

DIARY

Book 21

April 11 - April 20, 1936

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TO: Secretary Morgenthau

April 11, 1936.

FROM: Jacob Viner

Memorandum on the Applicability of Sec. 303, Tariff Act, to German Exports because of German Currency Manipulations.

(1) Section 303 provides that when any country, etc. "shall pay or bestow ... any bounty or grant upon the manufacture or production or export of any article," there shall be imposed upon the importation of such article into the United States "an additional duty equal to the net amount of such bounty or grant, however the same be paid or bestowed. The Secretary of the Treasury shall from time to time ascertain and determine, or estimate, the net amount of each such bounty or grant, and shall declare the net amount so determined or estimated."

(2) The provision is mandatory; if the Secretary determines that a bounty or grant is being paid on production or export, he must put Section 303 into operation. But cases may arise where there can be reasonable doubt as to whether particular practices involve the existence of a bounty or grant, and in such cases, the Secretary of the Treasury is surely justified in taking into consideration the broader questions of national policy and interest in reaching his decision.

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(3) The question as to the applicability of Section 303 to German exports arises in the main out of some peculiar aspects of the German currency situation. There are a number of different types of marks, of which all (except "scrip") are maintained through Government regulation at a uniform and undepreciated value in Germany, whereas abroad only one type is undepreciated in value, and the other types have different and fluctuating values according to the demand in the market. The acceptance by a German exporter in payment of German exports of depreciated or "low value" marks is subject to restrictions and limitations imposed by the German Government. Since within Germany all the types of marks have uniform value, whereas outside Germany they have different values, the German Government in permitting a German exporter to accept low-value marks in payment for his export enables him to quote a low price in dollars without reducing his price in marks. Does the acceptance by a German exporter in payment of his merchandise of a type of mark which has a depreciated value abroad and an undepreciated value at home involve a bounty or grant within the meaning of section 303? This is the most important question to be answered.

(4) The depreciation of the value of a currency is ordinarily not to be regarded as constituting a bounty or grant within the

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meaning of section 303, even though the depreciation tends to have the effect of promoting the competitive power in foreign markets of the export industries of the country whose currency has so depreciated, and even if the promotion of exports was one of the objectives of the Government when it permitted or even deliberately brought about the depreciation. Since the bounty-countervailing provision was first enacted in 1897, there have been many occasions of exchange-depreciation of foreign currencies, but there has been no instance of the application or even apparently of contemplation of application of the additional duties to imports merely because they came from a country with a depreciated currency. Many other countries have similar bounty-countervailing provisions, (though as a rule discretionary rather than mandatory in form) but I believe there has been no instance of the application of these provisions on the mere ground that the imports were being offered for sale in terms of depreciated currencies. Congress has on several occasions discussed the problem of protecting American industry against abnormal competition resulting from foreign currency depreciation, but the Congressional discussions give no indication that Congress has ever regarded the bounty-countervailing provision as intended to provide a remedy for, or as offering a means for dealing with,

imports sold in terms of a depreciated currency. No American court decision can be found which refers specifically to the reduction in the cost in dollars to American importers of foreign commodities because of a decline in the exchange value of the currency of the exporting country as constituting a bounty or grant within the meaning of Section 303. No ground exists, therefore, for holding that the additional duties provided for by Section 303 are applicable to imports merely because these imports are sold in terms of a depreciated currency.

(5) May it not be held, however, that the German Government, by deliberately manipulating the currency in such a manner as to maintain a uniform value at home for all types of marks whereas abroad different types of marks have different values relative to each other and to foreign currencies, and by regulating the percentages of the particular types of marks which the German exporter can accept in payment for exports, is in effect establishing a situation in which the German exporter can, without changing his price in German marks, reduce his price in dollars, and is therefore bestowing upon the German exporter a "bounty" or "grant" within the meaning of Section 303, with the intent of promoting German exports?

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The peculiarities of the German currency system consist of the limitations on the depreciation of the German currency rather than extensions of such depreciation. If the value of German marks of all types were permitted to fall in terms of dollars to the value of the cheapest type of mark, and if the German exporter were left free to accept whatever type of currency he chose in payment for his export, German exports would be promoted more than they are by the present partial depreciation of the German currency, but there would then clearly be no question of the applicability of additional duties under Section 303 to imports from Germany. Are there any grounds on which a partial depreciation of a currency may be held to constitute a bounty or grant under Section 303, where a complete depreciation of the currency would be conceded not to do so? To answer this question requires consideration of the meaning of bounty or grant as used in Section 303.

There are two decisions of the Supreme Court which are the crucial cases for the interpretation of the intent of the bounty-countervailing provision in the American tariff law. In *Downs vs. U. S.* (187 U. S. 496) aside from the definitions of "bounty" cited by the Court from other sources or which it itself offered, the relevant material is the finding that when the Russian Government,

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by a complicated system of regulation of the domestic sale and export of sugar, created a situation under which Russian exporters of certain sugar obtained as the result of such export not only (a) the money paid by the foreign purchaser but also (b) a certificate from the Government, which was transferable to other sugar producers, which secured to the holder the right to sell an equivalent amount of sugar in the domestic market free from excise tax, and which had a value at which it could be sold, there existed a bounty upon the export of sugar to the amount by which the sale value of the certificate exceeded the amount of excise tax exemption from which was conferred by the certificate. Under this decision, therefore, the exporter of sugar was held to have received a bounty because in addition to what he received from the foreign buyer of his sugar he obtained additional remuneration from the sale of the certificate which the Government had granted to him because of the export.

In *Nicholas & Co. v. U. S.* (249 U. S. 34), the opinion of the Court stressed the inclusion in the text of the bounty-countervailing provision of the word "grant", and stated: "If the word 'bounty' has a limited sense the word 'grant' has not. A word of broader significance than 'grant' could not have been

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used. Like its synonyms 'give' and 'bestow', it expresses a concession, the conferring of something by one person upon another. And if the 'something' be conferred by a country 'upon the exportation of any article or merchandise' a countervailing duty is required by Paragraph E."

If this be accepted as binding, then it would appear that whenever a Government grants to an exporter any privileges, or in any way by its efforts creates for him any facilities, whereby his ability to export is promoted, the exporter is receiving a bounty or grant within the meaning of the bounty-countervailing provision of the tariff law. It would then appear that the German Government, by maintaining for all types of marks within Germany a uniform and undepreciated value, by permitting or even bringing about deliberately a depreciation abroad of some types of marks, and by giving permission, subject to limitations, to German exporters to accept in partial payment for their exports types of marks which have a depreciated value abroad though a full value at home, was thereby bestowing upon German exporters a "grant" within the meaning of Section 303.

The nature of the actual decision of the Court in *Nicholas v. U. S.*, the consistent practice of the Treasury previously and subsequently to that decision, and the absence in subsequent

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Congressional legislation and discussion of any evidence that Congress accepted so broad an interpretation of the meaning of "grant" as used in the tariff law, indicates, however, that the matter cited above from *Nicholas v. U. S.* was mere dictum, and has no bearing on the immediate question in issue. In *Nicholas v. U. S.*, what was involved was the question whether the British Government, in granting to British exporters of alcohol both a remission of excise taxes and a small additional payment as compensation for the extra costs resulting to distillers from the necessity of adhering to the excise regulations, was bestowing a "bounty" or "grant". The Court found in the affirmative, but only to the extent that the exporter received compensation for the extra expenses in which the administration of the excise taxes involved him. Had the Court followed its own definition of "grant", it should have found that the remission of excise taxes also constituted a grant, to say nothing of any privilege or advantage conferred upon the exporter as exporter by the general trade promotion activities of the British Government, by the maintenance of lighthouses and harbors, and by the protection afforded to British trade by the British navy and the services rendered by British diplomatic and consular officials.

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From the actual decisions in these two cases, it would seem that in order to find that an exporter had received an export bounty or a grant, the exporter must receive, in addition to what is paid to him by the purchaser of his merchandise, an extra payment from some other source but contingent upon the fact of export. From the wording of Section 303, it would seem also that an extra payment, to be subject to the additional duties, must be a payment made "upon the manufacture or production or export of any article" and that a payment to the importer would not be a bounty or grant subject to additional duties under Section 303. If it should be argued, therefore, that the bounty or grant in connection with the German currency manipulations consisted in the maintenance by the German Government at depreciated value in New York of marks which in Germany had full value as compared to other marks, the bounty or grant would be given to the American importer rather than to the German exporter, and while constituting a bounty or grant, would not be of a kind making the merchandise with which it was associated subject to additional duties under Section 303, because it was granted upon the importation into the United States rather than upon the exportation from Germany. But the chief argument against holding that the permission to German exporters to accept payment for exports in marks which are lower in value relative

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to gold marks abroad but are not lower in value relative to gold marks at home constitutes a general advantage derived by the German exporter from the nature of the German currency system, and does not constitute a specific payment to the exporter from some definable source and additional to what he receives from the purchaser, such as would make his case parallel with that of the Russian exporter in the Downs v. U. S. case or the British exporter in the Nicholas v. U. S. case. In general, the closest parallel with the German situation is provided by the case of general or uniform exchange depreciation, and in such cases, as has been argued above, Section 303 is not applicable.

(6) The additional duties provided for by Section 303 would, however, be applicable to imports from Germany, in the light of the Supreme Court decisions, in any case where the German exporter receives, upon export, in addition to what was paid to him by the American importer, a payment from some other source. Such payment would, in effect, be received by the German exporter, if he were permitted to exchange what he received from the American importer for something else at the market value of the latter, and if in turn he were then given, by an official agency, more than its market or ordinary value for the commodity which he had thus acquired. Two types of German transactions appear clearly to fall within this class.

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(a) The German Government pays interest and principal on certain foreign-owned German securities in part in "scrip", which is deposited with an agency of the German Government. This scrip is purchased by another agency of the German Government, the gold Discount Bank, and is sold freely by them at a 50 per cent discount from its face value (or a slightly less discount when sold to German exporters). Scrip, therefore, not only abroad but also in Germany has a value which is substantially less than its face value in German gold marks. Exporters may, however, within prescribed limits, redeem the scrip at an official agency of the German Government at its face value in full-value marks. The German exporter to the United States who is permitted to buy scrip at a discount from one agency of the German Government and resell it to another agency without discount is, therefore, receiving upon export to the United States both payment from the American importer and an additional payment from another source. He is therefore clearly receiving a bounty or grant within the meaning of the bounty-countervailing provision as construed in *Downs v. U. S.* and *Nicholas v. U. S.*, and the amount of the bounty or grant is equal to the excess in German full-value marks of what he receives for his scrip over what he paid for it.

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(b) German bonds sell at a discount in gold marks, or their equivalent in foreign currencies, in countries outside Germany, and this discount exceeds the discount at which they sell within Germany itself. The maintenance of a persistent and substantial differential in the prices of these bonds in gold marks or their equivalent in Germany and abroad is to be explained by the fact that Germans are ordinarily not permitted to purchase such bonds outside Germany either with marks or with foreign currency. The German Government, to promote export, does, however, grant special permission to German exporters to use the proceeds of their foreign sales to purchase German bonds abroad at a discount, and then redeems these bonds at their face value, which is higher not only than their value abroad but also than their value in the open market in Germany. Since the German Government could make such purchases on its own account in the foreign or the home market at the lower market prices, the excess of the price received by the German exporter for these bonds over what he paid for them is an extra payment to him over and above what he has received from the foreign purchaser of his merchandise, and therefore, constitutes a bounty or grant within the meaning of Section 303, to the extent of such excess.

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(7) It is recommended, therefore:

(a) that where a German exporter receives extra compensation upon export to the United States over and above what is paid to him by the American purchaser of his merchandise, it be found that he has received a bounty or grant within the meaning of Section 303 to the extent of such extra payment.

(b) that it be found that German exporters receive such extra payment when they are permitted because of export to buy scrip at one price in marks and resell it at a higher price, or to buy bonds at one price in marks and to resell them at a higher price.

(c) that to facilitate the administration of Section 303, the consular invoice be revised, so as to include specific questions, to which answer by the exporter is required, bearing on the receipt by the exporter of extra compensation from any source other than the American purchaser of his merchandise.

(d) that to avoid the necessity of applying additional duties where the bounty or grant does not clearly involve injury to American industry, and merely offsets a special disadvantage to which the exporters of the country

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granting the bounty are subject as compared to the exporters of other foreign countries because of a relative appreciation of their country's currency or of other types of disability or handicap resulting from measures adopted for other reasons by their Government, the Treasury should support revision of Section 303 so as to make additional duties applicable only when the Tariff Commission, after investigation, finds that injury to American industry results from such bounty, and that the additional duties would lessen or eliminate such injury.

April 11 - (Dictated Sunday at H.M.Jr's house)

Saw the President at dinner last night. I found him looking exceedingly well. He was in the best of spirits. Saw him alone for about half an hour. The President said he did not want to talk any business. He said that I should only work half a day and that I ought to take long week-ends. I said, "how about my suggestion to have Cabinet on Thursday instead of Friday" and he said, "we will start that next week". He said, "I have had plenty of time to think things over and I am sure that the political situation is all right and I am just going to sit back and do nothing about it" from which I gather that he meant, because he did not explain his remark, that he was not going to put on an aggressive campaign at this time. He urged me strongly not to work afternoons or evenings.

At Cabinet the day before I told him that Bell and I wanted to see him soon about various appropriations which had a chance of passing which were over and above his budget. I gave him the memorandum that Bell had prepared for me and he kept this.

I also told him that Oliphant and Helvering and I wanted to see him about the tax bill, that we both felt that everything was all right in the House but that we were going to have some very difficult times in the Senate and that the sooner he saw Pat Harrison the better.

The President said at Cabinet that he was interested in simply three pieces of legislation; the Appropriation Bill, the Tax Bill and Relief Bill and, as far as he was concerned, he did not care whether any other bill passed or not.

I reported at Cabinet that we had gotten together with the State Department about the Canadian liquor situation and then Mr. Hull said that somebody from the State Department had called up Senator Harrison and told him that we wanted 30 days postponement and that Senator Harrison had said that he would not postpone it unless the President asked him to do so. Mr. Hull suggested that the President call up Senator Harrison about it and he said he would.

Last night I told the President that we tried our best to get his letter to Congressman Buchanan and others about pending legislation released to the newspapers, that Gaston had worked with Early on it and that parts of the letter had been released. I urged him strongly to write Buchanan releasing the whole of the letter and he said, "it is all right as far as I am concerned and tell Buchanan so. If Buchanan wishes to release the letter he should call up the White House and they will O.K. it". Saturday morning I called up Bell and asked him to pass this along to Buchanan. He did and called me back and said that Buchanan wanted to think it over as he was not sure that it was good politics to release it at this time as it might anger certain of the groups on the Hill.

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I spoke to the President about Sedgwick of Boston as a possible Special Assistant. The President knows him very well and does not think very highly of him. He says he is not over-bright. He said he went as one of the Masters to Groton with the hope of succeeding the Head Master (whose son-in-law he is). The President thought that Sedgwick was not very tactful. Then I think he gave me his real reason for not wanting him when he said, "you know Sedgwick belongs to that branch of the Democratic party which is at odds with Governor Curley and at this time I, the President, do not want to do anything to irritate Governor Curley". I said, "his record is excellent and so was his scholastic standing at Harvard". The President said, "well if you did appoint him it certainly would be pleasing the intelligentsia of New England". I repeated this conversation to E. F. M. and she reminded me that Sedgwick's uncle is Editor of the Atlantic Monthly and was so very critical when we last met him of Jimmy Roosevelt and said that Jimmy ought to be thrown out of Boston for the way he acted and the things he had done. Possibly the President knows about Editor Sedgwick's attitude towards his son. E. F. M. said that most likely young Sedgwick belongs to the decent element in Massachusetts in the Democratic party who are all opposed to Governor Curley. Notwithstanding what the President said I am going to see Sedgwick and see whether I like him.

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MR. BELL:

The following bills apparently have some possibility of being enacted into law at this session:

<u>Bill No.</u>	<u>Title or Purpose</u>	<u>Cost</u>	<u>Status</u>
<u>VETERANS' ADMINISTRATION</u>			
H.R. 9269 (or similar bill)	To continue retirement pay for certain emergency officers.	\$4,500,000 annually	In Committee. Veterans' Administration thinks some bill of this type will pass.
<u>NAVY DEPARTMENT</u>			
H. R. 10976	Major alterations of naval vessels.	\$35,000,000	In Committee. This bill has the approval of the Department and the Administration.
H. R. 10977	Major repairs of vessels.	\$ 6,000,000	In Committee. This bill has the approval of the Department and the Administration.
H. R. 11369	Construction of auxiliary naval vessels.	\$175,000,000	In Committee. This bill has the approval of the Department and the Administration.
H. R. 11584	Public Works Projects.	\$30,000,000	In Committee. This bill has the approval of the Department and the Administration.
<u>WAR DEPARTMENT</u>			
S. 3531	To amend Mississippi River Flood Control Act.	\$290,000,000	Pending in Senate. In view of flood conditions this year there is considerable pressure to pass this bill promptly.
H. R. 8455	To authorize the construction of Public Works on rivers and harbors for flood control.	\$370,450,000	Passed House and pending in Senate Committee. There is likewise considerable pressure behind this bill and indications are that the cost will be increased by the Senate Committee.

<u>Bill No.</u>	<u>Title or Purpose</u>	<u>Cost</u>	<u>Status</u>	
H.R. 10179	Authorize construction of military posts in Hawaii.	\$12,500,000	In Committee.	This bill has the approval of the Department and the Administration.
H.R. 10849	Construction of ammunition storage.	\$ 2,700,000	In Committee.	This bill has the approval of the Department and the Administration.
H.R. 11321	Construction of Army posts.	\$30,000,000	In Committee.	This bill has the approval of the Department and the Administration.

DEPARTMENT OF AGRICULTURE

H.R. 11687	Authorization for public roads and elimination of grade crossings.	\$440,000,000	Pending in House.	This bill might be approved at a cost of \$250,000,000.
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FARM CREDIT ADMINISTRATION

S. 4180	Reduction of the interest rate on Federal Land Bank loans.	\$100,000,000	Pending in Committee.	Report on this bill has been requested from the Departments concerned and the question of whether or not it is in accord with the President's financial program is now before the Budget Bureau for determination. The Farm Credit Administration has reported unfavorably on the bill.
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RECONSTRUCTION FINANCE CORPORATION

H.R. 11968	To authorize rehabilitation loans.	\$20,000,000	Passed the House.	This bill has the approval of the Administration.
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RURAL ELECTRIFICATION ADMINISTRATION

S. 3483	To establish the Rural Electrification Administration.	\$450,000,000	Passed the Senate and reported in the House.	This bill has the approval of the Administration.
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<u>Bill No.</u>	<u>Title of Project</u>	<u>Cost</u>	<u>Status</u>
		<u>UNITED STATES HOUSING AUTHORITY</u>	
H. R. 12884	To provide for low cost housing.	\$600,000,000	This bill and a companion bill in the Senate (S. R. 12884) were introduced on April 8. It is doubtful if there is sufficient time left in this session for these bills to pass.

The total of this pending legislation is \$6,000,000,000 plus an annual cost of \$4,000,000.

April 13, 1936

Secretary Wallace called HM, Jr. today and told him that the beet sugar growers having been pressing him in connection with the matter of benefit payments to the beet sugar growers under the Soil Conservation Act. Under the Act these payments are only about one-fifth of what they were under the old plan.

They are very anxious to see the President and the President has asked Secretary Wallace and HM, Jr. to "keep these people off his neck."

HM, Jr. told the whole story to Taylor and asked him to handle the thing for him.

April 13, 1936

HM, Jr. called the President. He said to him, "I feel nearer like myself today than I have for the last five weeks."

The President told HM, Jr. he would lunch with him Tuesday of this week rather than on Monday, as usual.

HM, Jr. discussed with the President the possibility of France taking action towards devaluation of the French franc. He said, "It ties in with this whole English situation. England is holding up the franc by buying gold. You will undoubtedly get information from the State Department that I would not get. Anything you get that will throw light on it, I would appreciate your letting me know. We have everything drawn up should France make any move."

HM, Jr. asked the President, "Will you do anything on tax or relief today in so far as I am concerned?" The President said no; everything would have to wait until tomorrow.

The Secretary told the President that he would like to try out the Central Statistical Board in helping him to make a study of unemployment figures. He said, "If it works out all right, then I want to go back to my original idea of six months ago and get them to do more of it. I want to let them analyze what the New York Times wrote yesterday about the New York City unemployment. The article was by Russell Porter." The President said, "I hope you will confine it only to statistics in working with them and if you do, they will not prove a damn thing!"

April 13, 1936

At the 9:30 group meeting this morning all were present with the exception of Mr. Haas, who is out of town, and Miss Roche, who is attending the meetings of the State Health Officers who are here for two days of conferences.

Oliphant reported that the Ways and Means Committee is not meeting today or tomorrow. This is to give their boys an opportunity to do some drafting. Oliphant said he would devote these two days to prepare himself for the Senate hearings on the tax bill.

HM, Jr. told the group that this was what he had on his calendar for the week: "I may want to work tonight to get myself in readiness for a meeting tomorrow. I will let you know later in the day whether I will have the meeting at my house this evening. I will want White, from Haas' office, Taylor and Lochhead and Oliphant." Oliphant said he was tied up and suggested sending Oppen, but HM, Jr. felt that Oppen would not contribute anything and did not want him.

The Secretary also told the group that Viner has come through with what looks like an excellent report on countervailing duties; that Viner had taken a new view on it and that he, HM, Jr. wanted the Legal Division to take Viner's report, digest it and then come back with their recommendations in the light of Viner's changed viewpoint. HM, Jr. said he wanted to get a complete meeting of minds within the Treasury and would then answer Secretary Hull's letter. Oliphant said he would be ready to discuss countervailing duties on Wednesday. (See diary of April 15, 1936.)

In connection with the meeting tomorrow in the Secretary's office, when Mr. Broderick, Acting Chairman of the Federal Reserve Board, Governor Harrison and Dr. Burgess will confer with the Secretary, HM, Jr. told Upham he also wants someone to represent George Haas and suggested Seltzer. When Seltzer comes to the meeting he is to have the usual charts for HM, Jr. The Secretary also said he wanted Goldenweiser present. He decided to call Dr. Burgess while the group was present and the following is a transcript of their telephone conversation:

HM, Jr.: Hello.  
 Dr. Burgess: Hello, sir, how are you?  
 HM, Jr.: Good morning, Burgess. Just to tell you what this meeting is tomorrow -- you might want to sound out some people in New York today.

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Dr. Burgess: Yes.  
HM, Jr.: There's a possibility that we'll now be getting fifty million bills --  
Dr. Burgess: Yes.  
HM, Jr.: Selling them into December --  
Dr. Burgess: Yes.  
HM, Jr.: Beginning maybe next week.  
Dr. Burgess: Yes.  
HM, Jr.: See?  
Dr. Burgess: Yes.  
HM, Jr.: And we'll have our figures for you --  
Dr. Burgess: Yes.  
HM, Jr.: On what our needs are from now until the fifteenth of December.  
Dr. Burgess: I don't think I ought to talk about that with these people.  
HM, Jr.: All right, that's up to you.  
Dr. Burgess: Because it -- there's a bidding for bills today, you see?  
HM, Jr.: All right.  
Dr. Burgess: And it will give somebody the advantage.  
HM, Jr.: Well, all right. But that's what it's about.  
Dr. Burgess: Yes. We know the way out, all right.  
HM, Jr.: O.K.  
Dr. Burgess: Fine.  
HM, Jr.: Thank you.  
Dr. Burgess: I'll be there.  
HM, Jr.: Goodbye.

The Secretary related to the group that he spoke to Secretary Hull after Cabinet on Friday and that Hull had said he was going "tooth and nail" to make the Canadian Government come through. Taylor then remarked that Mr. Hume Wrong was still disgruntled and HM, Jr. said he would have to see Mr. Wrong but that in view of the fact that Secretary Hull has taken the attitude that he will work side by side with the Treasury, Wrong would have to change his attitude.

HM, Jr. called attention to Russell R. Porter's article in yesterday's New York Times in which the writer pointed out that since WPA went into effect, the cost of relief in New York City has risen about 50% and about 25% more persons are being furnished relief, the total costs including both the WPA and ERB running now about \$30,000,000 a month compared to about \$10,000,000 more than before WPA. Mr. Porter also showed by comparable

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tables the various types of relief, the increase in the number of home relief and associated cases over the number of ERB cases of the week of April 5, 1935 and the cost of administering relief both for ERB and WPA. Under the latter table he showed that New York City takes care of more people at less cost per man while WPA takes care of less people at a greater cost per man.

HM, Jr. felt the normal thing would be to have the Budget check these figures, but he just can't load Bell down and do to him what he did last summer when he had to send the man away for a couple of weeks to regain his strength. Haas, he pointed out, has worked so intensely on the tax thing that he has had to be sent away to build up his resistance. Therefore, the logical place to check up on the figures which Harry Hopkins has been furnishing the Secretary and those which Ickes has been supplying would be in the Central Statistical Board. In this connection, he asked McReynolds to get for him the Executive Order that was drawn up about six months ago, under the terms of which funds were to be transferred from WPA to the Statistical Board. HM, Jr. reminded him that at that time Frank Walker and HM, Jr. were very anxious to have this done, but they were blocked. He again wants to try to get this Executive Order through. He said he had cleared it with the President and the President had given his approval.

HM, Jr. said that Myers had told him that the President is transferring \$7,000,000 from Tugwell to Farm Credit Administration without giving Tugwell a hearing.

The Secretary also told Taylor to contact Jesse Jones for him and tell Jesse that HM, Jr. wants to talk to him. What he has on his mind is that he would like to have Jesse, between now and June 1, clean his shelves of any securities that he has taken over from Ickes. He wants Jesse to be able to show on July 1 that he has cleaned up all of Ickes' securities but the reason he wants it done between now and June 1 is because he does not want Jesse to have to sell any during the month of June. He added that this does not apply only to Ickes' securities, but to any and all securities that he may have taken over.

Gibbons brought in to the Secretary copies of letters he had written to Congressman O'Connor about placing a constituent of his in the Procurement Division of the Works Progress Administration. A political angle had developed and information was

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given indirectly to Mr. Gibbons that Mr. Forde, in charge of the Procurement work for WPA in New York has secured most of his personnel by contacting Bob Moses. In presenting this correspondence to the Secretary, Mr. Gibbons stated that he had talked it over with McReynolds who had said he would go to New York and straighten it out.

HM, Jr. told Gibbons and McReynolds very definitely that he did not want McReynolds to get in on any political situation; that he wanted this matter turned over to Admiral Peoples and that Admiral Peoples could keep his own "nest clean" since he was "no baby" when it came to politics.

# RELIEF COSTS HERE INCREASED BY 50% SINCE START OF WPA

Rise of 25% in Number Getting Aid Also Shown by Survey—\$30,000,000 a Month Spent.

## EMPLOYMENT LAG SEEN

Miss Carr Lays Situation to Fact Jobs Have Not Kept Pace With Added Production.

## DEFENDS WORK PROGRAM

Says Restoration of Dole Would Create Grave Social Problem—Denies ERB Frauds.

By RUSSELL B. PORTER

Despite the continued business and industrial improvement of the past year, a survey of the relief situation in New York City shows that Federal, State and city taxpayers are supporting about 25 per cent more persons at a cost of about 50 per cent more than before WPA went into effect.

The all-time peak of the city's relief rolls just as WPA was getting under way saw the Emergency Relief Bureau, with about 240,000 cases, in round numbers, on both home relief and work relief. Now there are about 85,000 more cases, representing 255,000 to 300,000 additional men, women and children, on government payrolls through WPA and ERB combined.

Until last August, the month WPA was put into operation, the total costs of the ERB, including home relief, work relief and administrative expenses, was about \$20,000,000 a month. Of this the city paid about \$5,000,000, the State Government about the same, and the Federal Government about \$10,000,000.

### Cost \$30,000,000 a Month

At present the total costs of relief in the city, including both the WPA and ERB budgets, are running about \$30,000,000 a month, or \$10,000,000 a month more than before WPA. ERB is costing about \$9,000,000 a month, of which the city's share is about \$3,700,000. The

State pays the rest. WPA is costing the Federal Government from \$20,000,000 to \$22,000,000 a month.

WPA went into effect on Aug. 1, 1935, but there was delay in getting under way. That explains why ERB reached its peak on Aug. 9, 1935. On that date its roster of cases stood as follows:

Home relief.....	229,471
Work relief.....	85,478
Supplementary relief.....	11,541
Local homeless.....	8,367
Transients.....	8,976
<b>Total.....</b>	<b>343,833</b>

The first to be transferred to WPA were the work-relief cases, together with several thousand non-relief administrative employees. Home-relief cases were then transferred to WPA in accordance with its ability to absorb them.

By Nov. 14 the transfer of home-relief employables to WPA jobs brought the total case load on home relief and supplemental relief down to 145,111, with the total of all ERB cases 165,396. Thereafter it began to increase and has continued to rise steadily.

The latest ERB figures available, those for the week ended April 3, 1936, show that the total number of relief cases has increased to 200,321, distributed as follows:

Home relief.....	175,485
Supplementary relief.....	12,640
Local homeless.....	11,615
Transients.....	581
<b>Total.....</b>	<b>200,321</b>

This would indicate that in the past five months the number of home-relief and associated cases has increased by about 35,000. This represents from 105,000 to 140,000 men, women and children, according to the ERB method of figuring an average of from three to four persons to a case. Fifteen thousand of the number added to the case load have come in the past eight weeks.

A comparison of the ERB case load, exclusive of the work relief cases transferred in a body to WPA, between the ERB peak period and the present, follows:

	Aug. 9, 1935.	April 3, 1936.
Home relief.....	229,471	175,485
Supplementary relief.....	11,541	12,640
Local homeless.....	8,367	11,615
Transients.....	8,976	581
	<b>255,355</b>	<b>200,321</b>

### WPA Peak on Feb. 19

Meanwhile, the WPA rolls reached their peak with 248,474 cases on Feb. 19. Subsequently, in an effort to reduce WPA costs, thousands of workers were dismissed, but it was found that some had large families and they are

being reinstated. As soon as this readjustment is completed, unmarried workers will be dismissed in their places.

On April 3, 1936, there were 230,523 cases on the WPA payroll; on April 9 there were 231,831.

A compilation of all relief cases, both WPA and ERB, as of April 3, 1936, the most recent date on which both figures are available, and the ERB peak load follows:

	Aug. 9, 1935.	April 3, 1936.
ERB home relief, &c.....	255,355	200,321
ERB work relief.....	85,478	—
WPA.....	—	230,523
<b>Total.....</b>	<b>343,833</b>	<b>430,844</b>

In the above table the work relief cases are assigned to ERB instead of WPA. Although they were ordered transferred to WPA on Aug. 1, 1935, ERB continued to carry them on its rolls as of Aug. 9 because of the confusion which surrounded the early days of WPA, when there was much delay in getting men to work and getting their Federal pay checks.

In each instance the total number of cases must be qualified by subtracting the number of supplementary relief cases. These are cases where a worker on WPA, or previously in the works division of ERB, receives or received an additional home relief allowance for special reasons.

This gives the following result:

	Total cases
April 3, 1936.....	418,234
Aug. 9, 1935.....	332,292
<b>Increase.....</b>	<b>85,942</b>

According to the ERB-WPA method of computing three to four persons to a case, the total number of persons benefitting from governmental aid on Aug. 9, 1935, was between 966,876 and 1,329,188. The total number on April 3, 1936, was between 1,254,702 and 1,672,926. The increase was between 287,826 and 343,768.

The figures as to the number of persons are necessarily estimates because neither WPA nor ERB is able to tell exactly how many of its cases represent heads of families or how many are unmarried persons. The ratio of three to four persons to a case, on an average, is used as a rough working method.

### Totals of Year Ago

ERB figures for the week of April 5, 1935, a year ago, are as follows:

Home relief.....	215,186
Work relief.....	83,998
Supplementary.....	8,323
Local homeless.....	9,353
Transients.....	8,286

**Total..... 325,146**

This shows that the ERB rolls increased by only 10,000 cases in the four months before WPA came into existence, compared with the 35,000 increase in ERB cases in the past few months.

Payroll data show that in April, 1935, the ERB cost \$19,590,066, including home relief, work relief and administrative costs. Of this

the city paid \$5,122,542, and the Federal and State Governments \$14,408,594.

In July, 1935, the month before WPA went into effect, the ERB budget was \$19,412,860, of which the city's share was \$5,020,070, and the Federal and State shares \$14,392,780.

The ERB budget dropped in August, 1935, to \$11,809,050, of which the city's share was \$3,652,318, and the shares of the Federal and State Governments \$8,156,734.

For February, 1936, the ERB cost \$9,562,000 and for March \$9,481,000.

**ERB Budget Is \$9,436,000**

The ERB budget for April, 1935, is \$9,425,000, of which the city's share is \$5,739,500 and the State's share is \$3,685,500. Under the present arrangement the city pays 60 per cent and the State 40 per cent of ERB costs, whereas before WPA the Federal Government paid 50 per cent and the State and city 25 per cent each.

WPA's expenditures for February were \$19,479,300 for payroll and \$3,808,595 for other spending, including materials, making a total of \$22,287,895.

Thus the February total cost of relief and work relief in the city was:

WPA .....	\$22,752,895
ERB .....	9,562,000
	\$32,314,895

The WPA payroll went down to \$17,833,678 in March because of the dismissal of workers, but the non-payroll expenditures for the month have not yet been computed.

Despite the rise in home relief cases in the past few months, the ERB budget has been kept down by the dismissal of more than 11,000 administrative employees since WPA took over work relief. On Aug. 9, 1935, ERB was paying 23,661 administrative employees. It now has only 12,300 of these workers on its payroll. Several thousand were taken over by WPA from the old work division of ERB.

WPA case figures do not differentiate between relief and non-relief workers. Because of the lack of skilled workers on relief rolls in certain occupations, WPA was permitted to engage up to 10 per cent of non-relief workers on most projects and up to 25 per cent on art, theatre and similar projects. It is explained at WPA headquarters that its statistical division has not had time to make this break-down, but it is generally believed in informed circles that about 10 per cent of WPA workers did not come from relief rolls, as was the case in the old work division of ERB. In any event, all are being paid by the government. Correspondingly, the 35,000 new cases since WPA came into being are not all new relief cases, but are all additions to the combined Federal, State and city governmental burden of caring for WPA and ERB.

**Says Re-Employment Lags**

Miss Charlotte E. Carr, ERB executive director, in explaining why total WPA-ERB cases have not decreased under the old ERB

figure, instead of increasing, points out that business and production increases have not been accompanied by proportionate increases in re-employment. The New York State Department of Labor factory employment index for New York City, she emphasizes, is now only 14 per cent higher than a year ago, and is 25 1/2 per cent lower than normal employment between 1925 and 1927.

"From the viewpoint of the relief load," she adds, "the most significant index is the employment index because a rise in production may be due to better production methods and full-time or overtime work for workers already employed."

As to why the home relief load has actually been increasing in the past few months, despite WPA, Miss Carr says that ERB has not changed its regulations for eligibility to relief since WPA came into being. These rules require that the applicant prove destitution. Consequently, the new applications in recent months, she holds, mean that so many more persons have come to the end of their resources and have been obliged to apply for public relief.

Miss Carr also points out that the Mayor's Committee on Unemployment Relief in its report last year estimated, on the basis of a survey by the Russell Sage Foundation, that about 1,000,000 men and women able and willing to work were unemployed, representing 689,000 families and about 2,664,000 persons. This, she adds, shows that hundreds of thousands of unemployed persons and their dependents were not on relief but were living with relatives and friends.

**Rush to Qualify for WPA**

When WPA was started its regulations providing that any those on the relief rolls could get WPA jobs, except for certain skilled occupations, caused a rush to qualify for WPA jobs by going on relief. Last November, as a result of this situation, applications for relief rose from the previous average of 8,000 or 7,000 a week to 10,000 to 11,000 a week, although the rate of acceptance continued at about 50 per cent.

"Many applicants," it is said at ERB offices, "frankly told us that they were seeking relief only to qualify for WPA jobs. Some added that they had been living with relatives or friends, who did not see why they should not take the opportunity of getting on the WPA payroll when so many government jobs were being opened up. We did nothing to encourage this situation, but we could not stop it. All we could do was to investigate thoroughly and apply our regulations before granting relief."

Miss Carr strongly rejects the theory of critics of the relief system who argue that the present system of government aid, especially since WPA was started, has made it too easy to get relief, has broken down standards of independence on the part of the public and has encouraged people to go on relief when not absolutely necessary. "It is a rare case," she replies,

when some one wants to go on relief. Most of them go through terrible mental anguish before trying themselves to apply."

Some persons closely associated with ERB field work, however, report a noticeable difference in the attitude of applicants for relief as compared with a year or two ago. In these circles it is said that relief appears to have been made "respectable" in the public mind, and that the shame-faced, head-hanging appearance which formerly characterized most applicants at home relief district offices is now much less common.

**Denies Frauds in ERB**

Miss Carr denies emphatically charges that some persons are fraudulently getting home relief while they or members of their families are working on WPA. The careful inspection service of ERB, she asserts, makes such frauds impossible.

She explains that the 13,640 persons now receiving supplementary home relief in addition to holding WPA or other jobs are entitled to do so. When a member of a home relief family is transferred to a WPA job paying at least \$2 less than the family's home relief budget, it is explained, ERB on application supplements the WPA wage to the extent of the difference between that wage and the previous home relief budget allowance.

For example, a family of ten persons on home relief might receive \$57 a month. A member of such family might be transferred to a WPA job paying \$60 a month. ERB would then give supplementary relief in the extent of \$37 a month, in addition to about \$8 a month allowance for the employed member for clothing, care for and from work and luncheon on actual working days.

When two members of a family have WPA jobs no supplementary relief is allowed.

Other cases involve women workers who receive supplementary home relief and whose earnings ERB has found that their earnings are inadequate for the support of themselves and their families. Most of them are domestic servants, factory workers, clerks, janitresses and other service employes. Many are part-time workers. Three-fourths, according to ERB, receive less than \$5 a week.

**Would Continue the WPA**

Miss Carr argues for the continuance of WPA, predicting that a serious social problem will result if the government fails to provide work for the unemployed and lets them remain idle on home relief or the dole. Unless the government or the private industry provides work for the unemployed, she says, millions of former workers will lose their work habits and become unemployable.

An encouraging note is struck by Miss Carr in emphasizing that new applications for relief have been decreasing and the "closing" of cases going off relief has been increasing in ratio to applications in the last

few weeks. Immediately after WPA announced in November that no more jobs were available, applications for relief began to drop. From more than 10,000 a week, they have now fallen to 2,184 in the week ending April 3, 1936. In the same week there were 2,644 re-applications from persons formerly on relief. To meet the problem of those afraid they could not get back on relief if they took regular jobs which might prove only temporary, ERB gives a letter to every person taking such a job and reinstates him within forty-eight hours after he appears with the letter at the end of the job, if investigation shows him still in need.

Although the recent dismissal of thousands of WPA workers has sent many back to ERB for reinstatement, WPA and ERB officials are cooperating on this problem. The decision of WPA to reinstate dismissed workers with large families, and to confine dismissals largely to single men and others without dependents is expected to help this situation.



## TREASURY DEPARTMENT

WASHINGTON

ASSISTANT SECRETARY

April 15, 1936.

MEMORANDUM FOR MRS. KLOTZ:

I am attaching hereto the copies of letters to Congressman O'Connor, of New York, that I discussed this morning with the Secretary at the 9:30 meeting.

As you will notice from the attached file, I was able to locate Frank McNally in the Procurement Division of the Works Progress Administration in New York. Mr. McNally, who is a World War Veteran, is an arrested tubercular as a result of his service, and as the position to which he was assigned was indoors, he could not continue in same. Captain Collins, of Admiral Peoples' office, advised me that Mr. Herzog, who is in charge of the Works Progress Administration in the State of New York, could place McNally in an outside position in his organization. I contacted Vincent Dailey in behalf of McNally, but he wanted some assurance that we could persuade Mr. Forde, who is in charge of the Procurement work for W. P. A. in New York, that he should have some recognition in Mr. Forde's office. He insists that Forde has secured most of his personnel by contacting Bob Moses.

The particular thing that I spoke to the Secretary about was the fact that I had previously discussed this matter with Mr. McReynolds, who thought it would be well for him to visit Forde's office, and without attaching any political significance to same, to discuss the matter of personnel in general with Forde in an endeavor to ascertain whence he secured most of his personnel.

Will you please return the attached file when it has served your purpose?

*Stephen B. Gibbons*

January 28, 1936

Dear John:

Referring to your telephone call in behalf of Frank McNally of 56 Seventh Avenue, New York City:

Captain Collins advises me that at his request Mr. Forde had McNally call on him and Forde regards him as very high class and hopes to be able to place him within the very near future. Captain Collins has assured me that he will follow the matter up with Mr. Forde, and I in turn will follow it up from this end, so that I hope to see him placed without much delay.

Sincerely yours,

(Signed) Steve

Hon. John J. O'Connor,  
House of Representatives,  
Washington, D. C.

SBG/hm

COPY

February 15, 1936

Dear John:

Referring to my letter to you of January 28 regarding Frank McNally, of 56 Seventh Avenue, New York City, I am glad to advise that Captain Collins informs me that McNally has been placed as a Voucher Examiner under Mr. Forde in New York.

Sincerely yours,

(Sgd) Steve

Hon. John J. O'Connor,  
House of Representatives,  
Washington, D.C.

COPY

February 29, 1936

Dear John:

Thank you for your letter of February 26, advising that Joseph Flanagan, Jr., has been appointed a Deputy Marshal in New York.

I note that you state you are particularly interested in Frank McNally. Under date of February 15 I wrote you advising that I had been informed that Mr. McNally was placed as a Voucher Examiner under Mr. Forde, the State Procurement Officer.

Sincerely yours,

(Signed) Stephen B. Gibbons

Honorable John J. O'Connor,  
House of Representatives,  
Washington, D.C.

April 13th

Charles Schwarz, one of Mr. Gaston's publicity men in Chicago, came in to see the Secretary yesterday and told him that the District Attorney's office in Chicago is filled with a lot of crooks. Mr. Morgenthau called the Attorney General and told him that he would like to send over Mr. Gaston and Mr. Schwarz who have some very interesting stories to tell him about Igoe and his office. H. M. Jr. felt that since Schwarz has proof that these stories are true that the Attorney General would want to know about them. H. M. Jr. asked the Attorney General whatever use he makes of the information Schwarz gives him to please protect Schwarz as he comes from Chicago.

