

DIARY

Book 123

May 4 - May 8, 1938

**Bank Examinations**

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RE: BANK EXAMINATION POLICY

May 4, 1938.  
10:30 A. M.

Present: Governor George L. Harrison (Federal Reserve Bank NY)  
 Mr. T. J. Groom (Washington)  
 Mr. W. C. Taylor (Treasury)  
 Mr. Tom K. Smith (St. Louis)  
 Mr. Joseph A. Broderick (New York)  
 Mr. T. J. Coolidge (Boston)  
 Mr. Lawres (New York)  
 Mr. R. M. Hanes (Winston-Salem)  
 Mr. W. R. White (New York)  
 Mr. C. B. Upham (Treasury)

H.M.Jr: Where is Lawres?

Lawres: Right here.

H.M.Jr: The reason I asked you gentlemen to come down is this: Some of you know since 1934 there's been continuous agitation to have more uniform examination of banks for the Federal Government, and they have again been agitating this thing, and, at the request of the President, I got together the technical men, or the actual fellows that do the examinations for the Comptroller's office and for the F. D. I. C., and for - well, that's all, because (to Mr. Upham) Mr. Paulger .....?

Upham: Paulger - yes sir.

H.M.Jr: ..... doesn't do bank examining; he does review bank examiners' reports. And I did ask Governor Harrison here because I understand the Federal Reserve Bank examines state members. So, we've got everybody, more or less.

Now they have made certain recommendations, and I am not a bank examiner, and I am not in the banking business, and I wanted to put this thing up to you people that are in this business - some in the banking business and some state bank examiners, and I understand you (Mr. White) are President of the State Bank Examiners, aren't you?

White: Yes.

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H.M.Jr: That's why I picked on you. I don't want to make a move as important as this unless it is in the right direction, and I've acted as an impartial chairman and have listened, and these people met with Mr. Upham afternoon after afternoon, and I am going to let you (Mr. Upham) read through the recommendations once, and then I'd like for you people to talk perfectly frankly, and when we get through you can have as much, or little, publicity as you want. If you want publicity you can have it - I don't care. What I want is the benefit of your advice. This is pretty important. I don't want to go off half-cocked on this.

Upham: Mr. Secretary, I made up some questions in addition to this statement which sort of .....

H.M.Jr: All right.

Upham: The three things we went in to is, first, the "slow" column in examination reports - the classification of certain loans as slow, and on that, the first two pages represent the majority agreement; that is, two of the three chief examiners; and the second one, the minority position with respect to the treatment of slow loans.

"The majority agreement with respect to the classification of loans is that the three columns in the examination report now known as slow, doubtful, and loss will be continued. Their present form, and that of the instructions to examiners as to the type of loan to be included in each of the three columns, will remain the same as at present. It is proposed to label these three columns by the roman numerals I, II and III. At the top of each page upon which this tabulation occurs, there will appear the roman numeral I and following it a definition of the type of loan which is included in the column; there will also appear roman numeral II followed by the single word "doubtful"; and there will also appear the roman numeral III followed by the single word "Loss".

Getting away completely from the use of the word "slow."

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"Where there is a recapitulation of the columns now known as slow, doubtful and loss, the same device will be used, i.e., the use of the three roman numerals as symbols with the accompanying explanation of what is included under each. As now, on the recapitulation page only the totals in columns II and III will be included in figuring the net sound capital of banks."

That is, the slow column will not be deducted in figuring net sound capital.

Now, "The minority position," one of the three, "with respect to the classification of loans in the examination report is that the column now known as 'slow' should be eliminated from the pages upon which it now appears and that provision be made elsewhere in the report, under a heading 'Loans Listed for Information or Comment', or other suitable heading, for listing, with appropriate comment, not totaled and not included in any recapitulation, such loans as the examiner feels should be set out for the information of the directors and proper officers of the bank, with the clear understanding that such loans are not being classified as doubtful or loss and are not necessarily to be regarded as criticized assets."

H.M.Jr: I'd go through the whole thing, if I were you.

Upham: All right. Then the next question had to do with appraisal of bonds in the portfolio. "The majority"- and this is the same two who constitute the majority in this case.

"The majority agreement with respect to the appraisal of bonds is

1. That depreciation in stock and defaulted bonds be classified as loss and that securities in these groups (III and IV) be listed and priced in the report of examination. (The minority does not disagree on this point.)
2. That depreciation on securities in group II and in the fourth grade of general market obligations in group I be deducted in the report in com-

puting the net sound capital of the bank, and that securities in these classifications be listed and priced in the report of examination.

- 3. That depreciation in all group I securities except the fourth grade of general market obligations be disregarded and that these securities not be priced in the report of examination."

And fourth and fifth, the three are in agreement there

"That unrealized appreciation be not allowed." and

"That a premium on bonds purchased at a premium be amortized."

