled in accordance with the customs laws, but they may be the basis for the smuggling rumors.

W. R. Johnson