April 13

The Secretary entertained at dinner last night in honor of Mr. K. P. Chen, head of a delegation of Chinese bankers and government officials now in this country. Mr. Chen is managing director of the Shanghai Commercial and Savings Bank and a member of the standing committee of five of the Currency Reserve Board of China. Others of the delegation, who were guests at the dinner, were Mr. P. W. Kuo, Director of the Foreign Trade Bureau of the Ministry of Industry and President of the South-eastern University at Nanking, and Mr. Y. C. Koo, Sub-Manager of the Chung Foo Union Bank and Counselor of the Executive Yuan. The guest list also included:

Ambassador Sze,  
 Speaker Joseph W. Byrns,  
 Mr. Shiu Lao, First Secretary of the Chinese Embassy,  
 Mr. Ling Tsui, Second Secretary of the Chinese Embassy,  
 Senator King,  
 Senator George,  
 Congressman Hamilton Fish, Jr.  
 Congressman Sol Bloom,  
 Mr. Joseph P. Broderick, Acting Chairman of the Federal Reserve Board,  
 Dr. Stanley K. Hornbeck, Chief of the Division of Far Eastern Affairs, State Department,  
 Mr. Maxwell M. Hamilton, Assistant Chief, Division of Far Eastern Affairs, State Department,  
 Mr. Warren Lee Pierson, President of the Export-Import Bank,  
 Mr. Robert V. Fleming, President of the American Bankers Association,  
 Mr. Martin R. Nicholson, Treasury Attache at Shanghai,  
 Mr. Herman Oliphant, General Counsel of the Treasury Department,  
 Mr. Wayne Taylor, Assistant Secretary of the Treasury,  
 Mr. Henry Morgenthau, Sr.,  
 Mr. Archie Lochhead, Technical Assistant to the Secretary of the Treasury.

Monday Night,  
April 13, 1936

The Secretary requested Assistant Secretary Taylor, Mr. H. D. White, and Mr. Archie Lochhead to meet at his home at 8:30 PM to discuss the probable proposals which might be made by Mr. K. P. Chen of the Chinese financial mission, and what the attitude of the Treasury Department should be toward these proposals. There was a general discussion of the Chinese monetary system and the difficulties and uncertainties with which it had to contend. The silver policy of the United States in relation to the Chinese problem was also discussed.

The Secretary stated that unless his decision was changed by subsequent information or developments he would propose to them that the Treasury enter into a contract to purchase an amount of five million ounces of silver each month for the remaining months of 1936, beginning with May, the price of this silver to be fixed each month at the rate of the day, or an average rate over an appropriate period. His reasons for this decision were as follows:

(1) The purchase of this amount of silver would have no particular effect one way or the other on the monetary position of the United States, but on the other hand might help to tide China over the critical period. The real facts concerning China's position and ability to maintain a managed currency are extremely difficult, if not impossible to obtain, and in the circumstances an arrangement for the purchase of a large block of silver from them might be difficult to justify.

Monday Night, April 13, 1936

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(2) The Silver Purchase Act authorizes and directs the Treasury to purchase silver until it equals 25% of the monetary reserves, or until the price reaches \$1.29, so that the purchase of a reasonable amount of silver from China would be in keeping with the terms of the Silver Act.

MEMORANDUM

April 13th, 1936.

Dr. Stuart A. Rice, Chairman of the Central Statistical Board, Dr. M. A. Copeland, of the Central Statistical Board, Dr. Seltzer, Miss Lonigan and Mr. McReynolds met with the Secretary at 11 A. M. Monday the 13th. The Secretary explained that the information available with respect to relief activities of the Federal Government, as well as state and municipal governments, indicates that although business activity is increasing to a considerable extent and private employment is increasing slightly, the relief burden is also increasing. Furthermore, he pointed out that the cost per person of relief employment is increasing rapidly. The Secretary explained what information along this line had been gathered by the Treasury, under Miss Lonigan's direction, and asked that the Central Statistical Board undertake to produce, or have produced for them, reliable and current information as to the number of people on work relief and home relief in the various states, comparable in scope and form to the financial statements on emergency appropriations furnished him in ten-day periods by the Treasury Accounts Office.

Dr. Rice promised to study the problem for a day or two and come back to discuss it further with the Secretary. The Secretary offered Dr. Rice assistance by Miss Lonigan and any other Treasury personnel now connected with this work that he might require.

McR:gmc

To: The Secretary  
From: H.E.G.

April 14

Mr. Oliphant was in your office when I came in at 9:15. You said that I had talked to you on the walk down from your house this morning about whether you should appear at the tax hearings and that I had said I thought it important that you should appear, the reason being that newspaper men were already expressing the thought that you were deliberately avoiding the hearings and probably "had your fingers crossed" on the whole plan. I repeated that I had that opinion and ~~that I had that opinion and~~ that I ~~thought~~ thought we would not get a satisfactory bill unless it was made as plain as possible that the project really had the Administration's backing and was not just a gesture. Mr. Oliphant then said that this consideration put a different face on the matter and that he thought you ought to appear. In not advising you to get into it he had been thinking mainly of the physical strain, ~~which~~ to which you would be exposed. You said that we would be surprised to learn the names of some of the people who had advised you to keep out of it, giving as a reason the harm that it would do to your future. I said I hadn't considered that angle of it, because I knew you wouldn't give it any consideration, and the only argument against your appearing that would have any real weight would be the physical one. You said that as for that you were feeling better every day and were able to do a lot of work and that we both knew that taking care of your political future meant nothing whatever to you; that our object here in the Treasury was to do the job. We then discussed the preparation of your address to the Senate committee and you said you thought you should have material to meet some of the principal arguments against the plan. You hoped to have a chance to speak to the President about it at lunch today; though he would be in a hurry on account of the ball game.

April 14, 1936

Ambassador Sze, Mr. Chen, Mr. Koo, Mr. Taylor, Mr. Lochhead and Mr. White from Haas' division, met with the Secretary today.

Mr. Chen presented the Secretary with various memoranda on the Bank of China, Central Bank of China, Farmers Bank, Bank of Communications and funds of the Boxer Indemnity and agreement with Otto Wolff.

There follows a report of the discussion:

Mr. Chen: The other day I gave you a memorandum in behalf of Dr. Kung. Have you any question to ask in connection with that?

HM, Jr.: No, not just now. I thought I would throw out a couple of suggestions today to try to advance this thing, if agreeable to you and to the Ambassador. I thought possibly Mr. Taylor, Mr. Lochhead and Dr. White might take the time, if you had the time, to go into more detail on this thing. I just wanted to throw out a couple of suggestions -- a lot of these things are technical -- coins; all that business -- and it takes more time and if I just gave out a couple of suggestions then you might take a couple of days to talk it over with these people, because Dr. White has been making for me and Mr. Haas an intense study of China. He is an economist. We have been following this thing ever since we got interested and he has been collecting statistics on China and particularly on silver. I don't like to use the word "authority", but I will say he has acquainted himself with the silver question.

Mr. Chen: I am sure I will learn something from Mr. White.

HM, Jr.: You will learn from each other and there are a lot of things he would like to know. In the first place -- I can't give a technical explanation -- they want to discuss this; as we understand it, Chinese money at present is technically attached to Sterling. That is the way you understand it?

Mr. Lochhead: Official rates are quoted Sterling and Dollars. You quote your official rate, each day, Sterling and Dollars. Sterling rate has remained constant and Dollar rate shifts.

Mr. Chen: So far, the Sterling rate in relation to the Dollar rate has been comparatively stable. Our currency is

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attached to world's currency. We have not linked to any particular currencies.

Mr. White: But when there has been a shift in the Sterling-Dollar rate which has in your opinion necessitated a change, you have changed the Dollar rate and kept the Sterling rate, the official rate, the same so it has not changed officially. The Bank of China rate has remained exactly the same.

Mr. Chen: Because we had to change it, we were afraid Shanghai market would sell against Sterling.

Mr. Lockhead: The same thing would be accomplished either way. You would have to shift one or both to accomplish that.

Mr. White: But you have shifted the Dollar.

Mr. Chen: The Dollar, yes. We have shifted the rate after consultation. Dr. Kung sent a telegram ....

HM, Jr.: I just want to throw out these things and then it gets into a technical discussion and it will take hours to develop it and while it is being discussed, I do not want to sit in on it. The thought these gentlemen have -- the Canadian dollar is not officially tied to either Sterling or the United States Dollar and they operate in between, and the thought they had was that we simply follow -- we will be perfectly frank; it just does not make much difference, but we believe (maybe we are wrong), the way the matter stands now is that England can say China is in the Sterling area. Again, maybe it's one of these matters of "face"; maybe we are wrong. On the other hand, take the Canadian dollar, which is a part of the British Empire. It is neither attached to Sterling nor the Dollar and operates in between both.

Mr. Chen: Yes.

HM, Jr.: I am just throwing that out. The only suggestion we make is the possibility of your examining how the Canadian exchange is handled as between the Dollar and Sterling. Canada is not considered in the Dollar area and is not considered in the Sterling area and she operates in between. As we understand it today, Great Britain could say that China is in the Sterling area. It's not very important, but on

the other hand, it's one of the things that I would like to "throw into the pot" and I would like you to discuss it with these people. I don't consider it unreasonably; only suggesting you might do it as Canada does.

Mr. Chen: What is Canada's?

HM, Jr.: I would rather not now, but they have all the time and are at your disposal, Mr. Chen, to go into that discussion. As I say, it will take hours or days and I wanted to advance this thing.

The other thought we had in mind is this: We make a suggestion of the possibility of your sending silver over to San Francisco or New York and the possibility of your borrowing against that silver. We have done something like that with Mexico. It may interest you; it may not. It is something you can take under consideration. When I say "borrow", I mean on exchange. The other thing, when it comes down to a question of buying more silver, quite frankly we don't want to buy, at this time, a lump sum of silver for a number of reasons which I will go into if you wish me to, but as a counter proposal, the thing we are suggesting is the possibility of our buying 5,000,000 ounces of silver a month for the next eight months, which would take it up to the first of January. In the first place, the silver we have from you now we have not been able to refine it and it will take us to the first of January to refine the silver we have now and melt it down, but there is not capacity in the United States to melt it down. Is that right?

Mr. Lochhead: It will take pretty nearly to the end of January before we finish up the last 50,000,000 ounces.

HM, Jr.: But the suggestion we would like to put on the table is the possibility of our buying 5,000,000 ounces of silver a month, beginning with May, the price to be determined each month, either the middle of the month or take the average of the month; whatever is fair; whatever is fair. But it will have to be a monthly price. In other words, we fix the price every day with Canada and Mexico and we would like to do something like that with China. It will be an average price for the first two weeks of the month -- the United States price; the Treasury price. We post a price every day at noon. From our standpoint, there

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are many advantages to buy this each month. So there will be 40,000,000 ounces of silver to the first of January, the proceeds from this silver to be used just the same way as previously -- deposited here. This, I take it, would be Bank of China silver so it will all be deposited with the Federal Reserve.

Mr. Chen: I think Bank of China also has some accounts with other banks. That's their commercial deposit.

Mr. Lochhead: This would not be a commercial deposit; it would be fiduciary money.

HM, Jr.: We would very much prefer to have it with the Federal Reserve, because, as I understand, some of the other silver was not Bank of China silver so it could not be treated as National silver, so I take it that this silver that we would buy would all belong to the National Government.

Mr. Chen: I think proceeds from such sales will be proceeds as previously; the same as last time.

HM, Jr.: Yes; that the money would be used for your stabilization purposes and if you wanted to convert part of it into gold, it would be entirely agreeable to us.

Mr. Chen: The question is, Shall we discuss it together or later?

HM, Jr.: Please.

Mr. Chen: I just got telegram from Shanghai. The nationalization of silver in China is quite successful. More silver came in so our silver is accumulating more than we expected, so probably, for discussion, for your consideration, probably we will find it necessary, in order to maintain the confidence of our new currency, it will be necessary for us to have more foreign exchange, so I just like to ask ...

HM, Jr.: Yes, but you people -- I am not going to tell you anything you don't already know. You have the largest floating supply of silver in the world. From 1 to 2 billion ounces in China with the people and, if I may say so, it's more to your interest what the price of silver is going to be

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than to almost any other country in the world.

Mr. Chen: Yes.

HM, Jr.: We want to be practical about this thing.

Mr. Chen: Yes! Yes!

HM, Jr.: As far as I can tell, we don't contemplate any particular move which would disturb the price of silver and talking for myself, personally, the thing I would like to see is to see the price of silver as near stable as possible. I think everybody recognizes that the thing that is good for everybody who has silver is a stable price.

Mr. Chen: Our interest in that respect is just the same as yours.

HM, Jr.: The fact that you have a lot of silver does not make our problem more difficult, but makes your problem more difficult because, let's be frank, the price of silver could go to 24 cents and it would not disturb the internal or external value of the dollar. Quite true, the amount of silver we now have in our vaults for which we paid 85 cents would be greatly depreciated, but on the other hand, it would not be a national calamity for the United States. But, on the other hand, you having been a hard money country and your money having been silver, it's tremendously important to you what the price of silver is.

Now, we want to do everything we can within reason to help you and, so far, the negotiations which we have had through the Ambassador and the purchase of the silver and what you did with the silver have been entirely satisfactory to us. Everything that the Ambassador said your Government would do, they have done it. So up to now, everything has been fine. Everything, as I told the Ambassador, as far as I am concerned, everything on the paper is not worth that, but his personal word to me is worth something; worth a lot, and I did it on his personal word, but all the agreements and all the signatures, it has been demonstrated, in this world are not worth anything; it's a matter of confidence between the people.

Mr. Chen: Yes.

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HM, Jr.: Everything up to now, everything has been fine.

Mr. Chen: What we are worrying about -- what you said is true. The silver price is very important to both of us, but worse, say, is this international payments made in certain periods of the year. We found it necessary to have more foreign exchange where, if we have it, the confidence is strengthened; if too small an amount, might find it difficult to carry it through successfully.

HM, Jr.: Would you give us a list of your payments for the balance of the year?

Mr. White: That is one of the things we want to get.

HM, Jr.: When we went into this thing before with Russia we had their foreign balance payments for the next five years.

Mr. Chen: I brought two tables with me. The table of 1934 and 1935 -- 1933, 1934 and 1935.

HM, Jr.: You have not got it for the future? Looking ahead, how much money you have to have?

Mr. Chen: We do not have table showing loans payments.

HM, Jr.: Could you cable for that?

Mr. K: We have figures for our future foreign loan services.

HM, Jr.: How much is coming due?

Mr. Chen: We have this figure here.

Mr. White: Do you also have an estimate for balance of payments?

Mr. K: For the coming year, we have not made that.

Ambassador Sze: That list they have would not include any settlement for credits in default.

HM, Jr.: Let's have the whole picture.

Mr. White: As default goes through you know what the

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commitment will be.

HM, Jr.: I don't think I understand.

Ambassador Sze: Suppose we have loan with Chicago bank which has not been paid since 1923. If settlement comes, that is not included in the annual payment.

HM, Jr.: But could not they say, These are the payments which we agreed to make over the next so many years, and then These payments are doubtful, or something like that?

Mr. K : We can make allowance for that.

HM, Jr.: This is the maximum if we pay everything and this if we get a settlement, and this is the minimum, and that would not only be Government but also include railroad.

Mr. White: You would have to go into some other details.

HM, Jr.: If you make an estimate of balance of payments, it is very important because 40,000,000 ounces may be useless to you or we might arrive at a figure that will do the trick from now until the first of January. No use trying to help them when before we start we know it is going to fail. No use making a gesture which we know before we start is going to be useless.

Mr. Chen: Our last figures for 1935, we found item on debt side is \$272,000,000 against us. Except in 1934 and 1935, these are two years payments against us. Before that we had favorable international balance.

HM, Jr.: To go into the whole question of balances, payment on the debt, is very important.

Mr. Taylor: That's the only way you can tell whether any fund which is set up will take care of the situation.

HM, Jr.: And if Mr. Chen will tell us "this is our estimated revenue. If we lose so many northern provinces, we will lose so much revenue." All this talk in the papers of what the Japanese are going to do -- if they take this province, how much loss of revenue does that mean?

Mr. Chen: The revenue for northern provinces is about \$100,000,000 a year, but payments there for troops and other

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expenses is over that, but financially it does not affect it very much. But this information is bad. People lose confidence in Government bonds, domestic bonds. And maybe there is also a pact. People lose confidence in currency.

Mr. White: Then there are numerous questions about the budget which are not clear from data they have given us, which we might want to pursue a little further.

Mr. Taylor: Did you want to mention at all the coinage problem?

HM, Jr.: That's a very difficult thing on the coinage. And the way I feel is this: for us to sit here and attempt to advise you how much silver to put in your coins, I think is a rather thankless task because it is obvious that the more silver you use in your coins -- how shall I put it -- the more of an outlet you get for the silver you have on hand, but for us to tell you so much fine or to figure the thing out, I don't think it is as important as some of these other things that we have talked about. After you have studied these things, I think you will find what is the best thing for China and whatever the best thing for China is, I am satisfied. And I don't want to have to say -- all I can say is I think (I don't know) but if you can use the maximum amount of silver, all right. I am not going to say, as so many people say, China has always had hard money; she has to have hard money. The answer is they have paper and they are taking paper. Whether silver is more useful to you in your coins or as monetary reserve, you have to think it over. It's a very difficult thing.

I think it would be a nice gesture, as long as we have always made your dies here, to have them made here rather than in England. There is a little feeling that you have always had your dies made here. We are trying to be helpful. Why take them to London? They play all these things up so. They keep throwing that in our face all the time. If you always got your dies in England, I would not say I think you ought to move them here, but you have them here so why move them to England?

Mr. Chen: I have memorandum with me on the full question of coinage and probably will postpone this discussion until I get in touch with your expert.

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HM, Jr.: Let's put it this way: I would not like to see you do anything with your coins which would look like a reflection on the United States and a leaning towards England. If, on the other hand, you do something which does not indicate a departure from what you have been doing in the past, that's agreeable to me as long as it is good for you. Do you see what I mean?

Mr. Chen: Yes.

HM, Jr.: They make so much of this Leith-Ross business. Leith-Ross, this; Leith-Ross, that! I am not asking you to do anything that isn't good for China, but, on the other hand, I get sore, you know, all the time that this is what Leith-Ross told China and this is what they are doing because Leith-Ross told them so. And we buy the silver, but China does what Leith-Ross tells them to do!

Mr. Chen: That is great deal newspaper propaganda, not actually.

HM, Jr.: I know. I am being very frank.

Mr. Chen: I come from China and I know it. Our last conferences, I wired here for your information, because you know it. But too much newspaper talk. You see, he has been there long; naturally newspapers get misinformation.

HM, Jr.: But you fellow me, Mr. Chen. I don't want you to do a single thing -- I am not going to ask you to do a single thing that is not in the interest of China, but I just don't want to give the English a little chance "to crow." That's all.

Mr. Chen: We know that. Your attitude is much appreciated in China. We know it.

HM, Jr.: This whole coinage question I think you can see a great deal more clearly after some of these other things are straightened out.

Mr. Chen: I have this memorandum, these ideas here, when we are ready for discussion, to hand over to your experts to study this matter together.

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HM, Jr.: And I would like to study it with you.

Mr. Chen: You just said about shipping silver to San Francisco and making exchange on that. What is your amount; the terms, just for study purposes.

HM, Jr.: The amount I cannot say; any reasonable amount; depends upon the study. But what we did for Mexico -- I don't think there is any secret -- they have 11,000,000 ounces in New York and San Francisco and we agreed to loan them up to 95% of the value; to give them dollars in exchange for pesos. I must keep in my memory not to say "loan!" We charge them 3%.

Mr. Chen: In connection with these two questions, we come back to that afterwards; after we have answered all your questions, we will come back to that question.

Mr. Lochhead: We exchanged pesos for dollars. We did it on exchange basis rather than on straight silver basis.

HM, Jr.: On exchange basis.

Mr. Chen: The purpose of my mission to come over here is, first, to find out how we can work this thing together. It is not spirit to get rid of our silver. We have not given that spirit. But we want to be practical as far as our currency, protection of currency, is concerned and I for myself like to be very frank in all my questions and answers and to tell you exactly what we want. You may not find it convenient to do it, but I like to give you the ideas and maybe I cable back this can't be done. It will take some time, but never mind.

HM, Jr.: I told the President at lunch today that anything I asked you, you answered me; that there was not anything I had asked that you had not answered and I was very hopeful that we could get together.

Mr. Chen: Certain things I may not be able to answer you. I have Mr. Koo here. He knows technical things more than I and I have Mr. K here to attend these conferences.

HM, Jr.: Fine! Fine! I think that's all for today. When would you like to start in really working?

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Mr. Chen: Any time. I have nothing to do here.

HM, Jr.: Taylor, how are you fixed?

Mr. Taylor: I am all right now.

HM, Jr.: Why don't they adjourn to your office?

Mr. Taylor: We can adjourn there and I am all right for an hour. That will be enough to get a pretty good start because there are a lot of questions.

HM, Jr.: How would that be? Then I think if they could go ahead with White and Lochhead and spend as much time as possible to keep pushing this thing.

Mr. Taylor: Is there anything, Mr. Chen, that you would like to introduce right now while the Secretary is here so he can be thinking about it, or would you rather wait?

Mr. Chen: I think the Secretary knows all that I am trying to ask. So I like to find out from Mr. Secretary what you would like China to do in connection with the silver price, silver situation and your picture of the reserve for Chinese currency, the use of silver. I would like to find out that.

HM, Jr.: I think what we have talked about so far is enough to keep you busy for a couple of days.

Mr. Chen: The whole question for Chinese currency is find out best way to maintain the confidence. That's only question we have in our mind; except that, we don't have anything to ask.

HM, Jr.: If you could start on some of these things and go into Mr. Taylor's office. Have you time, Mr. Ambassador, or are you going to leave Mr. Chen? That's up to you.

ABSTRACT  
of  
Agreement Made Between  
THE MINISTRY OF RAILWAYS  
and  
THE SIEMENS CHINA CO.

1. PURPOSE

For the purchase of materials for the rehabilitation of the Ping-Han Railway.

2. SINKING FUND

The Ministry has established for the purpose a Rehabilitation Sinking Fund in charge of a Special Sinking Fund Committee in accordance with the Regulations as agreed upon.

3. VALUE OF EQUIPMENT AND MATERIALS

The total value of equipment and materials which the Railway requires and which the Company agrees to supply shall not exceed 39 (thirty-nine) million Chinese Standard Dollars. These supplies shall be spread over a period of six years and the value of each yearly supply shall not exceed the amount of seven million dollars.

4. PRICES

The CIF-Prices of the equipment and materials ordered by the Railway from time to time shall be mutually agreed upon and stipulated in each individual sales contract covering such order; but in case the Ministry is of the opinion that the prices quoted are too high compared with the prevailing market prices, it reserves the right to call for tenders giving the Company the privilege to submit their tenders.

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Both parties concerned agree to adopt as permanent standard of value for the duration of this Agreement and until all promissory notes issued thereunder have been met in full the Chinese Customs Gold Unit of the present weight of fineness, namely GU 1. - being equal to 60.1366 centigrams of pure gold.

5. SALES CONTRACT

Equipment and materials shall be supplied in separate lots within six years from the date of signing this Agreement as and when ordered by the Railway and for each lot so sold there shall be signed a separate individual sales contract.

6. PAYMENTS

Upon signing of each individual Sales Contract the Ministry will remit to the Company in cash (TT) 10% of the Contract Price. The balance shall be paid to the Company separately for each shipment in two equal installments: the first in cash (TT) at the date, and the second six years from the date, of the delivery of the equipment and materials contained in each shipment.

Correspondingly at the date of delivery of each shipment under such Sales Contracts there shall be issued to the Company a Promissory Note dated on said day with interest at 6% p.a. and corresponding to the amounts and the due dates of the second instalment as set forth above.

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7. SECURITIES

The Ministry hereby declares that the Sinking Fund aforementioned is to serve exclusively for the credit extended by the Company and that the redemption of the Promissory Notes accepted by the Company shall be effected out of the said Sinking Fund in accordance with the rules agreed upon.

The Ministry hereby declares and guarantees that it will make up on its part any deficiency that may occur with regard to the remittances from the Railway Administration to the Sinking Fund and from the Sinking Fund to the Company assuming thereby the responsibility for the fulfillment of the regulations and requirements concerning the Sinking Fund.

## THE BANK OF CHINA

### A Brief Sketch

#### I. ORGANIZATION

The Bank of China was established in the first year (1911) of the Republic of China as a result of the reorganization of the Ta Ching Bank of the defunct Imperial Ching Dynasty.

The authorized capital of the Bank of China was originally fixed at \$60,000,000, a part of which to be subscribed by the Ministry of Finance, which was authorized to solicit private subscribers and to draw up measures for the organization of the Bank. The Ministry of Finance was also authorized to promulgate the laws and regulations of the Bank of China and to grant the Bank the special rights of issuing bank notes and acting as the Government depository and fiscal agent of the Government. During the tenth year (1921) of the Republic of China, the total paid up capital of the Bank, both governmental and private, amounted to over \$19,000,000. By nature, therefore, the Bank of China is semi-governmental.

When the Central Bank of China was established in the seventeenth year (1928) of the Republic of China, the status of the Bank of China underwent a change. The National Government formulated the banking laws for the Bank of China, under which the Bank of China has become a bank for international exchanges. At that time, the amount of Government shares in the Bank was only \$5,000,000, with private shares amounting to \$20,000,000. Despite this change of status, the Bank of China has retained the special rights of issuing bank notes and acting as a partial Government depository.

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In March of last year, for the purpose of relieving the desperate condition of industrial and commercial enterprises and enhancing the activities of the money market, the National Government appropriated \$15,000,000 for increasing the capital funds of the Bank of China, bringing the Bank's present paid up capital to the amount of \$40,000,000. At the same time, the Bank of China Law has been amended and sanctioned to take effect.

According to the provisions of the amended Bank of China Law, the organization of the Bank shall consist of 21 directors and 7 supervisors. Nine directors and three supervisors shall be appointed by the Ministry of Finance, while the other twelve directors and four supervisors shall be selected from among the private shareholders holding over one hundred shares of the Bank's capital stock by the entire body of private shareholders.

The term of office for the directors shall be four years, and the term of office for the supervisors shall be three years. A Committee of Managing Directors of seven shall be elected by the Board of Directors, and the Ministry of Finance shall appoint among the Managing Directors a Chairman for the Board of Directors.

There shall be one General Manager to execute the banking business. The General Manager shall be selected among the Directors jointly by the Chairman of the Board of Directors and the Managing Directors, and, then, the name of the General Manager-elect shall be submitted to the Ministry of Finance for approval.

The Head Office of the Bank of China is situated in Shanghai. Under the Head Office there are a number of branches and sub-branches, bank agents and correspondents, and foreign branches and agents.

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The Bank of China has a history of more than twenty years, which fact has given it the opportunity for the establishment of branches and agents all over the country. Although Bank of China has only one branch office in London and one in Osaka, Japan, at the present time, it is going to have another one in New York in the immediate future, and its future prospect for establishing more foreign agencies cannot be slighted. As to the financial standing of the Bank of China, up to the end of June last year, its total assets amounted to over \$1,000,000,000, which suffices to prove the strength of the Bank and the condition of its business.

## II. CONDITION OF ASSETS AND LIABILITIES

The condition of assets and liabilities of the Bank of China is vividly revealed in the accompanying balance sheet of the Bank as of June 30, 1935.

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Bank of China

Balance Sheet June 30, 1935.

ASSETS.

Subscribed Capital	40,000,000.00
Reserve Funds	2,185,919.83
Special Reserve Funds	1,251,000.01
Undivided Profit	16,671.59
Bank Notes Issued	168,789,494.93
Remittances and Drafts Issued	11,623,611.21
Travellers' Letters of Credit Paid in advance	22,678.60
Bankers' Deposits	120,719,051.51
Overdrafts with Bankers	5,010,404.34
Current Accounts	112,168,557.72
Special Current Accounts	33,904,697.86
Dividends Payable	90,573.00
Temporary Deposits	16,629,088.44
Inward & Outward Bills Prepayments	1,371,107.27
Certified Checques	457,369.91
Cashiers' Orders	13,051,886.58
Accounts Payable	1,312,497.41
Items Payable Under Contract	1,234,241.63
Fixed Deposits	175,217,753.85
Special Fixed Deposits	5,985,303.15
Staff Savings Accounts	719,410.65
Staff Annuity Accounts	611,053.23
Contingent Accounts	14,056,684.23
Reserve Interest Account	20,015,564.90
Special Deposits	101,242,430.35

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Accrued Interest Payable	8,051,417.58
Interest Received in Advance	76,835.76
Collections	7,986,252.48
Contracts Payable	140,507,782.47
Due to Customers for Bonds Brought Forward	3,352,168.65
Bonds Sold Forward	3,352,516.24
Engagements (Liability of Bank) Account	23,277,517.90
Liabilities Under Trust	9,949,247.74
Savings Department Current Account	495,573.96
Net Profit	<u>235,779.84</u>
TOTAL	\$ 1,044,972,044.82

LIABILITIES

Cash	45,724,907.40
Reserve for Bank Notes Issued	168,789,494.93
Bankers' Overdrafts	2,039,097.25
Call Loans to Bankers	10,968,356.40
Deposits with Bankers	116,540,604.41
Overdrafts on Current Accounts	41,813,573.88
Secured Overdrafts on Current Accounts	60,502,650.49
Short period Secured Loans	32,189,195.13
Temporary Debits	18,374,235.83
Items Receivable Under Contracts	2,388,680.52
Bills Discounted	5,797,000.83
Inward Documentary Bills	3,451,692.76
Outward Documentary Bills Purchased	13,784,295.12
Outport Bills Purchased	9,832,000.99
Fixed Loans	41,794,706.62
Fixed Loans Secured	37,425,982.48
Packing Credits	1,147,299.28

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Rent Deposits Made	228,106.16
Loans to Central Government	99,993,729.78
Loans to Local Governments	10,768,092.51
Overdue Loans	24,526,186.85
Forfeited Securities	3,582,131.99
Accrued Interest Receivable	4,406,340.67
Investments	86,646,903.02
Bank Premises	7,570,684.84
Business Fixtures	850,854.29
Preliminary Branch Expenses	85,266.81
Bank Notes Tax and Printing Cost	273,533.78
Customers' Collections	7,986,252.48
Exchange Contracts Receivable	140,558,736.79
Bonds Brought Forward	3,352,168.65
Due from Customers for Bonds sold Forward	3,352,516.24
Engagements (Liabilities of Customer) Account	23,277,517.90
Trust Assets	9,949,247.74
Savings Department Capital	<u>5,000,000.00</u>
TOTAL	\$ 1,044,972,044.82

THE CENTRAL BANK OF CHINA

CONDENSED STATEMENT OF CONDITION, HEAD OFFICE AND BRANCHES,  
AS OF DECEMBER 31, 1935.

	<u>ASSETS</u>	<u>DOLLARS</u>
Cash:		
Cash in Vault . . . . .	\$44,675,547.21	
Cash in Transit . . . . .	42,733,870.11	
On Call with Banks. . . . .	<u>176,063,992.03</u>	263,473,409.35
Reserve against Notes in Circulation:		
Cash. . . . .	\$119,115,545.81	
Securities. . . . .	<u>60,808,000.00</u>	179,923,545.81
Loans, Discounts, and Overdrafts . . . . .		154,313,340.66
Securities Owned. . . . .		252,904,406.16
Advance of Capital to the Central Trust of China. . . . .		10,000,000.00
Bank Premises. . . . .		14,549,509.17
Furniture and Fixtures . . . . .		656,732.84
Accrued Items and Accounts Receivable. . . . .		8,049,807.90
Bills Received for Collection as per contra. . . . .		1,524,056.31
Customers' Liabilities for Letters of Credit issued and Acceptances and Guarantees given as per contra. . . . .		33,293,452.30
Other Assets . . . . .		<u>12,854,508.70</u>
TOTAL		<u>\$931,542,769.20</u>

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<u>LIABILITIES</u>	<u>DOLLARS</u>
Capital . . . . .	\$100,000,000.00
Reserves . . . . .	3,845,136.17
Notes in Circulation . . . . .	179,923,545.81
Deposits . . . . .	595,940,737.27
Accrued Items and Accounts Payable . . . . .	3,241,849.45
Bills for Collection as per contra . . . . .	1,524,056.31
Letters of Credit issued and Acceptances and Guarantees given as per contra . . . . .	33,293,452.30
Other Liabilities . . . . .	4,725,652.25
Net Profit for the Year ended December 31, 1935 . . . . .	<u>9,048,339.64</u>
TOTAL	<u><u>\$931,542,769.20</u></u>

Preliminary figures, not yet approved either by the Board of Directors or by the Supervisory Committee.

The Farmers' Bank of China.

This bank was founded in April 1933 in Handow by the Military Headquarters of General Chiang Kai-shek, with a capital of \$2,500,000 and it assumed the name of the Agricultural Bank of Honan, Hupeh, Anhwei, and Kiangsi Provinces. In 1935 it adopted the present name and increased its capital to \$5,000,000.

Originally established to facilitate the rehabilitation of farm land recovered from the communists, the object of the Bank now is to help agriculture in China in general. Its branches, now numbering more than 20, are doing business in a wide area far beyond the limits of the above mentioned four provinces.

The Bank since its inception was authorized to issue notes. In February of this year, by a special order of the Ministry of Finance, the Bank was permitted to continue enjoying the right of note issue with a maximum limit of \$100,000,000, qualified by the proviso that the note issue reserve should be in the custody of the Central Bank of China. The Bank was also authorized to take over, for the account of the Currency Reserve Board, the unissued notes and the reserve against the issued notes of the provincial banks in the provinces where the Bank has branches.

Although the Head Office of the Bank is at present in Hankow, it will be moved to Nanking in the near future. Its Board of Directors is presided over by Dr. H. H. Kung, Minister of Finance.

The following tables show the financial position of the Bank at the close of February, 1936:-

Report of note issue of the Farmers' Bank  
February 1936.

	<u>Issue at end of last month</u>	<u>Issue at end of this month</u>
10 cent subsidiary notes	\$6,823,123.00	\$ 6,673,293.00
20 cent subsidiary notes	4,977,209.00	4,948,509.00
50 cent subsidiary notes	972,379.00	970,079.00
Dollar notes	16,998,596.00	16,998,376.00
Total	<u>\$29,771,307.00</u>	<u>\$29,590,257.00</u>

Farmers' Bank Deposits  
February 1936.

Fixed deposits	\$ 8,311,902.80
Current deposits	45,593,261.36
Special current deposits	7,165,835.85
Interest payable	6,100.00
Cashier Orders	84,285.00
Total	<u>\$61,161,385.01</u>

Farmers' Bank Loans  
February 1936.

Loans on credit	\$ 3,242,212.34
Loans on security	7,733,480.08
Discounts	233,165.00
Bills purchased	630,200.51
Overdrafts on credit	12,051,818.77
Overdrafts on security	1,811,280.32
Letters of credit	387,110.00
Loans to farmers	99,989.06
Accounts receivable	41,044.56
Total	<u>\$26,230,300.64</u>

## THE BANK OF COMMUNICATIONS

(For the Development of Industries of the Country)

Its Organization: The Bank of Communications was established in the Eleventh month of the 33rd year of Emperor Kwang Hsu, Tsing Dynasty (November 1907). It was a joint enterprise of the Government and the merchants with a capital of 5,000,000 Kuping Taels. In February of the following year, the head-office at Peking began operation. In June the capital was increased to 10,000,000 taels, with 5,000,000 Kuping taels actually paid up.

After the founding of the Republic, the Bank of Communications Regulations, were promulgated authorizing it to issue bank-notes and act as Government depository and fiscal agent, thus giving it, as well as the Bank of China, the status of a Government Bank. Its status, however, was changed on the establishment of the Central Bank of China in 1928. A set of new regulations of the Bank of Communications was promulgated, making its function to develop industries of the country. The Government shares amounted to \$2,000,000, the total amount of capital, with public shares, being \$10,000,000. It still retained the privilege to issue bank-notes and act as government depository and fiscal agent in a limited capacity.

In March, 1935, its capital, as well as that of the Bank of China, was increased for the purpose of relieving the various trades and the money market. \$10,000,000 Government shares were increased, making the total amount of capital \$20,000,000. The Regulations were amended and approved.

Under the amended Regulations, the Ministry of Finance appoints nine of the twenty-one directors and three of the seven

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supervisors, the rest to be elected at the shareholders general meeting from amongst merchants holding more than 100 shares. The term of tenure for the directors is fixed at four years; that for supervisors, three years. Seven of the directors are managing directors, one of whom is to be designated by the Ministry of Finance as chairman of the Board of Directors. For the actual management of the Bank, the chairman of the Board, with the advice of the managing directors and the approval of the Board, appoints one general manager from amongst the directors, whose appointment to be reported to the Ministry of Finance for approval and record.

The head-office is located in Shanghai; branches have been opened in the various commercial ports in the country and abroad. There are now 7 branches, 72 sub-branches, and 25 sub-offices. It can make remittances to 581 places in the country.

The bank has a history of 30 years and its business is very prosperous. Its assets amount to \$500,000,000 at the end of June, 1935.

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BANK OF COMMUNICATIONS

(Balance Sheet, 30th. June, 1935.)

Commercial Banking DepartmentA. Liabilities.

Capital paid up	\$ 19,715,650.00
Reserve and undivided dividends	3,617,638.35
Notes in circulation	91,591,972.98
Deposits	252,810,414.79
Due to Banks	20,000,000.00
Inter-departmental accounts	46,516,646.79
Reserve for bad debts	9,520,077.63
Other liabilities	14,853,794.03
Net profits for the term	<u>474,466.77</u>
Total liabilities	\$459,100,661.34

B. Assets.

Cash in vault and due from other banks	\$ 68,227,646.63
Reserve against notes in circulation	91,591,927.98
Loans, discounts, and overdrafts	236,786,462.34
Securities purchased	37,733,290.76
Bank premises, furniture and fixtures	5,429,934.41
Advance of capital to Savings Department	500,000.00
Other assets	<u>18,831,354.22</u>
Total assets	\$459,100,661.34

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Savings DepartmentA. Liabilities.

Capital	\$ 500,000.00
Reserves	246,501.19
Deposits	37,712,167.29
Sundry deposits	551,345.19
Interest accrued payable	737,963.68
Other liabilities	35,720.16
Net profits for this term	<u>199,386.11</u>
Total liabilities	\$39,983,083.62

B. Assets.

Cash	\$ 2,389,977.58
Loans	7,789,967.55
Securities bought	9,966,305.49
Bank premises, furniture and fixtures	1,664.13
Inter-departmental accounts	<u>19,135,666.79</u>
Total assets	\$39,983,083.62

RULES GOVERNING THE DISPOSAL OF FUNDS  
OF THE SINO-BRITISH BOXER INDEMNITY  
FOUNDATION

1. Railways and other productive enterprises wishing to apply for long term or temporary loans must send in their application to the foundation for consideration.
2. The application must state in detail the plan of the enterprise, the sum needed, the condition of repayment of capital and interest, and other relevant information.
3. Such application involving funds either deposited in China or in London must be submitted to the Board of Trustees for approval. After this such applications must be handed over to the Technical Committee and Finance Committee for examination and reported back to the Board of Trustees for final decision.
4. If the request is granted, the office of the Foundation will at once negotiate with the proper authorities and draw up the necessary agreements.
5. The organization, in drawing up the agreement, must first fulfil all legal and administrative requirements. Once the agreement is signed, they cannot use them as pretexts to delay the execution of the agreement.
6. The draft agreement or contract should include the following items:
  - a. Name, kind, and quantity of material to be bought.
  - b. Price of material must specify C.I.F. Shanghai or other ports. If the price is not certain, give the estimated price.

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- c. All required duties and taxes to be paid by the organization concerned.
- d. Date of delivery, once or in instalments.
- e. Methods of repayment of capital.
- f. Method of repayment of interest at 5% per annum.
- g. Price of materials in pounds sterling must be calculated into Chinese currency.
- h. Require payments specified in f. and g. must be paid out regularly from the regular income or receipts of the organization or enterprise.
- i. All loans must be guaranteed by the party responsible for the organization.
- j. Draft agreement or contract must be signed by the following parties:
  1. The organization applying for the loan.
  2. The enterprise applying for the loan.
  3. The Board of Trustees.
7. When draft agreement is signed, one copy of it will be sent to the Sino-British Purchasing Commission for execution and one copy to be kept by the office of the Foundation.
8. Upon the receipt of the report from the Purchasing Commission that the material has been purchased, the Foundation will proceed to sign the final agreement or contract in place of the draft agreement.

9. After the complete arrival of the material purchased, the repayment of capital and interest should be made once a year or semi-annually.
10. Capital and interest on all loans should be calculated in Chinese currency. In case of loans for materials calculation should be based on the average price of silver in London on the day of payment.

ABSTRACT OF AGREEMENT

between

THE BANK OF CHINA, acting on its own behalf and on behalf of a Banking Syndicate, and  
THE FIRM OF OTTO WOLFF, acting on its own behalf and on behalf of a group of German Manufacturers.

1. PURPOSE

To build a railway line in Kiangsi between the cities of Yueshan and Nanchang.

2. FINANCING

The Ministry of Railways of the National Government of the Republic of China and the Provincial Government of Kiangsi agreed each to issue and hand over to the Bank of China bonds of an aggregate amount of Yuan 12,000,000.00 (Yuan Twelve Million), that is altogether Yuan 24,000,000.00 (Yuan Twenty-four Million) for the purpose of securing and repaying the advances to be made by the Banking Syndicate and the Company to the Railway.

3. MATERIALS

The Company agrees to furnish railway materials such as rails, bridge materials, rolling stocks, etc. to the Railway on the terms agreed upon, up to a value of not exceeding at the time of deliveries Yuan 8,000,000.00 (Yuan Eight Million) on credit.

4. INTEREST RATES

The advances to be made by the Company shall bear interest at the rate of seven percent (7%) per annum to be paid semi-annually on June 30 and December 31 of each year. The payment of interest shall have priority over the payment of capital.

5. PAYMENTS

The Company agrees that all proceeds whether of interest or redemption payments accruing from the Bonds shall be pooled in the joint interest of the Banking Syndicate and the Company, the Company to receive out of the pool in repayment of interest and advance the amounts agreed upon.

In case of the proceeds of the Bonds falling short of the amounts receivable by both the Banking Syndicate and the Company, the amounts falling short are to be distributed by the Bank to the Company and to the Banking Syndicate in the proportion of the amounts payable to either party according to the schedule agreed upon. In such case the unpaid portion of such amounts shall be paid as soon as the proceeds of the Bonds permit, subject however to distribution of surplus proceeds, if any, in proportion to the amounts in arrears and receivable by the Bank and the Company.

6. PRICE OF MATERIALS

The prices of the Railway materials to be supplied by the Company shall be fixed by mutual agreement between the Company and the Railway as soon as the specifications of the more important materials such as rolling stocks, rails, bridge materials, etc., are available.