Now the minority, on the position of appraisal of bonds is

- "1. That only depreciation in stocks and defaulted bonds be classified as estimated loss, and that securities in these groups be listed and priced in the report of examination. (This is in accordance with the views of the majority.)
- 2. That securities in groups I and II be not priced, and preferably be not listed, in the report of examination. A complete list of all securities, however, should be attached to the report of examination sent to the supervisory authorities.
- 3. That depreciation, other than in stocks and defaulted bonds, should not be taken into consideration in computing 'net sound capital.' On the other hand, it can not be affirmatively stated that depreciation in any securities constitutes sound capital. Therefore, the minority feels that the schedule showing a computation of net sound capital be eliminated from the reports of examination."

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And fourth and fifth are the same:

- "4. That unrealized appreciation be not allowed.
5. That a premium on bonds purchased at a premium be amortized."

Now the third proposal had to do with setting up a reserve against the securities account, and "The majority agreement with respect to the treatment of net profits from the sale of securities is that until adequate reserves against the securities account have been built up, all such profits should be impounded and be unavailable for any purpose other than to take care of losses resulting from the sale of securities."

And "The minority position with respect to the treatment of profits from the sale of securities is that

1. Estimated losses should be charged off.
2. Banks should be required to establish and maintain adequate reserves, including reserves against the securities account.
3. Banks should not be required to earmark individual items of profit, regardless of source.
4. Speculation should be severely criticized and penalized."

H.M.Jr: You fellows start any way you want and you can take your shirts off and call a spade a spade. You <sup>who</sup> have worked with me before know me enough to know I didn't ask you in here to pass the time of day, so you can start anywhere you want. You know me by now, Tom.

Smith: Well, Henry, I've been - are they afraid they'll tell - I don't just understand why they should want to lessen the information that an examiner gives a bank. It looks like they are afraid they'll tell the bank something about - tell the

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directors something about the bank, if they lessen the requirements.

H.M.Jr: You mean as to the whole spirit of this thing?

Smith: Yes. That is the impression I got from this. Bank supervisory authorities make an examination of the bank for the purpose of passing on the condition of that bank and getting the trend, as far as the bank is concerned, and they list certain information such as the slow column. There is where you get your trend - in the slow column. When they reach the doubtful column, and loss column, the thing's gone - it's too late there, but in watching the slow column you get the trend. It may be a good idea to change the name.

H.M.Jr: My idea was - I didn't want to expose you people, unless you wanted it, to the people who advocate this. If you want to have them come in - the people who are pushing on this, and have them give their side, they are available, but I first thought I'd have you come in and see me without anybody who's got something to sell. Get me? If you want the fellows who want this, and let them come in and let them sell this to you, I can get them quickly.

Smith: I've got a very definite idea about this. We run a very small bank out in the middle west .....

H.M.Jr: I thought you had fifty thousand.

Smith: That's small. I think the examiner's report - I can understand that isn't a good word. That has to do with the maturities, whereas "slow" - if the slow came up, they put - the sub-standard assets, and it is the thing you are watching. I should regret very much having that column eliminated from the report in the present - as it goes in at present in the National banking system. Now, as to the securities, I think - I don't believe you can judge an institution and its investment policies unless you see in the report all of the securities of that institution - good and bad. As I understand it here, this would eliminate any mention of the good securities and only mention the bad ones.

Upham: That's right.

H.M.Jr: Is this right?

Smith: That's correct, isn't it, Cy? I think you should list all the securities.

Broderick: That is, the second plan would eliminate it.

Upham: No, the minority proposed to eliminate it. They would prefer to see the good bonds not even listed and certainly not priced.

Smith: I think they ought to be priced, because after all, you're looking at your bank - you look at it in two ways - cash basis and ultimate payments - and if the examiner doesn't price them the banker will price them himself, but why not have them in the examiner's report?

Harrison: I thought both groups agreed that depreciation in the stocks and defaulted bonds be listed and priced.

Upham: That's right. Defaulted bonds and stocks. Of course, National banks are not permitted to buy stocks, so that is .....

Smith: The second - the minority here would not price the high grade - would neither list nor price the high grade bonds.

Upham: Governments and municipalities in the first three grades of corporates.

H.M.Jr: Can't you take that first section first. I don't think it necessarily follows, but you can divide it up, can't you?

Upham: These questions that I made more or less give the clashes that exist in these two agreements. First, should the use of the word "slow" as a classification of loans by bank examiners be abandoned? Some of them proposed that.

Hanes: You're speaking of just the word, or the whole column?

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Upham: Just the word there. There seems to be pretty much agreement on that.

Second, should loans of the character described in the instructions to national bank examiners in 1934 - those are what go into the slow column now - be listed in a column parallel to the doubtful and loss columns; or would it be preferable to eliminate this column and list such loans on a separate page?

Smith: Why don't you poll them on that?

H.M.Jr: You fellows are too quick. You know out in St. Louis you are so snappy - we don't go that fast. Are we ready for a poll?

Upham: They are pretty well informed.

Smith: Gosh, you run a bank - that slow column is what you look at every day.

Upham: Number one. Should the use of the word "slow" be abandoned?

Taylor: Why don't you poll them on each one of them?

Upham: All right. Mr. White?

White: Is this confined to yes and no answers?

H.M.Jr: No. This is very informal - do it any way you want.

White: We had a meeting of the Executive Committee of the National Association of Supervisors some weeks ago and we discussed this question of the use of the word "slow", and it was unanimously agreed that it was a bad word and we ought to try to find something better. That was about as far as we got, but I think it is pretty well agreed, among bank supervisors, that the word is in bad repute and some effort should be made to find a better word. I agree with what Mr. Smith says though, that the idea of having a column to put the banker on notice that here are certain loans which should require special attention should not be eliminated and that that idea should be retained.

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- Upham: That comes in with some of the other questions. Should the word "slow" be eliminated with that proposal. There is another proposal that takes its place.
- H.M.Jr: Would you ask the gentlemen two questions - "Do you want to eliminate the word 'slow' and if so .....
- Upham: Do you want to say yes or no to that?
- White: I agree it should be eliminated.
- Upham: Mr. Hanes?
- Hanes: I have no objection to the word "slow."
- Upham: Mr. Lawres.
- Lawres: I vote with Mr. White.
- Upham: Mr. Coolidge.
- Coolidge. No.
- Upham: Mr. Broderick.
- Broderick: I feel the same as Mr. White, provided the proper term goes in. I might bring up one point in regard to listing the three columns. It has a bearing on the word that might be adopted instead of "slow." Quite often you will find a loan will be part slow, part doubtful, and part of it will be a loss. Very often you find it that way, so you might have to list them two different places. The word "slow" has given trouble for years. In years gone by we have just used the words "special mention." I personally think it's a mistake not to give the directors sufficient information in regard to their own institution. You're fooling yourself, and you're fooling them. There is a bigger point involved than this particular question, the terms - the report is entirely too complicated. If you start off with a simplification of the examination report, you wouldn't have much trouble with the classification, so my answer is "Yes" on number one.

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Upham: Taylor, you want to vote?

Taylor: (Nods "No.")

Upham: Governor.

Harrison: I - oh, I vote yes on number one.

Upham: The second question is, should loans of the character described in the instructions to national bank examiners in 1934 - and they were, substantially, that the slow column wasn't to include slow loans in the sense of maturities but was to include sub-standard assets subject to criticism. Should loans of that character be listed in a column parallel to the doubtful and loss columns, or would it be preferable to eliminate this column and list such loans on a separate page? The minority makes a great point of putting it on a separate sheet instead of listing it along with doubtful and loss, so between the examining agency - the supervisory - that is an important question.

Taylor: Whether it should be added up or not?

Smith: That is the next question.

Upham: That's the next question. Do you (White) favor the same page or a separate page, Mr. White?

White: Well, I wonder if this memorandum makes their point of difference entirely clear. I don't quite see what the great difference is, whether they are listed on a separate sheet or whether they are listed in a column.

Upham: It goes along with the next point, which Mr. Taylor makes - whether they should be totaled and recapitulated. They feel that listing these slow loans, some of which they feel are not subject to criticism at all, is a discouragement to the banker; that immediately he goes out and tries to clean them all up and that he's too severe in requiring the loans to be paid off, and that it is a deflationary influence, and their philosophy is that we should encourage more loans rather than fewer loans.

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- Smith: You're talking about the minority now.
- Upham: I'm talking about the minority - the reason for the total to be on a separate page. It scares the bank director.
- White: Well, I think that I would be inclined to use these three columns, and put the responsibility on the examiner to make up his mind in which column a particular loan belongs. I am fearful that if we put it on a separate page that it might become pretty much of a catch-all.
- Upham: That is the majority position - that it would; that they would put every loan in the bank on that sheet, if it were in that category.
- White: It seems to me creating this separate page gives the examiner an out. I think that page would have less significance to the banker than the column would.
- Hanes: I think they ought to have the column, by all means. I think they ought to be made to state the truth.
- Upham: Mr. Lawres.
- Lawres: I am in accordance with Mr. White.
- H.M.Jr: We'll get you after while.
- Coolidge: I don't feel I am particularly qualified on that point. We have no objection to the way it is now; don't know whether they need three columns or whether they need two or four. I am not particularly informed.
- Upham: Mr. Broderick.
- Broderick: I think with the majority agreement.
- Upham: Mr. Smith.
- Smith: I am in favor of the three columns because the first column often - often it's necessary to classify part of the loan in the three columns - that's the first thing. The second place, as loans get worse, there is progress from the slow

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to the doubtful to the loss column; therefore, they should be side by side and judged very carefully.