7. TRANSPORTATION OF MATERIALS

It is agreed that all the supplies by the Company from Germany are to be carried in German ships at a rate not less

favorable than those obtainable from shipping companies of other nationalities. The Bank agrees to pay the freight including insurance out of the construction loan provided for; such payment to be made in cash in Berlin or in Shanghai at the option of the Company on the day of Shipping from Germany.

8. BANK ACCOUNT

It is agreed that for any amount actually received by the Company out of the pool or out of the net revenues of the Railways, the Bank shall open an account for the Company either in Chinese Standard Dollars, and/or in Customs Gold Unit, and/or in any currency convertible at the current rate of exchange. The Company assumes all risks of exchange.

9. BANK AS TRUSTEE

The Bank will hold the entire property of the Railway as trustee not only for the Banking Syndicate, but also for the Company, and attend to all the matters necessary to secure fully and completely the advances of the parties hereto. If revenues of the Railways are available, it is agreed that two-thirds (2/3) shall go to the bank, and one-third (1/3) to the Company. After satisfaction of the Bank's loan, the whole is to go to the Company.

10. PREFERENTIAL RIGHT

In case foreign firms are invited to submit tenders for any construction work on the line from Yueshan to Nanchang in the Province of Kiangsi or any extension thereof, the Company to be invited to participate and to be given the preference on equal terms.

11. BANKING TRANSACTIONS

The Company will entrust the Bank of China with all banking transactions arising in China from the present contract, and in turn the Bank of China will share them equally with the Deutsch-Asiatische Bank of Shanghai.

12. ARBITRATORS

All disputes arising out of this Agreement are to be decided by arbitrators appointed by both parties according to agreement.

MEMORANDUM OF THE CENTRAL BANK OF CHINA

1. THE HISTORICAL BACKGROUND OF THE CENTRAL BANK OF CHINA

The first modern state bank ever established in China was the Hu-pu Bank. It was formed with a view to issuing notes and unifying silver currency. Four years later it was reorganized and incorporated into the Ta Ching Bank at the end of the Ching Dynasty. This Bank, with branches throughout the country, was forced to a close by the revolution of 1911. Its Shanghai branch was reorganized under the name of the Bank of China. A few years later, the Bank removed its head office to Peking and established branches in different leading cities. It was then considered somewhat like a central bank in an European style. But again time and circumstances did not allow the Bank to exercise its full control over note issuing and government deposits. Consequently, it could not play its activity as a bankers' bank but merely act as a partly government bank and partly as a large commercial banking house.

Realizing the necessity of creating a central bank for the future success of the construction of modern China, Dr. Sun Yat-sen rested this heavy responsibility on the shoulder of Mr. T. V. Soong, who founded a "Central Bank of China" in the year 1923 with its head office in Canton. This institution weathered many sterling tests during the subsequent crises and gradually gained the public confidence. Owing to the removal of the Central Government to Nanking, the Bank was later incorporated into the

PAGE 2

When the victorious armies of the National Government conquered the Yangtze Valley, a new branch of the Central Bank was established in Hankow in December, 1926. Owing to the communistic up-rising, this branch was forced to close its doors. In the winter of 1928, the revolutionary forces completed the military campaign and the country began to resume its peaceful order. The Government then promulgated the Charter of the present Central Bank of China which was passed by the State Council of the National Government on October 6th of the same year. On October 25th, the Regulations governing the Bank were sanctioned and promulgated by the State Council. In accordance with the Charter, the National Government appropriated twenty million dollars for its paid-up capital and the bank formally opened its office in Shanghai.

The Bank is empowered to do the following things:

1. Issuing notes.
2. Minting and distributing currency.
3. Acting as a government depository.
4. Underwriting domestic and foreign loans.

The Bank is permitted to pursue the following business:

1. Receiving deposits.
2. Custodying legal reserves of other banks.
3. Acting as a clearing house for banks.
4. Rediscounting interest coupons of treasury notes and bonds issued or guaranteed by the National Government.
5. Rediscounting domestic banks' acceptances, domestic commercial papers and time drafts.

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5. Rediscounting domestic banks' acceptances, domestic commercial papers and time drafts.
6. Buying and selling foreign drafts for collection.

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7. Buying and selling demand drafts and cheques of reliable foreign and domestic banks.
8. Buying and selling treasury notes and bonds issued or guaranteed by the National Government.
9. Buying and selling silver bars, gold bars and foreign currencies.
10. Making domestic and foreign remittances and issuing cashier's orders.
11. Making loans secured by silver and gold bars.
12. Making loans with treasury notes or bonds issued or guaranteed by the National Government as securities.
13. Transacting any business entrusted by the Government.

The Bank is organized upon the basis of three separate powers, namely, the legislative function, governed by the board of directors; the supervisory function, discharged by the supervisory council and the executive function, performed by the Governor and two deputy governors. In his inauguration speech, Mr. T. V. Soong, the first governor, emphasized that the policy of the Central Bank is mainly aimed at three points, namely, the uniformity of currency throughout the country, the unification of government depositories, and the readjustment of domestic finance. He also stressed that a state bank should aim at the interest of the people instead of profit making. The ultimate aim of the bank is to be a bankers' bank.

In the past few years, the Bank has proved to be very successful and branches were established in Nanking, Hankow, Hanchow, Tientsin, A'oy, Chengtu, Wuhu, Nanchang, Tsinan, Tsingtao, Chenchow, Yangchow, Kaifeng, Pieping, Hsiakwan, Hauchow, Penpu, Shaochen,

Kiukiang, Chinkiang, Loyang, Foochow, Sinpu, Ningpo, Shihchia-chuang and Chungking. In 1933 Dr. H. H. Kung succeeded Mr. T. V. Soong as Governor. Under his management, new spheres of activity have been scrupulously carried out. A Research Department was added to the Bank in 1933 for the purpose of making constant study of the economic condition of China as well as that of the world. In view of the constant increase of government deposits with the Bank, a Treasury Department was established in 1934 to act as government depository. During the recent years, the Central Bank has played a predominant role in the national finance and its original capital was hardly sufficient to cope with the situation. Dr. Kung petitioned the Government to increase its capital to \$100,000,000, which was approved in April, 1934.

## 2. THE PRESENT ORGANIZATION OF THE CENTRAL BANK OF CHINA

It may be well to give a detailed account of the organization of the Central Bank of China as provided in the Charter. The Bank has a Board of Directors consisting of 11 to 15 members appointed by the National Government. Among the directors at least one represents the agricultural, one the industrial, one the commercial, and one the banking interests. The directors' tenure is fixed for a term of three years but they shall be eligible for respointment. Seven of the directors are designated as Managing Directors by the National Government.

### The functions of the Board of Directors are as follows:

1. To formulate the business policy of the Bank.
2. To fix the amount of notes to be issued.
3. To plan the allocation of reserve funds.

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4. To examine and approve the budget and financial statement of the Bank.
5. To draft rules and regulations.
6. To establish or abolish branches and agencies.
7. To decide on the question of capital increase.
8. To decide on any business brought by the Governor.

The Charter also provides the Central Bank of China a Supervisory Committee consisting of seven members, who are appointed by the National Government. Among the members two represent the industrial, two the commercial, two the banking interests and one the Board of Audit of the Government. With the exception of the member representing the Board of Audit of the National Government, who may be changed by the Government from time to time, the term of office of the other six members of the supervisory committee is two years but three members, one represents each interest, of the first appointment shall retire according to Government order after one year of service.

The functions of the Supervisory Committee are as follows:

1. To audit the accounts of the Bank.
2. To inspect the reserve funds of the Bank.
3. To inspect the amount of notes issued.
4. To examine and audit the budget and financial statement of the Bank.

The Bank is composed of the following departments:

1. BANKING DEPARTMENT.

The Banking Department has a general manager who is appointed by the Governor of the Bank with the consent of the Board of

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Directors. One or more assistant general managers and per pro managers are to be appointed by the Governor as conditions require. The general manager manages the department under the orders of the Governor and Deputy Governors. The assistant general managers assist the general manager and the per pro managers attend to duties assigned by the general manager. The department is divided into the following divisions:

1. Correspondence division
2. Accounting division
3. Deposit division
4. Loan and discount division
5. Domestic exchange division
6. Foreign exchange division
7. Cashier's division
8. Custodian's division

2. ISSUE DEPARTMENT.

This department has one general manager and one or more assistant general managers and per pro managers. They are appointed in the same manner as those in the Banking Department. A number of issue agents are sent out by this Bureau in different provinces in charge of note issue, and recently a branch was organized at Chungking. In the near future, more branches will be organized in remote districts with a view to overcoming the difficulties of geographical barrier. This department is divided into the following divisions:

1. Correspondence division
2. Accounting division
3. Bank notes division
4. Cashier's division

3. TREASURY DEPARTMENT.

This department has one general manager and one or more assistant general managers and per pro managers. They are appointed

in the same manner as those in the Bank Department. This department is divided into the following divisions:

1. Correspondence division
2. Accounting division
3. Depository division
4. Bond division
5. Custodian's division

4. AUDITING DEPARTMENT.

This department has a chief auditor and an assistant chief auditor. They are appointed by the Governor with the consent of the Board of Directors. One or more auditors to be appointed by the Governor according to business conditions. This department is divided into the following divisions:

1. Correspondence division
2. Auditing and calculating division
3. Statistics division

5. SECRETARIAL DEPARTMENT.

This department has one chief secretary, an assistant chief secretary and one or more secretaries. They are appointed in the same manner as those officers of the Auditing Department. This department is divided into the following divisions:

1. Confidential division
2. Correspondence division
3. General affair division
4. Store division

6. ECONOMIC RESEARCH DEPARTMENT.

This department has a Director and an Assistant Director. They are appointed by the Governor with the consent of the Board of Directors. In this department there is a Research Committee, the members of which are either invited or engaged by special arrangement or appointed by the Governor. No salary but some

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allowance are given to those members on the committee engaged by invitation or special arrangement. The Committee divides its works among the following sections:

1. Section on agriculture
2. Section on industry
3. Section on commerce
4. Section on finance

This department has the following divisions:

1. General Affair Division
2. Compilation and Translation Division

3. THE BANK'S POLICY IN THE PAST PERIODS OF POLITICAL AND ECONOMIC CRISES

It has been six years since the establishment of the Bank, during which period, the Bank while struggling through repeated political disturbances and financial confusions, managed to strengthen its own position and fulfilled its duties as a state bank by constantly helping the Government in financial matters and controlling the money market. During the first spring after the establishment of the Bank in November, 1928, in spite of the military movements in the Wuchang and Hankow districts, the Bank has been able to maintain the financial situation of the country in a healthy state. In October, however, as a result of General Shih Yu-san's rebellion followed by the hostilities at Hankow, money became so tight that the native interest rose to as high as 50 cents per \$1,000 per day. The Bank, in order to meet this emergency, took up the leadership to advance a sum of \$2,000,000 to banks in form of overdrafts against mortgages and influenced the Bank of China, the Bank of Communications and some foreign banks to follow suit. Thus the critical moment was tided over.

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At the end of March, 1929, Hunan province rebelled against the central government. Negotiations failed to have any result, thus leading to troop movements along the Yangtze Valley. While the war clouds were hanging over the Central China, unscrupulous speculators took advantage of this opportunity to spread unfavourable news against the notes issued by the Bank in anticipation that they might reap handsome profits therefrom. A run on the Bank was started. This was the first incidence of its kind in the history of the Bank and it was caused by the complicated political situation. After four days of continuous run, during which the Bank freely paid its notes, with business hours extended, public confidence was restored and the crisis was over.

The following table shows the volume of notes redeemed during the four days of the run:

<u>DATE</u>	<u>NOTES CASHED BY BANKS</u>	<u>NOTES REDEEMED AT COUNTERS</u>	<u>TOTAL</u>
March 5	\$ 286,055	\$ 415,000	\$ 701,055
6	324,000	325,000	649,000
7	410,700	75,000	485,000
8	251,000	25,000	276,000

During the course of the run, an officer of the Bank made the following statement when interviewed by press representatives:

"This movement, instead of casting any bad effect on the Bank, has given the public a chance to test the soundness of the Bank. If it were not for this run, people would be unable to know the sufficiency of our cash reserves. I am glad that we have been given an opportunity to build up a stronger public confidence in our bank."

The revolt of General Shih Yu-san in 1929 again undermined

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the public confidence in the Bank's notes. On December 9, 1929 many people came for redemption. The Bank spared no effort to handle the crowd and the situation was smoothed out in a few days.

In the first half of the year 1931, the Nanking-Canton split, the unprecedented flood of the Yangtze Valley and the Manchurian trouble came one after another. Money was tight everywhere and the prices of the bonds were heading for a straight downward trend. The Bank in co-operation with the member banks of the Shanghai Bankers' Association extended loans secured by bonds to the extent of \$5,000,000. The run on the National Industrial Bank of China in October was brought to an end with the aid of \$1,000,000 advanced by the Central Bank. In October the Bank shipped \$3,000,000 to the Northern Provinces to release the financial stringency there. Soon afterward, the Shanghai money market became extraordinarily tight. Native bank interest rate boomed up to 60 cents. The Bank in conjunction with the Bank of China and the Bank of Communications extended loans amounting to \$5,000,000 and finally succeeded in bringing the interest rate back to normal condition.

At the beginning of 1932, the Sino-Japanese hostilities broke out at Shanghai. The whole community was panic-stricken. Business as a whole was suspended and the financial crisis reached its climax. However the financial leaders faced this critical juncture with calm and reserve. As soon as the banks resumed business, the Central Bank made no restrictions whatsoever either on withdrawals of deposits or redemption of bank notes. Other banks followed similar steps and the public was thus pacified. The fact that the Government could meet its financial needs satisfactorily without

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recourse to new bond issued throughout the year was mainly due to the tributary efforts of the Central Bank.

In 1933 quite a few unfortunate incidents happened such as the Gharhar affairs, the Yellow River Flood and the Fukien rebellion but they had created no alarming effect in the financial world. On the contrary, the prices of bonds witnessed a steady upward trend as a result of sound government financial policy and the easy money market in Shanghai which caused by the large concentration of cash here due to business depression and agricultural collapse in rural districts. During the year 1933, the Bank had played no small part in bridging government loans, in completing the work of abolition of tael, which is an important step toward standardization of currency and in furnishing sufficient money in the different financial centers.

Ever since August, 1934, the outflow of silver from Shanghai started to increase in an alarming figure. By an order of the <sup>Government the</sup> Central Bank, the Bank of China and the Bank of Communication organized an Equalization Charge Committee, which is empowered to fix the daily silver export equalization tax beginning from October 15th with a view to checking the continuous outflow of silver which was undermining the financial structure of the whole country.

In February, 1935, Shanghai was facing a financial stringency on account of the export of silver. The Bank again took up the responsibility of relieving the situation in collaboration with the aforementioned banks by advancing loans to banks and business enterprises. At the end of April, tightness was again strongly

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felt by the money market. The imminent financial crisis was averted only after the Bank had sponsored loans to the extent of \$20,000,000.

The foregoing account has shown us how the Bank fulfills its duty as a state Bank in helping government finances and in regulating the money market when occasions arise. The success in these efforts explains why the Bank has ever strengthened its own position.

4. THE RECENT DEVELOPMENT OF THE CENTRAL BANK OF CHINA

Ever since its establishment, the Bank has taken over a part of the work theretofore entrusted to the Bank of China and the Bank of Communications as a government depository. Formerly, there was only a treasury division in the Banking Department of the Bank to care for such matter. As the government deposits grew larger and larger in the Bank, it was felt necessary to organize a treasury department to meet the situation. On January 1, 1934, this department was formally established. It was entrusted with the custody of all kinds of government funds and the task of redeeming government bonds. Thus the Bank was made an important mechanism in the financial structure of the Government.

As time went on, the Bank gradually became the central pillar in the money market of the country. The lack of such a bank in the past has caused the financial circle great difficulties in meeting crises. The situation was further aggravated by the multiplicity of note-issuing banks. The danger of such a confusing note-issuing system was long ago recognized by western countries. The National Banking System of 1861 in America was designed as a

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remedy for such defects. The Bank of England after 1844, the Bank of France after 1848 and the Reichsbank after 1875 were all given the exclusive right of note issuing in order to regulate the amount of notes in circulation.

The Central Bank of China has cultivated a strong public confidence in their notes within a short space of time. Their success can be judged by the rapid increase of the volume of their notes in circulation for the past few years. At the end of 1938, the year of its establishment, the volume of their notes issued stood at \$11,712,923, and on September 27, 1935, it has reached \$117,630,529. More recently, after inception of the new monetary policy, the bank's notes issue reached \$224,324,443.00 on February 29th, 1936.

The following tables show the volume of notes of the Bank in circulation and its percentage to the total note issues of all banks in Shanghai.

TABLE IAMOUNT OF NOTES ISSUED BY THE CENTRAL BANK OF CHINA

1928 Dec. 31	\$ 11,712,923.00
1929 Dec. 31	15,739,862.00
1930 Dec. 31	22,669,228.00
1931 Dec. 31	25,173,349.00
1932 Dec. 31	39,995,360.00
1933 Dec. 31	71,063,301.00
1934 Dec. 31	86,049,610.00
1935 Nov. 3	135,664,764.00
1935 Dec. 31	179,923,546.00
1936 Feb. 29	224,324,443.00

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TABLE 2

PERCENTAGES OF NOTES ISSUED BY CENTRAL BANK OF CHINA  
TO THE AMOUNTS ISSUED BY ALL BANKS IN SHANGHAI

PERIOD	AVERAGE AMOUNT ISSUED BY CENTRAL BANK	AMOUNT ISSUED BY ALL BANKS	PERCENTAGE
1928	\$ 6,766,000.00	\$230,953,000.00	2.93%
1929	19,129,000.00	265,591,000.00	7.20%
1930	17,435,000.00	302,302,000.00	5.77%
1931	32,672,000.00	297,095,000.00	11.00%
1932	30,195,000.00	245,164,000.00	12.31%
1933	53,837,000.00	263,847,000.00	18.81%
1934	75,688,000.00	362,347,000.00	20.89%
1935 (1st 6 months)	92,626,000.00	378,942,000.00	24.44%

It is rather amazing that the Bank in a brief period of less than six years, has become one of the largest issue banks in the country, second only to the Bank of China which has a much longer history.

After the announcement of the new monetary decree on November 3, 1935, when the notes of the Central Bank of China, the Bank of China, and the Bank of Communications were made legal tender, the note issue of the Central Bank assumed still bigger percentage of total legal tender issued, being \$224,324,443.00 against \$700,046,392.42, or 32.04% <sup>on February 27, 1936.</sup> As the Government intends to unify all the notes issue at the end of two years, it is expected that the notes issued by the Central Bank of China by that time will may have a far bigger circulation.

Following the Japanese invasion in Shanghai, the local financial institutions founded a Joint Reserve Board with a view to consolidate the reserve position of its members in time of crisis.

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In many occasions, the Central Bank of China made advances to the Board so as to increase the volume of credit in circulation whenever it was needed. In February 1936 the Central Bank became a member of the Shanghai Bankers' Clearing House, which is a subsidiary organization of the Joint Reserve Board. A good part of the reserve of the member banks is <sup>now</sup> in the custody of the Central Bank, thus making the day nearer when the Central Bank will become the sole depository of all bankers' reserves.

Aware of its heavy responsibilities, the Central Bank has always followed safe and sound policies. As a result, its volume of business increased with rapidity. Deposits of various kinds at the end of 1928 only amounted to \$15,410,467.77 but they had reached \$249,485,830.36 by the end of 1934, and one year later the amount was more than doubled. Table 3 shows the volume of deposits at the end of each year from 1928 to 1935.

TABLE 3

DATE	DEPOSITS IN DOLLARS
1928 Dec. 31	\$ 15,410,467.77
1929 Dec. 31	39,984,707.05
1930 Dec. 31	66,042,175.07
1931 Dec. 31	89,750,920.34
1932 Dec. 31	153,981,387.89
1933 Dec. 31	227,154,807.71
1934 Dec. 31	249,485,830.36
1935 Dec. 31	595,940,737.27

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Similarly loans and advances (including discounts, overdrafts, and others) increased from \$15,265,174.20 at the end of 1929 to \$154,313,340.66 at the end of 1935. The volume of loans and advances at the end of each year during the years 1928 to 1935 is shown in Table 4.

TABLE 4

DATE	LOANS, DISCOUNTS AND OVERDRAFTS
1928 Dec. 31	\$ 4,419,714.54
1929 Dec. 31	15,265,174.20
1930 Dec. 31	28,279,545.87
1931 Dec. 31	75,041,108.13
1932 Dec. 31	97,741,867.23
1933 Dec. 31	142,843,709.23
1934 Dec. 31	85,163,824.79
1935 Dec. 31	154,313,340.66

As seen from Table 5 below, the profits of the Bank in 1929 (including the few months in 1928 after the opening of the Bank) was \$1,692,683.39, in 1933 it increased to \$10,734,244.84 and by the end of 1934, it had reached a sum of \$14,821,505.46. In 1935 because of monetary stringency the amount was reduced to \$9,048,339.64 according to a preliminary estimate.

TABLE 5

DATE	NET PROFIT
1928	\$ 239,360.13
1929	1,453,323.26
1930	2,726,341.22
1931	4,870,403.73
1932	11,961,933.39
1933	10,734,244.84
1934	14,821,505.46
1935 (Preliminary figure)	9,048,339.64

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From the following table it can be seen that the reserve fund of the Bank has also been growing. In 1930, the reserve stood at a figure of \$1,352,231.15 and in 1933 it went up to \$15,847,222.76. After recapitalization the reserve was reduced to \$3,698,534.90 by the end of 1934. When the profits made in 1935 are distributed no doubt the reserve fund would receive a handsome addition.

TABLE 6

DATE	RESERVES
1930 Dec. 31	\$ 1,352,231.16
1931 Dec. 31	3,496,455.68
1932 Dec. 31	7,405,559.36
1933 Dec. 31	15,847,222.76
1934 Dec. 31	3,698,534.90
1935 Dec. 31 (Before distribution of Profit)	3,845,136.17

5. CONCLUSION

The organization of the Central Bank of China as well as its development have been briefly described in the preceding chapters. With her capital increased to \$100,000,000, of which a good portion shall be sold in the near future to the general public and banking community, with the adoption of the new monetary policy by the Government, with her new charter now in discussion in the Legislative Yuan purporting to strengthen her status as a bankers' bank, she will no doubt play a very prominent part in the destiny of China's finance and currency. Hencefort the Bank will pursue her activities

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in the following directions.

1. To obtain exclusive right of note issue. As the volume of the Bank's note issued has been enlarging rapidly, she will soon be in a position to petition the National Government to grant her an exclusive right of note issue so as to expedite the plan of unification of currency of this country.
2. To act as a clearing house for all the Shanghai banks. This will make the Bank a center of activities of the Chinese money market.
3. To rediscount for all the banks. Through the improvement of the money market and discount system, the Bank will aim to be the sole authority of rediscounting. With the instrument of discount policy at hand, the Bank will be able to control the mobility of capital.
4. To be the cash reservoir. Through the clearing process, the cash reserve of the Shanghai money market will be concentrated in the Bank.
5. To exercise currency control throughout the country by establishing branches in all the important cities.
6. To effect perfect co-operation with the Ministry of Finance so that the Bank will be given the right to act as the sole <sup>facilitate the</sup> treasury of the government and to issue treasury notes to assist the money market like the Bank of England.

However, China is a country endowed with abundant supply of raw material. When the plans of the Industrial Development of China laid down by Dr. Sun Yat-sen materialize, the Great Southern Port, the Great Northern Port, and Hankow in Central China will all be the centers of financial activities in addition to Shanghai. By

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that time the central banking system of China will probably be forced to make changes in order to cope with the new economic situation. The new activities like cash reserve, note reserve, the adjustment of cash mobility in these financial centres will be the guiding principle of the future central banking policy. Thus it is now idle to predict the exact system or policy which the Bank will adopt as it entirely depends on the future economic development of the country.

PAGE 1Note Issue of the Central Bank of China for the Last Four Years

<u>1932</u>	<u>Total Amount</u>	<u>1934</u>	<u>Total Amount</u>
July 30	\$29,529,531.-	Jan. 31	\$ 70,440,275.-
Aug. 31	30,435,937.-	Feb. 28	71,298,922.-
Sept. 30	30,162,192.-	Mar. 31	68,368,222.-
Oct. 31	30,925,618.-	Apr. 30	69,319,270.-
Nov. 30	34,480,996.-	May 31	71,101,020.-
Dec. 31	39,145,360.-	June 30	70,844,349.-
		July 31	74,440,206.-
		Aug. 31	77,841,337.-
		Sept. 29	80,216,875.-
		Oct. 31	83,302,703.-
		Nov. 31	85,746,535.-
		Dec. 31	85,339,300.-
<u>1933</u>		<u>1935</u>	
Jan. 30	46,742,121.-	Jan. 31	89,056,751.-
Feb. 28	46,039,639.-	Feb. 28	89,932,353.-
Mar. 31	44,414,521.-	Mar. 30	92,694,871.-
Apr. 29	44,685,919.-	Apr. 30	92,031,583.-
May 30	44,390,966.-	May 31	83,312,819.-
June 30	45,533,179.-	June 29	98,727,916.-
July 31	50,256,879.-	July 31	106,890,620.-
Aug. 31	54,623,994.-	Aug. 31	110,294,947.50
Sept. 30	60,481,539.-	Sept. 30	118,655,639.-
Oct. 31	66,144,168.-	Nov. 3	135,664,764.-
Nov. 30	69,119,130.-	Dec. 31	179,923,546.-
Dec. 30	70,271,542.-		
		<u>1936</u>	
		Jan. 25	220,641,090.-
		Feb. 29	224,324,443.-

No notes in local currencies are issued by this Bank.

April 14, 1936

The Mexican Ambassador came in today and presented the following copy of telegram from Mr. Suarez:

"To be discussed with the Honorable Henry Morgenthau, Jr., Secretary of the Treasury, personally.  
Strictly Confidential.

As it might be recalled, the possibility of the purchase of some of the silver surplus of the Bank of Mexico, was discussed some time ago.

After careful study, the Mexican Government is in a position to amend its Monetary Law to put in circulation metallic currency in sufficient quantities. However, in order to have the system function on a solid basis, it would be imperative to dispose by sale of the silver surplus.

Should the Secretary of the Treasury of the United States be prepared, in principle, to acquire such surplus, ample details of the plan would be explained to him by a person who would come to Washington for the purpose."

HM, Jr. asked the Ambassador what the word "surplus" meant, but the Ambassador could not answer him. HM, Jr. then asked the Ambassador to inquire with the idea of finding out something more about it. He also asked the Ambassador to ask Mr. Suarez what is meant by "amend its monetary law to put in circulation metallic currency in sufficient quantities"; what kind of coins he refers to; how many and how much silver in the coins; how many pesos are they talking about.

HM, Jr. invited the Mexican Ambassador to come in again to talk to him about it after he had received the information requested because he, HM, Jr., would then be in a better position to decide whether it is worth while for anyone to come to Washington from Mexico to discuss the subject matter of Mr. Suarez' telegram.

EMBAJADA DE MEXICO

TO BE DISCUSSED WITH THE HONORABLE HENRY MORGENTHAU, JR.,  
SECRETARY OF THE TREASURY, PERSONALLY.- STRICTLY  
CONFIDENTIAL.

As it might be recalled, the possibility of the purchase by the Government of the United States, of some of the silver surplus of the Bank of Mexico, was discussed some time ago.

After careful study, the Mexican Government is in a position to amend its Monetary Law to put in circulation metallic currency in sufficient quantities. However, in order to have the system function on a solid basis, it would be imperative to dispose by sale of the silver surplus.

Should the Secretary of the Treasury of the United States be prepared, in principle, to acquire such surplus, ample details of the plan would be explained to him by a person who would come to Washington for the purpose.

\* \* \*

April 14, 1936

The Secretary today met with the following gentlemen to discuss the arrangements for sending out the bonds and bonus checks to the veterans:

Brig. Gen. Frank T. Hines, of the Veterans Administration  
 Harold W. Breining, Assistant to Gen. Hines  
 Daniel W. Bell, Commissioner of Accounts and Deposits, Treasury  
 William S. Broughton, Commissioner of the Public Debt, Treasury  
 Roy M. North, Deputy Third Assistant Postmaster General  
 John A. King, of the Registered Mails Division of the Post Office  
 Department  
 Thomas Kirby, Legislative Chairman of Disabled American Veterans  
 of the World War  
 Ray Murphy, National Commander, American Legion  
 Col. John T. Taylor, Director of the National Legislative Com-  
 mittee of the American Legion

The following is a stenographic transcript of the meeting:

HENRY MORGENTHAU, JR.: I am unusually glad to have a chance to sit down and talk with you gentlemen and as you know, the job that you people have been given was one of the most difficult the Treasury has ever had to handle and I think everybody connected with it has been very anxious to see that the machinery runs smoothly and properly and with as little difficulty to the man who is to receive this bond and check as possible. Now we have about two months to go until pay day and the thought was that we open the can and let you look inside it and tell you just what the Veterans' Administration, the Post Office and the Treasury have done to prepare for this tremendous task. And then after you have seen it if you have any suggestions or criticisms we would like to have them and if you think that the thing is all right, we want to help you make it go.

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I think some of you gentlemen have made statements that you will urge the veterans to keep their bonds. I think it is important not because we want to raise the money or haven't got the money because we will have it to pay but from their own standpoint, it is a good investment. It is about as good an investment as they can get. I think it is important for their sake and their family's sake if they did keep it and I do hope that there will be statements made urging them to keep these bonds until maturity -- for their sake not for ours. We can take care of ourselves.

And so I think the best thing to start in with is to have Mr. Bell just tell you -- or do you want to start with the General and let him explain how he sends the names to us and what we do when we pick it up and turn it over to the Post Office?

GEN. HINES:

I would just like to say this. You have just made a reference to statements made by the organizations. I feel that they have done an excellent piece of work in that regard. They have answered loads of questions; their commanders are constantly traveling throughout the country; they have urged the men to keep the bonds; they have explained the procedure as well as they knew it and their cooperation has been most helpful to us and I am sure that it will prove helpful to the Treasury when

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you finally issue these bonds. We have had a number of problems that have arisen, particularly the competition among some of our worthy citizens to invent schemes to get hold of the veterans' money or the money from the bonds as early as possible and we have tried to thwart in every way their getting a list of the veterans because then the veteran is pestered with every kind of scheme known to man to get his money. The service organizations have cooperated with us splendidly in that and I feel confident that, with very few exceptions, the lists are coming from individuals or small groups of veterans who find a market for lists of names. Recently we found it necessary to issue instructions that the bonds be sent to the address given on the application and delivery made to the man himself and not in care of any particular person or place, feeling that would tighten it a little more. From the standpoint of the Veterans' Administration, I may say that we are now in full operation. We are making certifications to the Treasury now at an increased rate.

H. M. JR.: How many names are you giving us a day?

GEN. HINES: From this office here, over ten thousand a day. From the field, how many, Briening?

MR. BRIENING: About two hundred and twenty-five thousand up to date but we have only gotten started.

GEN. HINES: How many a day?

MR. BRIENING: Probably running about twenty-five thousand a day.

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GEN. HINES: We expect to be soon up to a rate of over a quarter of a million a week.

H. M. JR.: When will we get the last name? What's your time table?

MR. BRIENING: Of those that are in now we should get the last names by the first of July; about that or maybe a little later. Our biggest trouble is getting personnel to handle the job.

H. M. JR.: Then we won't have all the names by the first of June?

GEN. HINES: You will have over two million I feel by the 15th of June. There are eight hundred thousand veterans that have not applied up to date. How long they will hold off we have no way of telling but all together there are over two and a half million.

MR. BRIENING: About two million seven hundred thousand.

GEN. HINES: That number have applied. You ought to have most of that load by the 15th of June. The rate those will come in depends upon the veterans.

MR. BELL: There will be a great many of these applications which will require a lot of correspondence; the application will be wrong and have to go back. You will probably have 10 or 15% that will cause a delay.

GEN. HINES: Some will prefer holding back to protect their beneficiaries. As soon as they make application, they lose control of their certificates. Many are holding it on that score.

H. M. JR.: What is our set-up for payment, Mr. Bell?

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MR. BELL: We have set up organizations in the eleven Federal Reserve districts and the Treasury here making twelve organizations to handle certifications from the Veterans' Administration to issue bonds and the check covering the odd amount. In the Federal Reserve banks we have also created a branch disbursing office or right adjacent to it which will handle the check at the same time the bonds are issued and they will go in the same envelope and be ready for mailing on June 15th, as the Act requires. Just how many we will have on that date we don't know at this time and just what kind of problem that will present to the Post Office on that day -- but Mr. North tells me it will only be a matter of a few days when he will be current on that mail.

MR. NORTH: I think so. Those are details which we will have to work out and as soon as we do figure out or formulate some plan, we will be able to give you some definite assurance as to the delivery but delivery is going to be a big problem, as you are aware.

H. M. JR.: Let me ask you a question, Dan. Are you keeping up to date with the names that are coming over from the Veterans' Administration?

MR. BELL: We are a little behind but not much.

H. M. JR.: Are we getting more behind or are we catching up?

MR. BELL: We are getting more current as we go along and we will be current by June 15th.

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- H. M. JR.: Do we have any trouble getting personnel?
- MR. BELL: You see, our problem hasn't begun yet. We have enough personnel at the present time but probably by May 15th, we will get into difficulty.
- GEN. HINES: The trouble we have is this: We get registers from the Civil Service and promptly we send out and call the people in but only about 50% respond. The other 50% say they have employment, which I think is an excellent sign, but it delays us to that extent. We have to start all over again and get new lists.
- H. M. JR.: But you feel we are not going to slip on it?
- MR. BELL: No, sir, I do not because what we have done in a good many cases is to transfer our people from the local disbursing office over there and to the branch offices, as far as issuing the checks, and we can rely on the Federal Reserve Banks to take their own personnel if we get short on our side.
- H. M. JR.: I think it interesting to explain. We had these organizations in existence due to the fact that we pay all WPA workers in the field and we built up this organization in the field and Bell is using that organization. And the fact that it is already set up makes it a much smoother organization than if we had to build a field organization overnight. But this organization is there, located in these different districts and is already to go to work.
- MR. BELL: We are using the very same set-up that we are using to pay WPA workers and we are in a little different position than Gen. Hines on that

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score because we can rely on the Federal Reserve banks for personnel if we get short in the Bond Section.

H. M. JR: How about the post office? I wonder if these gentlemen realize that all these bonds and checks are going out by registered mail?

GEN. HINES: That's going to be a big problem.

MR. NORTH: Tremendous! I think when we formulate some plans and analyze our situation we may call on these same gentlemen for some cooperation in delivery after it has been decided upon. For instance, if they are all mailed at once, it is going to present quite a problem to us and it might be better for them all to be mailed at once and to be received at delivery offices more or less at one time rather than have different volumes at different times.

H. M. JR: But you haven't worked it out yet?

MR. NORTH: No. We have not because we are just agreeing with the Treasury on our basic instructions and regulations.

H. M. JR: What is the answer to this question the newspapermen asked me yesterday? When the veteran gets his bond and check by registered mail, does he or does he not have to give his thumb-print?

MR. NORTH: No. It is elective with the postmaster whether he will require fingerprints on the bond. We don't require finger-prints of the receipt.

H. M. JR: How about the check? When he wants to cash it either for the bond or the actual check? If he wants to cash the bonds and get his money, does he have to establish his identity through finger-prints?

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- MR. NORTH: He may if the postmaster is not satisfied as to his identity. He may require, I presume, more or less for the psychological effect, his finger-prints.
- H. M. JR.: Because on his application he has his finger-prints but when it comes to cashing, do you make them finger-print again?
- MR. BELL: It's optional with the postmaster who identifies him.
- H. M. JR.: Because I think if he did not have to do it, it would be much better because it sort of makes the fellow feel we think he is a crook.
- GEN. HINES: The theory was that where the postmaster was satisfied with the identification, that was all he needed; but if a question arose and he became suspicious that the person who presented the bond was not the correct owner, he could require finger-prints.
- H. M. JR.: Is he going to have the original application?
- MR. NORTH: No. It's more psychological.
- MR. BELL: I don't think it will happen once in one hundred thousand cases.
- H. M. JR.: He knows the finger-prints are on the application.
- GEN. HINES: He could check up by getting the application in his hands on questionable cases but as I understand it, it would only be necessary in cases where evidence showed that there was some racket going on.
- MR. BELL: Only in questionable cases will it be secured.
- H. M. JR.: The picture as I get it is that the thing is pretty well set up, up to the Post Office and the Post Office needs more time.
- MR. NORTH: We are just now agreeing on our regulations with the Treasury.

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H. M. JR: And you haven't decided whether you want all the mail bags dumped on you on one day?

GEN. HINES: We lose control after we certify and they go to the Treasury and from the Treasury to the Federal Reserve banks, as I understand it. I was going to ask you, Mr. North, when we sent out the original certificates, did you find at that time that we got better delivery by staggering the sending of them? That experience will be helpful in this particular case. Did you send them out by registered mail?

MR. BRIENING: No, they were not sent out by registered mail. We sent the big bulk at one time on January 1, 1925, and we had a very, very sad experience. A great many were lost.

R. NORTH: You don't have an analogy there. All the boys will be anxious to get their bonds pretty soon after they know they are coming out. It seems to me preferable to handle them all at one time. The Post Office gets the whole bunch at one time and can use its whole force of regular carriers and put substitutes on for regular mail delivery. It would be helpful for them to have the full complement of this registered mail for each regular carrier rather than piecemeal and then any complaint that might rebound would be both on you, Mr. Secretary, and the Postmaster General because those boys would certainly holler.

GEN. HINES: No, it's going to rebound on the Veterans' Administration.

MR. MCREYNOLDS: Mr. North, wouldn't you want to make dispatch directly from the Federal Reserve Board? -- have the branch office established there in order

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to make your distribution and make out your bills and everything, return receipts, right there? That office would be all set and ready to go.

MR. NORTH: I think for the mechanics, yes.

MR. MCREYNOLDS: That would mean that they would all go out at one time.

H. M. JR: What question do you have you would like to ask, gentlemen?

Veteran Representative: Do you anticipate having those envelopes all stamped, registered and everything before the 15th of June, or will that happen afterward?

MR. BELL: That's what Mr. McReynolds was talking about. We will have to work that out with the Post Office and I don't see why we can't work out the procedure a few days before the 15th in order to establish a branch in the Federal Reserve bank.

MR. MCREYNOLDS: You could write up the bills and make the distribution and have a clerk who knows the dispatches and the pouch actually there and have the stuff that is ready. I see no reason why you could not have it dispatched on the 15th of June or thereabouts and that would be your first delivery. Of course there will be a lot of it later because a lot of these things can't possibly be gotten ready. The applications will not be in. But the big bulk in one big operation probably would be easier than to just try to include it in the regular dispatches.

MR. NORTH: If I find some insurmountable problem, we will be glad to discuss it with you people but I think we will be able to take it whenever it

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is turned over to us.

E. MCREYNOLDS: You have a big post office at each one of these places and it will be a question of working between the big post office and the Federal Reserve bank.

Veteran Representative: What will the facilities be, Mr. Secretary, for those who wish to cash their bonds?

E. BELL: I would like to go into that.

M. M. JR.: Please.

Veteran Representative: And also as to veterans in foreign countries. We are receiving a great many inquiries on the foreign countries situation.

M. M. JR.: Go ahead, Dan.

E. BELL: This is the important question to the veterans. When is he going to receive his cash? The Act provides that the Secretary may make payment through any agencies that he may designate, including post offices. I think you realize it is quite impossible for the Treasury to designate forty thousand post offices as paying agencies. Many of these Fourth Class post offices have only a desk in a drug store or a grocery store in some little town and they would know nothing about bonds or Treasury checks. We have been working out tentatively a scheme with the Post Office Department whereby we will designate as fiscal agents of the United States between two and three hundred postmasters and that will cover the country very well and in most cases the veterans' bonds can reach the designated post office for payment within a day. Now we will use the other post offices as transmitting

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and certifying agents. The veteran can walk into any post office in the country and, where properly identified, the postmaster will take the bond and from then on, it is the responsibility of the Government. They will transmit the bonds to the closest paying agency and we will attempt with the cooperation of the post office to have sufficient personnel to keep practically current on the issuance of checks in payment of those bonds and return the check immediately to the veterans. That's going to require the cooperation of the various veterans' organizations and local units. I think the Post Office Department will have to be in pretty close touch with those organizations and require some of their help. But that in general is the scheme. Details and regulations will have to be worked out after we get a little piece of legislation that we are now requiring. While the Act authorizes you, Mr. Secretary, to designate post offices as agents, it does not authorize you to designate the postmaster as paying agent. The legislation is now in the Senate Committee and we hope to have it in the next couple of weeks.

H. M. JR.: How about veterans living abroad?

MR. BELL: We have not worked out just what we will do about sending them their bonds. We may attempt to use the State Department to some extent and send it through their pouches and work out some way of dealing through the consular offices. On the payment we would like to have them come to the Treasury. The regulation will provide that they

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may go before a consular officer and get identification and certification but that for payment purposes we would like to have them come to the Treasury.

H. M. JR.: Does that mean that a veteran living in Paris has it mailed to the American embassy and they deliver it to him and he wants to get it cashed, he has to send it over here?

MR. BELL: He has to certify before a consular officer and return it to the Treasury with request for payment and we will send him a check.

H. M. JR.: How does that sound?

Veteran Representative I was thinking it might be done through the army disbursing officer or the disbursing officer at the embassy.

GEN. HINES: That would work in France but how about.....

MR. BELL: Our difficulties will be in Italy and Greece.

GEN. HINES: The greatest amount will go to Italy.

H. M. JR.: Have we taken over diplomatic people as pay masters?

MR. BELL: No, we are still delegating that authority.

Veteran Representative I just had that thought in mind, Mr. Secretary, because there are a lot of veterans still abroad who can't get back home.

H. M. JR.: How many are there?

Veteran Representative I don't know.

GEN. HINES: Mr. Briening, how many checks are we sending abroad?

MR. BRIENING: Six thousand. That's only indicative of those who are getting compensation or insurance. I think one of the big problems abroad

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covers the heavy taxes levied against the payments that amounts to almost confiscation. That's what we ran into during and right after the War. Italy, Greece, Poland, Russia -- those are the countries where you are going to have a great deal of trouble. And many of the veterans would much rather have their bonds cashed in this country so they can make some arrangement for depositing the money in this country and draw against it as the occasion requires. A great many veterans do that now.

GEN. HINES: I believe the one reason above all others why it is desirable to deal through the State Department consular agents is that we have been dealing with them for years. They have certain personnel that we pay for. They should be in better touch with the veterans than any other agency I know of. They are acquainted with the problems Mr. Briening just mentioned and will take steps to safeguard their interests.

One of the important problems is the next step which relates to veterans abroad as well as those at home. That's in the case of the veteran after he receives the bond dying before he gets it cashed. There must be some simple way worked out that the bonds can go to the widow and children. Otherwise, if it is going to be difficult for those bonds to be handled after the death of the veteran, it's an incentive to the veteran to cash his bond but if it is simple he'll hold it, feeling his family can get the benefit

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of it and I think that matter should be given some consideration here and I'm particularly anxious to get the views of the service organizations on that.

MR. BELL: Our legal staff is working on that very problem now. I suppose we will be required, Mr. Broughton, to follow the usual procedure?

MR. BROUGHTON: In the case of registered bonds if there is a legal representative, we recognize him in all cases. If there is not and the state where the decedent has lived does not require administration, we don't require it and in no case do we require administration if the estate does not exceed \$500. That's an established procedure for other registered bonds and with these bonds it will not be any more stringent.

MR. HINES: Many veterans die without leaving a will. Presuming the wife has possession of the bond, she can cash them. And I think we should take steps to make whatever the procedure is well known in advance and it will have a very material bearing on the number of veterans who hold their bonds.

MR. BROUGHTON: There will be no trouble if it is a small estate.

Veteran Representative: If the estate is less than \$500, the widow will be able to cash the bond without going through the formality of administration?

MR. BROUGHTON: Yes, the Treasury does not require administration.

MR. BELL: That would take care of most of the cases.

Veteran Representative: That's very important. May I suggest that the three departments, the Veterans' Bureau, Post Office and Treasury Department, if any

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one of them has complications, administrative complications, that they be incorporated in Mr. Bell's proposed legislation to authorize the postmaster to act as fiscal agent. In other words, do you find any complications there due to the hurry of enacting that law which without any objection from anybody might cut the corners?

GEN. HINES:

We are now working double shift as you know. We will have no difficulty speeding up to keep up with the speed at which the Treasury can work. It means putting on another shift. I feel confident that while we have an excellent sign in employment from those on the Civil Service register, the Civil Service will soon solve that. They will hold new examinations to take others on so that that's only a temporary holdback and I think our production within the next ten days will be as much as we will want.

MR. BRIENING:

Of course, our expansion is always limited to the number of trained supervisors we have. If you put on more personnel, then you must train it; it retards rather than accelerates production. We have about fifty distinct types of computation on the interest. That's where we are having trouble. We have taken interest that has accrued and put it in as new principal each year and the amount due has to be recomputed all the way back.

GEN. HINES:

Do you know of any legislation we might use, Mr. Briening?

MR. BRIENING:

I only have this thought. If there is any way to safeguard the veterans against exploitation that appears to be going on; if you can do that with legislation, I think it would be highly desirable.

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H. M. JR: I know one piece of legislation I would like. I would like to see this thing fall July 1, two weeks later, rather than on the 15th of June.

Veteran Representative: May I ask Gen. Hines a question and that is; if he thought it desirable that there should be specific legislation where a veteran dies before he cashes the bond.

GEN. HINES: The committee considered whether it should go to his estate. I think the feeling was that the interest of the veteran and his family was safeguarded. The veterans have already discovered that if they wish to protect the present beneficiary, all they do is hold their certificate a little closer to the date and they are doing it undoubtedly. I know people who have said they were.

Veteran Representative: But you have a problem in your insurance where the veteran designated his mother and then got married and when he dies, there is his application designating his mother instead of his widow.

GEN. HINES: That is one of the reasons why the estate makes it better under those circumstances because his wife will take first in most states.

Veteran Representative: What progress is being made in the printing of the bonds?

H.M.JR: As far as I know they are up to date. Hall is up to date, isn't he?

MR. BELL: Yes.

MR. BROUGHTON: He is ahead of the schedule.

MR. MCREYNOLDS: You couldn't possibly catch up to Hall.

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Veteran Representative It seems to me that one of the sources of possible irritation will be the matter of identification out in the field. An extra cautious postmaster, especially in small towns, will have in his mind his own responsibility and may be very captious about his requirements and it seems to me that it would be advisable to have issued definite as possible instructions as can be devised so that there will be no unnecessary routine about that. For example, if the finger-print is required, of course that means weeks' delay to that individual and it may be a case where the need for the money is more important than others.

H. M. JR: You don't suppose that the various posts could have various men there for two weeks each, taking turn for a day, and be in the post office from the 16th of June to the 1st of July and have volunteers at other post offices for two weeks.

Veteran Representative That's exactly what I had in mind, Mr. Secretary, in that as the postmaster would be advised of the cooperation of the several veterans' organizations and as he would be satisfied with the identification which they in most cases would have already made to their own satisfaction, then it would speed up the matter considerably.

H. M. JR: If you don't get anything else out of this meeting, I want you to get the idea that we are doing everything we can to make this machinery run smoothly and nothing is being done to retard and

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there are no grains of sand in this situation. We have been given this job and we will do it as expeditiously as possible and with the least friction.

We all feel that way.

Veteran Representative

H. M. JR.:

So, if you don't get anything else, I want you to get that. Everything is being done to make this piece of machinery run smoothly. If anybody knows of anything that is being done to hold it up, I would like to know about it.

GEN. HINES:

The greatest problem for the veterans' organization is the question of identification in communities with small post offices. The posts in that community and the postmaster know the men. As they work together, they will undoubtedly solve many problems of identification.

H. M. JR.:

Well, we might as well call a spade a spade and I think that everything is now up to the Post Office. The Post Office is not ready yet.

MR. NORTH:

That's right. We will be ready but we are waiting for joint instructions and analysis between your Department and ours. We have not delayed. We are ready to go right ahead as soon as we agree.

H. M. JR.:

We are up to you now.

MR. BELL:

As soon as we get this legislation giving you authority to designate postmasters as fiscal agents we will be ready. The regulations will be out.

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- H. M. JR: Where is that legislation? What is its status?
- MR. BELL: It's in the Senate Committee. I talked to Senator McKellar.
- H. M. JR: Does it stand by itself?
- MR. BELL: It is attached to another piece of legislation which has already gone through the House. After McKellar has his meeting, I am going to the Chairman of the House Committee and ask him if he will not concur in the Senate bill as soon as it is passed and then it will not have to go into conference. I don't think we will have any trouble.
- Veteran Representative: I think it would be a good idea if the postmasters would call meetings of service representatives, something similar to this meeting.
- H. M. JR: That's a good suggestion. Let each postmaster be sent an instruction to call a meeting comparable to this and sit down and talk the thing over.
- MR. MCREYNOLDS: It will have to be done after the law is through.
- Veteran Representative: There will be better local understanding.
- H. M. JR: And call in the local newspaper fellows.
- MR. BELL: The post office has a real job and they are going to have the cooperation of the veterans' organizations.
- MR. NORTH: We have already anticipated asking you folks for this very cooperation, and the plan has been evolved for payment by checks. I think

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we can make our regulations, our requirements of the postmasters so lenient that we will not have confusion and congestion and it is the intention of the Post Office Department to call on the veterans' groups and permit the postmaster quite a bit of latitude in his discretionary handling of identifications.

H. M. JR.: I think we ought to have another meeting about the 15th of May and go over and check up again if that is agreeable to you gentlemen.

Veteran Representative Yes, sir. I understand from what Mr. North said that there is a feeling on the part of the Post Office to make delivery all on one day or periodically on one day. I wondered as to the desirability of deciding that they would be made every Saturday when a lot of the veterans are not on their jobs.

MR. NORTH: That will have to be worked out. If you make delivery all at one time, you probably will have to invite the veterans to be at home so delivery could be made. I don't know whether that would be more desirable than to wait for Monday. We will work out delivery details.

Veteran Representative Isn't the Post Office assuming that this whole thing is going to be done all at once? As we understand it, the thing is going to dribble over months. It is true that on the 15th of June you will have a terrific load but that will not complete the load.

MR. NORTH: We understand we will be intensively engaged for probably six months on this. We were just wondering if we don't deal promptly after the 15th with all those who have put in applications, there probably

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will be a lot of complaints that will come in against all three groups.

Veteran Representative

No, the point I am trying to make is you are assuming that on the 15th of June, this big job will be dumped on you but as we visualize it, there will be an abnormal bunch on that day but it will dribble over several months but you have to continue that thing for weeks and months. It is a question of planning when these bonds can be delivered to post offices for delivery on the 15th. In other words, if on the morning of the 15th, you get a million bonds, you are going to jam your machinery but if you get them a month ahead and get your forms all fixed with the understanding that it would start on the 15th, it seems to me that it would be smoother.

MR. BRIENING:

You are going to have 10 to 15% of the men change their addresses between now and the 15th of June and to prepare those checks and bonds and put in the envelopes, there will be a tremendous amount will not reach their destination.

Veteran Representative

Are we right in assuming that on the night of the 14th or the morning of the 15th, there will be a million bonds dumped in the post offices?

MR. NORTH:

Yes, probably two million.

H. M. JR:

I think you need a little more time, Mr. North. It is quite obvious we are up to you but you have not had a chance. You are not

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quite ready yet to tell your story and I think we should give you a little more time and you will be ready. And if these people will come back by the 15th of May, we will have the complete story. You are conscious of it. We are up to you but you really haven't had a chance.

MR. NORTH:

When it is decentralized, Mr. Bell told of the twelve points, two hundred thousand will go out from each point, from New York, from Chicago, etc. There will be no jam there. We can handle that. They are decentralized as they go out so there will not be so much confusion and I thank you, Mr. Secretary.

Veteran Representative

It will be like the Christmas rush.

MR. MCREYNOLDS:

Not as bad.

Veteran Representative

It looks to me as if we assume everything will run smoothly up to the time the bonds get into the hands of the men. The jam will be in the local post office when they come to apply for their money. I think it is quite important for many reasons that the bonds all be sent out promptly at the same time as nearly as possible.

MR. MCREYNOLDS:

There is no danger of congestion on this providing the thing is planned ahead and this will be taken out of the regular routine. They will be billed, they will be distributed, tied up in packages and the registry bill and the receipt go along with them. It will not go into the local post offices.

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GEN. HINES: We can't release them until the 15th of June.

Veteran Representative Does that mean they can't be released to the post offices?

MR. BELL: We can't issue them until June 15th but after all, the post office is a part of the Government and certainly there is not any objection to the post office and the Treasury getting together and holding these things until the 15th.

H. M. JR: We haven't tried to hide anything. The various discussions show that we still have more work to do and we are going to call on you and I think if there are any other questions -- I don't want to rush you but I did get off to a late start and I have people waiting --

MR. BELL: I would ask them if they have any suggestions, that they write up a memorandum in the next ten days so if we can cover them in our legislation, we will be glad to do it.

Veteran Representative I understand there will be another meeting on the 15th of May.

H. M. JR: Yes.

ooOoo

April 14, 1936.

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A group met in the office of the Secretary of the Treasury at 11 A.M. to discuss financing.

Those present were:

Henry Morgenthau, Jr., Secretary of the Treasury.

Joseph P. Broderick, Acting Chairman of the Board of Governors of the Federal Reserve system,

George Harrison, President of the Federal Reserve Bank of New York,

W.R. Burgess, Vice President of the Federal Reserve Bank of New York,

E.A. Goldenweiser, Director of Research & Statistics, Federal Reserve Board,

Wayne C. Taylor, Assistant Secretary of the Treasury,

D.W. Bell, Assistant to the Secretary,

L.H. Seltzer, Research & Statistics, Treasury Department,

C.B. Upham, Assistant to the Secretary.

Mr. Morgenthau referred to the fact that this is the first meeting of Treasury and Federal Reserve people on financing since the new organization of the Board of Governors, and that the meeting is informal, confidential and those present are there as individuals rather than representatives of the Treasury and the system.

Mr. Morgenthau asked Mr. Broderick if he felt it would be necessary to report back to the Board what went on and Mr. Broderick said he tried to keep the Board informed on such matters and that in all fairness he thought they ought to be advised. He said that Mr. Eccles related to the Board the matter discussed at previous similar conferences.

Mr. Morgenthau said that the immediate problem is that of raising money with which to pay the bonus. Several methods are in

contemplation. They have a bearing on excess reserves of the Federal Reserve system. The Treasury attitude is that of wanting to work with the Federal Reserve Board in their credit problems so that the activities of both agencies will fit into a general pattern. Meetings from now on, he said, will look more and more to the whole credit picture not just to raising money and raising it cheaply.

Mr. Bell stated that one plan is to raise money for the bonus in advance by increasing the weekly offering of bills. Beginning with April 29th there would be an additional \$50 million a week up to the end of June, all with maturities on December 15th in total amount of \$450 million. Then by a weekly increase of \$50 million through July, August and September with maturities on March 15th next, another \$700 million would be raised. In addition to this \$1,150,000,000 we would ask for \$750 million new money on June 15th, a total of \$1,900,000,000 new money. These amounts would permit us to run to December 15th before any other major financing would be necessary. On December 15th we would ask for \$600 million new money which would run us until March. In addition we will have to refund \$687 million of notes in June, \$364 million of notes in August, and \$514 million of notes in September. Moreover, on December 15th we would have a maturity of \$358 million notes and the \$450 million of bills which it is proposed to issue with that maturity.

Summarizing this program Mr. Bell said that it means \$1,350,000,000 new money on long-term, \$1,150,000,000 new money in bills, refunding \$1,900,000,000 of notes plus \$450 million bills in December.

Mr. Burgess commented that this will mean a debt of \$6 billion maturing in one year and raised the question whether it is wise to

pile up the short dated debt as large as this contemplates. It can be done, he said, but he has doubts about the wisdom of doing it when we could put out a bond in May for \$600 million to \$750 million and get that much out of the way. He wondered if it is prudent financing and referred to the criticism of the size of the short dated debt. He suggested that it might be better financing to put out a bond issue in May and another in June.

Mr. Morgenthau asked if he would pick up August and September maturities in June and Mr. Burgess said he would not pick up the September maturities because it would look as if we were afraid of the election.

Mr. Seltzer suggested that there is a splendid open date in September, 1938, for a 2-year note to be offered in September this year and that probably the rate would not have to be in excess of three fourths of one per cent.

Mr. Burgess said he thought to pile up the short-term debt and to duck altogether the September maturity would be signs of weakness.

Mr. Harrison said that the market wants a bond now and that it is consistent with the Treasury program to give the market what it wants. He would avoid an aggravation of the short-term situation. He liked the increase in the weekly bills when it was first discussed. He suggested that when the market wants a bond and when it fits into the Treasury short and long-term position, it might be well to have a bond.

Mr. Morgenthau suggested that the market has not been prepared for May financing to which Mr. Burgess replied that the market does

not know what to expect and that it has no idea of what the financing will be and that he has given it no indication. He advanced the possibility of an alternative program of a note in May and a bond in June, but Mr. Harrison and Mr. Bell thought that the only excuse for any financing in May would be that the market is ready for a bond.

Mr. Goldenweiser asked how long a maturity was in contemplation for a bond and Mr. Burgess said that that depended on whether it is desired to link it definitely with the bonus. The market will take a 2-3/4% with a longer maturity than the 1948-51's offered in March. He favored that or a very long bond.

Mr. Harrison asked how far we could go with the 2-3/4% and Mr. Burgess replied that 1952-55; 1952-54; or 1953-55.

Mr. Morgenthau explained that his original idea had been to put out 9 bonds to take care of the bonus, maturing about \$220 million each year. He had been told that those maturities were too small to scatter in among the present outstanding issues.

Mr. Harrison said he would like something that would be a constant reminder that the cost of the bonus had not yet been paid off and would act perhaps as an offset to the growth of a pension idea.

Mr. Burgess thought the same effect might be reached with a 10 year bond and a required sinking fund. On second thought Mr. Harrison thought it might be well to keep the whole amount of the bonus issue outstanding as long as possible.

Mr. Morgenthau commented that between now and the middle of December the Treasury would have to raise \$1,900,000,000 new money.

Mr. Burgess suggested \$700 million in May and \$750 million

in June and then an increase in the weekly Treasury bills beginning July 1 for \$500 million to \$600 million, part maturing in December and part in March. He said there is a grand market with a good appetite for bonds and it would be a sign of weakness not to have a bond issue.

Mr. Taylor asked if \$750 million in May and \$750 million in June would not be pressing things a little and Mr. Burgess agreed that maybe \$600 million would be better. Mr. Taylor doubted the wisdom of two bonds so close together.

There was some discussion of a 10 year bond in May and a 20 year bond in June and vice versa.

Mr. Morgenthau thought the May issue, if any, should be as long as possible, but Mr. Burgess thought the market might be better for a long term in June.

Mr. Harrison said the question now is shall we have bills or bonds.

Mr. Morgenthau said that the Daily Statement shows \$2,700,000,000 cash on hand now and that a big bond issue in May would raise that figure higher than he would like to see it while Congress is still in session.

Mr. Bell commented that expenditures would draw down \$400 million to \$500 million in the next month and a half.

Mr. Burgess said that additional bills would also increase the cash balance but it was agreed that the accumulation would be slower.

There was some discussion of the effects of the issuance of bills and of bonds on excess reserves and the point was made that it depended upon whether they were paid for in cash or credit. Bills

being paid for in cash would tend to draw down excess reserves. 125

Mr. Morgenthau asked if he could raise the money by bills and Mr. Burgess replied "yes". Asked by Mr. Broderick about the rate, he said that the rate would go up some but that would be a good thing.

Mr. Morgenthau said he hated to get away from quarterly financing and suggested the possibility of bills now and bonds in September if the market then looks good.

Mr. Harrison said he thought that would suit him better.

Mr. Morgenthau said he didn't like a bond issue in May. He referred to the fact that a couple of years ago we had almost monthly financing and that he had been repeatedly urged to give the market a rest and not interfere with private financing -- to adopt the more orderly quarterly financing.

Mr. Harrison said he thought the most desirable arrangement was to stick to quarterly financing with a \$750 million bond in June and a \$750 million bond in September. His second choice was for a long-term bond in May which he preferred to additional bills now.

Mr. Morgenthau asked about \$450 million in bills now and \$750 million in long-term in June and then on September 15th either a bond or more bills. He commented that 800,000 veterans have not put in their application as yet for the bonus.

Mr. Taylor suggested waiting until May 15th to start additional bills, to which suggestion Mr. Bell gave his support.

Mr. Morgenthau advanced the idea of \$1 billion new money in June. He said if a 1950-53 bond for \$600 million were offered in May the temptation would be to offer more of the same issue in June.

It was generally agreed that that should not be done.

Mr. Morgenthau suggested that those present think the matter over and meet again a week from today. This was later changed to Wednesday, the 22nd.

Mr. Bell suggested that Treasury bills were not such a short dated debt problem as they would be if there were a supply of bankers' acceptances on the market.

It was agreed that as many as \$3 billion in Treasury bills could be taken care of by the market without any worry.

Mr. Morgenthau asked Mr. Broderick if there were any immediate plans on excess reserves.

Mr. Broderick said that there was sentiment in the Board for raising reserve requirements before July 1, partly because of a feeling that it cannot be done afterward. He said there is no definite plan but sentiment is crystallizing very strongly. There has been no definite discussion but a date is being set for discussion. He thinks it will be done in the next 30 or 45 days or not at all.

Mr. Broderick said Mr. Harrison was getting some information to which Mr. Harrison replied that this was the best news he had heard in a long time.

It was the opinion of those present that the action of the Board, if any, and the Treasury financing, should be carefully meshed.

Mr. Burgess thought it would be bad for the reserve requirements to be raised right after a financing. There is nothing more upsetting to the bond market than an announcement for the future. He felt that the announcement of action and the effective date of action should both be before the bond issue announcement.

It was agreed that the June 15th bond should be announced on June 1st and that the market should have at least two weeks for a shakedown and adjustment following any reserve requirement action.

The very latest effective date of a raise in reserve requirement accordingly should be May 15th.

*Washington 128*  
*Also [unclear] [unclear]*  
*for this to [unclear]*  
*Apr 14/36*

IMMEDIATE POLICY OF THE UNITED STATES  
IF FRANCE - IN EFFECT - LEAVES GOLD STANDARD

1. Renewal of serious weakness in French exchange revives possibility of early abandonment of franc's present gold parity.

2. Not clear what steps could or might be taken by French authorities without action by Chamber of Deputies, not now in session. Chamber must authorize devaluation or embargo on gold exports, but it is believed Minister of Commerce could place prohibitive tax on export of gold, or Bank of France might raise minimum amount (now fr. 215,000) of francs which it will redeem in gold to prohibitive figure. (This latter procedure rests on a convention between Minister of Finance, representing government, and Governor of Bank of France, representing bank.) In any event, it is believed that if French want to prevent further loss of gold they will find a way to do it, and this will result in lowering external value of franc.

3. Our immediate policy, in the event of such action by France, should be to take whatever steps we can to minimize disturbances to the foreign exchange market, which probably would follow such action, leaving basic longer range questions of policy for subsequent consideration.

4. Suggested policy of United States, in immediate situation, if France - in effect - leaves gold standard:

- A. Liberalization of restrictions on acquisition of gold for export or earmarking in order to assure effective maintenance of the existing gold value of the dollar as an exchange market influence. The Treasury should declare its willingness to permit the sale of gold, for earmarking or export, to any foreign central bank or monetary authority willing and able to pay the established price in dollars. The fact that the Treasury is

willing to buy imported gold at a fixed price places a limit upon upward movements of the external value of the dollar in terms of gold. If there were no one to whom the Treasury would sell gold at a fixed price, which would be the situation if France and the other remaining gold standard countries were to "go off gold", there would be no check upon downward movements of the external value of the dollar in terms of gold.

B. Removal of obstacles to operations in dollars by British Equalization Account. The task of preventing undue disturbance in the foreign exchange market, if the French franc is turned adrift (which would probably result in serious unsettlement in other gold bloc currencies) will fall upon the United States and Great Britain. It is assumed that the British authorities would no longer be able to control the external value of the pound through operations in francs, and it is not believed that the pound could be successfully stabilized solely through operations in the London gold market, nor through operations in belgas or any other currency which might remain on gold. There would remain the possibility of operations in dollars, with our blessing. The British Equalization Account recently has been unwilling to operate in dollars, partly because, in so far as its direct operations are concerned, the dollar and gold are not interchangeable, and partly because the British are keenly aware of the disfavor with which its operations in dollars, during 1932 and early 1933, were regarded in some quarters in this country.

The first of these obstacles to official British operations in dollars would be partially removed by the

liberalization of our policy with respect to the sale of gold suggested in (A) above. This would not meet the immediate situation, however, if the pound were weak and the British wished to sell dollars and buy sterling - they haven't dollars to sell. To overcome this difficulty, arrangements should be made whereby the British authorities could receive dollars promptly, either by sale or pledge of gold which they might earmark for us in England, or by sale of gold which they would ship to the United States - loans on gold in transit. (One step already has been taken in this direction, by the renewal of the Treasury's offer to buy gold in London, to be earmarked in its name at Bank of England. If such purchases are made from British Equalization Account, the British immediately will be provided with dollars available for support of sterling.)

The second obstacle to official British operations in dollars - the dislike of some of our people for "foreign meddling with our currency" and their belief that the British play us for suckers - has already been removed to some extent by the developments of the past three years, during which there has been an opportunity to observe British currency management in action. It should now be possible, if we are working upon the basis of an understanding with the British, to remove this second obstacle, although there would have to be sharp watchfulness as well as good faith on both sides.

C. Operations in sterling by American Stabilization Fund. This probably would not be a question of immediate policy so long as the British have an ample supply of gold, by the sale of which they could obtain dollars, and, in any case, should only be done in

cooperation with the British, unless we want to engage in a currency war. The job of moderating or preventing fluctuations of sterling in terms of gold and gold currencies has been and should continue to be the responsibility of the British authorities. They are now equipped to operate in either direction. They can sell sterling when it is strong; they can sell gold for foreign currencies, and buy sterling, when it is weak. If, in the future, because of inadequate gold holdings, the British are not able to support the pound and if, in consultation with the British, our temporary intervention in the sterling market appears to be necessary to prevent wide movements of dollar-sterling rates, this should be done.

The question naturally arises here as to why we should do everything we can to make it convenient for the British authorities to operate in the dollar market, even to the extent of altering our gold policy so that the British can obtain gold for dollars (this does not, however, remove all exchange risk from their operations - they still have a position in sterling) when we must be so careful about operations in sterling and must run the hazards of holding a paper currency if we do so operate. The answer, it seems to me, is that we profess to be on the international gold standard and the British profess to be on a managed currency basis. Under these circumstances, the British should assume the task of management of their currency - including operations in dollars - and we should act the way a country on the international gold standard is supposed to act, especially as we can afford to do it, and should be the gainer thereby. The end to be sought in both countries, in this particular sphere, is international monetary stability. Each

country, working along its own lines, can move toward that end if the two countries know they are working together and are persuaded that their domestic interests, no less than the more abstract interests of the world at large, will thereby be served.

Federal Reserve Bank  
of New York,  
April 8, 1936.

*March 31, 1936*

Brookdale

T-V 1 h e L  
al



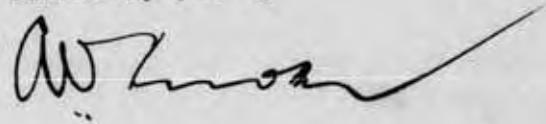
FEDERAL RESERVE BANK  
OF NEW YORK

April 17, 1936.

Dear Mr. Lochhead:

In accordance with your recent request over the telephone we have prepared the enclosed memorandum dealing with the years 1930 - 1933 inclusive in reference to British official operations in dollar exchange. Will you please be good enough to hand it to the Secretary.

Sincerely yours,



Mr. Archie Lochhead,  
Technical Assistant to the Secretary,  
Treasury Department,  
Washington, D. C.

Enc.

BRITISH OFFICIAL OPERATIONS IN DOLLAR EXCHANGE

1930 - 1933

I. Period Prior to 1931 Crisis

During the years which preceded the sterling crisis of the late summer of 1931, it was the practice of the Bank of England to employ a considerable volume of funds in this market, the bulk of these funds usually being invested in bankers' acceptances purchased through the Federal Reserve Bank of New York. During 1930 and the first six months of 1931 these funds were in the neighborhood of \$100,000,000. In this way, the Bank of England had available a reservoir of dollar exchange, which could be called into use when it was considered desirable to support sterling during periods of weakness, and for other ~~similar~~ purposes. In addition, in order to offset the seasonal weakness of sterling and to increase the supply of dollar exchange available in the market during the period of heavy agricultural exports, the Federal Reserve banks, acting through the Federal Reserve Bank of New York, usually purchased sterling bills through the Bank of England during the final few months of the year, and brought home their funds as the bills matured in the early part of the subsequent year. As is shown in Table I, the Federal Reserve banks purchased \$35,000,000 of sterling bills in the London market in the final quarter of 1930, withdrawing these funds from London during February and March 1931, after the period of heavy exports of American crops and seasonal pressure against sterling had passed. Such operations were undertaken regularly by the Federal Reserve banks during the late twenties, their scale varying somewhat from year to year.

II. The Emergency Credits of 1931

The European financial crisis, which began in Austria in April 1931, spread to adjoining countries and resulted in June of that year in a collapse of credit in Germany. Efforts to arrest the spread of this crisis through the

- 2 -

extension of outside support to the central banks of Austria, Hungary, and Germany, and through the American proposal for an international moratorium on intergovernmental debts were unsuccessful, and in July foreign balances began to be withdrawn from England in very heavy volume. Under date of August 1, 1931, the Federal Reserve Bank of New York and other Federal Reserve banks joined in an agreement to purchase up to the equivalent of \$125,000,000 of prime sterling bills from the Bank of England for a period of three months. When this agreement matured on October 31, 1931, drawings thereunder had been repaid fully, with interest, and the agreement was renewed in the reduced amount of \$75,000,000 to mature January 31, 1932, at which time the agreement expired without having been made use of and no renewal was sought. When this agreement originally was consummated, the Bank of England had received from the Bank of France a credit in like amount for a like period, which credit also was renewed in the reduced amount of \$75,000,000 to January 31, 1932, and expired without renewal on the latter date. On August 28, 1931, after the Bank of England had exhausted by drawings almost the full amount of the credits extended by the Federal Reserve banks and the Bank of France, the British Treasury completed arrangements for the following credits:

- (a). \$200,000,000 for one year by J.P.Morgan and Co. and associates.
- (b). \$100,000,000 (equivalent) for one year by a group of French banks.
- (c). \$100,000,000 (equivalent) by public issue in Paris of one-year Treasury bills.

In spite of the assistance provided through these credits, the outward movement of funds from London was so heavy that gold payments were finally suspended on September 21, 1931. On September 23, the Bank of England repaid \$110,000,000 under the credit extended by the Federal Reserve banks, leaving an unpaid balance of \$15,000,000. This unpaid balance was increased to \$40,000,000 through drawings under the credit during October, which balance was repaid in full on October 31. Following the renewal of the credit in the

reduced amount of \$75,000,000, no further drawings were made, and, as mentioned above, the credit definitely expired on January 31, 1932. The Morgan credit to the British Treasury was repaid in three successive instalments during March and the early part of April, 1932.

### III. Dollar Operations of the British Authorities from Autumn of 1931 to Spring of 1933

The character and approximate magnitude of the dollar operations of the British authorities, during the period from their suspension of the gold payments in September 1931 to our departure from gold in April 1933, are roughly indicated in Table II, which gives, as of the last Wednesday of each month, the amount of British official holdings of dollar assets and gold in New York, together with their actual net indebtedness to this market under the emergency credits granted in August 1931. The first column of the table shows the dollar balances and short term investments in bankers' acceptances and treasury obligations held here for account of the Bank of England and the British Treasury, while the second column gives the amount of gold held under earmark at the Federal Reserve Bank of New York for Bank of England account. The sum of dollar assets plus gold, shown in the third column, is an approximate measure of the amount of "quick" assets held in this market by the British authorities. The next three columns of the table show the indebtedness actually outstanding under the emergency credits extended during the 1931 crisis. The final column, giving the net excess of assets held in New York, or liabilities to New York, of the British authorities, constitutes an indirect but fairly accurate measure of British official operations in dollars prior to our departure from gold in 1933. By way of illustration, the change in the net position in this market of the British authorities from minus 198 million dollars at the end of September 1931 to plus 131 million dollars in the latter part of May 1932, as shown in the last column of table II, indicates that the British authorities purchased on balance about

\$320,000,000 in this period. Of this sum \$215,000,000 was used to repay indebtedness, while all of the remainder went to increase assets in this market.

In considering the movements of sterling exchange and the dollar operations of the British authorities from the autumn of 1931 to the spring of 1933, it will be convenient to analyse separately four distinct periods.

The initial period of unsettlement following the suspension of gold payments on September 21, 1931, extended until almost the end of the year, the pound-dollar rate touching a low of \$3.25 3/4 on December 7. Although the British authorities intervened in the market for brief periods and on a limited scale, they lacked the resources with which to undertake sufficiently sustained intervention to cushion the decline to an important degree. They were perhaps reluctant to make further drawings under the credit extended by the Federal Reserve banks for the purpose of giving support to sterling exchange after gold payments had been suspended. On the other hand, they presumably did not wish to accelerate the decline in sterling by <sup>actively</sup> accumulating dollars (and francs) with which to repay their indebtedness to New York and Paris. As the table shows, the net position of the British authorities in this market changed only \$90,000,000 during the final quarter of 1931.

The period from December 1931 to the middle of June 1932 was one of substantial general demand for sterling. After rising moderately in previous months, the pound-dollar rate advanced with particular sharpness during March to a high of \$5.82 3/4, reacting only moderately from this peak level during April, May, and the first half of June. An Exchange Equalization Account was established early in April to free the Bank of England from the necessity of using its own funds in moderating the movements of sterling exchange. The firmness of the pound in that period does not appear to have had its origin in any substantial basic improvement in the British international position, but was due rather to the huge flow of foreign funds towards London, together, no doubt, with some repatriation of British funds. Among the forces which

influenced the flow of funds and which may be separately observed, the following were the most important:

- (1). The mood of extreme pessimism concerning the British financial situation during August and September 1931, which made necessary the utilization of emergency credits by the British authorities, was followed by a reaction in sentiment after the suspension of gold payments, which in turn enabled the British authorities to acquire a part of the exchange necessary for the repayment of these credits. Speculators who had taken a short position in sterling, took advantage of the fall in the exchange to cover their position and repay their obligations. Other foreigners, owing debts payable in sterling, anticipated their maturities or met their obligations with unusual promptness. Obviously, this could not be a continuing factor in the exchange position.
- (2). In connection with the balancing of the British budget, there developed an attitude of optimism concerning the British situation. This sentiment led to a movement of short term funds to London and to foreign purchases of British securities.
- (3). Repayment of the central bank credits and gradual prepayment of the British Government credits of 1931 had a most favorable effect on sterling. In fact, early in March 1932, when most of the British Government credits were prepaid, sterling jumped over 30 points.
- (4). The demand for sterling was in part a result of fears concerning the ability of the United States to maintain gold payments. While private foreign balances in London were increasing rapidly, such balances in this country were reduced to a working minimum. In addition, there were periodic reports of the sale of American securities by British investment trusts and by other foreign holders, as well as of purchases of British securities by Americans.

The net position of the British authorities in this market changed from minus 188 million dollars at the end of December 1931 to plus 151 million dollars in the latter part of May 1932, indicating net purchases of dollars by the British authorities of \$299,000,000, of which \$200,000,000 was used to repay indebtedness and almost all of the remainder to increase their dollar balances and short term investments. British official purchases of dollars served to offset in part the short term forces responsible for the advancing tendency in sterling in this period, and, but for the intervention of the British authorities, the pound-dollar rate would probably have advanced much further. The dollars accumulated when the pound was strong constituted a reservoir which the British authorities were able to draw upon to support sterling during periods of weakness.

From the middle of June to the latter part of November 1932, British dollar holdings were drawn down, owing largely to the fact that as a result of a reversal of the character of the short term forces in play sterling had to be supported through official intervention. On the one hand, the viewpoint became increasingly general that although the financial crisis in England terminated with the suspension of gold payments, the general economic crisis had not yet been substantially relieved. The activity of industry and employment had shown little or no improvement, and the difficulties concerning the budget appeared not to have been wholly solved. On the other hand, the ability of the United States to withstand the two waves of heavy European gold withdrawals in the autumn of 1931 and again in the spring of 1932 was quite widely interpreted as a sign of the strength of the dollar, and of the general financial stability of this country. These changes in the market attitude were reflected both in the international movement of short term funds and in the movement of securities. A further general withdrawal of foreign short term funds from London accompanied a moderate increase in foreign balances here. Moreover, reports were current, appearing both in the British and in our own financial press, of substantial British purchases of American securities, at a time when the conversion of the British Government debt to a lower interest basis was inducing many foreign holders of these securities to dispose of such holdings in the London market. During the autumn, sterling exchange was also affected adversely by the incidence of the usual seasonal pressure accompanying the movement of agricultural products to Great Britain, and, in addition, by uneasiness and uncertainty regarding the future status of the British and other war debts to this country following the expiration of the Hoover moratorium. In spite of the fact that the British authorities drew heavily upon their assets in this market in order to cushion the decline in sterling, permitting their resources in this market to fall to \$39,000,000 in the latter part of October, the pound-dollar rate declined sharply to an extreme low of \$3.15 1/2 on November 29.

The period from the middle of November 1932 to our departure from gold on April 19, 1935 was one of renewed strength in sterling. The payment in full of the December 15, 1932 instalment on the British War debt to the United States Government served to remove a factor of uneasiness as an immediate influence on the exchange market. Of much greater importance, however, was the outflow of both foreign and domestic funds from this market owing to increasing banking difficulties, culminating in March 1933, and owing to uncertainty concerning the future status of the dollar. The British authorities purchased dollars against sterling on an extensive scale during these three and a half months, most of which were converted into gold and placed under earmark at the Federal Reserve Bank of New York. As a result of these operations, the resources of the British authorities in New York rose from \$39,000,000 in the latter part of October 1932 to \$337,000,000 in the latter part of April 1933. In spite of these extensive operations, the increased market demand for sterling was sufficient to bring about a sharp rise in the dollar-pound rate, the rate closing at \$5.51  $\frac{3}{8}$  on April 18, 1933.

Reviewing British operations in the dollar market during the whole period from September 1931 to April 1933, the conclusion seems warranted that, although the amplitude of the fluctuations of sterling was considerable, the effect of British intervention was clearly to reduce their extent by offsetting in substantial degree the influence of periodic changes in market attitude, which otherwise would have had an even more marked effect on the supply of and demand for sterling. The British authorities sold sterling against dollars when, as a result of short term forces, the pound was strong. They sold dollars against sterling when short term influences were reversed, and the pound was weak. In general, therefore, the declarations of British spokesmen that the exchange operations of the British authorities were designed merely to cushion the effect of short term forces affecting sterling exchange, and that these operations were not designed to, and did not in fact, exert a continuous influence on sterling in

one direction, are confirmed by the accompanying data.

IV. Liquidation of Assets Held in New York by British Authorities - Spring 1933 to early 1934.

Following imposition of an embargo on gold exports from the United States on April 19, 1933, the British authorities discontinued operations in dollars as a means of moderating fluctuations in the gold value of sterling, confining their exchange operations to dealings in French francs, the principal remaining gold currency. During the final eight months of 1933, British official funds on deposit or employed at short term in this market were gradually liquidated, being reduced from \$137,000,000 in the latter part of April to only \$5,000,000, at the end of the year. The Equalization Account presumably incurred a considerable exchange loss in the liquidation of these dollar holdings.

Of the \$200,000,000 of gold held at the Federal Reserve Bank of New York by the Bank of England, \$150,000,000 was released and shipped to Paris during the period from July to October 1933. The remainder was "swapped" in December 1933 and the early part of 1934 against gold purchased and held abroad by the Reconstruction Finance Corporation and the Treasury. Thus, the British authorities during 1933 and early in 1934 disposed of virtually all of their "quick" assets previously held in this market.

Federal Reserve Bank of New York

April 17, 1936.