Coolidge: I'd like to bring out a point. When they put a column - a loan in three columns, one of estimated loss - where slow loans run that you expect to be paid in full..... Now you people know more than I do about that; it's all - always surprised me to see the same loan in three columns.

Smith: You take collateral, for instance.

Coolidge: Then I think it would be totaled. If a loan is going to be a probable loss it would be in the doubtful column.

Upham: Part of it is sure loss, part is doubtful, and part is slow. There is some collateral that makes pretty good a part of it.

Coolidge: That is true of a doubtful loan. I have never been clear on that. My instinct is that the doubtful loan should be in the doubtful column.

Broderick: The trouble is in putting a loan in the doubtful column the examiners will charge off fifty per cent of it against the surplus shown. In New York it's been the custom there to estimate the loss and charge the whole thing out. In New York the doubtful column is really the slow column. In the national examining departments, and the F. D. I. C., well the doubtful column is really a loss column. I've seen commercial loans in three different columns.

Coolidge: It doesn't seem to me you're following the theory, as I see it, when you put them in the three columns.

Upham: Mr. Groom.

Groom: I favor the slow column. I think it is the most valuable column in the report.

Upham: Governor.

Harrison: I think I would favor having it on a separate page. I'd like to make a statement, if I have to answer each of these questions, that will just about sum up my position on this whole thing.

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I think the banking system is pretty much on the spot, both with the public and with Washington, in the broader sense. I think it is particularly significant that La Follette, in his program for a new party, recognizes the tremendous advancement that has been made in industry and business in adapting itself to new positions; the implication is that the banking system has not done so at all. We have frequently, criticisms from Washington. "The banking system is altogether too liquid, and is not doing its part in financing business," and, as a result, you have a demand for all sorts of collateral agencies to do the business the banking system is not doing. Why is that so? Well, there are probably lots of reasons, but certainly, one reason is - and the reason given, not so much by any of the banks represented here in this room, but by the large groups of smaller banks throughout the country - that the examinations are so strict that they are afraid to reach out and do what is necessary to finance business during and over a period of depression. It is easy enough, they think, to do it in good times.

Now where it is possible, by some alleviation of the demands of the bank examiners, to facilitate the banking system doing more of the business that politicians and the public think they ought to do, without prejudicing the position of the banks, I am not at all certain, but I do feel that there are some things that can be done to remove the fear of the banker that if he does what the people at the top think he ought to do by way of financing business, he will then be criticized by the field examiner when he comes into his bank.

But, we are making industrial loans in the Federal Reserve Bank time and again, and one of our new directors - and I'm sure he would have no objection to my quoting him - Mr. Potter - recently said, "Why isn't this bank taking care of a certain loan, instead of a member bank. It's a perfectly good loan - a three or four year loan," and the response of the junior directors - directors representing smaller banks, say "If we do we will get in dutsch with the bank examiners. Either the loan will be very promptly put into the slow column, which is recapitulated and flashed before

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the directors' minds, or it may be even put in the doubtful column."

What I am afraid of is that - and it may be an unavoidable part of the banking setup - we've got so many individual small unit banks throughout the country - what I'm afraid of is that we are getting into the position, generally, where banks, whether justly or unjustly, fear the examiner to the point where they are not doing things that properly they might do. If you assume that a bank is to finance business for a period other than just a short ninety-days commercial loan, you are always running the risk, immediately they go beyond ninety days, that you've got assets - one-year assets or two-years assets, or three-years assets, which intrinsically seems perfectly good, whose payments are current on interest, and you have no doubt it will, in a period of great depression, fluctuate in market value to a point where the bank is naturally criticized by the examiner. I don't blame the examiner. I would do it myself if I were put in to examine a bank.

It applies not merely to loans and mortgages but also to bonds. In other words, the examiner approaches the bank more or less from the point of view of what its assets are worth today rather than from the point of view of what the bank may be expected to realize from that loan if it is allowed to run its term.

I - if you will forgive me, I want to mention one experience I had that pretty well crystallizes what is in my mind. I happened to be at the B. I. S. in 1934, as an unofficial attendant, and after the meeting was over I had dinner with twelve of the Governors of the principle central banks, and they twitted me very considerably about bank failures in this country, and asked me what we were going to do about it; and I rather flippantly said, because I was on the spot, "that if I had my way I would give every bank examiner a two-years' vacation and I'd bring them over here to Europe and I'd put them in all your banks and ask them to examine them on the same basis that they examine our banks, pointing out to you that over here in Europe you close a bank

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only if you can't pay off your depositors. In the United States we close them if we can't pay off the depositors - which is a pretty good test - but also if the balance sheet doesn't balance on a cash basis."

Shock, who was sitting next to me and had asked me the question said, "My God! I never thought of it that way."