(IN MILLIONS OF DOLLARS)

TABLE II

	DOLLAR ASSETS AND GOLD HELD IN NEW YORK BY BRITISH AUTHORITIES			AMOUNT ACTUALLY UTILIZED OF EMERGENCY CREDITS EXTENDED TO BRITISH AUTHORITIES			NET EXCESS OF ASSETS (+) HELD IN NEW YORK OR LIABILITIES (-) TO NEW YORK OF BRITISH AUTHORITIES		
	Dollar Assets	Gold	Total	By Federal Reserve Banks	By Private Banking Syndicates	Total			
<b>1931</b>									
June 30	120	-0-	120	-0-	-0-	-0-	+	120	
July 29	58	-0-	58	-0-	-0-	-0-	+	58	
August 26	20	-0-	20	119	-0-	119	-	99	
September 30	17	-0-	17	15	200	215	-	198	
October 28	50	-0-	50	40	200	240	-	190	
November 25	30	-0-	30	-0-	200	200	-	170	
December 30	32	-0-	32	-0-	200	200	-	168	
<b>1932</b>									
January 27	62	-0-	62	-0-	200	200	-	138	
February 24	105	-0-	105	-0-	200	200	-	97	
March 30	109	4	115	-0-	20	20	+	95	
April 27	104	-0-	104	-0-	-0-	-0-	+	104	
May 25	125	6	131	-0-	-0-	-0-	+	131	
June 29	85	44	127	-0-	-0-	-0-	+	127	
July 27	46	44	90	-0-	-0-	-0-	+	90	
August 31	49	44	95	-0-	-0-	-0-	+	95	
September 28	74	44	118	-0-	-0-	-0-	+	118	
October 26	25	14	39	-0-	-0-	-0-	+	39	
November 30	55	14	69	-0-	-0-	-0-	+	69	
December 28	87	14	101	-0-	-0-	-0-	+	101	
<b>1933</b>									
January 25	145	32	175	-0-	-0-	-0-	+	175	
February 21	157	124	281	-0-	-0-	-0-	+	281	
March 29	105	200	305	-0-	-0-	-0-	+	305	
April 26	137	200	337	-0-	-0-	-0-	+	337	
May 31	132	200	332	-0-	-0-	-0-	+	332	
June 28	108	200	308	-0-	-0-	-0-	+	308	
July 26	97	181	278	-0-	-0-	-0-	+	278	
August 30	78	125	205	-0-	-0-	-0-	+	205	
September 27	65	85	148	-0-	-0-	-0-	+	148	
October 25	47	50	97	-0-	-0-	-0-	+	97	
November 29	6	50	56	-0-	-0-	-0-	+	56	
December 27	5	47	52	-0-	-0-	-0-	+	52	

(IN MILLIONS OF DOLLARS)

	<u>BANK OF ENGLAND FUNDS IN NEW YORK</u>				<u>FEDERAL RESERVE FUNDS IN LONDON</u>		
	<u>Balances</u>	<u>Acceptances</u>	Short Term Gov't. <u>Securities</u>	<u>TOTAL</u>	<u>Balances</u>	<u>Bills</u>	<u>TOTAL</u>
<u>1930</u>							
January 29	7.7	70.5	-0-	78.2	0.5	0.2	0.7
February 26	6.4	68.8	-0-	75.2	0.5	0.2	0.7
March 26	6.1	66.5	-0-	72.6	0.5	0.2	0.7
April 30	4.2	61.2	-0-	65.4	0.5	0.3	0.8
May 28	5.6	59.9	-0-	65.5	0.5	0.3	0.8
June 25	6.4	78.2	-0-	84.6	0.5	0.3	0.8
July 30	6.4	106.5	-0-	112.9	0.5	0.3	0.8
August 27	6.4	104.5	-0-	110.9	0.5	0.3	0.8
September 24	6.4	97.7	-0-	104.1	0.5	0.3	0.8
October 29	6.4	95.3	5.0	106.7	0.5	18.3	18.8
November 26	6.3	97.2	5.0	108.5	0.5	29.6	30.1
December 31	6.0	89.0	5.0	100.0	0.5	35.2	35.7
<u>1931</u>							
January 28	16.5	92.5	5.0	114.0	0.5	35.3	35.8
February 25	9.0	109.3	5.0	123.3	0.5	25.6	26.1
March 25	7.4	104.7	10.0	122.1	0.5	0.2	0.7
April 29	9.5	88.8	25.0	123.3	0.5	0.3	0.8
May 27	6.7	76.4	35.2	118.3	0.5	0.3	0.8

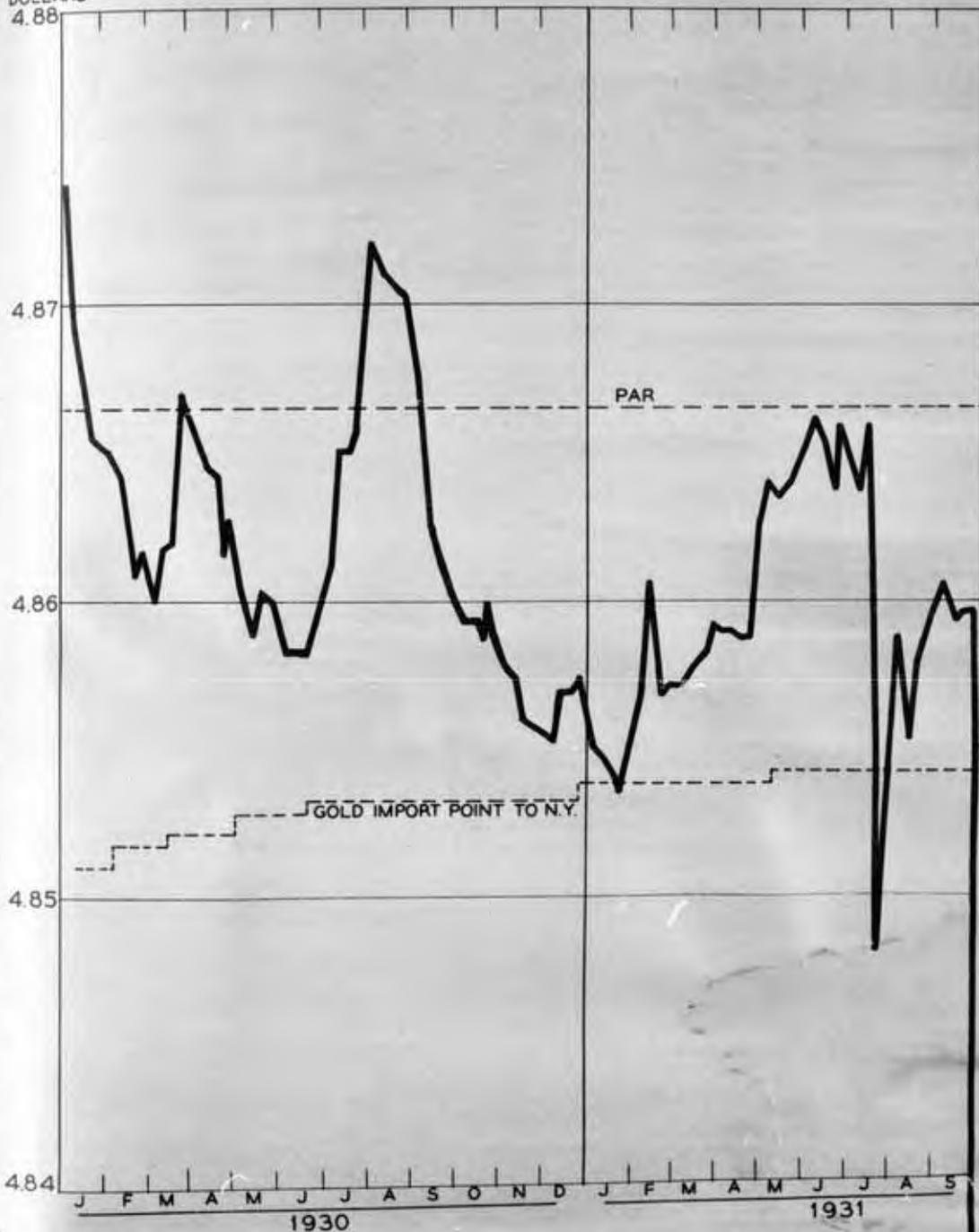
# STERLING EXCHANGE AT NEW YORK

WEEKLY AVERAGES OF DAILY CLOSING RATES

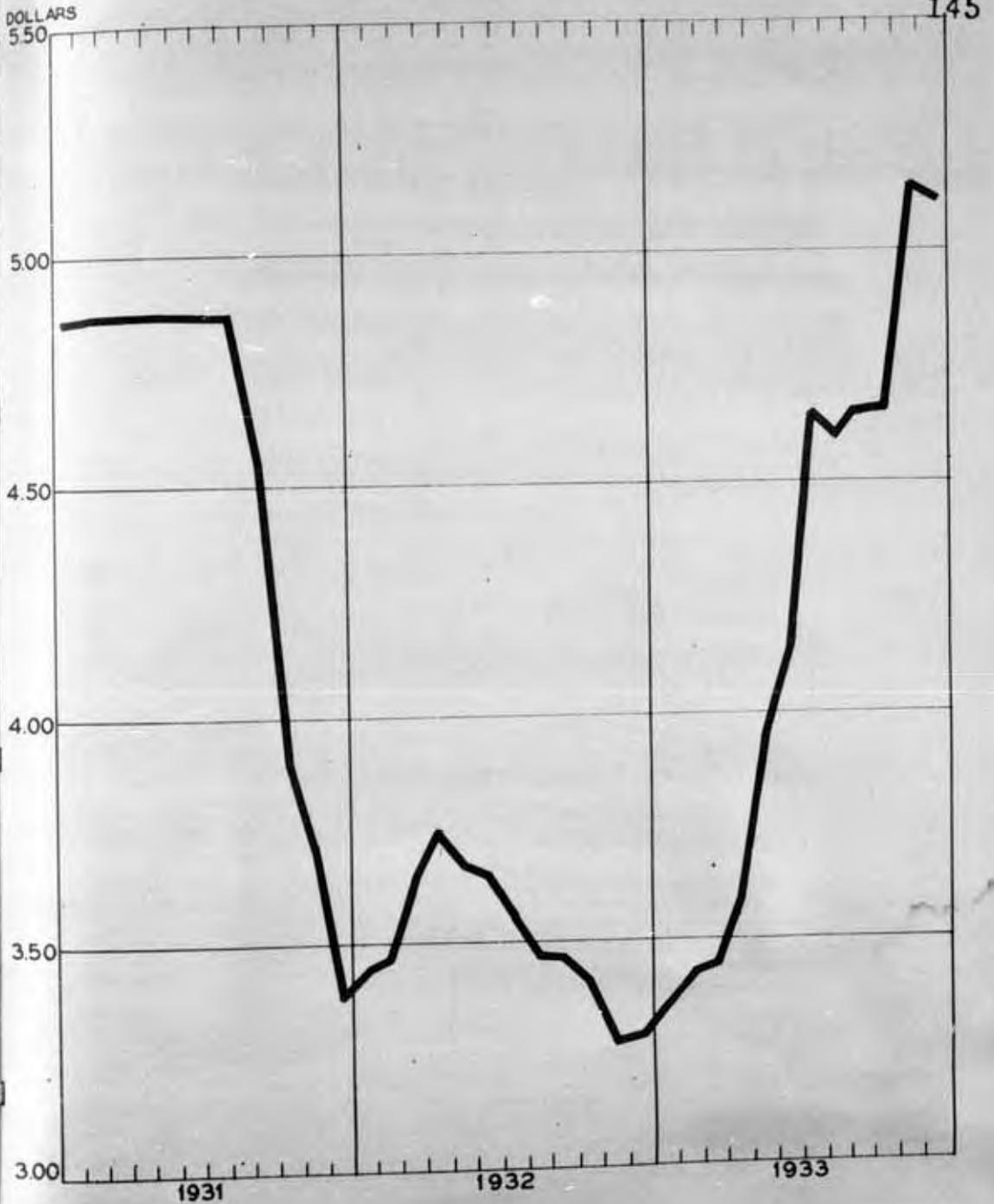
(JAN, 1930 - SEP, 1931)

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DOLLARS



STERLING EXCHANGE AT NEW YORK  
MONTHLY AVERAGES OF DAILY CLOSING RATES  
(1931 - 1933)



FOREIGN INFORMATION DIVISION  
APRIL, 1936

April 14th

Lunched with the President. Spent most of the time telling him about my conversation with K. P. Chen. The President was intensely interested and asked me a great many questions, particularly as to whether Chen was pro or anti-Japanese. I assured him that he was anti-Japanese.

I told the President that I see the foreign situation as follows: That if Hitler can protect himself in Europe so that he will not have any conflicts on his hands on either of his borders that he is very apt to join hands with Japan and attack Russia. The President agreed that this is a possibility. I said that China was in bad shape and that unless Japanese activities were diverted through a conflict with Russia that China's chances of pulling through were not too good.

I told the President that my present plans were to offer to buy from China 5 million ounces a month beginning with May and running for 8 months or a total of 40 million ounces and that we would make a price each month. Furthermore, that we would ask China to unhook herself from sterling and manage her currency in the same way that Canada does, namely, to work in between sterling and the dollar and not to be tied to either.

The President asked me particularly about Sir Frederick Leith-Ross. I told him that since we had refused to buy silver from Hong Kong and let the price drop that Leith-Ross had steadily lost face and we had steadily gained since that episode.

I told him that the Mexican ambassador was in this morning and had a memorandum offering me his surplus silver. I told the President that I thought we were doing enough for Mexico by buying their newly mined production each month and that we should not do any more. He agreed.

I tried to discuss the Tax Bill with him but could not get him to put his mind on it because he said, "there is no use discussing it until it is reported out, which will not be until next week". I asked him whether he did not think I ought to go on the Hill as there was talk around town that I was really not interested in the bill. He said that I certainly should go.

I told him that we were working on German counter-vailing duties but that there was considerable argument in our shop pro and con and that also the State Department had written a memorandum opposing our taking any action. The President said, "if it is a border-line case I feel so keenly about Germany that I would enforce the counter-vailing duties". I told him that Cliphant thought I ought to leave town and let someone else sign it and Gaston thought I very definitely should sign the order. I told him that I thought I should sign the order as otherwise

people would think that I was running away from it and he said unquestionably that I should sign the order. I asked him whether we could bring it back when it was finished and discuss it with him and he said he very much would like me to do that, particularly because he would like to delay the order until about the time that Chester Davis comes back - for the following very very interesting reasons: He said the Republicans are most likely going to advocate some form of export debentures for agricultural products so that we can dump our products on the rest of the World at a cost to us of around sum of 750 million dollars a year. He said, "when Davis comes back he will have seen Baldwin, Hitler and Mussolini and others and will say that each of these countries have quotas and bounties and that if we attempted to dump any of our goods on them they would immediately evoke extra tariffs to keep us from doing so" and here the President said, "if Davis will be able to say 'just the way the Treasury Department evoked counter-vailing duties against Germany' - that is our answer to the Republican agricultural program. Don't you think that is clever?" I told him that I would try and convince the State Department that we were right before I brought the matter to his final attention.

He asked me whether I thought there would be any serious financial break over the summer and I said that everybody in the Treasury thought there would not be unless something went wrong in the rest of the World. He said, "I would say that the chances for war for the rest of this year are about one in three although in the last twenty-four hours things have gotten much more serious because the British citizens are now getting worried about the Italian occupancy of Lake Tsana.

I then showed him the chart which I had prepared on unemployment which particularly showed that the cost of Home Relief and Work Relief had been steadily rising; also that the amount of money contributed by the localities had stayed constant between 40 and 50 million dollars for the last year and a half. He said, "If your figures are right then the figures I used in my speech last night were wrong". When I showed him that there are still 8 million families on relief he just would not believe it. He again said, "Henry, there is something wrong" and I said, "Mr. President, that is what is worrying me and I think somebody has been kidding you", and when I showed him how the total cost of relief was steadily rising he said, "there is no reason for these figures to have gone up so high and they should have leveled off long ago". He was quite upset by the whole thing and I told him that I was having my figures checked by the Central Statistical Bureau and I was going to let Harry Hopkins see what was wrong with them, although the source of all the figures is from Hopkins' own shop.

ADMINISTRATOR ICKES TODAY DENIED CONNECTION WITH A CONGRESSIONAL RESOLUTION APPROXIMATELY \$100,000,000 FOR PUBLIC WORKS CONSTRUCTION UNDER THE NEW WORK RELIEF PROGRAM, THIS ISSUE A FORMAL STATEMENT ASSERTING THAT HE COULD EMPLOY ONE JOBLESS MAN FOR ONE YEAR AT LESS COST THAN HARRY L. JACKSON'S WORKS PROGRESS ADMINISTRATION.

IWA ALSO PRACTICALLY ELIMINATED FROM THE CURRENT \$1,200,000,000 WORK RELIEF PROGRAM (AND DOES NOT FIGURE IN PRESIDENT ROOSEVELT'S PLAN TO SPEND \$1,000,000,000 FOR MAJOR WORK DURING THE 12 MONTHS AFTER

CONGRESSMEN, HOWEVER, ARE CIRCULATING A PETITION TO BARWARE ALMOST HALF THE NEW MONEY FOR PUBLIC WORKS.

"I HAVE NOTHING TO DO WITH IT," ICKES SAID. "THE ACTION WAS STARTED WITHOUT MY INSTANCE OR WITHOUT MY ASSISTANCE, AND I HAVEN'T EVEN TALKED WITH ANY OF THE MEN BACKING IT."

IWA THEN ANNOUNCED THAT, FROM A TOTAL OF 4,000 COMPLETED PROJECTS THE ANNUAL JOB COST TO THE GOVERNMENT FOR ONE DAY HAD PROVED TO BE \$1,000. THE WORKS PROGRESS ADMINISTRATION, SCHEDULED TO SPEND ALMOST \$1,000 NEW MONEY, FIGURES ITS JOB COST AT \$65 A MONTH, OR \$780 A YEAR. ICKES DENIED, HOWEVER, THAT HE WAS ANY LONGER DEALING WITH JACKSON'S JOBS PROGRESS POLICY.

and I said to him, "Franklin, I am showing you something as your friend" and I said nothing more. When he came to the figures that said that PWA could give a man a job for \$741.60 a year the President said, "that is absolutely wrong" and he kept repeating that and I said, "of course it is. I showed this statement, while I was waiting outside of your office, to Charlie West and when he saw the figure of \$741.60 he said that that was crazy." Charlie West says that the trouble with the statistical organization in the Interior Department is that they are crooked." Then the President said, very angrily, "I do not know what is the matter with Harold Ickes. Why can't he keep his mouth shut. Last week he attacked Wallace now he attacks Hopkins. Why can't he mind his own business. Leave this statement here because Ickes is coming right in now and I'm going to show it to him". Then I said to the President, "the reason I showed this to you is because in the final analysis whom does it hurt - it hurts you". I was awfully glad that I showed it to him and I did not know whether he would get angry at me or not - but he didn't.

I said, "how would you like to have Todd Duncan sing the songs Friday night from "Porgy and Bess" and he said, "why I have heard them sung and the leading role was done by Lawrence Tibbett". Then I said, "oh no Lawrence Tibbett sang one of the songs for you on March 4th but the man who originated the role is Todd Duncan" and he said, "I would love to have him do the songs".

Tuesday  
April 14, 1936.

Operator: Mr. Jones

HMjr: Hello -

Jesse

Jones: Hello -

HMjr: Hello, Jesse?

J: Yes

HMjr: How are you?

J: Fine, how are you today?

HMjr: I hear you want to put Wayne Taylor on a couple of Boards of Directors?

J: Well, what I've got in mind there - we - you know we increased the capital of this Commodity Credit?

HMjr: Yes, I read about it in the paper.

J: And the Board is now constituted of Wallace, Secretary Wallace and Chester Davis and Ward Buckles and Oscar Johnston from Agriculture and Governor Myers and Deputy Governor of Farm Credit - Governor Tyler and Ben Johnson and Stanley Reed over here. And I thought possibly we'd put Jim Alley, our present General Counsel in Stanley Reed's place and I thought possibly I'd go on the Board and probably it'd be nice to have Wayne on it.

HMjr: Well, has the Treasury had anybody on it?

J: Well, I don't suppose they have.

HMjr: No

J: I just happened - to just -

HMjr: Well, Jesse - Wayne is sitting here - I haven't asked him -

J: Yes

HMjr: But - this is - business and not personalities.

J: I know it, but -

HMjr: I- I'd a little bit rather not have the Treasury people on any boards.

J: All right

HMjr: Now I - just a minte, let me ask Wayne. Do you mind a minute?

J: All right, all right.

HMjr: It's awfully hard to do it snap judgment - I'd like to tell you why some time -

J: All right.

HMjr: But the boards we're on - all right. But, I - I -

J: - not have any more -

HMjr: Pardon me?

J: You'd just a little rather not have any more?

HMjr: I'd a little bit rather not have any more. I personally don't think that the Treasury should be on any boards.

J: Yes, sir

HMjr: And that's what I said about the Federal Reserve.

J: I was just trying to keep it in the family was all.

HMjr: Well, I appreciate it and mind you there's nothing that - I'm thinking of the big thing -

J: Yes, I understand.

HMjr: And it's just the way I told Congress I didn't care about being on the Federal Reserve -

J: Yes

HMjr: I'd like to be a little bit consistent.

J: All right - I think probably your position is right, but I - I would like it and I wanted -

HMjr: Well, I -

J: I'm not urging it at all but I think if I was in your position I would make the same decision you've made.

HMjr: It - you see, it's a little bit like sitting on both sides of the table.

J: That's right.

HMjr: And some time I may make a bum decision against myself. (Laughter)

J: That's right. Well, I've been -

HMjr: Was that the only thing, Jesse?

J: That was the only thing I had at the moment, yes.

HMjr: But you need it before four o'clock?

J: Yes, we're going to have a meeting at four.

HMjr: Well, some time this week I'd like to sit down with you.

J: All right, why don't you make it the lunch hour?

HMjr: Well, the trouble with -

J: Well, any time at all you say.

HMjr: I'll call you, because what I've been doing the last week and this week - I'm going home for lunch.

J: Oh, you are? That's good.

HMjr: And so - I - I'm not - so it will have to be during the business day.

J: That's quite all right - just call me any time.

HMjr: All right, Jesse.

J: Goodbye.

April 15, 1936

HM, Jr. had with him in his office today, discussing German countervailing duties, Mr. Oliphant, Mr. Taylor, Mr. Gibbons and Mr. Johnson from Customs. McReynolds was called in to the conference not long after it started. There follows a transcript of the discussion which took place.

HM, Jr.: I have read Dr. Viner's memorandum very, very carefully and I take it that you people are prepared to discuss it.

Mr. Oliphant: What I have here -- I think it is the way to get at it and save time -- is my opinion on the legal question involved.

(Mr. Morgenthau read aloud Mr. Oliphant's statement. Copy is attached.)

HM, Jr.: On the amount of the particular articles under discussion, how much of it would come under the currency manipulation and how much under the other?

Mr. Oliphant: You will come to that.

(HM, Jr. read further.)

HM, Jr.: I mean what proportion is coming in under each of those two methods?

Mr. Johnson: There isn't any way to answer that question definitely, Mr. Secretary, but I can say with assurance to myself that the currency manipulation is the more predominant method of subsidizing the goods and that the tendency is to confine the subsidization to bond procedure and currency manipulation.

HM, Jr.: Now let me ask you this. How many articles, roughly, are involved?

Mr. Johnson: We have ten on the present list and we contemplate expanding it.

HM, Jr.: Do you happen to remember them, from memory?

Mr. Johnson: I have a list right here and they constitute

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a very important factor in German trade: cameras, china tableware, cotton and rayon gloves and other gloves, surgical instruments, glass Christmas tree ornaments, metal covered paper, thumb tacks, toys and toy figures.

HM, Jr.: In arriving at this, do you file the record of complaints?

Mr. Johnson: We have complaints from domestic manufacturers. We have inquiries of all sorts. A typical example is the Woolworth man who arranges for all purchases in Germany. Each year for the past three years he has come to the Bureau of Customs in the spring of the year. This year, I think, in February, and has begged us to give him some assurance as to what the situation is going to be in the coming year before they entered into their commitments. Several millions of marks are to be involved in purchases of that company alone. He had to go this year for the third time and enter into his contracts without knowing what he was facing.

HM, Jr.: For instance, do you have a letter from a glove manufacturer or our own manufacturers complaining against this kind of competition?

Mr. Johnson: Oh, yes, sir. You are familiar, Mr. Gibbons with the horseshoe case.

Mr. Gibbons: We have one case up in Massachusetts where a fellow went over and bought a lot of leather. Congressman McCormack, Mrs. Rogers and two or three others saw me about it.

HM, Jr.: Do we have many like that?

Mr. Johnson: The horseshoe case is a very vociferous one.

HM, Jr.: Do this for me. Go through your files and take actual names of the manufacturers and divide the thing into these different kinds of classes it falls under.

Mr. Oliphant: You mean by commodities?

HM, Jr.: No. Which would be better. Also the name of the association or whether it is a particular manufacturer of horseshoes. Just two lines: the XYZ Horseshoe Company complains that the dumping of German horseshoes in the American

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market has hurt their sales to such and such an extent due to either the Germans being able to sell these things at so much less or due to their using German scrip currency.

Mr. Johnson: It would be very difficult and would not give a fair picture.

HM, Jr.: Let's go at it another way. How many different cases do you have? Take the ten commodities. Can you give me an idea who are the complainants?

Mr. Johnson: We did not determine these commodities on the basis of complaints. They are based on evidence.

HM, Jr.: What I am trying to get at is this: if we do this thing, who can we say brought it to our attention?

Mr. Johnson: Our appraising officers are the particular ones under the law who are required to bring it to us plus the Treasury agents in Germany. You want to know who in the public is requiring this action?

HM, Jr.: Right!

Mr. Gibbons: Get it from the appraisers in New York.

HM, Jr.: Is the horseshoe manufacturer -- is the manufacturer of Christmas tree decorations -- are there any particular people or any particular Congressmen, like Congressman McCormack -- I want to see who will come to our support.

Mr. Johnson: Of course, it's quite a difficult task.

HM, Jr.: There must be a file on this thing.

Mr. Johnson: Oh, yes.

HM, Jr.: How many horseshoe cases have you?

Mr. Johnson: We have the horseshoe industry of the United States.

HM, Jr.: How many others?

Mr. Johnson: The paper industry.

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HM, Jr.: How many others? If you are going to do this thing, I know who will jump on us, but who is going to come to our support? If there is a row in Congress, who is going to come to our support?

Mr. Johnson: Congress passed the law. They will have to come to our support.

HM, Jr.: It has no bearing on what the decision is, but if decision is made I want to know who is for it and who is pushing it.

Mr. Gibbons: I will get it.

HM, Jr.: Now let me get this. Herman, you have to help me. You have taken a purely legal standpoint which you think is the correct one? This is a legal opinion?

Mr. Oliphant: There is nothing else anyone can make. The facts are admitted.

HM, Jr.: You once said to me that we can only refer a legal question to the Attorney General if there is any doubt.

Mr. Oliphant. That's true. That's our general practice. In this case it is coupled with the further fact that the whole administrative machine, administering the Tariff Act, is built up on the practice that where construction of the Tariff Act is involved the Treasury construes the tariff. Now, the effect of that, of course, has been that these questions are disposed of in the Treasury. And they have not set up in Justice any machinery for hearing all the people who would want to be heard if they would first see us.

HM, Jr.: No, but I still say, in a special case like this.

Mr. Oliphant: We discussed that angle with Mr. McReynolds -- the administrative aspects of the case in the terms of the general Government set-up.

(HM, Jr. telephoned for McReynolds.)

HM, Jr.: While we are waiting, how about Viner's sug-

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gestion that he said or made to me -- at least I paid no attention to it, in connection with the invoice.

Mr. Oliphant: It's a little more complicated than Viner anticipated.

HM, Jr.: Is that being studied?

Mr. Oliphant: Yes, we are working on that now.

Mr. Johnson: The final form of the invoice document will depend somewhat upon the action taken here.

HM, Jr.: Mac, we are talking about countervailing duties on Germany and I have raised the point, is there anyone we could possibly refer this opinion to because the State Department is on record that we don't need to impose countervailing duties? Mr. Oliphant said he talked to you about it.

Mr. McReynolds: He discussed the question of referring it to the Attorney General. The precedent for that would be, as far as I know and as far as Mr. Oliphant knows -- the Treasury has undertaken to make its own decisions in the administration of those tariff problems. I see it broken down. If we can get by with it, taking care of our own stuff rather than shifting it over to Justice, I think we ought to do it. Of course, there is nothing basically wrong if we submit it there. But if you start it you will be headed toward having them take care of all of our cases, just as they do in compromise cases.

HM, Jr.: This is not a matter of Governmental procedure if you want to follow right down the middle of the road. I think this is distinctly an exceptional matter. As a matter of fact, after talking this thing over with Hull it seems to me if you are going to get Governmental on these things, the Tariff Commission should make the decision and we as their agent carry it out.

Mr. Oliphant: That is not the law.

HM, Jr.: I know it isn't, but if we start from scratch they have the machinery over there and they are a judicial body and so if we start with no law at all these things should be put up to them, who are a judicial body; they hear them and they would advise us what to do and we carry

them out. But that decision can't be made today.

Let's go at it from a different angle, Mac. Whatever I do in the case, the President wants to be consulted. I have to show him this memorandum from Hull. He will say, The final decision is yours, but I want to talk to you about it. He, the President of the United States, wants to refer this matter to Justice, not to see all the people but just as a straight legal question. There are particular circumstances connected with this thing and the President said, I would like to have the Attorney General advise me so I, the President, can say to the Secretary of the Treasury, You are my appointee and you have consulted me about this, I want you to do this thing.

Mr. McReynolds: My judgment on that would be there would be no damage done from our procedural standpoint if the President asked the Attorney General for his opinion.

Mr. Oliphant: Is that clear in connection with non-discretionary power of the Secretary? You see, the President has no authority at all to pass on this under the Statute.

HM, Jr.: No. But let's say I have some doubts about this thing. Let's refer to the Silver Act. I have some doubts as to just what that sentence means "in the public interest." What does that sentence mean? I go to the President of the United States. I say, You appointed me. I interpret it that it means that I should buy no more silver and I have been so advised by my counsel and I can interpret it that way. Here is a mandate of Congress which orders and directs that I buy silver until one or two things happen, but there is a clause "in the public interest." My counsel advises me that in the public interest I should not buy any more silver. Mr. President, it is very important and I have come to you. I feel that I have this right and I am acting under a mandate of Congress which gave me this order. The President said, Your counsel advised you. Well, I disagree with you. I think you should and I am going to ask the Attorney General.

Another Bureau has raised some question. Suppose the President said, No, Henry; I don't think this interpretation is right. I say I think it is and I want to do it, but the President says to me, No, you should not and I don't think you are being advised properly. I want to do it, Mr. President, and if I can't do it, I want to

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resign. Well, the President says, let me ask the Attorney General if you are right and if he says your legal opinion is wrong and you want to do it and if you can't you want to resign, you will have to resign. Is that straight thinking?

Mr. Oliphant: Yes.

HM, Jr.: Are the cases comparable?

Mr. Oliphant: Yes.

HM, Jr.: I want to do the thing that is legally right and ethically honest.

Mr. Oliphant: I would feel differently if I had any legal doubts.

HM, Jr.: Herman, your legal opinion has always been right. It has never been questioned. When we were in Farm Credit; the whole gold business -- we have sailed along beautifully, so it is not questioning my General Counsel because I have entire confidence in my General Counsel and I am perfectly willing to follow my General Counsel's advice on this matter.

Mr. Oliphant: I appreciate your saying all of that.

HM, Jr.: This is for the record. I have never once questioned the legal opinion of my General Counsel.

Mr. Oliphant: It is very generous of you to take this occasion to say that, but my statement was not directed in that direction. If we had a question on the interpretation of a Statute about which I could advise you, which was doubtful, then what I am seeking to do, the thing I had in mind in connection with this thing is, it ought to be handled in an ordinary, routine manner. If they had a case here where I could advise you and there was a question of legal doubt, then it would be a perfectly proper thing.

HM, Jr.: I feel we are following a perfectly proper thing. This is a very important case. I go to the President of the United States and say, Mr. President, I want to do this. The State Department says I should not. There is a difference of opinion between two Cabinet officers involved in this case. I would like to do this. But I think that before taking a position which is contrary, I think I

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ought to lay this in your hands. Then the President turns to me and says, On this question I would like to have the Treasury position checked by the Attorney General who is my (the President speaking) my lawyer, my counsel. Or again, Very sorry, Mr. President, I feel very strongly that I have to do this and if I can't do it, I have to resign. Mr. Oliphant and I feel very strongly that we should go on this thing or both resign.

Mr. Oliphant: Yes. Your very serious oath is involved.

HM, Jr.: On stabilization I have never threatened to resign. I either resign or I don't. But you remember the other case where they had our backs against the wall and the Attorney General was in and we fought like hell.

Mr. Johnson: The Secretary is advancing the question of policy. I don't see how you are going to the Attorney General without someone disagreeing with Mr. Oliphant.

McReynolds: I don't think the Secretary of the Treasury should go to the Attorney General, but should go to the President because there is the question of disagreement with the Secretary of State.

Mr. Oliphant: I would rather have the Attorney General's O.K. on this, as a human proposition, if I disassociated myself from official obligation, then take sole responsibility for the decision, but if it is true -- I haven't thought this thing through -- I would say that disagreement between the two Departments is not a disagreement on question of law involved. In effect, the Secretary of State says this is a very unwise law and ought to be changed.

(The Secretary read aloud the letter from Secretary Hull.)

HM, Jr.: If he is not interpreting the law, then what is he doing?

Mr. Taylor: He is raising questions which bothered the Committee.

HM, Jr.: He is raising the question as to whether this is general currency depreciation or special and he is interpreting this law.

Mr. Oliphant: Everybody admits it is not general currency

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depreciation. Everybody admits that Germany did not devalue the mark as we did with the dollar.

Mr. Johnson: His point is this: that (1) uniform general currency depreciation has never been held to be in the scope of Section 303; (2) we have here not a general or uniform depreciation, but a special type of depreciation and, following that, (3) just a claim or urging that we apply the considerations which have heretofore been applied to uniform depreciation to what he terms special case of depreciation. That's answered in Mr. Oliphant's memorandum.

Mr. Oliphant: The question the Secretary is asking is, Does the Secretary of State raise a question of law here on which we can hang the position that the Departments are disagreed and which the President wants to refer to the Attorney General.

HM, Jr.: What are Secretary Hull's objections based on? That's the point.

Mr. Oliphant: These are his objections: "However, I am in agreement with the view presented in the subcommittee's report that there is considerable doubt whether currency manipulations fall within the meaning of the term "bounty or grant" as used in Section 303, and whether they may not more appropriately be regarded as a special form of currency depreciation." I think you can hang it on that.

Mr. Johnson: I agree with Mr. Oliphant.

HM, Jr.: I don't think there is any question about it. If Mr. Oliphant is satisfied -- I have given you both time; that is not your snap judgment -- I don't think there is much question. Let's say the President said, O.K., go ahead and do this thing, and then we have a whole group and Mr. Hull's memorandum comes up and, My God! here it has me doing this thing in the face of a very, very strong memorandum from Mr. Hull that we were on the eve of having a new treaty with Germany! Where does it leave me? If you take this thing cold -- Hearst wouldn't be interested in this, but take the Baltimore Sun, the Journal of Commerce -- right on the eve of the treaty and Morgenthau steps in because he is prejudiced against Germany and in the face of what Mr. Hull says he jams this thing through!

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Mr. Gibbons: You have to be super-careful.

HM, Jr.: Here he says practically, we are on the eve of a treaty with Germany. Just on the eve! Now, Herman, you are satisfied that there is no question of interpretation of the law involved?

Mr. Oliphant: I am perfectly clear on the law. Every lawyer in my shop is too. Now, I think, second, that you can read that letter and say the State Department takes another view on the question of law.

HM, Jr.: All right. Now the thing for me to do is this. Say, look here. I have this thing. We think you are wrong and we think we are right. Do you think we can get together? I don't think there is one chance in five of getting together, do you? Let me mark it out this way. I am going to take the attitude that I am going to do this on the recommendation of my General Counsel.

(HM, Jr. dictated the draft of his letter to the President as follows:

My dear Mr. President:

On the recommendation of Mr. Oliphant, General Counsel of the Treasury Department, I feel called upon to invoke Section 303 (etc., the legal language).

I am attaching hereto a copy and summary of Mr. Oliphant's opinion, which is the basis for my action.

However, before taking this action I feel it is my duty to bring to your attention Mr. Hull's letter of April 2, in which he raises the following legal question as to whether this action is to be taken.: (to be quoted).

On account of Secretary Hull raising the question, it seems only proper that I lay this matter before you for your advice and counsel.

You work on this, Herman, and let's have another meeting and take a look at it. Let's go around the table.

Mr. Taylor: All right.

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Mr. Gibbons: Absolutely.

Mr. Johnson: I have my reservations.

HM, Jr.: As to what?

Mr. Johnson: If this goes to the Attorney General, I want some assurance ....

Mr. Oliphant: Oh, I meant to bring up that time element. He has in mind a case that went to the Attorney General which meant not only construction of the Tariff Act, but also doubt, and that has been before the Attorney General for twelve years. Have you any other reservation.

Mr. Johnson: I still want to urge that that be more specific.

Mr. Oliphant: Do you want to talk about legal merits?

HM, Jr.: If I start in to analyze every one of your legal opinions . . .

Mr. Oliphant: Not every one.

HM, Jr.: Is this something that you familiarized yourself with?

Mr. Oliphant: Intimately, personally, and am absolutely satisfied.

HM, Jr.: This is not something that one of your bright young men ....

Mr. Oliphant: No. Everybody has worked on it for a long time.

HM, Jr.: If I want an economist, I get Jacob Viner and if I want the legal end, I have Herman Oliphant. Mac, are you satisfied?

Mr. McReynolds: Entirely satisfied, without any reservation. I think this is the way to do it.

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# TREASURY DEPARTMENT

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(See also 151-185)

INTER OFFICE COMMUNICATION

DATE April 15, 1936.

TO Secretary Morgenthau,  
FROM Herman Oliphant.

## Countervailing Duties on German Goods

After a careful review of the memoranda addressed to you by Assistant Secretary Taylor and Mr. Viner, and upon reconsideration of the entire matter, I find nothing to warrant altering my opinion that the law requires the application of countervailing duties under Section 303 of the Tariff Act of 1930 upon certain German goods, as contemplated by the draft of a Treasury Decision recently approved by me, and that it is the mandatory duty of the Secretary of the Treasury to direct that such bounties be imposed.

The facts are not in dispute and the statute is admittedly mandatory on the Secretary of the Treasury. Once its applicability to the facts in the case before him is determined, he has no discretion. The only question open for discussion is the usual legal one of statutory construction, that is, the facts being admitted, what is the law as fixed by the statute?

German exports to the United States of particular commodities dutiable under the Tariff Act of 1930 are being aided by numerous devices which fall into the following classes:

- (1) Payment of direct cash bounties by German industrial associations.
- (2) Scrip and bond procedures.
- (3) Currency manipulations.

It is my opinion that the statute requiring the imposition of countervailing duties applies to all three of the foregoing classes.

Those in the State Department considering the matter and your advisers in the Treasury Department are agreed that payments of the first class would require the imposition of countervailing duties. The State Department has transmitted to us the formal denial of the German Government that such cash bounties are being paid from a specified fund but the Treasury has evidence that such bounties are being paid in connection with some commodities from that or other funds.

Mr. Viner construes the law to apply to the second class mentioned above. On this, Mr. Taylor's memorandum expresses no opinion.

Mr. Viner and Mr. Taylor agree that the statute should be so construed as not to apply the third class mentioned above.

Apart from minor changes in the rates set out in it, the Treasury decision which I have initialed for issuance could, as a matter of law, rest entirely upon bounty payments and the scrip and bond procedures without reference to currency manipulations, but I hold also that the law applicable to the currency manipulations requires the issuance of this Treasury decision and make this holding for the future guidance of the Bureau of Customs in recommending assessment of countervailing duties under this Treasury decision.

The reasons for the decision that the statute in question applies to the currency manipulations can be stated briefly, but are stated without any purpose of construing the statute beyond the point

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necessary for the future guidance of the Bureau in dealing with these manipulations. Other practices may develop, and, as they do, the law applicable to them will have to be examined on the basis of the facts which they present.

In the first place, the statute in question is itself as clear as any legislation of similar scope could be. In fact, its language discloses that it was framed with great care, having passed through a process of perfection of language and enlargement of scope in the series of tariff legislation.

In the second place, the controlling decisions of the Supreme Court construing this statute leave no doubt that the statute means what it says. That this is true appears from the following quotations from one of the leading cases on the subject:

The statute was addressed to a condition and its words must be considered as intended to define it, and all of them — "grant" as well as "bounty" — must be given effect. If the word "bounty" has a limited sense the word "grant" has not. A word of broader significance than "grant" could not have been used. Like its synonyms "give" and "bestow", it expresses a concession, the conferring of something by one person upon another. And if the "something" be conferred by a country "upon the exportation of any article of merchandise" a countervailing duty is required by Paragraph E.

We have the fact of spirits (the commodity upon which countervailing duties had been imposed) able to be sold cheaper in the United States than in the place of their production, and this the result of an act of government because of the destination of the spirits being a foreign market. For that situation Paragraph E was intended to provide. (Nicholas v. United States, 249 U. S. 34).

(Underlinings and parenthetical phrase added).

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The standards for construing the statute set out in the above quotations dispose of the argument that the law governing the discriminatory currency manipulations here under consideration is to be determined by what law might govern cases arising under uniform depreciation of a country's currency. The factual differences between the two situations are substantial.

The action of the German Government in blocking funds held in Germany for foreign account and restricting the disposition and use of such funds by their foreign owners has brought about reduced market values for marks held in such accounts. The marks are purchased at these reduced values by American importers of German goods. The German Government then, as a grant of privilege or concession to a favored German exporter, permits him to receive a specified amount of the controlled marks in full or part payment for certain kinds of privileged goods exported to the United States. In the more usual case, when only part payment in controlled marks is permitted, the balance of the price must be paid in "free" marks costing the American importer a price measured by the value of the gold mark. When the controlled marks are released to the German exporter, their value is restored -- and by ~~that~~ act of the German Government restored -- to the value of marks in free circulation in Germany. This latter value can be measured for our purposes only by the price of "free" marks in United States currency. That price is the value of the gold mark, the value that is regularly paid by American importers who require substantial quantities of "free" marks to finance their purchases of German goods.

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The German exporter who is paid in controlled marks for exports from Germany to the United States receives, therefore, a benefit measured by the difference between the prices paid by American importers for the particular type of controlled marks involved and the "free" mark. The cost of this difference does not fall upon the American importer. The value of the difference is granted to the German exporter by acts of the German Government on, or by virtue of, the exportation of the goods. Thus, in terms of the Court's language already quoted, the exporter is thereby enabled to sell his goods more cheaply in the United States in competition with our domestic goods.

That there may also result a benefit (bounty or grant) to the American importer is beside the point. No bounty or grant can achieve its purpose without some benefit in the form of lower prices to purchasers of the subsidized goods; and a direct money payment by a foreign Government to an American importer could be such an indirect bounty on the exportation of goods from the foreign country as to fall within the statute.

*Herman Oliphant*

April 15, 1936.

MEMORANDUM OF CONVERSATION WITH THE CANADIAN CHARGE D'AFFAIRES.

The Canadian Charge d'Affaires handed me this afternoon the accompanying memorandum containing the substance of the replies of the Canadian distillers to the proposals for a conference submitted to the Canadian Government in our memorandum of April 10th. Mr. Wrong pointed out that in substance the companies had agreed to accept these proposals. At the same time they make certain observations, which Mr. Wrong does not believe of any material importance.

I pointed out that in paragraph (c), page 2, there was some danger in the words "after the conclusion of the conference", since it seemed to give approval to the idea that the conference could break up without definite conclusions being reached. After some further conversation Mr. Wrong agreed to omit the words "after the conclusion of the conference", and said that in sending over the memorandum to the Treasury he would authorize us to omit the phrase.

William Phillips.

(Delivered to Mr. Graves by Mr. Hickerson, Wednesday afternoon, April 15, at 4 o'clock.)

MEMORANDUM

- (1) The Canadian distillers will give commitments not to increase their exports of whiskey to the United States over the present volume during the period which is to be set aside for negotiating settlements; some allowance may be made for normal increase in business.
- (2) The Canadian distillers will give commitments not to dispose of their stocks of American type whiskey elsewhere.
- (3) The individual companies will give commitments to "sit down with Treasury officials and discuss the nature and quantum of the claims alleged to exist with a view to reaching some solution". This proposal is understood to mean (a) reaching an amicable settlement out of court, or failing this, (b) discussing terms, conditions and practical measures in respect to the companies' submitting to the jurisdiction of the American courts and protecting the United States against losses on judgments which might be obtained. Officials of the Department of Justice will take part in the conversations.

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Subject to the above mentioned conditions, the Treasury Department will agree to a delay not exceeding one month (dating from April 13) in the pending legislation, during which the following steps will be taken with a view to obviating the necessity for the legislation if possible.

(1) The Treasury and the Department of Justice, acting jointly, will receive representatives of the Canadian companies individually and undertake to arrive at a satisfactory settlement of the United States Government's claims against them, subject to the condition that the two Departments will state the amount, as at present calculated, of the Government's claims against each company but will not be required either to disclose the particulars of the claim or to discuss the facts or laws supporting it.

(2) In the event of the failure of the parties to agree on a settlement, they will undertake to make an arrangement which will bind the companies to submit to the jurisdiction of the United States courts so that the claims may be litigated on their merits, and to provide satisfactory security for the payment of any judgments which may be rendered in favor of the United States Government.

(3) The Canadian companies are to be informed that any persons designated to represent them in conferences with the two Departments must be fully empowered then and there to bind their principals with respect to the points covered above.

(4) If the negotiations with the companies carried on in accordance with the foregoing should be fruitless as to any one of the following companies, namely:

Distillers Corporation - Seagrams;  
Hiram Walker - Gooderham and Worts;  
Consolidated Distillers; and  
United Distillers,

the Treasury Department and the Department of Justice will be free to proceed with the proposed legislation.

MEMORANDUM

Representatives of Distillers' Corporation-Seagrams, Hiram Walker-Gooderham and Worts, and Consolidated Distillers, have severally agreed to accept the proposals for conference along the lines indicated in the Memorandum of April 10th, 1936. Word has not yet been received from United Distillers. The agreement is subject, however, to the following observations:

(a) In all instances the companies desire to make it clear that they do not admit any liability on the merits. They are, however, prepared to attempt to work out a reasonable solution of the problem in a manner satisfactory to all concerned.

(b) There seems to be some possibility of a misunderstanding of the obligations involved in paragraph (3) of the first page of the Memorandum and in paragraph (2) of the second page. It is assumed that the words "undertake to make" in the latter paragraph are to be construed as meaning "discuss" and that the words "and to provide" are to be construed as meaning "which will provide", so that the paragraph will be interpreted in the light of the provisions of paragraph (3)(b) on the first page. In other words, the true intention of the Memorandum is that the parties will first make an effort to reach an amicable settlement out of Court, and, in the event of failure, will discuss conditions and practical measures in respect to

jurisdiction and the protection of the United States against losses on judgments which might be obtained; but that, in the event of failure to reach an agreement, neither the companies nor the Treasury are to be bound. The matter would then be governed by the provisions of paragraph (4) on the third page.