I think we are in - maybe it's an impossible task, where we expect banks to finance, over a period of time, but where we know perfectly well that in periods of severe reaction such as we've had in '31 and '32, and as we are now having, in asset values where if you really appraise everything at what it can be sold for promptly, you know you're apt to wipe out the capital of a great many gains, because - that is, assets can't be sold for cash promptly. Query, therefore, whether the job before us now is to try to do something with bank examinations which will recognize intrinsic values over a period of reasonable expectations rather than market values of today.

My comments on this, therefore - the reason I am in favor of shifting the slow to a separate page rather than to the one group of doubtful and loss is because I think it is a step in the direction that I have in mind. But what I say applies more particularly to accepting the market values of bonds during a period of depression. We took a day at random, at the end of March, and found that there are a hundred and seventy issues of railroad bonds that didn't even have a bid in bonds, many of which, banks were being forced either because of pressure by examiners, or encouragement by the examiners, or fear by directors, or concern by the officers, to try to get out of some of these lower grade railroad bonds, and the mere effort to sell five bonds might run

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the price down five to ten points the market which was as thin as the market has been.

I can't believe that that decline in market values due to forced sales by a bank - had to get rid of bonds - represents a decline of book values. So I think we've got a real job, and it isn't just a question of concealing facts. I am for a full disclosure as much as anybody, but I like to recognize other facts which I think really are vital to the whole future of the banking system because if we continue too strictly to appraise assets on a cash basis or an early cash basis, then you're going to have more and more competitive agencies set up all over this country, under the Government's supervision, or the Government capital is going to eat in gradually, which - in what might be continued.....

Broderick: George, would you favor its elimination?

Harrison: I would take the majority report here - eliminate the word "slow" and have a separate column, not to be added up or recapitulated, where the examiner can list any particular loans where he is concerned, about, explaining why he is listing it and without taking it off the first page and putting it back on some other page, merely to avoid the possible implication that it is meant as a serious criticism of that particular loan.

Smith: Read the definition of the word "slow."

Harrison: Just a minute, and I am finished today.

H.M.Jr: I would .....

Harrison: If I felt that the bank examiners and bank officers could all be infallible, that would be one thing, but we know they are not. We know that bank examiners, and again I say this with no criticism on the part of bank examiners, because I would accept the same legal responsibility that they have if I were in their place, list the slow and doubtful - a great many assets in a period of 1931 and '32 which make for the greatest earning of banks in a year of recovery.

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Smith: That is true. Absolutely.

Harrison: That's why, in periods of depression new loans in the banks terrify them in the depression, force liquidation and deflation because you are criticizing the loan when you, by records, know a substantial percentage of those in the past listed as slow and doubtful do come back and make for the secondary profit.

Smith: According to - you see, they have modified the definition of "slow" and I can't, for the life of me, see why, with this modified definition, you could every object to putting it anyplace.

White: In other words, I'd understood that the majority view here would be pretty much in accord with what you say, that it should not be classified.

Harrison: I accept that. That would satisfy me, except one fact, that there is another group - minority group - and a lot of bankers who feel that the slow group being listed with doubtful and loss are in bad company, and it's hard enough for any of us who are spending a good deal of time on our examinations to find out just exactly what the slow column means, anyway; and when you put it up before a Board of Directors, they immediately get concerned about it and there's pressure on the official staff of the bank concerning loans, that way.

Query, whether you might alleviate that by putting it out of bad company and putting it on a separate list. I don't think you lose a thing. You don't fail to disclose what is in your mind, but you do avoid implications which I don't think you intend to make.

Hanes: Am I right - do I understand that the length of time of loans - three or five years, providing you have a definite amortization - if the loan runs five years with no amortization, it would be listed as slow?

Upham: It would be a sub-standard loan.

Hanes: If they aren't watched, and watched carefully, you certainly are going to wreck a lot of banks.

Harrison: It's just a joke - taking this present bond market as a measure of value.

Hanes: I agree with you, Governor; yes.

Harrison: And I think it is also approaching a joke when in a period of severe depression, when values go down, as in the last six months, banks should begin to throw over in the doubtful item, loans that are effective, but which, with any chance of recovery at all, have a fair chance of coming back, and the risk of putting them in the doubtful column today is that you concern the directors and you begin to make pressure on their part.

H.M.Jr: Excuse me. I'll be back in a minute.

Harrison: I didn't mean to drive you out, Mr. Secretary.

Hanes: You take a loan that's been running five years in a bank; they continue letting it run five years more, and it is - in a great many cases it will materialize into a loss. Where they can look - that means nothing - pay no attention to it.

Harrison: I think it is caused by the fact that our banking system permits a commercial bank to accept both commercial demand deposits and savings deposits, with pressure of certain groups to apply savings deposits in long-time assets, and another .....

Smith: Why don't you go on further, and then for the Government to keep - (to reporter) don't put this in there - keep the rate of Postal Savings up to two per cent.

Upham: Mr. Taylor says that this leads into a good many other .....

Coolidge: I don't see any point at all to have a slow column unless it is intended to put into the bank, loans that it .....

Smith: Read the definition of it there.

Upham: In 1934 they had a conference here on this slow column, and following that, this went out to all national bank examiners:

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"It is evident that in some instances reports of examinations contain some items classified as slow by the examiner which by reason of ultimate collectibility may properly be eliminated. This is particularly true with respect to loans secured by real estate, and is also true as to other classes of loans. To illustrate:

1. Loans secured by mortgages on real estate which are in good standing and which are reasonably well protected whether conforming to Section 24, Federal Reserve Act or not should not be listed by examiners as slow.
2. Loans which are reasonably well protected as to ultimate payment by reason of the sound net worth of the maker and/or endorser, even though their assets or a large part thereof may not be of a liquid nature under present conditions, and loans which are reasonably well protected by collateral or other security of sound intrinsic value but which due to present or local conditions may not be saleable at this time, should not be classified as slow.

"It will be understood that the foregoing will include industrial, agricultural, commercial and all other classes of loans.

"In other words, it is believed that under present conditions the examiners should only list as slow loans which in their opinion will become doubtful or worthless in whole or in part unless placed in proper bankable shape by the bankers.

"The examiners when classifying loans as slow should state briefly the reasons for such classifications but should bear in mind that the responsibility for determining and taking such action as may be necessary to place such slow loans in proper bankable shape rests entirely with the bankers. The examiners, therefore, should refrain from instructing the bankers as to what course they should pursue with their customers whose paper is classified as slow."

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Now, since that time, I think you have, on the third page there - I don't know whether it's included in those or not.

In 1934 twenty-seven per cent of the loans were classified as slow, and it is now the end of 1937 - below ten.

White: Making progress.

Upham: There have been some difference of opinion as to just how significant those figures are.

Harrison: How much has that been responsible for the depression?

H.M.Jr: (Returns to room.)

Smith: Mr. Secretary, Mr. Upham just read the definition of "slow" as they fixed it in the Comptroller's office.

H.M.Jr: Yeah. Everybody interested in the strong bond market? Very slow, just a little bit off at this time. Very strong bond market.

Smith: Now in the light of that definition, George, is there anything listed under those instructions that shouldn't be listed prominently so - so the bank should have it before them?

Harrison: I think it should be.

Smith: What difference where they put it?

Harrison: I think it makes a difference. I don't feel very strongly about it, but I do think it is the emphasis which is brought to the attention of the officers of the bank, and more particularly the directors of the bank.

Smith: Mr. Secretary, Governor Harrison raises the point that time shouldn't be an element. These instructions issued by the Comptroller in 1934 remove that element, and they say, "Don't list anything unless it is headed for the doubtful column."

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- H.M.Jr: May I just say this. I got this after listening to George Harrison. I think he's raising a very important question as to how the Federal Government, through its bank examiners and agencies should look at loans - loan trends - let's call it that. But I gravely question that problem could be solved by whether we put it on one page or two pages.
- Harrison: That is purely why I related what I did.
- H.M.Jr: Doesn't help - I mean, if a Board of Directors of a bank - I mean, would really be influenced by the fact that that is removed by putting it on another page, that doesn't get to the heart of the thing you're raising.
- Harrison: No, and I said - "related to everything, more particularly ....."
- Smith: But this definition gets to the heart of the thing, though.
- H.M.Jr: Check.
- Harrison: Bank examiners ought to read that once a week.
- Smith: That is up to the supervisory authorities to see that they do that.
- H.M.Jr: Did Cy Upham point out what happens in the slow column?
- Smith: Yes.
- White: Mr. Secretary, I'd just like to make one comment. I assume what we are aiming at here is better improve, or to further extend credit and make it possible for people to, who are more or less on the borderline, who probably should be allowed to have credit, to get it, and so we want to take the burden off the bank director. I don't know whether Mr. Broderick will bear me out in this or not, but I would say that ninety per cent in number, or perhaps ninety-five per cent, of our banks in New York, don't need any encouragement to take a chance when the possibility of a loan comes along.

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Now that other five per cent in number of banks represents much larger funds, but that five per cent are not inhibited from making these loans on account of what the bank examiner is going to say. They are concerned there about their dividends to stockholders and they are turning the loans down just because they don't want to take a chance with them, and anything we do here to let up on the examination doesn't concern that volume of credit at all.

H.M.Jr:

May I ask you - I don't think your definition will quite describe what I had in mind. Perfectly frankly, since I've been here, I've not, in any way, injected myself into this question of bank examinations; I've kept entirely out of it myself. In the first place, legally there is a question; it is just how much of the responsibility I have in the Comptroller's office; whether he is responsible to the President or the Treasury. The F. D. I. C. is responsible to the Treasury. It's a great question, as to my responsibility, but when there is a question as to my responsibility, I don't go into these things until the President asks me. I mean, my back yard is big enough without trying to play in somebody's else, but he has asked me to do this.