(c) With regard to paragraph (3) on the second page, it must be remembered that the companies are public companies and that it would be legally necessary for counsel acting for them to obtain confirmation of their actions by means of specific approvals required by the company laws in force in Canada. In view of the facts, it is hoped that there will be no objection to including a qualification "unless disapproved by the principals within one week after the conclusion of the conference".

(d) With regard to provisions of the paragraph (1) of the second page, it is assumed that the stipulation that the Treasury Department and the Department of Justice will not be required either to disclose the particulars of the claim or to discuss the facts or laws supporting it, will not preclude the furnishing of sufficient information to enable the making of an effort to arrive at a satisfactory settlement. The force of the position of the Treasury and Justice Departments is fully realized, but it will also be apparent that a company sincerely convinced that no ground exists for a claim against it would not be warranted in proposing settlement unless some indication of ground is given. It is believed, however, that

the Departments appreciate the situation and that the difficulty will be solved in actual conference.

With regard to paragraph (4) on the third page of the Memorandum, it is understood that the acceptance of the proposals of the Government of the United States for discussion in accordance with the provisions of the Memorandum is not in any way to be construed as an acquiescence by the Government of Canada in the principles involved in the proposed legislation or as debarring the Government of Canada from renewing their representations against the legislation in the event that the discussions with the companies, or with any of them, should prove fruitless. The present course of action is regarded as a sincere effort on the part of all concerned, whether Governments or private interests, to reach an agreed position which will ensure substantial justice both to the Governments and to the private interests concerned.

April 15th, 1936.

April 15th

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H.M.Jr. called Mr. Hull and told him about the Mexican Ambassador's visit yesterday in connection with our buying their surplus silver. He informed Mr. Hull that he was getting more details and before we did anything definite he would call Mr. Hull again.

Mr. Morgenthau told Mr. Hull that as we approach the possibilities that we may have to let England talk to us on the question of stabilization if France goes off gold, he would like to have what happened at the London Economic Conference as it affected stabilization. He said all he has had up to now is rumors and he would like to have a full report. He is interested to know just what George Harrison did and what Warburg did and what we are trying to accomplish on stabilization - in other words he really just wants the stabilization end of the London Economic Conference. He said that after the memorandum is ready he would like to come over and have Mr. Hull go over it with him.

H.M.Jr. told the 9:30 group about the Mexican Ambassador's visit. Also in connection with China that we have now gotten down to making a study of balance of payments.

H.M.Jr. reported that he got some excellent unemployment figures; that they were so startling that he turned them over to the Central Statistical Board to be checked. He said that the figures he received showed that we are taking care of 5 million people - 2 million on direct relief and 3 million on work relief; that the cost per family of direct relief is constantly increasing.

Bell said that some time ago he had a discussion with Mr. Morgenthau on the matter of investing government trust funds in Federal Land Bank bonds. He asked whether Mr. Morgenthau wanted to continue that policy. H.M.Jr. inquired whether they were unguaranteed and, when Bell replied that they were, the Secretary definitely said, "no, I do not want to do it; that as Trustee of government funds I would rather receive a little less interest but have a safer investment".

Upham reported that Jesse Jones would be willing to clean his shelves before June 1 of any securities that he had taken over from Ickes - also that he would clean his shelves of other securities before the 1st of June as nearly as he can.

H.M.Jr. told the group that Jesse Jones telephoned yesterday and asked to have Taylor put on as a Director of the Board of Commodity Credit inasmuch as Agriculture and Farm Credit were represented on the CCC Board. H.M.Jr. turned him down.

April 18, 1938

HM, Jr. called the President this morning and told him he wants to sign an order imposing countervailing duties on German goods. Secretary Hull does not feel that such action should be taken. HM, Jr. said with the President's permission he was going to use a bit of strategy, that is, he will have a letter prepared and will bring it to Cabinet today. In this letter he will say that he wants to sign the order putting on countervailing duties and will attach to it a memorandum from Secretary Hull in which he objects, and he further told the President, "I want to bring this whole thing to your attention. Then the next move would be for you to say that inasmuch as the two Departments disagree you will refer the whole thing to the Attorney General for an opinion. I have talked this over with Oliphant and Taylor and they both agreed that this would be a good move." (Copies of letter to the President and from Secretary Hull are attached to countervailing duties file.)

He told the President that Bob was operated on for appendicitis last night; that it was a very necessary operation and that was the reason the dinner had to be called off for tomorrow night. Mrs. Morgenthau had spoken to Mrs. Roosevelt and explained it. (The President and Mrs. Roosevelt were to have been present for dinner at the Morgenthau home on Friday night to celebrate the twentieth wedding anniversary of the Secretary and Mrs. Morgenthau.)

The President said that the important thing for Bob is to be very quiet for the next three or four months and keep out of athletics. Mr. Morgenthau said he would tell Bob of the President's interest.

Yesterday Mr. Oliphant told HM, Jr. that Stanley Reed had called him and said that he would appreciate it if Mr. Morgenthau would call Charlie West, and say that it is his (HM, Jr.) understanding that the bill limiting lawyers' fees is not to be attached to the general tax measure, but can be tacked on the Miscellaneous Tax bill which will deal with administrative procedure. Having been unsuccessful all day in reaching Charlie West, HM, Jr. called the Attorney General and asked him to speak to Stanley Reed and have Stanley Reed handle the whole thing for him.

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There was no regular 9:30 meeting. Helvering, McReynolds, Gaston and Oliphant were called in to talk about the tax bill with the Secretary. HM, Jr. told Mr. Helvering that the purpose of having the "get-together" now (and that he wanted to have one every now and then) was so that all could be kept informed of what was happening on the tax bill, so that if the President telephoned and wanted anything, the Treasury people would all be posted and up-to-date.

HM, Jr. reported that not having been able to get hold of Charlie West and not having the time to keep after McIntyre, he decided to call the Attorney General and told him that he would appreciate it if Stanley Reed would handle the matter of seeing that the Frankfurter-Corcoran lawyers' fee bill was not attached to the general tax bill. While the group were present, HM, Jr. called the Attorney General again about what had happened in connection with the fee bill. He could not reach the Attorney General and spoke to Stanley Reed, who said that he has not yet been able to reach Charlie West. HM, Jr. asked Stanley Reed to have the Attorney General bring a memorandum on the matter to the Cabinet meeting and that he, HM, Jr., would also have a memorandum to be presented at Cabinet.

Oliphant asked the Secretary to also bring up at Cabinet the processing tax problem. He asked, "If we are not to have any, what will take its place?"

The Secretary told Mr. Helvering that if the Senate insisted that he, HM, Jr., come up to the Hill to testify on the tax bill, he would be very glad to go and that he had talked to the President who is anxious to have him go up on the Hill.

HM, Jr., told the same group to come in at 9:15 on Monday morning to have another talk on the tax bill.

The Secretary walked down with McReynolds this morning. During this walk he had discussed with McReynolds an idea he has had and which he wanted to present to the group for their reaction. It is his thought, he said, to have two or three national economists appointed as advisers to the Treasury. They will function in the same manner that the Advisory Committee on Architectural Design does with the Procurement Division. He would have the economists come to the Treasury twice a month and confer with them on various

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matters that come up in the Department, such as, what we will do in case France devalues; the Chinese situation; our charts on unemployment, on the deficit, on expenditures. He has in mind, he said, men like Wesley Mitchell and Dr. Viner. He feels that they would come in fresh from the outside and would be able to contribute a great deal.

Oliphant wanted to know if this advisory service would be confined solely to economists and HM, Jr. said, "No; I might want a political scientist, or have a fellow like Magill who has no private practice, or one who confines himself to teaching." Gaston thought there might be leaks, but HM, Jr. said he feels that the standards of men like Viner and Magill are so high that this would never happen and he has convinced himself of this since his dealings with the men from the various universities. He asked the men to think about the suggestion.

Yesterday Mr. Gaston told the Secretary that he had learned that D'Arcy, the advertising firm in St. Louis working on Baby Bonds, had been approached by a representative of the Democratic National Committee who had solicited from Mr. D'Arcy a page ad in the Democratic Hand Book. The representative told Mr. D'Arcy that Albert Frank-Guentner Law, the New York advertising agency employed by the Treasury for Baby Bonds, had agreed to take a page. HM, Jr. told Gaston he would talk to all these people himself.

Today, Howard Allen and Russell Clevenger, both Vice-presidents of Albert Frank-Guentner Law, and Gaston took them in to see the Secretary. HM, Jr. said, "I want you to know that you are doing this work for the Treasury on a strictly business basis. We selected you on your merit because we thought you could do the work. You do not have to give a nickel to anybody. Is that plain?" They both replied, "Yes." HM, Jr. continued, "There is no reason why you should have to take advertising anywhere or give commissions. If I find that you do, then I will have to reconsider our doing business with you."

Mr. Allen explained that he had been approached by the representative of the Democratic National Committee and had not sought the work. HM, Jr. said to him, "I don't run the Treasury that way. I don't care what they do in any other Department, but that does not exist in the Treasury. I want

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you to cancel that advertising and if they want to know why, tell them I told you to do so; that you get your orders from the Secretary of the Treasury."

Miss O'Reilly came in to talk to the Secretary about Louie Howe's request that the Treasury renew the practice of issuing proof coins. H.H., Jr. wanted to do this for Louie if it is possible. Miss O'Reilly explained that the coins are sold at face value plus a small charge for special preparation of the dies and blanks to produce the highly polished surface. She said there was no reason why the practice could not be revived; it had only been discontinued because of pressure of work in the Mints. He told Miss O'Reilly he would like to have the Treasury again issue proof coins and Miss O'Reilly said the Superintendent of the Mint at Philadelphia will be instructed to start the work. Copy of her letter to the Superintendent is attached.

April 16, 1936.

My dear Mr. President:

I have before me for signature a Treasury Decision giving notice of the imposition of countervailing duties on certain imports from Germany under Section 303 of the Tariff Act of 1930. This Treasury Decision has been approved by the General Counsel for the Treasury Department and is accompanied by his opinion that, under the facts, the Secretary of the Treasury is under statutory duty to sign and issue this Treasury Decision. I am attaching hereto a copy and a summary of the opinion of the General Counsel for the Treasury Department.

I am satisfied that, under the circumstances, I have no choice but to sign and issue this Treasury Decision. However, before taking this action, I feel it is my duty to bring to your attention a letter from Secretary Hull dated April 2, 1936, copy of which is attached, in which he questions some of the legal conclusions in the opinion before me. On account of Secretary Hull having raised these questions, it seems only proper that I should lay this matter before you for your advice and guidance.

Faithfully,

Secretary

The President

The White House

April 16, 1936.

Superintendent,  
United States Mint,  
Philadelphia, Pennsylvania.

Dear Sir:

The Secretary of the Treasury has authorized the Mint to renew the practice of issuing proof coins and this letter will be authority for you to proceed with the preparation of sets of silver and minor coins in proof condition, to be sold to the public either singly or in sets.

The charges for these proof coins, in addition to the face value and postage of 8¢, will be as follows:

Fifty-cent piece.....	25¢
Twenty-five cent piece...	25¢
Ten-cent piece.....	10¢
Five-cent piece.....	15¢
One-cent piece.....	15¢

It is, of course, understood by you that no proofs of silver dollars will be made unless a substantial coinage is authorized during the current calendar year.

The charges collected for the proofing of coins will, as you are aware, be turned in to the Treasury as a miscellaneous receipt.

Very truly yours,

Acting Director of the Mint.

Approved:

Secretary of the Treasury.

"McR"

April 16, 1936.

Superintendent,  
United States Mint,  
Philadelphia, Pennsylvania.

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TREASURY DEPARTMENT

WASHINGTON

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Faithfully,

Secretary,

The President

The White House

Atty. Gen. for report & recommendations  
F.H.

COPY  
April 15, 1936

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Secretary Morgenthau  
Herman Oliphant

Countervailing Duties on German Goods

After a careful review of the memoranda addressed to you by Assistant Secretary Taylor and Mr. Viner, and upon reconsideration of the entire matter, I find nothing to warrant altering my opinion that the law requires the application of countervailing duties under Section 303 of the Tariff Act of 1930 upon certain German goods, as contemplated by the draft of a Treasury Decision recently approved by me, and that it is the mandatory duty of the Secretary of the Treasury to direct that such bounties be imposed.

The facts are not in dispute and the statute is admittedly mandatory on the Secretary of the Treasury. Once its applicability to the facts in the case before him is determined, he has no discretion. The only question open for discussion is the usual legal one of statutory construction, that is, the facts being admitted, what is the law as filed by the statute?

German exports to the United States of particular commodities dutiable under the Tariff Act of 1930 are being aided by numerous devices which fall into the following classes:

- (1) Payment of direct cash bounties by German industrial associations.
- (2) Scrip and bond procedures.
- (3) Currency manipulations.

It is my opinion that the statute requiring the imposition of countervailing duties applies to all three of the foregoing classes.

Those in the State Department considering the matter and your advisers in the Treasury Department are agreed that payments of the first class would require the imposition of countervailing duties. The State Department has transmitted to us the formal denial of the German Government that such cash bounties are being paid from a specified fund but the Treasury has evidence that such bounties are being paid in connection with some commodities from that or other funds.

Mr. Viner construes the law to apply to the second class mentioned above. On this, Mr. Taylor's memorandum expresses no opinion.

Mr. Viner and Mr. Taylor agree that the statute should be so construed as not to apply the third class mentioned above.

Apart from minor changes in the rates set out in it, the Treasury decision which I have initialed for issuance could, as a matter of law, rest entirely upon bounty payments and the scrip and bond procedures without reference to currency manipulations, but I hold also that the law applicable to the currency manipulations requires the issuance of this Treasury decision and make this holding for the future guidance of the Bureau of Customs in recommending assessment of countervailing duties under this Treasury decision.

The reasons for the decision that the statute in question applies to the currency manipulations can be stated briefly, but are stated without any purpose of construing the statute beyond the point

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necessary for the future guidance of the Bureau in dealing with these manipulations. Other practices may develop, and, as they do, the law applicable to them will have to be examined on the basis of the facts which they present.

In the first place, the statute in question is itself as clear as any legislation of similar scope could be. In fact, its language discloses that it was framed with great care, having passed through a process of perfection of language and enlargement of scope in the series of tariff legislation.

In the second place, the controlling decisions of the Supreme Court construing this statute leave no doubt that the statute means what it says. That this is true appears from the following quotations from one of the leading cases on the subject:

The statute was addressed to a condition and its words must be considered as intended to define it, and all of them -- "grant" as well as "bounty" -- must be given effect. If the word "bounty" has a limited sense the word "grant" has not. A word of broader significance than "grant" could not have been used. Like its synonyms "give" and "bestow", it expressed a concession, the conferring of something by one person upon another. And if the "something" be conferred by a country upon the exportation of any article of merchandise" a countervailing duty is required by Paragraph E.

We have the fact of spirits (the commodity upon which countervailing duties had been imposed) able to be sold cheaper in the United States than in the place of their production, and this the result of an act of government because of the destination of the spirits being a foreign market. For that situation Paragraph E was intended to provide. (Nicholas v. United States, 249 U.S. 34.)

(Underlinings and parenthetical phrase added).

The standards for construing the statute set out in the above quotations dispose of the argument that the law governing the discriminatory currency manipulations here under consideration is to be determined by what law might govern cases arising under uniform depreciation of a country's currency. The factual differences between the two situations are substantial.

The action of the German Government in blocking funds held in Germany for foreign account and restricting the disposition and use of such funds by their foreign owners has brought about reduced market values for marks held in such accounts. The marks are purchased at these reduced values by American importers of German goods. The German Government then, as a grant of privilege or concession to a favored German exporter, permits him to receive a specified amount of the controlled marks in full or part payment for certain kinds of privileged goods exported to the United States. In the more usual case, when only part payment in controlled marks is permitted, the balance of the price must be paid in "free" marks costing the American importer a price measured by the value of the gold mark. When the controlled marks are released to the German exporter, their value is restored — and by act of the German Government restored — to the value of marks in free circulation in Germany. This latter value can be measured for our purposes only by the price of "free" marks in United States currency. That price is the value of the gold mark, the value that is regularly paid by American importers who require substantial quantities of "free" marks to finance their purchases of German goods.

The German exporter who is paid in controlled marks for exports from Germany to the United States receives, therefore, a benefit measured by the difference between the prices paid by American importers for the particular type of controlled marks involved and the "free" mark. The cost of this difference does not fall upon the American importer. The value of the difference is granted to the German exporter by acts of the German Government on, or by virtue of, the exportation of the goods. Thus, in terms of the Court's language already quoted, the exporter is thereby enabled to sell his goods more cheaply in the United States in competition with our domestic goods.

That there may also result a benefit (bounty or grant) to the American importer is beside the point. No bounty or grant can achieve its purpose without some benefit in the form of lower prices to purchasers of the subsidized goods; and a direct money payment by a foreign Government to an American importer could be such an indirect bounty on the exportation of goods from the foreign country as to fall within the statute.

(Signed) Herman Oliphant.

(Preliminary Draft)

Secretary Morgenthau

Mr. White

Subject: China - Her exchange situation.

SUMMARY

I. Will our purchases of 40 million ounces of China's silver during 1936 strengthen the yuan?

The effect will be chiefly psychological. It would tend to strengthen the expectation of speculators and silver holders that the present yuan rate will be maintained.

The effective increase such sales would have in the strength of China's reserves is negligible. It is negligible because the added exchange would not represent an increase that can be utilized to protect the present 30-cent yuan rate. China's silver reserves are at present only 46 per cent of her note issue. Should pressure on the yuan develop, China would be forced to lower her pegged rate long before that point would be reached.

Even if China was able to convert 100 million yuan of silver into gold, she would still be forced to protect sharply dwindling reserves by drastic measures involving either further depreciation, or embargoes on imports, etc. A drop of from 66 per cent to 46 per cent would only accentuate the flight from the yuan.

Additional sales of silver to the United States offer, therefore, only psychological support to the present yuan position of 30 cents.

The situation would not be significantly altered if the present rate of silver acquisitions by the Government banks -- reported to be 6 million ounces a week -- continues. Were no additional notes issued, except such as are necessary to pay for the silver turned in to the banks, the silver reserves of the Government banks would be in the neighborhood of 50 per cent of the outstanding notes.

Purchases of silver by the United States must, therefore, be evaluated solely for their psychological effect on the exchange market and on holders of silver in China.

II. Has China enough "free" gold and foreign exchange to settle her balance of payments?

Almost everything depends upon capital movements. Exclusive of these movements, China will have an adverse balance of payments of

Secretary Morgenthau - 2 -

from 100 to 500 million yuans. She has now less than 50 million yuans in excess of 60 per cent reserve and she may have, before the end of the year is over, another 100 million.

The 60 per cent requirement is imposed by an earlier decree and could, of course, be changed by another decree. But, if the change is made while the yuan is under pressure, the effect may well be to increase that pressure rather than to strengthen the yuan position. Confidence in the future of the yuan is crucial. It will determine whether some of the capital which has left China will return, and whether more silver will be exchanged for notes, thereby strengthening the yuan's position, or whether a further flight from the yuan will take place, which would make it extremely difficult - if not impossible - for China to maintain the 30 cent rate. Therefore, anything the United States does for China must be evaluated in terms of the increase in confidence in the future position of the yuan that it will furnish.

### III. Is China's budget situation a critical factor in her ability to maintain the 30 cent rate?

The deficit for the first half of the current fiscal year is greater than had been expected. If the second half year is as bad, the fiscal year may end with a deficit of about 300 million yuans, a sum greater than has occurred for many years.

There appear to be reasonable grounds for expecting the deficit to be closer to 200 million than 300 million yuan. Only if the deficit should greatly exceed 300 million yuans will the psychological effect of the large deficit (plus the reduction in reserves consequent upon such increased note issue as would result from increased Government borrowing from the Government banks) be important enough to initiate fear for the yuan.

So large a deficit seems, at the moment, to be unlikely. Nevertheless, the budgetary situation is delicate enough to warrant the conclusion that the payment or postponement of sums due the Export-Import bank -- amounting to over 20 million yuans for the remainder of the current year -- would make a substantial difference in the appearance of the budget and would help a little in maintaining confidence in the yuan.

### IV. Is it feasible for China to use new silver coins?

Definitely, yes. Both Mr. Chen and Mr. Koo expressed the belief that new 50-cent coins containing 500 to 600 fine would be quite popular in China, and ventured the opinion that the community could absorb 200 to 300 million such <sup>coins</sup> during the course of the next year.

Secretary Morgenthau - 3 -

They also felt that the Chinese Government would prefer to issue such silver coins rather than notes because of their saving in silver reserves and increase in seigniorage profit. They assumed that reasonable restrictions would be devised to prevent over-issue.

China would not be able to mint nearly that many coins, but Mr. Chen and Mr. Koo stated they believed China would not be at all averse to having the coins minted abroad.

V. Measures suggested for consideration.

(a) Increasing the size of the purchases tentatively suggested by the Secretary, and shortening the period over which the purchases are to be consummated.

The purchase of possibly 10 million ounces of silver per month for the next three months (under conditions suggested by the Secretary) without any statement as to subsequent purchases, but with the understanding that the situation will be re-examined at the end of that period. The advantage of shortening the time during which the purchases are promised and increasing the monthly sum is to enhance the psychological effect of those purchases during those months when it is most necessary. The next few months should give definite evidence of China's ability to maintain her currency position, and the next few months, furthermore, are likely to be the critical ones for her exchange position.

If China is able to maintain her currency position until the fall, there are good grounds for expecting her to continue, at least until the following spring. There will then be no need to make further purchases.

If, on the other hand, her position shows no improvement after we have purchased 30 million ounces of silver and after we have assisted her in other ways to be enumerated below, the wisdom of continued purchases is open to question.

(b) Postpone payments on notes due Export-Import Bank during the current year.

There appears to be no reasonable ground for demanding a longer postponement than one year. China at present is not a good long term credit risk and postponement of the monthly installments is warranted only because the improvement such postponement would have on China's budget for this year may help China to maintain the present

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yuan rate. In other words, it is not China's financial circumstance, but her precarious exchange position, that provides the possible justification for a postponement of payments. Since the objective is the hope of favorable repercussions on confidence in the yuan, there appears no reason why payments should not be arranged for after the critical period for her yuan is passed.

(c) Grant China the privilege of borrowing up to possibly 50 million U. S. dollars on the condition that:

- (1) Collateral in the form of silver be deposited with the U. S. Treasury.
- (2) The amount loaned should not exceed 25 cents an ounce for the silver.
- (3) The loan be made only for the purpose of supporting the yuan. An interest charge of possibly 3 per cent could be made (plus the transportation and carrying charges).

The effect of such a loan would be twofold:

- (1) It would provide an addition 50 million dollars of exchange in case of pressure against the yuan and alteration in 60 per cent reserve requirement, without exposing ourselves either to a risk of loss or to purchases of silver. It is hardly likely that the price of silver would reach 25 cents an ounce in the next few years and therefore it is not likely that China would forfeit the collateral.
- (2) The knowledge that China has arranged for a 50 million U. S. dollar loan would be a powerful factor in strengthening confidence in the yuan.

Admittedly, neither the loan nor the silver purchases would be sufficient to prevent the yuan from depreciating if the political situation in China becomes more acute, or if China's finances are not well handled, or if her balance of payments grows sharply against her. But in the absence of these special adverse circumstances, the purchase of silver, plus the loan, should go a long way towards increasing confidence in the present yuan position, and it is quite possible that the loan may not need to be used.

The Chinese Government would be restrained from making the loan unless necessary because: (a) She would not be expected to resort to

Secretary Morgenthau - 8 -

the loan unless her foreign exchange holdings decreased, and (b) resort to the loan would be regarded as a sign of exchange weakness.

(d) It would be the hope of the United States Government that China would issue such amounts of 50-cent coins containing silver as she would feel could be assimilated by her people without in any way interfering with the efficacy of her monetary system, or reducing the confidence the Chinese have in the circulating media. It would further be the hope of the United States Government that such coins as could not be minted by the mints of China would be ordered in the United States so that the placing of silver coins into circulation would not be delayed by lack of minting capacity.

HUN:ls  
4/17/56

## SILVER COINS

Coin Denominations	Gross weight	Fineness	Composition		Coining value of 1 ounce silver
			Silver	Alloy <sup>1/</sup>	
	Grains	Thousandths	Grains	Grains	
<u>United States</u>					
Dollar - - - - -	412.5	.900	371.25	41.25	\$1.2929+
Half dollar - - - - -	192.9045	"	173.614	19.29	
Quarter dollar - - - - -	96.4522	"	86.807	9.64	
Dime - - - - -	38.5809	"	34.723	3.86	
<u>Canada</u>					
Dollar - - - - -	360.	.800	298.	72.	\$1.6666+
Half dollar - - - - -	180.	"	144.	36.	
Quarter dollar - - - - -	90.	"	72.	18.	
Dime - - - - -	36.	"	28.8	7.2	
Half dime - - - - -	18.	"	14.4	3.6	
<u>Mexico</u>					
50 Centavo - - - - -	123.042	.420	51.6791	71.3629	Pesos 4.644 \$1.28 about
<u>Great Britain</u>					
Crown - 1/4 £ - - - - -	436.3636	.500	218.1818	218.1818	\$0.38 \$1.10 \$2.67 about
Half crown - - - - -	218.1818	"	109.0909	109.0909	
Florin - - - - -	174.5455	"	87.2727	87.2727	
Shilling - - - - -	87.2727	"	43.6364	43.6364	
Sixpence - - - - -	43.6364	"	21.8182	21.8182	
Fourpence - - - - -	29.0909	"	14.5455	14.5455	
Threepence - - - - -	21.8182	"	10.9091	10.9091	
Twopence - - - - -	14.5455	"	7.2727	7.2727	
Penny - - - - -	7.2727	"	3.6364	3.6364	

<sup>1/</sup> The alloy of United States silver coins consists of copper; this is true of foreign silver coins also, so far as known.

Friday  
April 17, 1936

Archie  
Lochhead: Hello -

HMjr: How are things going, Archie?

L: The - there is nothing much - the Stock Market is about stationary. The bonds are off about one or two thirty-seconds and the Exchanges are not doing anything.

HMjr: I see.

L: And everything is quiet.

HMjr: I see.

L: Mr. Taylor is here now if you wish to speak to him.

HMjr:

L: Shall I put him on the phone?

HMjr: Is Mrs. Klotz

L: Mrs. Klotz is listening, yes.

HMjr: All right.

L: O. K.

HMjr: Now, is Taylor there?

L: Yes

HMjr: I'd like to speak to him.

Wayne  
Taylor:

Good morning -

HMjr: Hello, Wayne, - I've got a suggestion which is very confidential and keep it to the three of you. You know silver is - I think it's forty-six cents in London?

T: Yes - a little louder, can you?

HMjr: Hello -

T: Yes, fine

HMjr: You get it now?

T: Yes

HMjr: Now, the suggestion that I'd like to have you make, if you and Lochhead think well of it, a kind of a dangerous suggestion, is send for Chen and ask him to sound out his government what they would think of selling a million ounces in Bombay.

T: Yes

HMjr: Now, I'd like to - the reason that I want to do it is two-fold. One, I'd like to stabilize the market; and two, depending upon what they say I'd like to find out whether they're interested in trying to push the price of silver up a notch, see?

T: Yes

HMjr: Get me?

T: Yes

HMjr: See? And the other thing is three, - they may be pushing it up in order to get a better price from us.

T: Archie says that Chen has just left.

HMjr: Yes - well, they can send for him. - Hello?

T: Yes

HMjr: Do you get the idea?

T: Yes, I get the idea.

HMjr: And - I'd just like to tell him that I'll be back Sunday and we'd like to hear from him Sunday - what answer he gets, as to the - what their reaction is. - Hello?

T: Wait just a minute. Archie's got something he wants to tell you about that.

HMjr: All right.

Lochhead: Chen dropped by the office this morning after he saw White -

HMjr: Yes

L: And I told him what the price was in London -

HMjr: Yes

L: And said it looked rather interesting.

HMjr: Yes

L: And he said, 'Well, - ' he said, 'In the first place I don't think that my government at the present time would think it right to sell any silver...'. But he said, 'The main point is I doubt very much whether there is a real market there'. He said, 'I think if China was going to try to sell any silver in London the news would immediately come around and the price would disappear before we could sell anything'. Now that's -

HMjr: I've given you three pretty good reasons. I'd like to have them tested out.

L: Yes, well, now, there's another thing. You wanted them to try in Bombay, too?

HMjr: Yes

L: Yes - so as I say, there are two things - you wanted to find out whether they'd be interested and whether they'd want to try out in Bombay?

HMjr: And - or London

L: Or in London - either one of the three markets and get their official reaction on it?

HMjr: Yes

L: Right - Well, I just wanted to mention that I had already mentioned it to Chen but I mean just in an off-hand way.

HMjr: Yes, but I don't want anything in writing for months.

L: Oh, no, not at all.

HMjr: You see?

L: Yes

HMjr: But I wouldn't put it beyond those fellows to shove the market up -

L: Yes

HMjr: - in order to get a little bit better price out of us.

L: I see. Well, there is no reason why we shouldn't give them the - the chance to say whether they want to sell it or not over there.

HMjr: I - I'm very much - Do you or Taylor see any reason why we shouldn't do that?

L: No, I don't see any reason why we shouldn't - I wouldn't like to see the market go up much further than this because it starts in making these speculators active again.

HMjr: Right - I think there is <sup>every</sup> reason why we should sound them out.

L: Right - all right, then, well, we'll get in touch with Chen and put that suggestion to him immediately.

HMjr: All right.

L: O. K., sir

HMjr: Is Mrs. Klotz there?

L: Yes

HMjr:  
H. S.  
Klotz: Lochhead wants to know whether you want anything mailed up him - to you tonight.

HMjr:

K: What?

HMjr: Better leave it at the house.

K: Leave it at the house? - All right.

HMjr: I'll call up after lunch again.

K: All right, fine.

HMjr: Anything come in?

K: No - nothing -

HMjr: All right.

K: I mean nothing that can't wait.

HMjr: Thank you very much.

K: All right - goodbye.

HMjr: Goodbye.

SEW:eb

April 18, 1936

The purpose of this meeting, <sup>Apr 20.</sup> as we conceive it, is to state the basis upon which negotiations between us are to proceed.

But before stating our position on that I should like to explain the reason for our reluctance heretofore to discuss these cases with you. That reason simply is that both the Treasury Department and the Department of Justice have all along entertained grave doubts as to whether or not this Government's claim against you was of a nature which permitted us to consider a compromise of it. However, your Government has made earnest representations to our Government that we meet you and see if it is possible to come to an adjustment of our claim without litigation. Our invitation to you to come to Washington today has been issued in deference to these representations and to those of our own State Department.

After the break down of the former conferences with you held by the Treasury Department on March 30 and 31, your Government requested a further conference and in doing so made this proposal:

1. The Treasury Department will agree to drop the legislation for "a month or six weeks, at least", with the understanding that if, after full and frank negotiations, it cannot obtain satisfactory settle-

ments or commitments from the Canadian companies, the legislation will then be enacted.

2. The Canadian companies will agree not to increase their exports of whiskey to the United States over the present volume, with some allowance for normal increases in business.

3. The Canadian companies will agree not to dispose of their stocks of American type whiskey elsewhere.

4. The Canadian companies will agree to "sit down with Treasury officials and discuss the nature and quantum of the claims alleged to exist, with a view to reaching some solution".

5. This was understood to mean (a) reaching an amicable settlement out of court, or, failing this (b) discussing terms, conditions, and practical measures in respect of their submitting to the jurisdiction of American courts and protecting the United States against losses on any judgments which might be obtained.

Upon receipt of this request, a conference was held between representatives of the State Department, Treasury Department, and Department of Justice, with the result that this Government agreed to a further conference with you upon the following basis, to wit:

1. Subject to the conditions transmitted by Secretary

Hull, the Treasury Department and the Department of Justice will agree to a delay not exceeding one month from April 13 in the pending legislation, during which the following steps will be taken with a view to obviating the necessity for the legislation, if possible.

2. The Treasury Department and the Department of Justice, acting jointly, will receive representatives of the Canadian companies individually and undertake to arrive at a satisfactory settlement of the Government's claims against them, subject to the condition that the two Departments will state the amount, as at present calculated, of the Government's claim against each company but will not be required either to disclose particulars of the claim or to discuss the facts or law supporting it.

3. In the event of the failure of the parties to agree on a settlement, they will undertake to make an arrangement which will bind the companies to submit to the jurisdiction of the United States courts so that the claims may be litigated on their merits, and to provide satisfactory security for the payment of any judgments which may be rendered in favor of the Government.

4. The Canadian companies are to be informed that any persons designated to represent them in conference with the two Departments must be fully empowered there and then to bind their principals with respect to the point covered above.

5. If negotiations with the companies carried on in accordance with the foregoing should be fruitless as to any one of the following companies, namely: Distillers Corporation-Seagrams, Hiram Walker-Gooderham and Worts, Consolidated Distillers, and United Distillers, the Treasury Department and the Department of Justice will be free to proceed with the legislation.

In pursuance thereof, the State Department notified the Canadian Charge d'Affairs of our willingness to again meet with you, on the terms and conditions set out above.

On April 15, the Canadian Charge d'Affairs responded in a written memorandum, which reads as follows:

(Here read the memorandum.)

With respect to paragraph (a) of the Canadian memorandum, we understand, of course, that the companies do not admit any liability on the merits.

We agree to the interpretation of the Canadian Government of the memorandum of the United States as set out in paragraph (b) of the Canadian memorandum.

We likewise agree to the amendment suggested in paragraph (c) of the Canadian memorandum, but with the understanding that the action of your representatives at our conferences must be finally acted upon by your companies within the thirty day period from April 13; otherwise the provisions of paragraph 4 of the memorandum of the United States will apply.

With respect to paragraph (d) of the Canadian memorandum, we must insist upon the terms of the memorandum of the United States, as set forth in paragraph 1 thereof, to wit, that we "will state the amount, as at present calculated, of the Government's claim against each company but will not be required either to disclose the particulars of the claim or to discuss the facts or law supporting it." We cannot agree to state the ground upon which we assert these claims, other than to say that they arise out of the bringing in of the liquors of your companies into the United States during Prohibition days, either by you directly or with your aid and assistance or connivance and the consequent liability therefor arising under our customs, excise, and income tax laws. We are frank to confess that we expect that it will be quite difficult for us to reach an agreement in this matter, and we therefore recognize the fact that litigation may eventually ensue. For this reason and others, we must respectfully decline to go any further in the statement of the ground upon which our claim rests than the statement I have just made, which is, to repeat, that our claim arises out of the bringing in of your liquors into this country during Prohibition days, either by you directly or with your aid and assistance or connivance, and the consequent liability therefor arising under our customs, excise, and income tax laws.

The chief purpose of this conference today, as we conceive it, is to ascertain if you desire to proceed with

these negotiations with this understanding. If you do, we are prepared to proceed with them at the proper time. Before doing so, however, we desire to receive representatives of the other companies and ascertain whether or not they desire to proceed with the negotiations on this basis. If all are willing to do so, we will later call you into conference, one after another.

Before concluding, we understand that the acceptance of the Canadian Government of the proposals of the United States is not to be construed as an acquiescence in the principles involved in the proposed legislation. We also note that the Canadian Government does not regard itself as debarred from renewing their representations against the proposed legislation in the event that the discussion with the companies or with any of them should prove fruitless.

We should now like to hear from you as to whether or not you desire to proceed with the negotiations at the proper time on the basis which we have set out above as frankly and definitely as we could.

\*\*\*\*\*

If this basis, after discussion, is finally accepted, it should then be stated that we will call the other parties into conference and ascertain from them whether or not the basis is satisfactory, and, if so, you will be notified later of a time when we should like to enter into discussion with you, first, of a possible settlement of our claims against you,

and, second, failing in this, of arrangements which might be made to insure your submission to the jurisdiction of our courts and to insure against losses on any judgment that we might be able to obtain against you.

We shall expedite our conferences with you as much as possible, since, to be perfectly frank, we intend to proceed immediately after the expiration of the thirty day period, to wit, on May 13, to secure passage of the proposed legislation if, in the meantime, we have not come to a satisfactory agreement.

C O P Y

April 18, 1936.

From: Spagent, Shanghai, China.

To: The Secretary of the Treasury.

Message from Professor Buck: Kung appreciates amount of time you are giving Chen and delegates and says anything you do now to help China is also a help to United States and the world. He also suggests you feel free to communicate with him on any problems arising from conversations with Chen. He states Japanese are urging Governor of Shantung and Mayor of Tsingtao to retain customs and other national revenues for local use. Also states that Chinese must take stiffer attitude. He asks you to let him know if any statement from him will help present administration in coming election.

April 19, 1936

3:15 p.m.

Dr. Edouardo Suarez, Minister of Finance of Mexico, came in to see the Secretary. Mr. Taylor was also present and Mr. Lochhead joined the meeting later. Following is a stenographic report.

HM, Jr.: I thought the Ambassador would come with you.

Dr. Suarez: The Ambassador had an appointment with the Secretary of State.

HM, Jr.: You are sure it isn't baseball?

Dr. Suarez: Do you like a baseball game, Mr. Secretary?

HM, Jr.: Very well.

Dr. Suarez: I was in New York at the game.

HM, Jr.: You are sure the Ambassador is not at the baseball game?

Dr. Suarez: Yes, I am.

HM, Jr.: All right. Things going along nicely in your country:

Dr. Suarez: Yes, Mr. Secretary, they are moving along fairly well. At present we have no particular problem; everything going regularly.

HM, Jr.: Fine!

Dr. Suarez: And our revenues are increasing. Our normal revenue has been 275,000,000. Last year we had revenue of 384,000,000. We thought for this year we would have over 400,000,000.

HM, Jr.: How much favorable balance of trade?

Dr. Suarez: We have been increasing. Our Bank of Mexico business is 45 times.

HM, Jr.: What do you do with all the money down there! You

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have gold, oil, silver.

Dr. Suarez: Mild amounts.

Mr. Taylor: They build bridges.

HM, Jr: You have a big balance of trade?

Dr. Suarez: Yes, I think so. I think we have improved. We have been purchasing -- the Government has been purchasing for the last two years. We have purchased in the United States, in machinery, nearly 400,000,000 pesos -- machinery for building dams, agricultural implements.

HM, Jr: Are your people continuing to buy the land? Do your farmers buy the land? Is that going on -- dividing up all the land?

Dr. Suarez: Yes; that's the policy.

HM, Jr: Do you lend them the money to buy that land or do you give it to them?

Dr. Suarez: We give them the land.

HM, Jr: As far as the United States Treasury is concerned and your Treasury, we have nothing, unless you have something.

Dr. Suarez: No, Mr. Secretary.

HM, Jr: We are perfectly satisfied. You did what you said you would.

Dr. Suarez: I don't think there is any problem.

HM, Jr: You borrowed, as you remember, some money for a short time against that silver. You paid it off.

Dr. Suarez: At the time I spoke to you, last year, we were in rather deep waters, but things now are bright. We paid the Treasury and we hope to use that facility if an emergency comes, if that should come in the future.

HM, Jr: Have you kept that silver here?

Dr. Suarez: Yes.

HM, Jr: What is that, 5,000,000 ounces?

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Dr. Suarez: No, 11,000,000 ounces.

HM, Jr.: That's right. We loaned you \$5,000,000 against 11,000,000 ounces of silver. You still have that?

Dr. Suarez: Yes. For the time being we have no particular problem. We are a little worried about the future -- when the London Agreement comes to an end. That will be next year.

HM, Jr.: Who knows there is a London Agreement!

Dr. Suarez: Nobody. The United States have the policy.

HM, Jr.: (To Mr. Taylor: Did the State Department ever get a report from the various countries?

Mr. Taylor: It isn't complete yet.

HM, Jr.: I don't think legislation here -- after all, while one never knows -- it does not fall with the London Agreement as I understand it. It has no ending, unless silver reaches \$1.29 an ounce or 1/4 of our reserves is silver.

Dr. Suarez: Is silver, yes.

HM, Jr.: But I don't attach, personally, any importance to the London Agreement. At the time of the London Agreement I think it was important and subsequently this so-called Silver Act of ours was so much more important than that, that everything else was in the shadow.

Dr. Suarez: That is true.

HM, Jr.: After all, we are human and we all have the weaknesses of human beings, so we don't know how long this thing --- but I think it's desirable and I think everybody wants to continue to see the world price of silver stable. I think that that is very important and that has nothing to do with the domestic price of silver in the United States, but I think the world price of silver -- I think we have gone so far with both silver and gold that it has demonstrated the importance for your monetary system and our monetary system to be based on silver and gold to take those metals out of speculation.

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Dr. Suarez: Yes, sir.

HM, Jr: And certainly I don't want to have to go through another silver speculation. My heart could not stand it. Wheat goes from 50¢ up to \$1.00 -- it's too much.

Dr. Suarez: This situation could be kept -- we don't want a high price. We think it is better to have a stable medium price, not going up or down.

HM, Jr: I think we have all learned that and I think that some of our Senators now know that the low price of cotton is not due to the coolie labor of China. When cotton got to 5¢ or 6¢ they blamed the coolie labor of China because they said they had 28¢ or 24¢ silver. They realize now that that's silly and it has nothing to do with it. The surprising thing is the way they keep selling gold and buying silver.

Dr. Suarez: That is of much importance to silver.

HM, Jr: I think where your people have been particularly smart is that you have been mining the low grade silver and saving the better.

Dr. Suarez: That has been the policy of our Government.

HM, Jr: I think that is smart.

Dr. Suarez: And now, at the present price of silver, we are putting aside some reserves and I think if that policy could be continued the good of the country would be altogether happy.

HM, Jr: What do you think of some of the countries south of you? What are they going to do?

Dr. Suarez: It is difficult to foresee. Perhaps Brazil and Bolivia would have some interest in silver.

HM, Jr: How do you think Brazil is going to come out of this?

Dr. Suarez: Very good, but they don't have silver. They don't produce silver.

HM, Jr: But what are they going to use for money in Brazil?

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Dr. Suarez: Some gold and paper currency. They have to settle their balance of trade with merchandize -- coffee and cotton -- and I think that is their policy to draw as much cotton as they can to settle their balance of trade.

HM, Jr: The Cuban thing is not so good -- they keep taking silver and using the profit.

Dr. Suarez: I heard sometime ago, about six months, that there was a scheme -- some New York bank was interested to make some issue of money covered by silver.

HM, Jr: We hope that won't happen. It is more or less for speculative purposes.

Dr. Suarez: Perhaps it is.

HM, Jr: We don't think it will last and won't put Cuba on a sound financial basis. It's purely speculative.

Dr. Suarez: Purely.

Mr. Taylor: That has pretty well quieted down.

HM, Jr: That smart boy ever come back?