Now I am trying - of course, we've all had this depression in mind; we've all got the unemployment situation in mind, and we're all trying to do everything we can to get the train back on the track. But at the beginning what I am trying to do here, is for the first time really just take some of what you might call rather minor criticisms which are being agitated by certain of the lending agencies here in Washington - of other lending agencies in Washington, you see? I mean, this is what you might call an inter-family scrap, and I felt that asking you people - for the hour we've spent together so far has been most useful to me. I hope it has to you. If you want to meet some of these fellows - they are just shouting at each other.

Harrison: Well, Mr. Secretary.....

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H.M.Jr: Just a second. And, as you say, if out of this thing today - I'll take just as long as you people will give to it - if we can get a certain understanding, and then I told the President - this is what I recommended, and he approved it - we'll be making a start, and then if I had the backing of you people - publicly wouldn't be necessary, but just morally, I mean, I'd be willing to go the mat with the agency which is stirring this all up, you see, and out of this may come, not this session, a final recommendation - a thing which has been going on here for four or five years - and what agency should have bank examinations. I mean where should it rest, you see? I don't think there is any question that we don't need both the F. D. I. C. and the Comptroller's office doing bank examinations. Should it be in the Treasury; should it be outside the Treasury? My mind is entirely open. Out of this might grow a recommendation - I don't mean today - and amongst other things, I mean I've learned - I suppose I should have known it - the Federal Reserve Board really has nothing to do with bank examinations. Isn't that right?

Harrison: What was that?

H.M.Jr: The Federal Reserve Boards have nothing to do with bank examiners.

Harrison: I didn't get all your question.

H.M.Jr: I said the Federal Reserve Board - your responsibility is state member banks. Right? As far as examination goes? The Federal Reserve Board has no responsibility as far as bank examination goes. They can't issue any laws on banks. If for instance we agree on this thing I'd have to put it up to you, for instance, in New York, and say, "Will you go along with us?" The Federal Reserve Board can't order you to do this.

Harrison: I don't know whether they can, but they do.

Smith: That's good.

H.M.Jr: Well, I've been learning a lot, and I just wanted to say that for the moment I am just looking at a very small segment. I'm going to start in a very

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small way, and if we can get just one or two little things - I am just going to take one step at a time, because I don't want to do anything, certainly, to shake anybody's confidence. On the other hand, this always blaming the bank examiner, I think, is silly. I get an enormous amount of mail - I get very little from the examiners. I get a tremendous mail upstairs, and I get very little from bank examiners; and, I mean, if people would just thrash it around here in Washington to find a go. Today is Labor Relations Board; next week it may be somebody else - but they are just thrashing around. A couple weeks ago it was bank examiners. I want to satisfy myself how much responsibility really rests with the banks. I hope to get to what you said. I am just going to go very very slowly.

- Coolidge: My hunch is that many many bankers tell customers they won't make a bank loan because the bank examiner won't approve it, when the real reason is they don't want to make it themselves.
- Smith: And when they want to collect it they say the bank examiners are riding them.
- H.M.Jr: Now, can we go ahead a little bit?
- Upham: Third, is it objectionable to total the criticized loans, other than doubtful and loss, and show them on the recapitulation page?
- Mr. White. Is it objectionable to total them and recapitulate them?
- White: I have never been an examiner either. It seems to me this is more or less a technical question. I don't see that it's very important.
- H.M.Jr: Why did they make it, Cy?
- Broderick: Why, it's very important.
- Upham: For the same reasons.
- Smith: It's very important that it should be totaled.

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Broderick: No, I don't see any reason for them to be totaled. They can total them if they want them. The idea is to bring attention to those loans which I call "special mention" loans, or loans listed for information or comment, and then the Directors or the officers could go right down and list, or at least make a total of those they wanted. In that list the number of loans are there for different reasons. Some, just a comment there, intended for the information of the officials. Why put a total down for all those loans which they have mentioned for some particular reason?

Smith: Mr. Secretary, it all gets back to "What is the definition of the loans?" Let's get away from the word "slow." If you are going to put in this column, loans of such a character, then it is important that you know all about those loans; that you know the total as regards the total assets of the bank, and everything else, because whenever a bank has ten per cent of its loans in that column, then they'd better get busy. This discussion always gets off to "special mention" and things like that. I think if you get a definition here today of loans you are going to put in column one, then you've served a purpose, because until that is done, you get off on sidelines and that only includes the dangerous loans. You never could ask - there could never be any circumstances under which a bank could be asked to make a loan which would find itself in that column, because the elimination - time and everything else .....