Mr. Taylor: No. Which probably means that it has quieted down.

HM, Jr: They had a Cuban whom we thought did not know finance with some New York banker to put the thing over, just to make a little profit on the side, but he never came back. Our Tripartite Agreement has worked beautifully and it's made all the difference in the world to the French particularly. It has enabled them to devalue their money and not have the rest of the world try to devalue under. You see?

Dr. Suarez: Yes.

HM, Jr: And, as you know, they were particularly fearful of Japan and Japan had her troubles in January. For a time, I don't know how your country was, but our people could not get any money out of Japan for about six weeks. But now they are sending gold to keep their yen on an even basis and I don't think they are going to change the value of the yen,

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but I think if it had not been for the Tripartite Agreement standing there as a warning, they might have and what we are hopeful of more here is gradually, in this very much upset world, to get one country after another to sort of even out its currency and then maybe after a while we will have stabilization all around the world and then business will follow. You take China. They are doing beautifully in China. They are getting along fine. You have quite a lot of business with China.

Dr. Suarez: Yes, we do.

HM, Jr.: And they are doing very well and not looking from week to week or month to month, but year to year, the picture looks much better.

Dr. Suarez: Looks much better; yes.

HM, Jr.: You remember when you came here, a little over a year ago, things were upset in this country and in your country and none of us knew from day to day where we were at and there is an entirely different feeling now.

Dr. Suarez: Yes, altogether.

HM, Jr.: You like the new silver content?

Dr. Suarez: Yes; that was a political success and we are sending the old coins in at .720.

HM, Jr.: How much hard money have you out?

Dr. Suarez: The silver? About 80,000,000 pesos.

HM, Jr.: Down to 80? When you were here it was 100,000,000.

Dr. Suarez: In circulation 80,000,000 is the present figure.

HM, Jr.: And contrary to what everybody said, your farmers took paper money.

Dr. Suarez: Yes, particularly in towns. In towns people accepted paper money, but the farmers have a dislike for paper money. It was a political success. Everybody was satisfied. It was successful.

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HM, Jr: They did the same thing in China.

Dr. Suarez: Yes.

HM, Jr: They said they never could get Chinamen to use paper money.

Dr. Suarez: So it happened with us. In big towns people knew what that paper money meant and they accepted it, but in the country they continued to use silver coins. It was, from political standpoint, it was a success. Of course we were very much pleased with the way the measure was taken by the people.

HM, Jr: How's our highway coming?

Dr. Suarez: Very good, Mr. Secretary. From Laredo to Mexico City it is very good.

HM, Jr: Is it all the way through?

Dr. Suarez: Yes, all the way. It is paved and with protection.

HM, Jr: I did not know you could go from Laredo to Mexico City.

Dr. Suarez: Yes. Magnificent, very fine scenery.

HM, Jr: Are there places you can stay along the way?

Dr. Suarez: There are some places. Monterrey is a large town with a fine hotel.

HM, Jr: I suppose as the tourists come they will build places.

Dr. Suarez: They are building hotels and tourist camps.

HM, Jr: Is the Government doing anything -- I mean as to the tourist places?

Dr. Suarez: Yes, the Government has been consulted and now perhaps we make a special bank to finance construction of the hotels.

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HM, Jr: How much capital will you give them?

Dr. Suarez: We think 10,000,000 pesos. In some places they have ruins and something to see and we will put that in good condition and the President would like to help people to see those things.

HM, Jr: How many miles is it from Laredo to Mexico City?

Dr. Suarez: About 800 miles.

HM, Jr: It must be a very beautiful drive.

Dr. Suarez: The mountains are marvelous and gorgeous. Everything is very nice. We have many tourists from your country by train but particularly by car.

HM, Jr: When they begin to come, are they going to be able to get through those swamps from Mexico City south to Panama?

Dr. Suarez: The President is very interested in the building of that road from Mexico City. We are now beginning. That might cost about \$20,000,000 to build that highway and we can finance those by issuing excellent bonds. It is a good investment in Mexico to build roads.

HM, Jr: You lease the gasoline along the highways?

Dr. Suarez: We put a tax on the gasoline and with increase in gasoline tax we will build a new road. Gives us about 18% on the investment we make on the highway.

HM, Jr: 18%? That's pretty high.

Dr. Suarez: Yes. The way we finance it, we put receipts of the gasoline tax in trust in the Bank to pay the interest and the amortization of the bonds and we issue bonds to build the new highways. By that way we build a highway from Mexico City to Le---- and I think will be finished by the end of the year and will be opened from Mexico City to Tehautepec (?) about 400 miles.

HM, Jr: These bonds -- how long are they?  
*or Guadalupe?*

Dr. Suarez: Short time. Four to five years.

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HM, Jr: How much interest?

Dr. Suarez: Six percent or five percent. We pay the contractors.

HM, Jr: Oh! You pay the contractors and they in turn sell them?

Dr. Suarez: Yes.

HM, Jr: Do they sell at par?

Dr. Suarez: 98 is easy to get in the open market.

HM, Jr: How many metres wide will this highway be?

Dr. Suarez: I think standard make for two cars.

HM, Jr: That's going very well with the gasoline tax?

Dr. Suarez: Yes.

HM, Jr: You make them pay the tax at the factory?

Dr. Suarez: Yes.

HM, Jr: And not at the pump?

Dr. Suarez: We receive the taxes from the oil companies.

HM, Jr: So you know it is paid.

Dr. Suarez: On the 5th of every month the Bank collects the money, pays the contractors and give the Treasury the balance.

HM, Jr: And you get it from the oil company?

Dr. Suarez: Very inexpensive tax.

HM, Jr: You have how many oil companies?

Dr. Suarez: There are at present five large companies.

HM, Jr: So it is very easy.

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Dr. Suarez: People do it with pleasure. Five cents goes to the Federal Government and three cents to the State and the State also has a tax to build local roads so we are improving our system of highways.

HM, Jr: Now I would like to ask you something -- has nothing to do with finance. You may not want to answer. How do you think this Spanish thing is going to come out?

Dr. Suarez: That is very difficult to answer.

HM, Jr: I just wondered how in Mexico they felt?

Dr. Suarez: We sympathize with the Government -- with the Administration. We think it is a democratic administration, was elected by the people and we are for the Government because rebellions of military movement go against the will of the majority of the people. So we have been in favor for the Government and sympathize sincerely. We have had in the past difficulties, the same thing, military men to get the army and overthrow legitimate Government by force. It is natural that the feeling of the people should be for the legitimate Government.

HM, Jr: I was just curious, because the Spanish Government recently seem to be getting along much better.

Dr. Suarez: It seems so and we are very, very happy.

HM, Jr:  
I can't understand what they have done with all their gold and silver. They had so much.

Dr. Suarez: I think they have used some of it, part of it, to buy munitions.

HM, Jr: They could not have used much.

Dr. Suarez: I don't think so. I think they have great majority of their gold in Barcelona and Madrid, hoping that the Government will be able to suppress the rebellion.

HM, Jr: This was just a side thing, just a personal question. It has nothing to do -- the reason I am interested is because it looks as though the Spanish question is going to be settled. The price of wheat dropped 5 cents on Friday on the announcement

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that the Russians and the Italians were going to sit down and talk it over. Friday our wheat dropped 5 cents, just on that news, so it affects our market. Cotton dropped several dollars a bale and as the news gets good or bad ...

Dr. Suarez: Prices go up, or down.

HM, Jr.: Oh, yes. It makes a tremendous difference here and it makes a tremendous difference in the flow of capital here. It is surprising how we are affected .....

Dr. Suarez: ... by impending war in Europe.

HM, Jr.: It is surprising. You would be surprised. The price of cotton and copper and all those things just go up and down. You can almost say when Franco has a victory -- the price of cotton goes up. When he loses, it goes down. It's really so. You take our chart and when it goes up, it's Franco and when it's down in the valleys, it's the Government. So I am interested for that reason.

Dr. Suarez: Perhaps if the European Powers would leave it alone, the Government would have a chance to succeed because she has the people. It would be quite different.

HM, Jr.: As far as I am concerned, talking just for the Treasury, there is nothing that I have.

Dr. Suarez: I think that is true.

HM, Jr.: Isn't that right, Wayne? We have nothing. Let me ask Mr. Lockheed to come in. I don't know of any Treasury worries. I know that your State Department and ours have their worries, but I don't like to mix the political and the money. They don't mix any better than oil and silver.

(Mr. Lockheed came in at this point.)

HM, Jr.: I was saying that as far as we are concerned, I think everything is going along beautifully, as far as money -- silver, gold. Have we any troubles?

Mr. Lockheed: Everything has been working out very well. Things have been coming up marked properly. Of course, there has not been so much coming up. You have been taking advantage of the London market and taking advantage of the London price.

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There has been no hitch at all as far as I have seen. They have been shipping to either New York or Denver and it has become almost automatic. There has been very little excitement. Of course, they must be shipping gold up a little. You shipped some to the Federal Reserve in New York. You have a fairly good stock of gold at present in New York. The situation must be fairly stable.

HM, Jr: You see, I lost most of my hair when silver went up.

Dr. Suarez: I think the same thing happened to me.

HM, Jr: There is really nothing.

Mr. Lockheed: You know, Mr. Secretary, I very rarely mention about Mexican silver because there is nothing.

HM, Jr: We hinted pretty broadly, why didn't they take advantage of the London market when the price there was better?, which they did. And outside of that, nothing; nothing.

Mr. Taylor: The 11,000,000 you have in New York, you plan to keep that as a secondary reserve?

Dr. Suarez: Yes, sir.

Mr. Lockheed: You are shipping silver to San Francisco?

Dr. Suarez: We have some silver and some gold in New York.

Mr. Lockheed: That was silver held by the Federal Reserve as backing of gold. That was held by the Federal Reserve, San Francisco, and you are shipping that to New York?

Dr. Suarez: Yes.

HM, Jr: If, while you are here, anything comes up, I wish you would let me know.

Dr. Suarez: I will, sir.

HM, Jr: I think I will have the pleasure to see you tomorrow night and Mrs. Suarez?

Dr. Suarez: Yes, sir. Are you planning to make some

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trips to our country for a rest? We will entertain you.

HM, Jr: We would like very much to go, but this summer we are thinking seriously of going to Hawaii, but Mrs. Morgenthau and I have often talked about Mexico. Is it nice in the winter time?

Dr. Suarez: Yes, very nice.

HM, Jr: Which is a good month?

Dr. Suarez: In summer, when here in the States it is too hot, in Mexico you have sometime heavy showers in the afternoon which make it a little bit more pleasant.

HM, Jr: What's it like in November or December?

Dr. Suarez: Beautiful. In June and July you see the beautiful flowers we have in Mexico.

HM, Jr: Is it very dry in November?

Dr. Suarez: Yes, very dry. We have some more rains in December. In June and July, sometimes August, we have showers. Only little ones. We will have ones that last only a few minutes.

HM, Jr: Do they make much of a celebration of Christmas?

Dr. Suarez: Yes, and the first of the year. We have eight days before Christmas, ending at Christmas, balls and local dances, but that's the week before Christmas.

HM, Jr: That must be very nice. We certainly want to come. You see, we have three children and we have to do the things which they also like to do and it's sort of hard to fit it in for everybody.

Dr. Suarez: Any time that you prefer to make a trip, we would be very happy to entertain you.

HM, Jr: I know Ambassador Daniels has asked us a number of times to come down.

Dr. Suarez: I think he is very happy in Mexico. We like him. He is a very nice, kind gentleman and has great popu-

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larity among every sort of people.

HM, Jr: He's so polite and kind. Any time, formally or informally, if there is something on your kind, just let me know or drop in. How long will you be here?

Dr. Suarez: I will stay until the end of the week.

HM, Jr: If there is something, you let me know.

Dr. Suarez: I will, Mr. Secretary.

oOo-oOo

C O P Y

April 20, 1936.

From: Spagent, Shanghai, China.

To: The Secretary of the Treasury.

Referring to your message of April 19, Kung says he has already cabled Chen informing you results London sales originally suggested by you. Two million five hundred thousand (2,500,000) ounces sold at 20 shillings and 58 by Chase National Bank without revealing identity original source silver.

## TREASURY DEPARTMENT

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## INTER OFFICE COMMUNICATION

DATE

Apr 20

TO

FROM

Subject: China - Monetary situation.

## SUMMARY

Whether or not China will be able to stabilize her exchange at the current level depends on:

- (1) The magnitude and make-up of her metallic (and foreign exchange) reserves.
- (2) The state of her budget.
- (3) The movement of her balance of payments.

All these three factors are closely interdependent and each of them is strongly affected by and in turn affects the political situation in China.

What is the condition now of China's currency reserves, of her budget, of her balance of payments?

What changes are likely to occur in them during the next eight months?

## I

## CHINA'S METALLIC RESERVES.

A. At present China's "free" reserves consist entirely of gold and foreign exchange.

The three Government banks had, on March 28th, 748 million yuans of notes outstanding, and a cash reserve of 492 millions in gold, foreign exchange and silver. The reserve requirement calls for only 60 per cent in cash. With a note issue of 748 millions, the minimum cash reserve permitted is 450 millions. That means that China has only 42 million yuans of excess reserves or "free" cash. Since her cash reserves already include 150 million yuans of gold and foreign exchange, a sale of her silver holdings (at current prices or less) will not strengthen her "free" reserves.

If China intends to keep her cash reserve ratio against notes above the 60 per cent requirement, she has no use now for more gold

in place of her silver. So long as the silver holdings of the Government banks remain less than 60 per cent of her note issue, China does not strengthen her reserves by selling her silver stock.

But:

How long will her silver holdings remain below 60 per cent of note issue?

Cannot the cash reserve requirement be permitted to drop below 60 per cent?

The Government's present cash reserve situation is as follows:

(All sums in yuans)

Note issues of the 3 Government banks.....	748 million
Gold, silver and foreign exchange reserves .....	492 "
Ratio of reserves to note issue .....	66 per cent
Silver in reserves .....	342 million
Ratio of silver to note issue .....	46 per cent
Ratio of silver to total reserves .....	70 per cent
Gold in reserves .....	38 million
Foreign exchange in reserves .....	112 "
Gold and foreign exchange .....	150 "
Ratio of gold and foreign exchange to notes	20 per cent
Ratio of gold and foreign exchange to total reserves	30 per cent

Outstanding note issues of banks other than three Government banks on February 29, 1936, were reported to be 161 million. Against this 161 million of notes, about 50 million yuans (31%) of silver are being held in trust by the Government banks pending settlement.

B. What could the Chinese Government do to increase her "free" cash?

1. She could obtain more silver.
2. She could reduce the amount of her notes outstanding.
3. She could lower the reserve ratio requirement below 60%.
4. She could modify her balance of payments.

(1) How could it obtain more silver?

- (a) From silver coins being turned in for notes and token coins.
- (b) From tax collections.
- (c) From the holdings of the Japanese banks.

There are still outstanding from 1 to 1½ billions of silver coins. But that sum includes hidden hoards, and silver coins circulating in North China, Kwantung, and other areas not effectively controlled by the Central Government. The silver from those areas will not be turned in for a long time to come - if ever. In the five months since the nationalization of silver was inaugurated, only about 150 million yuans of silver have been acquired, and of that amount 25 millions had been turned over by the foreign banks (other than the Japanese).

During the first two months, the high price of silver doubtless encouraged some silver holders to smuggle out their silver or hold it, but in the past few months a low price of silver has prevailed. The rate of inflow of silver is reported to be 5 to 6 million yuans a week.

The bulk of the National Government revenue is of the type that provides a steady flow of cash into the Government treasury. The fact that in five months less than 75 million silver yuans were deposited with the banks (about one-half of the 150 was exchanged for notes, and Government expenditures did not take the form of silver) shows how small was the portion of taxes paid in silver.

The Japanese banks are the only ones which have not yet turned over their silver to the Chinese Government. They hold about 10 million yuans and refuse to accept the terms already accepted by the other foreign banks. Whether China can count upon that silver to add to her reserves in case of need is not yet certain.

An increase in her silver holdings increases the excess reserves only if the note issue does not expand at the same time. For every hundred yuans of silver turned in to be exchanged for notes, the excess reserves are increased only by 40 yuan. If the Government is going to increase its borrowings to the full extent permitted by additional cash reserves, obviously no excess reserves will result.

(2) How could it reduce the note issue?

The issue of notes could be lowered by reducing loans to both Government and to business.

The possibility of reducing loans to the Government is very slim. It is more likely that the Government will increase rather than decrease her borrowings. Contraction of credit to business likewise is not likely to occur. It would be an unwise step to take right now. It would help

Secretary Morgenthau - 4 - (Summary)

people to lose confidence in the currency reform, and it would create more unemployment and poorer business.

The Farmers Bank has already been granted the right to issue 50 million more yuan of notes, and there is no evidence as yet that it doesn't intend to utilize the privilege.

There remain also about 161 million notes of other banks outstanding that have to be cared for. The reserve against these is 50 million yuans. Whether the final settlement will be such as to reduce or increase the excess reserves is not yet known.

(3) Can the cash reserve requirement be lowered?

The 80 per cent requirement was imposed by a decree and could, of course, be lowered by another decree. It is even possible that no public statement of the change need be made. However, so much uncertainty prevails as to the success of recent currency changes, and 80 per cent has been so long regarded as the safe minimum, that it is doubtful if a change could be introduced during a period in which the yuan is under pressure. Change of the cash reserve ratio at such a time may increase the pressure rather than relieve it.

It might be possible to lower the rate without decreasing confidence in the yuan when the position of the yuan is not threatened, but in time of emergency the lowering of the reserve ratio cannot be regarded as a safe means of increasing the excess reserves.

(4) Can the Government alter her balance of payments?

She can increase the credit (i.e., "favorable") side of the balance of payments by:

- (a) Postponing payments on some of her foreign obligations.
- (b) Placing further restrictions on imports of merchandise.
- (c) Increasing the confidence in the stability of the yuan and thereby stimulating an inward flow of capital.

China's foreign loan service for the whole of 1936 is in the neighborhood of 125 million yuans, not counting the loans that are in default. Of the 125 million, about 20 million yuans are due to the United States during the remainder of 1936 on the Farm Credit and Reconstruction Finance Corporation loans. If these are postponed, the demand for foreign exchange would be less by that amount. None of the remaining payments can be defaulted, as they are amply secured by specific Government revenues. Nor is it very likely that arrangements can be made to reduce any of them.

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The Government could impose further restrictions on imports. This would be difficult for four reasons:

- (1) Any increase in restrictions will increase the incentive for smuggling. Smuggling is already very high; for 1936 it is estimated to equal one-fourth of the total recorded imports.
- (2) Further restrictions on imports reduce the revenue from customs. Customs revenue constitutes half the total revenue and Government finances can hardly bear further reductions in revenue.
- (3) Imports have already been severely reduced, and further restrictions will not only interfere with her export market, but will tend to still further lower the standard of living.
- (4) Any drastic limitation of imports would be regarded as a sign of weakness and might easily defeat its purpose by stimulating flight from the yuan.

Whether confidence can be stimulated sufficiently to induce capital to flow back to China depends largely on the way the Government will handle its finances, on the trend in the balance of trade, on the price of silver, and on the foreign support the Government can obtain.

Considering all the ways open to the Chinese Government through which her excess reserves can be increased, one fact stands out -- namely, they almost all require time. Therefore, should pressure against the yuan occur soon, China will have between 50 to 100 million yuans (15 to 30 million U.S. dollars) to use in defence of the yuan. When that is gone she will have to choose between:

- (a) Lowering her cash reserve ratio and thereby releasing more gold and foreign exchange for defence of the yuan,

And

- (b) Permitting the yuan to depreciate.

C. But that is true of only her present reserve set-up. What will China's reserve set-up be during the remainder of the year?

That depends chiefly on the Government's budget and China's balance of payments. The smaller the budget deficit, the more favorable is the balance of payments likely to be. The more favorable the balance of payments, the more foreign exchange will China have, and the greater will be the excess reserves. The excess reserves will be greater for two reasons: more silver will be turned in for notes because of the greater confidence in the yuan; and more foreign exchange will be acquired with legal tender. Silver will increase until it constitutes by itself 60 per cent of the note issue, thereby releasing all the gold and foreign exchange for defence of the yuan.

## II THE BUDGET

The expenditures of the National Government last year were 918 million yuans, and the deficit 196 million. In November the Government announced its intention of balancing its budget in 18 months. But instead of growing less, the deficit grew larger, and by January 1st it was estimated to be 150 million.

In the last six months of 1935 (first half of current fiscal year), the revenue from import duties declined from 130 to 100 million yuans. In January the decrease showed an even larger rate of decline. The fiscal year will probably end with a deficit of 200-250 million because in January a saving of 85 million a year was introduced by scaling down the amounts necessary to pay on the principal of the domestic debt.

If payments due the United States are postponed, about 20 million yuans will be lopped off the 1936-37 deficit. But China is in default on foreign loans to the amount of almost 1 billion yuans. That sum includes from 35 to 40 million U. S. dollars in arrears to American banks and corporations. Should a settlement be made on any of these defaulted loans, the payments called for during the next year should, of course, be added to the deficit.

The revenue formerly obtained from the two Northern provinces now virtually under the control of the Japanese amounted to about 80 million yuans. Offsetting the revenue from that area, the Central Government, it is reported, used to spend in that area about 100 million yuans on troop maintenance, etc. The revenue from those two Northern provinces has ceased to be paid in to the Central Government, but it is claimed that the National Government expenditures in those provinces has declined even more. Whether that is true or not cannot be stated, but it is certain that many more Chinese troops have been sent to the North, and that the rate of military preparation has increased.

There can be no doubt that the Nanking Government is taking steps to be prepared for an outbreak of hostilities with Japan. The preparation is largely disguised as preparation against the Communists, but there is considerable pressure against the Central Government to be adequately prepared to defend herself against further Japanese incursions. That means that there is pressure to increase military expenditures. Military expenditures have been greater each year, and it would be surprising if the preliminary budget estimates for 1935-36, which call for a 12 million yuan decrease, are not found to be an underestimate.

Altogether, China's budgetary situation would have been very bad had the Government not drastically reduced the Government loan service by cutting down the annual payments on principle. As it is, the budget deficit will be greater than last year, but probably not enough greater to justify fears of inflation.

### III CHINA'S BALANCE OF PAYMENTS

A careful examination of the various items entering into the balance of payments of China yields the conclusion that for the calendar year 1936 China will have -- exclusive of capital movements -- an adverse balance of payments of from 100 to 400 million yuans.

The chief item in her balance sheet is merchandise trade. Last year her recorded import excess was 345 million, but the excess was at least 130 million greater if the smuggling, undervaluation, etc., were included, as they should be when attempting to estimate the demand and supply of foreign exchange.

The December 1935, and January 1936 figures showed a marked change in trend. For the first time in many years China had a favorable balance of trade two months in succession. It looked as though China might end the year with a much smaller adverse balance of trade. February trade, however (March figures are not yet available), showed a return to the unfavorable balance. The import excess for the first two months of 1936 is 7 million yuans. Though this is a much smaller excess than was true of last year, the February figures alone were not much better than February of last year.

One source of foreign exchange for China last year was the smuggled silver. Smuggled silver amounted to over 200 million yuans. How much of the resultant foreign currency was kept abroad (i.e., flight of capital) is not known, but some of it may have been sold for local currency in order to collect the profit on the smuggling.

The other items will not show significant changes over last year.

The above analysis does not include capital movements. There is little likelihood that the Chinese will be able to borrow any considerable sum from abroad. Such loans as will be made will, for the most part, be tied to sale of commodities. Consequently the loans will not result in additional supplies of foreign exchange for the Chinese Government. The loans will take the form of increased imports. It is possible, however, that if conditions appear favorable to maintenance of her present currency position, some of the capital that has flowed out of China in the past few years will return. It is entirely possible that the return capital, plus such amounts China will be able to attract in the form of investments by foreigners, will be more than enough to convert China's unfavorable balance of payments to a favorable balance of payments.

It is also possible, however, that an unfavorable turn of events -- such as, for example, increasing excess of imports -- will stimulate a further flight of capital. The same forces which would stimulate a flight of capital from China would also check the presentation of silver

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for notes. The Government would not be able to successfully resist a severe drain because of her small reserves and because the condition of her reserves will be narrowly watched by speculators who will become heavily bearish on yuan exchange the moment signs of severe weakness in the underlying situation appear.

The purchase by the United States of 5 million ounces of silver a month would not be enough to protect the yuan from depreciation if confidence in the future of the yuan were weakened. The addition of 2 to 3 million U. S. dollars to China's reserves of foreign exchange would hardly furnish significant additional support for the yuan unless it created, or were accompanied by, some measure, or some steps which would help restore confidence in the yuan and in the ability of the Chinese Government to successfully defend its currency against attacks.

#### IV

What then is likely to be the metallic reserve position of China eight months from now?

The following two estimates represent the likely situation,

(a) If all factors discussed in this memorandum are favorable to China;

(b) If all factors are unfavorable.

(a) If factors are favorable:

(1) Silver acquired by the Government banks between April 1 and December 31, 1936 .....	350 million
(2) Inward movement of capital - (chiefly return of funds which had fled China 1934-36) .....	300 "
(3) <u>Adverse</u> balance of payments (exclusive of capital movements .....	100 "
(4) Increase in notes issued by the Gov't banks ..	325 "
(5) Issue of 75 million yuans of token coins and 50-cent new silver coins .....	75 "
(6) Sale of 40 million yuans of silver to U. S. and 15 million yuans on the open market .....	55 "

If the above six changes occur, the monetary picture of China eight months from now will be as follows:

Cash reserves	(approximate)
Gold and foreign exchange.....	400 million
Silver .....	600
Total cash reserves .....	1,000
Note issue .....	1,075
Ratio of cash reserves to note issue .....	93 per cent
" " silver " " " " .....	56 " "
" " gold and foreign exchange to note issue .....	3 " "
" " silver to total cash reserves .....	60 " "

(b) If factors are unfavorable:

(1) Silver acquired by Government banks .....	150 million
(2) Capital movement <u>outward</u> (further flight of capital .....	100 "
(3) <u>Adverse</u> balance of payments (exclusive of capital movements) .....	400 "
(4) Increase in notes issued by Government banks .....	200 "
(5) Issue of 25 million yuans of token coins and 50-cent new silver coins .....	25 "
(6) Sale of 40 million yuans of silver to U.S. and 5 million on open market .....	45 "

If the above six changes were to occur, the monetary picture of China eight months from now would be as follows:

Cash reserves	(approximate)
Gold and foreign exchange .....	minus 300 million
Silver .....	450 "
Total cash reserves (in silver) ....	150 "

(This assumes that China could sell 300 million yuans of her silver stock in order to obtain the gold and foreign exchange necessary to meet the adverse balance.)

Note issue .....	950 million
Ratio of cash reserves to note issue .....	16 per cent
" " silver " " " " .....	16 " "
" " gold and foreign exchange to note issue .....	zero
Ratio of silver to total cash reserves .....	100 " "

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Obviously, the yuan exchange rate would decline long before the end of the year if the factors were unfavorable.

It should be emphasized at this point that unfavorable factors do not include outbreak of hostilities with Japan, or war between Japan and Russia. Such an occurrence would alter the picture drastically and the yuan would probably break precipitously even though China's financial condition were better than now. Favorable and unfavorable factors refer to financial and economic conditions. These are, to be sure, influenced by political conditions, but in this memorandum the analysis excludes war.

The prospect of an outbreak of hostilities is not remote, but war is not the only event that can bring about yuan depreciation. Economic and financial events, if unfavorable, can do it easily without war.

#### CONCLUSION:

1. If factors are favorable to China -- i.e., her Government finances get no worse, her balance of payments become favorable, silver continues to be turned into the banks at the same rate as at present, and silver does not drop much in price -- China's currency position will improve steadily, and she will be able to maintain stability of her exchange without any support from us.

2. If factors are unfavorable -- i.e., a budget deficit of 300 million or more; an adverse balance of payments, a marked reduction in the amount of silver turned in -- China's monetary position will grow rapidly worse and the yuan will depreciate.

3. Our purchase of 5, or even 10, million yuans of silver a month will be of material help only insofar as <sup>it</sup> creates additional confidence in the ability of the Chinese to successfully defend its currency against attack.

If factors become unfavorable, the additional foreign exchange provided by our purchases will not prevent yuan depreciation. If factors are favorable, the additional sum will not be needed.

4. Therefore, our assistance to China, unless it takes the form of a potential loan of a large sum to China on her exchange (with silver as security), must be wholly evaluated on the basis of the psychological effect.

The psychological effect bears on two all-important matters:

(a) The future price of silver, if our assistance or action can be interpreted to be favorable to stability of the price of silver.

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(b) On the extent to which we stand ready to assist China to maintain her present yuan position.

More important as an aid to China, I believe, than purchases of silver are actions or statements that may obviously be interpreted as an intention upon our part to keep the price of silver stable, and to assist China if necessary.

April 20, 1936

Mr. Chen met with the Secretary, Mr. Taylor, Mr. Lockheed and Mr. White today. A record of their conversation follows:

HM, Jr.: I think this is a nice rest for you.

Mr. Chen: Yes, if not for the work.

HM, Jr.: You haven't really worked yet.

What do you think of my hunches as to when it is a good time to sell silver?

Mr. Chen: Very good! Appreciate it very much.

HM, Jr.: And you got the top price!

Mr. Chen: Yes.

HM, Jr.: ✓ How much did you sell?

Mr. Chen: 2,250,000 ounces.

Mr. Lockheed: Frankly, I did not think the market would take that much.

Mr. Chen: We appreciate it very much, your suggestions.

HM, Jr.: I tell you, Mr. Chen, that's the advantage of having you over here for a while. After all, the thing we are trying to do now is to stabilize the price of silver and if some fellow, some speculator, thinks he can make a turn out of these conversations that we are having, it would be the worst thing that could happen.

Mr. Chen: Sure! That's right.

HM, Jr.: The worst thing that could happen! If silver shot up five or ten cents now, it certainly would not help you any.

Mr. Chen: This movement is good for silver. We don't want high silver. We want to have a price we can hold that is good for everybody.

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HM, Jr.: That's why I called up the boys the other morning and told them to make this suggestion because the market is so narrow that I was afraid it might wake up Monday morning and see it was 50 cents.

Mr. Chen: Yes; yes.

HM, Jr.: They must have sold futures.

Mr. Chen: I have not received a cable.

Mr. Lochhead: I presume so, because I understood you had no silver in the London market and that's the future price.

HM, Jr.: That is the future price?

Mr. Lochhead: Yes; future price. Of course, Mr. Chen, that is one point -- that you have no stock of silver in the London market. That is something to consider from an operating standpoint, whether or not you should have stocks in various parts of the world.

HM, Jr.: It has its advantages and disadvantages. You don't know whether they are going to sell any more?

Mr. Chen: Still attempting to sell.

Mr. Lochhead: But if you had a limit of 20-9/16, you were not able to sell any silver this morning because the rate was fixed at 20½.

HM, Jr.: What is the New York equivalent of 20-9/16?

Mr. Lochhead: 45.70 cents.

HM, Jr.: I think you just caught the market unaware and most likely just hit it right.

Mr. Lochhead: Silver might have gone up to 50, but it would not mean there was any greater demand for silver.

HM, Jr.: Now since I have given you such good advice, are you going to bring this money to New York?

Mr. Chen: I think, my understanding is, we will concentrate in the Federal Reserve here, in the natural way.

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HM, Jr.: Will you ask Mr. Kung if he will bring the proceeds of this silver to New York?

Mr. Chen: I will ask. If we don't have any requirements just now, we don't know yet.

Mr. Lochhead: If they sold futures they would not get their money for 60 days.

HM, Jr.: No, but I would just like to know as to policy. I would just like to know; roughly it is a little more than a million dollars; and are they going to bring it to New York and add it to their funds or do something else with it?

Mr. Chen: Our policy is to work with you. There is no question about that. But probably in the last three conferences you do not understand that; I like, this morning, to say few words.

HM, Jr.: Yes. But you will ask Dr. Kung about depositing the money here?

Mr. Chen: Yes. Our first policy is not the idea to sell you a lot of silver. We want the silver market stabilized and if it is stabilized, the silver has a value. We are one of the big holders of silver and naturally we have big interest in that. And you are a big holder of silver and we are naturally partner in this. So it is policy of Chinese Government to come here and make contact. We want create understanding so that we will know in the future we can work together. That is the most important point.

The second point, where I said before, we are already decided to use more silver, to encourage the use of silver for commercial arts. Our laws only allow 30%, but after I left China we are going to change that; we are going to encourage more use of silver by the silversmith. Question of coinage, we want to put silver in that. Possibly we want to find out more about it, how we proceed about it. On this we would like to have your help, your technical help.

HM, Jr.: And we haven't made any progress on that?

Mr. White: We have made some progress.

HM, Jr.: But you haven't discussed that with me. I have no memo.

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Mr. White: No.

Mr. Chen: The third question, of reserve for legal tender, amount of silver we should have. That is question involving so many other conditions, so many other factors. What should be appropriate amount depends upon the amount of confidence we enjoy for the future success of our currency. If we don't have attack, probably a little more will be quite sufficient, but for today in China the condition is not settled, not fixed, uncertain. It is still open to all kinds of possible attack. The Japanese situation, for instance. If with these conferences we should be able to create some sort of understanding, when I go back where the people feel that everything is all right, it is no reason to attack our currency. So this matter we have touched more or less today, whether or not we have come to any conclusion.

HM, Jr.: No.

Mr. Chen: There are just three points -- our policy from Chinese Government. And we would like to sell some silver, but that's not whole idea.

HM, Jr.: No.

Mr. Chen: Whole idea is in what way we can cooperate. We are new in this matter of managed currency which is so highly technical question and sometimes we are afraid we are not fully understood, so also we want to go back home with the understanding from you and following these three policies we will continue to make conversations. That's my trip and there is no other reason.

HM, Jr.: That's all right. As I say, Mr. White has just given me this memorandum this morning, just before you came in, which I have not had a chance to study, and I just want to say this to you. This is a confidential message (you can give it to the Ambassador here and to Dr. Kung). There is a Japanese that is coming here from London to see me. What's his name?

Mr. Taylor: Mr. Yutaro Tomito.

HM, Jr.: I don't know a thing about it. I don't know why he is coming. He is not coming on my invitation. The

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State Department has asked me to see him. So if you hear something about it, I just don't want you to think that I am playing both sides. But I can't refuse to see him.

Mr. Chen: We understand.

Mr. Taylor: He is Commissioner of Commerce and Finance attached to London, Paris and New York embassies.

Mr. Chen: They have Financial Commissioner in London.

Mr. Taylor: This evidently is the man.

HM, Jr.: He has never been in the United States?

Mr. Taylor: He has not been very recently. He is attached officially to all three embassies.

HM, Jr.: I just wanted you to know, Mr. Chen, that he is coming in when I get ready to see him. Undoubtedly he is coming in to find out what I am doing. He is not going to find out!

Mr. Chen: Yes.

HM, Jr.: They evidently figured this is so important they will try to find out and it's none of their business. And if you could find out something for me from your London embassy, if the Ambassador could cable to London and find out who is this man?

Mr. Chen: Yes. Yes, I will do this.

HM, Jr.: Find out who is this man. He undoubtedly is going to try to find out something and he isn't going to find out anything. I may make a speech and say how fine I think China is coming along and ask them to cooperate.

Mr. Chen: (Laughing) Domestic bonds will go up 2 yuan 50!

HM, Jr.: The only important thing is I would like to be kept informed and I wish there were some way to get information quicker when they do something in silver, because we would like to know if they did anything in London today. Today is Monday. I would like to know by tonight because we would like to know before the London market opens Tuesday, our time, and I don't know -- you see, for instance, we did not hear -- I sent a

cable to Buck and we got an answer back. When did you send it?

Mr. Lochhead: About 9 o'clock last night. (Sunday)

HM, Jr.: And we had a message this morning. And he had seen Kung and this is a message directly from Kung. This comes from Buck to me:

"Kung appreciates amount of time you are giving Chen and delegates and says anything you do now to help China is also a help to United States and world. He also suggests you feel free to communicate with him on any problems arising from conversations with Chen. He states Japanese are urging Governor of Shantung and Mayor of Tsingtao to retain customs and other national revenues for local use. Also states that Chinese must take stiffer attitude. He asks you to let him know if any statement from him will help present administration in coming election."

And here is another message we got from him:

"Referring to your message of April 19, Kung says he has already cabled Chen informing you results London sales originally suggested by you. Two million five hundred thousand (2,500,000) ounces sold at 20 shillings and 58 by Chase National Bank without revealing identity original source silver."

That's everything I have got.

Mr. Chen: I wish to read paragraph from cable the Ambassador and myself received yesterday from Dr. Kung:

"Referring to your wire 186 glad Chen emphasizes aim is not get rid of silver but only obtain narrow foreign exchange to safeguard currency. Says desires this clearly understood."

I did not feel very good last few days because I did not make this point clear.

HM, Jr.: That's all right. We are going along. It is very important to both of our countries. And I want to ask, have you made any progress on the study of how Canada manages

its currency?

Mr. Lochhead: We discussed it that day with Mr. Chen.

HM, Jr.: That's clear? And you are giving that a thought?

Mr. Chen: Yes. Next important question for us here now is to study how much silver to put in our coins. It's very important.

HM, Jr.: Do you want to take that up with me?

Mr. Chen: I think, if suitable to you, I will talk to Dr. White or Mr. Lochhead and have Mr. Koo present.

HM, Jr.: When will you be ready, Mr. Taylor? Why don't you make an appointment for tomorrow?

Mr. Taylor: What time would you like tomorrow?

Mr. Chen: Any time.

Mr. Lochhead: This is going to be a technical talk.

Mr. Chen: Yes.

Mr. Lochhead: I think we should bring Miss O'Reilly in.

HM, Jr.: Do you want to say any particular time?

Mr. Chen: Any time you say.

Mr. Taylor: In the morning or afternoon? How about three o'clock in the afternoon.

HM, Jr.: That keeps the thing rolling.

Mr. Chen: I am preparing to make my report to Dr. Kung in Washington so I want to put in all the practical ideas and I will try to make it as complete as I can, as I know how, so for this I would like to have your gentlemen's assistance for future operations and include technical points as far as we can think about it. So personally I don't think this mission is finished. It will be continued for some time. We have so many things to work together, in common, some things I don't know yet.

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HM, Jr.: Quite frankly, the thing is not clear in my mind yet, because I have not absorbed it all yet, but I simply feel we are doing everything we can to advance it. I don't want to retard anything.

Mr. Chen: There is one question, I know as soon as I write to Shanghai the Chinese Government, the Minister of Finance, would like to find out what is United States Government silver policy?

HM, Jr.: Well, we can't answer that. All we can say is we have indicated to you here, over Friday, over the week-end, that the present policy is we would like to keep silver around 45 cents. We have demonstrated that and you have demonstrated to us that you would like to do it too, but I can't say that that will be so a year from now or six months from now, but certainly we have given you a concrete demonstration that we would like to keep it around that price. You have come back and said to us that you are not interested in the price of silver; you are interested also in stabilizing the price of silver. So between the two of us, we can do it because if the price goes up too high you have silver for sale and if it goes down too low we can buy it, so between the two of us we can keep it where we want it. See what I mean?

Mr. Chen: Yes. Yes.

HM, Jr.: If silver should go back to 42 cents, we will start buying and if it goes up to 47 cents, you can sell. That's in your interest and ours, but I can't give you a document and say, Mr. Chen, this is our word; this is the policy. But what I can do after I talk to the President, what I will try to do, before there is any big change, we will let you know, but I can't do that without the President's permission.

Mr. Chen: Yes. It is this contact which has been most beneficial to us.

HM, Jr.: But you know more about our silver policies than anybody else.

Mr. Chen: I don't know about it.

HM, Jr.: We have talked more frankly to you than we have

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to anybody else. We have not talked to the English or to anybody. But it is very difficult for me to say that this is the policy for the next three years; you can't do it because you never know what's going to happen. But this was a very nice demonstration over the week-end of what the two countries can do together, working together, to keep this silver -- we can put it anywhere we want it! Forty-five cents seems to be about right.

Mr. Chen: Yes. Yes.

H.M., Jr.: Seems to be about right.

Mr. Chen: Yes. This level, we can hold that.

H.M., Jr.: Let me read you a cable we receive once a week from our Consul in Bombay:

"Although Bombay silver market was officially closed during Easter holidays the quotation for ready rose from 44.3 cents to 46 cents equivalent New York rates on rumor that an agreement had been reached between United States Treasury and Chinese delegates. On rumor being contradicted market immediately declined and closed on April 14th at 45.5 cents. Owing to better advices from London market became steadier during latter part of week and closed at 46.8 cents. The existence of an oversold position is considered an effective insurance against any appreciable fall in prices. Offtake during the week averaged 250,000 ounces daily. The stock is estimated at between 6 and 7 million ounces.

"Fair amount export business in gold both for ready and forward was transacted. Stocks on hand about 37,500 ounces and average daily offtake about 375 ounces."

But India is taking over 200,000 ounces a day and, of course, from the Indian standpoint if we can keep the thing level, it's much better, but, you see, we get a cable once a week. I think that's about all. If you people get together tomorrow afternoon and then if you hear from Dr. Kung if they did anything today, or what further they will do, I hope you will let me know.

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Mr. Chen: All right.

Mr. Taylor: And the information about the Japanese.

HM, Jr.: If you know anything about the Japanese, let me know. Your London Ambassador might know.

Mr. Lochhead: Ambassador Sze might know.

Mr. Chen: When I passed Japan, they are much against our currency, much against it. But now they feel better but they still do not have much confidence.

HM, Jr.: I personally think it very encouraging that the Japanese are sending a man over here.

Mr. Chen: Yes.

HM, Jr.: He's going to get an ear-full from me! Anything I can do for you around Washington?

Mr. Chen: Thank you. Everybody has been taking good care of me. Appreciate it. Also the weather too!

MEMORANDUM ON INCREASING THE LIQUIDITY OF THE CASH RESERVE  
AGAINST NOTE ISSUES OF THE CHINESE GOVERNMENT BANKS

In another paper that is being submitted by the Chinese Monetary Delegation the statement is made that the amount of gold and foreign exchange now held by the Chinese Government banks against notes in circulation is relatively small as compared to the amount of silver held in the same reserve against notes. It is also pointed out that if the amount of gold and foreign exchange could be increased the confidence of the public in the ability of government banks to hold China's currency at the prevailing level of exchange would be enhanced.

The Chinese Monetary Delegation have been gratified by the fact that in several of their conferences with the Secretary of the Treasury he has indicated two possible ways of helping China to solve this monetary difficulty: One of them is for the United States Treasury to buy silver on monthly instalments from China, giving in exchange U.S. funds in New York to help strengthen China's currency reserve; the other is for the Chinese Government banks to ship silver to San Francisco and New York, to be taken in custody of by the Federal Reserve banks there, and arrange for credit facilities against the silver thus shipped.

Pursuant to the request of the Secretary of the Treasury,

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the Chinese Monetary Delegation are submitting two memoranda signifying the intention of their Government to enlarge the use of silver in China as well as to maintain an independent policy for the Chinese currency, in order to furnish the basis for discussing the two possible courses of action suggested by the Secretary of the Treasury. Believing that the content of the two memoranda will meet the approval of the Secretary of the Treasury, the Chinese Monetary Delegation, on behalf of their Government, beg to submit the following proposals for his sympathetic consideration:

First, the Chinese Government, through the Central Bank of China, offers for outright sale to the United States Treasury the amount of 75,000,000 ounces of silver, being part of the cash reserves of the government banks of note issue. The time of delivery, the price, as well as the method of payment shall be fixed by mutual agreement. The proceeds from this sale will be deposited by the Central Bank of China at the Federal Reserve Bank of New York, to be used for the expressed purpose of stabilizing China's currency.

Secondly, with a view to providing an additional guarantee against unexpected emergencies, and in order to be able to show in the published statements of the government banks a good increase in the holding of gold and foreign exchange, which the above arrangement for the sale of silver will not be able to reflect  
because

because the payments of the proceeds will probably be made on an instalment basis, the Chinese Government wishes that the Central Bank of China, as the representative of the government banks of issue, be allowed to negotiate for credit facilities at the Federal Reserve Bank of New York, or the Federal Reserve Bank of San Francisco - whichever is designated by the U. S. Treasury - with silver as collateral security up to 50,000,000 ounces. This silver will be shipped over in the form of unrefined coins to the United States. On the question of legal technicality China hopes to be advised by the U. S. Treasury as to whether a re-export license needs to be applied for before the shipment of the whole lot of 50,000,000 can be made.

The sums involved in the above proposals are calculated to be sufficient to meet China's present requirements of external funds for monetary purposes. That the amount offered for sale is not too great can be seen by the following calculations:

At present, the three government banks in China hold about Yuan 395,000,000 of silver against their note issue which has recently reached about Yuan 780,000,000. The nationalization programme is proceeding at the rate of Yuan 6,000,000 each week, notes being issued against silver coins taken in. Taking 25% of the present note issue as the amount of silver to be kept in reserve, and allowing the new coinage programme to absorb

nationalized

nationalized silver in the future, there is left free and available for disposal Yuan 200,000,000 of silver equivalent roughly to 150,000,000 ounces. This quantity is twice the amount China offers to sell. It is also larger than the combined amount of the white metal China offers for sale and as collateral against credit facilities.

MEMORANDUM ON INCREASING THE USE OF SILVER IN CHINA

## I

The conversations on Chinese currency now being held between the Chinese Monetary Delegation and the United States Treasury have been found most useful in bringing to light China's present urgent needs and the steps she should pursue in strengthening her currency position.

As China's note issue is covered to the extent of more than 65% by a cash reserve composed mainly of silver and to a lesser extent of gold and foreign exchange, it is most essential for her to achieve two objectives in order that the confidence of the public in the new currency may be maintained and further increased. First, the value of the white metal should be stabilized at around either the present or a higher level; secondly, the amount of gold and foreign exchange held in the cash reserve against note issue should be sufficiently increased so that there shall be no doubt in the minds of the public as to China's ability to hold her currency at the prevailing level of exchange. While the methods of achieving the second objective will be the content of another paper, in the present memorandum the Chinese Delegation

Delegation will offer, on behalf of their Government, the ways and means of achieving the first objective which has been the policy of the United States Government during the past three years.

## II

With a view to stabilizing the value of silver, China agrees with the United States that the use of the white metal should be widened. In this connection China is prepared to undertake the following three steps: First, to lift the present limitation on the use of silver in arts and industry in China; secondly, to commence in the immediate future the coinage and circulation of new silver coins, of the denominations of ~~50 cents~~ <sup>half yuan</sup> and one yuan Chinese currency; and, thirdly, to announce formally the maintenance of a definite reserve in silver, along with gold, foreign exchange, and other collaterals, against note issue.

## III

The use of silver in arts and industry in China has been an old and established custom and Chinese silverwares have always enjoyed a reputation and prestige for their artistic value. Since the adoption of the monetary reform, the Chinese Government has issued an order restricting the fineness of silver used in arts and industry to 30%, in order

order to prevent hoarding of silver coins and to insure the success of the nationalization programme. With the world price remaining stable at the present level China is no longer afraid of hoarding and smuggling of silver. The Chinese Government is ready, in order to prove its intention of using more silver in China, to rescind the restriction order on the fineness of silver used in arts and industry. It is certain that this action will result in an increased consumption of the white metal in China.

IV

The Chinese Government has given orders to the United States Government Mint in Philadelphia to make several sets of dies for the coinage of two silver coins: the <sup>100 cent</sup> ~~50 cent~~ piece and the 1 yuan piece. The Chinese Delegation have received definite instructions from their Government to state that the Chinese 1 yuan piece shall contain at least 138.24 grains of pure silver, and the 50 cent piece, at least 69.12 grains of pure silver. As soon as technical preparations allow, the 50 cent piece will first be coined and put into circulation, to be followed later by the 1 yuan piece. These coins have a monetary value for silver at US\$1.04 per ounce of silver.

The present capacity of the Central Mint at Shanghai is about 40 million pieces monthly including the necessary amount

amount of subsidiary copper and nickel coinage. The Ministry of Finance is making plans for the reconditioning of the mints at Hankow and Chungking. When reconditioned these mints will take over from the Central Mint the task of making copper coins, leaving the latter to bear the sole responsibility of making silver and nickel subsidiary coins.

The Chinese Government hopes that by issuing 200,000,000 pieces of each kind of coin during the period of inception, to be followed each year by say 50,000,000 pieces of the 1 yuan coin and 100,000,000 pieces of the 50 cent coin, 86,000,000 ounces of silver will be required for the initial period and 30,000,000 ounces for each succeeding year. That the Chinese people in normal times can absorb great amounts of silver currency can be substantiated by the following facts: During the ten years 1922 to 1931 there were imported into China 750,000,000 ounces of silver the greater portion of which went into the interior in the forms of coins. When economic depression came to China no less than 300,000,000 pieces of silver yuan flowed back from the interior to the Shanghai financial market during the years 1931-35. Since the order for the nationalization of silver was issued on November 4, 1935, old silver yuan at the rate of 6,000,000 pieces each week have flowed into the vaults of the government

ment banks. A tremendous potential requirement of hard coins must have been slowly built up during the last five years, intensified still more by the recent nationalization programme. On top of the potential demand must be added the requirement from the contemplated move on the part of the Government to substitute the new coins for the 1 yuan notes issued by the banks in China. The amount of this kind of money now in circulation is approximately Yuan 130,000,000.

It is evident from the above mentioned facts that the amount of the new silver coins can be increased very much before a saturation point is reached and no more silver needed. The Chinese Government, however, prefers to proceed with the new coinage programme in a cautious manner, realizing that public acceptance is usually hesitant at the beginning, and also that counterfeiting is a serious problem that warrants more than ordinary attention when the new coins are first issued.

V

The practice of maintaining silver as a part of the monetary reserve of the nation was adopted by the United States in 1934. As an evidence that China is in agreement with the United States in this matter, she has decided and will announce, as soon as complete accord is reached in  
the

the Washington conversations, the formal adoption of maintaining at least 25% reserve in silver against notes outstanding, using for this purpose the old silver yuan - which has a bullion value 10% above its monetary value - until such a time when the change in circumstances warrants the use of another method of valuation. As there are now issued by the three government banks legal tender notes to the amount of Yuan 780,000,000, a minimum amount of Yuan 195,000,000 in silver would be kept in China's monetary reserve. This announcement when made will afford conclusive proof of the contention of the Chinese Delegation that China does not want to dispose of all her stock of silver. It will also give strength to the price structure of silver, because, aside from allaying the fear of dumping from China, additional silver will be required by her as monetary reserve for the future expansion of her note issue. Such being the case, this action of the Chinese Government will prove to be an important factor toward the stabilization of the white metal.

MEMORANDUM ON THE QUESTION OF THE INDEPENDENCE  
OF THE CHINESE CURRENCY

In the course of the conversations on the Chinese currency between the Chinese Monetary Delegation and the United States Treasury the point has been raised that while the official declarations have claimed that the Chinese currency has an independent status, yet in all appearance the Chinese yuan has maintained a fixed relationship with the British pound sterling since the inception on November 4, 1935, of the new monetary policy in China. The advice was also given to the Chinese Delegation that China could pursue to great advantage the policy now adopted by the Canadian Government of making alternative changes in the Canadian exchange rates on London and New York, each change being dictated by Canada's own needs thus showing unreservedly the independent nature of the Canadian dollar.

The Chinese Delegation have since transmitted the above views to their Government and asked to be informed of the conditions under which the rate of exchange on London as posted by the Central Bank of China would be changed. The following reply and undertaking has been received from the Chinese Government.

When the Chinese Government decreed, on November 4, 1935,  
that

that the three government banks should so act as to hold the exchange value of the Chinese yuan at the then prevailing level, the rate on New York was fixed at 29-3/4 (i.e. US\$29.75 equals Yuan 100.) and the rate on London, at 1/2-1/2 (i.e. Yuan 1 equals 14.5 pence). These two rates were fixed to correspond to a London New York cross rate of 4.92 prevailing on the same date. They remained the same for almost two months when the London New York cross rate fluctuated within a small range. However, towards the end of January 1936 the London New York cross rate went up to above 5.00 and the Chinese Government banks were faced with an embarrassing situation. As long as the official exchange rates on both London and New York remained unchanged, the speculators doing exchange arbitrage operations could demand the right to sell American dollars to the government banks against simultaneous demand for the right to buy English pound sterling from the banks, at the respective buying rate for American dollars and selling rate for pound sterling posted by the Central Bank of China. Either the rate on London or that on New York would have to be revised if the government banks were to avoid losses resulting from arbitrage operations of the speculators. As the Government was then chiefly concerned with preserving the value of the Chinese  
currency

currency and was unwilling to give the public the impression that the Chinese yuan would show a downward revision of value each time the London New York cross rate changed, the rate on London was not reduced but the rate on New York was revised upward early in February this year. Since February 13 these two rates have remained unchanged at 30 for the American dollar and  $1/2-1/2$  for the pound sterling, while the London New York cross rate has fluctuated between 5.00 and  $4.93\frac{1}{2}$ .

As long as the London New York cross rate fluctuates within the above limits China's exchange rates on both London and New York will remain the same as at present. Should the London New York cross rate go down to 4.92, which was the rate prevailing on November 4, 1935, when China adopted her currency reform, then the Central Bank of China would restore the rate on New York back to  $29-3/4$ , the rate fixed on November 4, 1935.

If, after the rate on America is restored to  $29-3/4$ , the London New York cross rate should go down further reaching say 4.88, then the Central Bank of China would make a revision of the official rate on London from  $1/2-1/2$  to say  $1/2-5/8$ , leaving the rate on New York unchanged.

To

To sum up, the position chosen by the Chinese Government with respect to the exchange rate policy is as follows:

As long as the London New York cross rate fluctuates around 4.92, the rate prevailing on November 4, 1935, then China will keep her exchange rate on London at 1/2-1/2 and that on New York at 29-3/4, both being the original rates ruling on the first day of the currency reform. When the cross rate goes above 4.92 to such an extent that operators in arbitrage could profit at the expense of the government banks, then the rate on New York would be revised while that on London would remain unchanged at 1/2-1/2. On the other hand, should the cross rate fall below 4.92, reaching 4.88 or even lower, then the rate on London would be changed while that on New York would remain unchanged at 29-3/4. To change the rate on London now, while the cross rate stands above 4.92 and the rate on New York at 30, would lead to appreciation of the Chinese currency in terms of both the English and American currencies above the level ruling on November 4, 1935. Such an action would be open to objection by the Chinese public. By the same reasoning, to alter the rate on New York downward to below 29-3/4 and not that on London, when the cross rate goes below 4.92, would lead to suspicion on the part of the public that the Chinese Government might further depreciate her currency. For the sake

sake of upholding public confidence the Chinese Government has adhered to the policy, after bringing the value of the Chinese yuan down to the level ruling on November 4, 1935, of following either the English or the American currency whichever is comparatively dearer in value in their daily fluctuations above or below the ratio of 4.92. This policy is merely a modus operandi calculated to uphold public confidence in the Chinese currency for the time being. It is altogether different from the policy of linking a currency to another one, irrespective of whether the latter appreciates or depreciates in regard to other currencies. The Chinese Government is at full liberty to make revision of rates when conditions warrant it. In substance, the Chinese and the Canadian policies are essentially in agreement.

As pointed out above, the policy of always showing to the public either one of the two original rates fixed on November 4, 1935, (i.e. 1/2-1/2 on London and 29-3/4 on New York), is calculated to uphold public confidence. Should the confidence in the Chinese currency become unequivocally strong, then the present policy may give way to a new one whereby China's rates on both London and New York may be different from either of the two original ones ruling on November 4, 1935. Such a step is considered

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to be inopportune at the present moment. At any rate, the intention of the Chinese Government is quite clear. The Chinese yuan is to remain independent in terms of other currencies and is subject to change as circumstances demand. At the conclusion of the present conversations here in Washington another declaration will be made by China to reiterate her old stand.

Furnished by George Allen 252  
D.C. Commissioner.

SELF-LIQUIDATING STAMPED SCRIP

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4/20/36

Although proposed at least as early as 1890 in Argentina by the late Silvio Gesell, and adopted by a small town in Bavaria about ten years ago, by several others in Germany, later by the town of Woerl, Austria, and finally by several hundred (some of the Hawarden, Iowa, officials claim over 2,000) communities in the United States during 1932 and early 1933, and seriously proposed in 1935 for several large cities, and even for the United States as a whole, the use of self-liquidating stamped scrip has since all but disappeared. Professor Irving Fisher, the author of a book on stamped scrip and of the best known plan on a national scale, states that the only place where self-liquidating stamped scrip is now in operation is Chicago. There are now operating in one or more communities in Chicago, three issues of dated scrip amounting to between ten and twenty thousand dollars, and two kinds of transaction scrip.

Classes of Scrip.

Scrip consists of certificates, usually of one dollar denomination, issued in payment for services or goods, and received by merchants and other citizens assenting to the plan in payment for either goods or services. Self-liquidating scrip is scrip whose redemption value, usually including cost of printing and possibly other expenses, is recovered by the issuer

through the sale of stamps which must be affixed to the scrip by the buyer or seller. Transaction scrip is a type which must have a stamp affixed each time the scrip changes hands. In the case of dated scrip, the stamp is affixed at stated periods, usually two per cent on each Wednesday for 53 weeks.

History of Self-Liquidating Scrip.

Self-liquidating scrip was devised by Silvio Gesell (1862-1930), a German who spent a large part of his life in Argentina. Gesell acknowledges that he derived some of his ideas from the French Philosopher Proudhon, who was prominent in the time of the Second Republic. Gesell proposed the idea at the time of the Argentine monetary difficulties of about 1890, but nothing seems to have been heard of it until after the World War. In April, 1919, Gesell, then in Germany, joined the shortlived Soviet cabinet of Bavaria as Minister of Finance. After the establishment of a responsible government in Germany, he went to Switzerland, where he became active in the *Freiwirtschaft* movement. In 1923, a convention of the Swiss and German followers formed a *Freiland-Freigeld Bund*.

The first practical experiment in self-liquidating scrip seems to have been in 1926, in Schwansenkirchen, Bavaria. This town of fewer than 500 inhabitants had derived its income from a local coal mine which had been closed for two years. The inhabitants were in severe straits, when Herr Hebecker, owner

of the mine, offered to reemploy his former workers if they would accept payment in self-liquidating dated scrip which he called Wara. This Wara was issued by the town of Schwanenkirchen, and was liquidated by the requirement that a one percent stamp be attached to the scrip each month. The miners agreed when they learned that Herr Hebecker had received a loan of 40,000 marks in legal currency and that the village storekeepers would accept Wara for goods. The mine reopened, the workers promptly spent their pay in the shops, and the shopkeepers then forced some of the Wara on the wholesalers. Some of the latter might have been reluctant to accept Wara, but knowing that this was the only way they could collect from their customers, they took it and passed on a part of it to the manufacturers. The amount taken in by the manufacturers was apparently not large enough, in proportion to their total receipts, to inconvenience them seriously, since they were able to use it to pay creditors who were pressing them and glad to get something, or for purchasing Herr Hebecker's coal; According to Hans R. L. Cohnsen, an associate of Professor Fisher, Wara subsequently was accepted in a few thousand stores in Germany, and one or more communities besides Schwanenkirchen recuperated from the depression by its means. A few small banks even opened Wara accounts, accepting the deposits and at once lending out the Wara to those asking for credit. However, the national government in its efforts to suppress any inflationary tendency, forbade the use of Wara by an emergency law passed in 1931.

On August 1, 1932, the Wara system was introduced by the town of Woergl, Austria. This small Tyrolese village had a deficit of about 120,000 schillings because of the large relief roll. Banks were refusing loans and the few people who had money on deposit were retrenching as much as possible in fear of a further depression. Again, according to Mr. Cohrssen, business activity in Woergl sprang to life and the government receipts increased and its expenditures decreased. The Wara was accepted by everyone in Woergl except the post office and the railroad, and circulated to a considerable extent in the surrounding country. In \_\_\_\_\_ however, the Austrian government, like the German government, suppressed the use of Wara, both governments being, according to Mr. Cohrssen, influenced by the hostility of "the bankers", who considered the plan an invasion of their credit issuing power.

The first recorded use of self-liquidating scrip in the United States appears to have been in 1932, when a considerable number of small communities, mostly in the Middle West, adopted it as a means of paying people on relief. Municipal treasuries were empty and no other method seemed possible at the time. The most widely publicized scrip at this time was the transaction scrip issued by Hawarden, Iowa. A three cent stamp had to be affixed to each coupon each time it changed hands. When 36 stamps had been affixed, this scrip was retired by the town by a new issue

of scrip of the same kind. The town has a population of 2,500 and each of the two scrip issues amounted to only 300. The burden of the three per cent tax was not great. However, in

practice, after the first transaction, the merchants found that all they could do was to swap the scrip among themselves, except that they could use it to pay their light and water bills once a month. It really amounted to shifting the burden of relief from the general taxpayer to the merchants and, according to the magazine, Retailing, there was no compensating stimulation to business. The grocer whose gross profit was perhaps twenty-five percent could not use it to replace goods on his shelf. Landlords could not take it since they could not pay taxes or telephone bills with it. Banks would not take it because customers refused to take it in change. There was no incentive to speed up circulation, since the tax must be paid on each transaction rather than at stated intervals of time) and general acceptance of the scrip in the community had not been previously arranged. The result was that, although the plan aided the town over a temporary emergency, the second issue was retired, and no more scrip issued, as soon as the town received some real cash from the GNA and PWA early in May, 1934. At about the same time, Des Moines retired its \$100,000 scrip issue.

The Hawarden plan received more attention from journalists than any other scrip plan in the country. Writers did not all agree in their comment on the results of the plan, but the general

temer of opinion was that the town officials were pleased since it solved their relief problem, but that the merchants accepted it only as a patriotic duty to tide the town over an emergency and because the amount issued was so small.

It is difficult to establish the dates of developments in scrip subsequent to the bank crisis of March, 1933. From August, 1932, to March, 1933, newspapers and magazines were full of accounts of the initiation of scrip plans in one small community after another, or of this or that larger city considering its initiation. However, when a large city rejected the plan, the rejection appears to have received very little mention, and hardly any periodical notices came out to chronicle the successive abandonments of scrip by the hundreds (or 2,000 if there were that many towns in which it enjoyed a fleeting period of operation). Today it is believed there is not a single government, national, or local, which is sponsoring the self-liquidating scrip system, and, as far as is known, its operation persists only in Chicago, where it is handled by a group of merchants.

On February 17, 1933, Senator Bankhead offered a stamped scrip amendment to the Emergency Relief and Construction Act of 1932 prepared by Professor Irving Fisher. The amendment was also sponsored in the House of Representatives by Congressman Pettengill. The principal provisions were, (1) The Federal Government should issue \$1,000,000,000 of scrip in one dollar

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denominations. (2) The holder as of 12:01 A.M. of each Wednesday beginning with the second Wednesday of issue is required to affix a two cent postage stamp to the coupon in order that it be valid; when 52 stamps have been affixed, the coupon is redeemed by the Government at its face value. (3) The scrip is declared legal tender for all debts and dues, public and private, including customs duties and taxes. (4) It is forbidden to insert a clause in any future contract under which the creditor refuses to accept scrip. (5) The scrip is not legal tender for transactions of less than one dollar unless the payor adds an extra stamp. (6) A bank of deposit may charge two cents for each certificate deposited, as a service charge. (7) When the Bureau of Labor Statistics price index reaches 80% of the 1926 average, the issuance of scrip is to be discontinued and the outstanding scrip retired as it is presented for redemption. (8) Of the \$1,000,000,000 issue, half is to be used for regular Federal Relief and the other half apportioned to the States for their relief purposes.

The amendment was not adopted, and its proponents charged that the late Secretary Woodin was responsible for its failure despite the approval, as they claim, of at least three other members of the Cabinet.

Theory

Gesell arrived at his theory of self-liquidating scrip, which he called "Schwundgeld" (disappearing money) from a contemplation of the similarities and differences between money on the one hand and commodities and services on the other hand. Money, observed Gesell, is different from commodities and services in that it alone can be stored free and without deteriorating - that it can be withdrawn from the market without loss of value. The possessor of money, therefore, enjoys a superiority in a bargaining position compared to the owner of goods or services, so that the latter becomes ground down periodically. This was his explanation of crises and depressions; and since he believed the difficulty lay in the propensity of money owners to hoard it, his remedy naturally took the form of a provision designed to eliminate the tendency to store or hoard money. Obviously, no one will store dated scrip, which is the variety proposed by Gesell and the only variety of self-liquidating scrip used in Germany and Austria, where his influence was felt. The device of the transaction scrip seems to have been merely an emergency measure in certain United States towns to bale out bankrupt municipal treasuries.

It is interesting to note that John Maynard Keynes, in his latest book, "The General Theory of Employment, Interest and Money", comments favorably upon Gesell's observations on the above mentioned unique property of money, making, however, the

qualification, that money is not unique in this respect but only superior to other things. The British economist even says, on page 357, "the idea behind stamped money is sound. It is indeed possible that means might be found to apply it on a modest scale." He favors a rate of stamp tax equal to the difference between the current interest rate and the current marginal efficiency (productivity) of capital.

The fundamental difficulty with any system of fiat money or scrip (which is of course a form of fiat money) is that it is not, like gold, universally accepted without question. General acceptance of any currency is, of course, greatly facilitated by decreeing it legal tender. For this reason, the plan of Professor Fisher for a national legal tender issue of self-liquidating scrip would, if adopted, be more practical than a local scheme. On the other hand, the Fisher proposal would be, of course, a temporary inflation which would probably, American politics and human nature being what they are, tend to become permanent since new and greater scrip issues would probably follow upon successive redemptions of old issues. In any case, there is now no occasion for a national issue (according to the terms of the Fisher bill) since the price level has already risen to 80. Nevertheless, inflation feeds on inflation; hence, when 80 is reached, the goal is moved higher.

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A local issue of scrip as such as existed temporarily in Hawarden and in many other small towns in 1932 and 1933, and such as now exists in a restricted area of Chicago, cannot be made legal tender by any authority except Congress. The plan proposed for the District of Columbia does not contemplate that the scrip shall be made legal tender; in fact, it is not even to be accepted in payment for stamps which are required to be affixed to it each week. This at once materially limits its acceptability and hence its value, even though a number of merchants in the District express their willingness to take it in the hope that it will increase business. Unless adherence of practically all in the District is obtained, those adhering will find it impossible in most cases to continue to accept it in unlimited amounts.

#### Forces for and Against Scrip

Wherever self-liquidating scrip has been tried, it has been favored in general by those who have nothing to lose, and usually by relief authorities who conceive of it as a convenient solution of their problem. A varying number of shopkeepers are usually found to favor it where it has been tried, because it has always been proposed when business conditions were at a low ebb and the storekeepers clutched at the proposal as offering the hope of stimulating business. There is also an element in every community favoring any sort of inflation proposal on the

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principle that it stimulates things as far ahead as they can see. Some other shrewder minds favor inflationary proposals with the thought that they know how to take advantage of them and can "get out in time". Finally, some of the inflationary proposals for dated self-liquidating scrip are favored by perfectly honest and well meaning people who are impressed with the misery of the unemployed and the deficiencies of the present economic system and who are either not familiar with economic history or believe that "this case will be an exception."

Opposition to scrip plans is likely to be found among those opposed to any inflationary proposal, and consists generally of those who have a serious stake in the present economic system.

#### Why Scrip has been Abandoned

As previously mentioned, the abandonment of the Gesell scrip plans in Germany and Austria was due to governmental decree. It would be worth while to find out from the authorities in those countries exactly why the decrees were issued. The Fisher school attributes the suppression to the malign influence of bankers on the government, and the bankers apparently have nothing to say for publication. It may be taken for granted that bankers in both Germany and Austria opposed the scrip plan and that they had selfish reason. However, there were also no doubt unselfish and sound reasons for its suppression; otherwise, it would seem that there would have been more popular opposition to the bankers

than there seems to have been. That the general public tended to agree with the bankers rather than with the Gesellites seems apparent from the fact that in all the time before the November, 1931, decree in Germany and the 1933 decree in Austria, the plan had been adopted in only two or three towns in Germany and only one in Austria. If the Wera system was really so beneficial in Schwandenkirchen and in Woergl as claimed by its exponents, why was it not shortly adopted in many other communities? It is hardly possible that the bankers can be so all powerful as to prevent a determined group of people from setting up a scrip system as long as it is legal. They did not prevent it in Schwandenkirchen for some five years and surely there must have been other towns similarly situated where it might have been attempted.

The reasons for the failure of the numerous short-lived scrip plans in the United States remain to be chronicled. Definite reasons are, however, known why the system failed in a number of cases. Passing over the reasons which do not apply to the specific plan for dated scrip under discussion, it has been found that the following difficulties are created:

(1) A difficulty unquestionably encountered by all local scrip plans is the fact that no local community today is self-sufficient. Even if all of the town's citizens accept the scrip, how is payment to be made for goods necessarily produced

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outside and for other payments due to outsiders ? This may not be a serious matter to a purveyor of services or an essentially local industry, such as a florist who raises his own flowers on the outskirts of the village; but the greater part of the proceeds of the retail grocer's sales consists of the price paid the wholesaler or producer, located usually at some distant point where he would have no use for his customer's scrip. The florist accordingly might readily agree to accept scrip in turn for receiving one or more additional gardeners, delivery boys, etc., from the relief rolls, since he probably has relatively few payments to make outside of the town. The retail grocer could afford to take only a relatively small proportion of his receipts in the form of scrip. This was actually the difficulty experienced in Hawarden, and more especially in the extremely short-lived, in fact almost abortive, barter scrip in Inwood, New York City.

(2) Sporadic development of uneconomic operations; for example, Plant A accepting scrip might be technically less efficient or produce a poorer grade of product than Plant B, which did not accept it. Nevertheless, Plant A might get business away from Plant B merely by reason of accepting scrip which everybody was anxious to get rid of. The total amount of business would not necessarily be increased, but merely diverted from B to A, to the net loss of the community because of A's technical inferiority.

(3) Customary channels of trade were disrupted. Just as

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the blocked or restricted currencies and the bilateral clearing and compensation arrangements established in Europe during recent years have caused an uneconomic diversion of trade from its natural channels, the benefits of division of labor are thereby lost to the body economic as a whole. Certain groups gain, but their gains are less than the aggregate of the losses to the other groups. Local scrip systems indeed are rather similar in principle to the restricted currencies found in certain central European countries.

(4) There is a temptation to overissue hard to resist, as is exemplified in the case of the earlier Chicago scrip experiment as handled by Winfield H. Caslow. Caslow is a magnetic organizer, but his scrip soon lost acceptance because he issued too much.

(5) In many cases there has been no doubt a well-founded suspicion that redemption would not be effected at maturity. Failure of redemption might be caused either by overissue, by misappropriation of funds, or bad faith in general.

(6) A tendency to cause prices to rise and increase the cost of living. This is believed to have been one reason back of the German prohibition of scrip.

#### The Future of Self-Liquidating Scrip

It seems probable that the self-liquidating scrip idea is dead, except perhaps in Alberta, and will not be revived until near the bottom of the next depression. Fiat money schemes

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have nearly always been born of depression. Schwundgeld originated in the Argentine monetary depression of 1890 and actually took form in the post-war depression in Germany and later in the 1932 depression in Austria and the United States. Its principal alleged merit, that it increases the turnover, assumes greatest importance at the bottom of a depression, and might even be a detriment at the top of the business cycle. Irving Fisher indeed recognized this principle by providing in his 1933 bill that no more scrip should be issued when and if the price level arose from the 60% of the 1926 level then existing to 80%, which level was reached last year.

It was reported in April 12, New York Times, that the Alberta Social Credit dividend of \$25 per month would be paid in scrip like that used in Woergl. This and the small Chicago experiment should prove interesting experiments and should be studied intensively and objectively. An investigation should also be made of the actual results in Schwandenkirchen and Woergl and of the real reasons for the suppression of the Wara plan. The reason why the proposed introduction of the system in Reading, Pa., in March, 1933, was dropped should also be investigated, likewise the reason why it was never revived. It is said that the city authorities and the merchants were on the point of adopting a Fisher dated scrip plan when the order went out from Washington to drop all scrip. Mr. Cochrane

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explains that the Washington order really referred only to clearing house scrip (it will be remembered that the New York Clearing House Association even had quantities of scrip already printed), but the Reading people became either confused or timorous and feared to "get in wrong".

#### Conclusions

1. As the historical resume shows, numerous groups have tried and abandoned stamped scrip. So far as has been discovered, every stamped scrip plan in actual operation in the United States which has failed or been abandoned was of the transaction scrip type. The only dated scrip plans so far operating in the United States are said to be those of the Merchants Scrip Exchange, 3306 W. North Avenue, Chicago, and two smaller organizations in Chicago, and these plans are still operating. However, the dated scrip plans of Schwanenkirchen and Woergl were suppressed by order of the German and Austrian governments respectively. The Chicago plans should be watched, also the proposed Alberta plan, and the reasons for suppression of the German and Austrian plans investigated.

2. The fact that after all the numerous experiments in stamped scrip, so few are still operating, raises a presumption against the idea, but is not conclusive. Neither is theoretical analysis entirely conclusive. There is something to be said for the idea of dated scrip for use in a serious emergency to overcome

lack of currency caused by hoarding or lack of proper banking facilities. It is an historical fact that the plan has always been suggested in times of severe depression when any inflationary measure meets a ready welcome and when any form of circulating medium seems better than none.

3. The plan is sure to meet serious practical obstacles, judging from both experience and theory. It has been found difficult, at least in American experience, to obtain voluntary acceptance by an entire community. Unless substantially the entire community cooperates, the amount of scrip which could be issued without causing loss to the assenters is extremely limited, especially if the community is largely dependent on the outside for its supplies. Professor Fisher's group consider it essential to have a scrip exchange, as is done in Chicago, in which holders of excess amounts of scrip (amounts in excess of what the holder is able to use) can receive legal currency, subject to a discount of perhaps one stamp. Such a provision should facilitate the enrollment of assenting merchants and manufacturers who have outside commitments. The scrip exchange should possess an initial guarantee fund which would be replenished periodically by legal currency paid in by those in receipt of funds from sales outside the community. It should not be made compulsory to pay in legal currency to purchase scrip, or assent will be difficult to obtain from those dealing largely outside the community.

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4. If undertaken at all, the amount of the initial issue, as in the case of any fiduciary issue, should be small, so small that there is no question of the ability of the merchants to absorb it and so that the tax will not be felt. This means that the relief problem in a sizable community cannot be solved overnight by a large issue but can only be reduced gradually.

5. Unless the foregoing precautions are observed, the scrip will not meet general acceptance, at least after the initial enthusiasm dies down. It has been said that although the scrip cannot be hoarded itself, it leads to increased hoarding of legal money and bank deposits, which may more than offset, through fear psychology, the increased velocity of scrip. It should be remembered that 80% to 90% of payments are made by check, not cash.

6. Finally, there is the danger of causing economic dislocations through upsetting the usual channels of trade, resulting in losing the benefits of the division of labor.

7. A further and thorough investigation on the spot of past experiments both here and abroad should be made in any case before action is taken, and the progress of the limited experiments now being conducted should be carefully studied.

Monday  
April 20, 1936

HMjr: Right - Look, I've talked to the President this morning and telling him that on Wednesday that con-- very confidentially we're going to have a meeting with the Federal Reserve crowd to talk about my financing and also excess reserves.

Com.  
James M.  
Landis: Yes

HMjr: And he suggested that it would be helpful to have you sit in.

L: Yes

HMjr: He thought - he was under the impression that you have to do with Stock Exchange margins.

L: Yes

HMjr: But I told him you didn't.

L: Yes

HMjr: But that - I didn't - I'd be delighted on account of we're going to discuss the raising of excess reserves and of course it has to do with Stock Market speculation.

L: Yes

HMjr: Would you be free at eleven o'clock Wednesday?

L: Yes, I would.

HMjr: Do you want to bring anybody with you, your economist or anybody?

L: I might bring my executive assistant, I think.

HMjr: Who is that?

L: Thomas Gammack -

HMjr: Thomas - ?

L: Gammack

HMjr: Gammerick?

L: G-a-m-m-a-c-k

HMjr: G-a-m - ?

L: m-a-c-k

HMjr: That isn't - you have an economist over there, don't you?

L: Yes, I do, but - he's not - he's not the specialist on margins and matters related to things like that.

HMjr: Fine - and these meetings we have over here we keep - we don't announce them, we don't say anything and we keep them very confidential.

L: Yes, I - naturally -

HMjr: And I haven't decided yet - I don't know how Eccles wants to do it but I mean this is not the regular Open Market Committee.

L: Yes

HMjr: And until I have a chance I don't want the full Open Market Committee - see?

L: Yes - this will be over at the Treasury?

HMjr: In my office.

L: In your office?

HMjr: And the subject will be our financing and excess reserves.

L: Yes

HMjr: So, I mean, I think it would be helpful to have everybody in at one time.

L: Yes, yes - all right.

HMjr: I've got an open mind on it.

L: I - I may have an ignorant mind, I gather. (Laughter) Being ignorant it will be open.

HMjr: Good (Laughter)

L: (Laughter)

HMjr: All right, thank you.

L: Thank you very much.

Monday  
April 20, 1936

HMjr: Hello -

Operator: Commissioner Landis -

HMjr: Hello -

Landis: Hello -

HMjr: Landis?

L: Yes

HMjr: Morgenthau -

L: Yes

HMjr: I've just been talking to Eccles and he says he's not going to be ready to discuss excess reserves Wednesday.

L: I see.

HMjr: And he says he needs more time.

L: Yes

HMjr: So, I'll let you know when we do discuss it.

L: All right.

HMjr: So that meeting is off and he said we'll confine it to new financing which doesn't particularly -

L: Yes

HMjr: - interest you.

L: Yes

HMjr: So he isn't ready and he says he's got to have more time.

L: Yes - .well, I'll be working on it in the meantime.

HMjr: Good

L: trying to arrange my thoughts.

HMjr: Well, I've been working very hard on it for a couple of months and -

L: I imagine so.

HMjr: And - I'll let you know when we do meet.

L: All right, fine

HMjr: Thank you

L: Thank you very much.

TREASURY DEPARTMENT

*MA* 270

INTER OFFICE COMMUNICATION

DATE April 20, 1936

TO Secretary Morgenthau  
FROM Herman Oliphant

Justice decided to ask both the State Department and Treasury for formal opinions before deciding on the German countervailing duties, and requests for such opinions have gone forward.

The preparation of such an opinion by State Department may easily be the occasion of a great deal of delay.

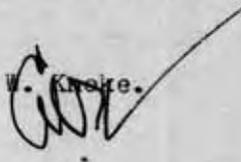
*HO*

April 20, 1936.

TO: Mr. Lochhead.

Mr. Eikichi Araki, New York representative of the Bank of Japan, is giving a luncheon tomorrow to Mr. Yutaro Tomita, the Financial Commissioner of the Imperial Japanese Government, formerly in New York, now in London and Paris, to meet a number of bankers and others. When Mr. Araki extended his invitation to me last week he stated that Mr. Tomita was the Chief of the Financial Section of the Ministry of Finance and that he was going to Japan via this country.

L. W. Kroske.



Phillips  
Hornbeck  
Barto.

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at 2201 R

Lee

April 20, 1936.

MEMORANDUM: Mr. Yutaro Tomita, Financial Commissioner of the Japanese Government in New York, London, and Paris; and Financial Attaché of the Japanese Embassy, Washington.

The office of Financial Commissioner for the Japanese Government in New York, London and Paris assumed great importance when the Japanese Government and Japanese municipalities were floating loans in European and American markets. This was especially the case during the Russo-Japanese War (1904-1905), when the Financial Commissioner was the late Mr. Korekiyo Takahashi, who later was Minister of Finance in a number of cabinets. The loans obtained in London and New York for the prosecution of that war were obtained through the agency of the Financial Commissioner. Although the Japanese Government has not floated any loans abroad in recent years, the office of Financial Commissioner is still regarded as one of great importance, and is held consistently by the most able of the financial experts of the Japanese Government.

The functions of the Financial Commissioner at times when no loans are being floated or redeemed by the Japanese Government are not known. It is understood that exchange transactions of the Japanese Government are carried out through the Yokohama Specie Bank, a quasi-official institution, and it is possible that the Financial Commissioner may work

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in conjunction with the officials of that bank. It is also understood that the Financial Commissioner has been purchasing, on behalf of the Japanese Government, such bonds of that Government as may be offered for sale in European and American markets.

Mr. Tomita is a career bureaucrat. Born in 1883, he graduated from the Tokyo Imperial University; was sent to Europe by the Department of Finance; was successively Chief of the Bond Division, Chief of the Division of Exchequer, Chief of the Economic Bureau, and Chief of the Savings Account Bureau of the Department of Finance; administrative officer of the Bank of Japan; adviser to the Washington Conference of 1921; appointed in 1934 Financial Commissioner of the Japanese Government in England, France and the United States, and also foreign representative of the Bank of Japan.

April 20th

Saw the President this morning. Talked to him first about the tax bill and for the first time since he is back from his vacation he was interested. He said, "I have got a meeting on at 2 o'clock which has to do with taxes. (I subsequently learned from McIntyre that this meeting has to do with the financing of the party. I do not think the two mix very well even though they evidently have in the President's mind). (I am trying to be funny).

The President said that tomorrow morning at 10 o'clock he would have Pat Harrison, Doughton and myself and the other people from the Treasury. He also said he would have me for lunch. I reminded him that we had not seen him or bothered him on the tax bill since he sent his Message up and there were a lot of new things in the bill that he ought to go over. He said, "right - what about the inter-corporate dividend?" I said we had gotten his message and were looking into it.

I then told him what I had done with the Chinese, namely, that when silver reached 46.40 I sent word to Chen via Taylor that it would be agreeable to us to have them sell silver in either London or Bombay. My reason for doing it was that I wanted to test out the Chinese and see whether they were trying to rig the market in advance of making a sale to us. I asked the President if what I had done was all right with him and he said, "fine". He said, "furthermore, the more silver that they sell in London and Bombay the less we will have to buy". I told him that my policy was to try to keep silver as near 45¢ as possible and he said, "fine". I also told him that this morning silver had dropped to 20½ pence, which is equivalent to 45.55, and that, while I had not heard, I took it for granted that this was a result of Chinese selling.

I told him all about my getting mad at George Harrison this morning and he said, "something has happened to George in the last two years. I think he has gotten to be a playboy". I said I thought he had lost interest in his job. I told him how he had shoved Allan Sproul over the head of Burgess and made Sproul First Vice-President. The President said, "for Heaven's sake who is Allan Sproul - I never heard of him" and I told him that he was Harrison's Assistant.

I also told the President that when we met last week with the Federal Reserve crowd they wanted me to sell some bonds in the middle of May and I told them that I did not want to do it. The President said, "well you understand why they want you to sell in the middle of May" and I answered, "frankly, I do not". He said, "that is perfectly obvious. They want to keep you from

having a big success in June just before the Republican convention". He said, "the main cry at the Republican convention will be 'look at the financing - look at everything that is wrong with the government'. How can they do that if, just when they are shedding crocodile tears, the Treasury has a great success". I said, "that never occurred to me".

I told the President that I had another reason for wanting to sell our bonds on the 15th of June. I said, "in the first place for the past year we have confined our financing to four quarterly tax dates. Furthermore, if we could stick to this policy, which I very strongly think we should, the announcement of the financing will fall on Monday, June 1st, which will be most likely the last week that Congress is in session and I am going to rely on you to tell Congress that they cannot pass a lot of cock-eyed half-baked financial legislation during that week. Can I count on you" and the President answered, "yes, you absolutely can" and he said, "furthermore, it will be very helpful to me to have this financing pending during the last week that Congress is in session". I said, "I wanted to tell you this because I had this in mind and I always put all of my cards down face up".

The President said, "I saw Eccles for a minute last Friday or Saturday and talked to him about raising excess reserves". The President said that he told Eccles that if he was going to do it he would like to see him do it in May. The President said, "I would like to show the country that we have the guts to use the new powers given to us to stop inflation and excess speculation in the stock market."

I told the President that at the meeting we had last Wednesday I told Broderick that if he was going to do anything about excess reserves to please do it between the 1st and 15th of May. The President said, "that is fine. That absolutely checks. Have you talked to Landis - because he has charge of regulating the margins on the stock exchange" and I said, "no, I had not talked to Landis, Mr. President, but that I believe you are wrong because Landis has nothing to do with the margins - that that function belonged to the Federal Reserve". The President said, "I think it would be nice to have Landis at your meeting" and I said I would be delighted to have him. (If it didn't sound Rooseveltian I would add on the side that I had already thought of it).

I told the President that with the exception of a small issue coming due in September that by July 1 we would have all of our major financing out of the way and that from that date until after election that he could forget about the Treasury. I said, "can anybody ask for anything more" and he said, "no that that was fine".

Waiting outside the President's room to go in to see him I saw McIntyre, Early, West and the new man, Dr. Stanley High of the Washington Post. He talked to me about the President's speech and I gather he is the new ghost writer.

The President said, "wait until next year, Henry, I am going to be really radical" and I said, "what do you mean" and he answered, "I am going to recommend a lot of radical legislation" and he gave me a sort of quizzical look and I said, "you are going to be very careful about money spending" and he said, "yes, I am" and I replied, "well then I do not care how radical you are in other matters".