Broderick: Mr. Secretary, I think it is well for us to keep in mind just what an examination report is. It isn't a statement of facts; it's the opinion of an individual as to the appraisal of the assets. It is the opinion of an individual as to certain loans that have been made there. You get two examiners going in one bank, and you'll have an entirely different opinion as to the assets. As a rule they are close enough to give a fair opinion as to what the condition of the bank is. I think it is perfectly proper for them to have - I like plan number one better than plan number two. It is - why they should be totaled, I don't know. In the first place, it would be impossible to get an examiner - unless we do

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as Mr. Harrison says here, for a review of the examiners every week as to what the definition of 'slow' is. He's going to put down in that column loans he's got hunches about, but why is the total going to be a red flag to the directors right along? I know a little bit on all sides of this question. I've seen bank directors get excited; I've been on Boards where they did get excited about some foolish remark made by the examiner. They take it as the gospel truth right now. If we can eliminate some of these figures, it is just as well, but I think the big flag is the total, whether you call it the slow column, special mention, or call it number one column. They say, "My, it's a criticism of ten per cent of our loans." I don't think it's necessary. That is my personal feeling, and I am strongly in favor of it being omitted.

Upham: Mr. Hanes, do you think it is objectionable?

Hanes: Personally, I do not.

Upham: Mr. Lawres.

Lawres: It would seem to me if it's worth while having a column there you might as well know how much of those kinds of items are in it. On the other hand, we might be adding up two or three different kinds of items, like adding horses and cows and trying to get a single unit.

Upham: Mr. Coolidge, is the recapitulation objectionable?

Coolidge. I feel so slightly for it that I'd give way to anyone that objected strongly to it. I don't think it's objectionable, but if other people do .....

Upham: Mr. Broderick thinks it's objectionable, and Mr. Smith does not. Mr. Broom.

Broom: I think it should be recapitulated. I've watched the trends, and I believe it should be.

Harrison: I think Mr. Smith is right. If you're making a clean-cut definition that it is one particular kind of loan, there's no objection recapitulation, but if you are going to call it slow, or you have

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a special comment column there where you can include more variety of things, then if you do that, then I would not be in favor of recapitulation because you are adding up different categories of assets.

White: May I make one further comment? I think I agree, in general, with the view taken by Mr. Broderick from this angle; that the thing the banker is most concerned about is the recapitulation page isn't ....., and the percentages that stand out there may be disturbing, whereas the same point can be made on another page, so far as giving information to the directors is concerned, without waving a red flag.

H.M.Jr: Do you have an agreement?

Upham: Well, no. Three of them think that recapitulation is all right; one of them objects to it, and four are sort of on the fence.

Harrison: Judging by the way it is done, realizing the facts of the situation regardless of the definitions, I would object to it because I don't think they do follow the definition so strictly as to have one kind of item in one column.

Janes: Under that, Governor, if you couldn't total it up you would not be in favor of setting up any sort of reserve against the slow ones?

Harrison: I think I probably would not, because I think if they got to a point where they have to have a reserve against them, I would throw them in the doubtful column anyway. I think you and I agree in substance to what we are after. If it's bad enough to have a reserve, I wouldn't put it in "slow."

Upham: Number four. Should the loans described in the 1934 instructions to national bank examiners be subjected to criticism at all? That is, these loans that we now agree should be listed. I guess everybody thinks they should be listed, either in the column or on a separate page. Do you think they should be criticized at all, Mr. White?

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- White: I wouldn't want to attempt to express an opinion on that. I don't know enough about what kind of loans the national supervisors had in mind there.
- Upham: Mr. Hanes.
- Hanes: I think absolutely they should be listed. I think any banker will tell you the majority of losses gets into a bank, lay there five years - ten years, and suddenly you wake up one morning and find they've gone sour on you.
- White: He didn't say listed - criticized.
- Hanes: If they have been there five years, or an abnormal length of years, without reduction, they should be criticized. Any amortization?
- Upham: I think, if I may, I will withdraw that question and go on to the next. Five. Would good bankers be deterred from making good border line loans by the inclusion of the slow column, renamed? Now that implies, are they now being deterred by making those loans, and if you rename it - don't call it "slow," but include what bank examiners are told to put in, would good bankers be deterred from making good loans?
- White: I think we can get an excellent answer on that by asking two bankers in the circle here.
- Smith: In the first place, good loans won't get in that classification there.
- Upham: Well, the minority feels very strongly, and Governor Harrison has seemed to indicate ....
- Smith: But he is talking about a broader definition than is now observed either by the Federal Reserve Banks or by the Comptroller.
- Upham: Well, you think you can't say yes or no to this question.
- Smith: I can answer it, but, do the supervisory authorities say yes or no?
- Upham: Mr. Paulger says there's no question about that - they would; Mr. Folger and Mr. Nichols say they would not.

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- White: I think it would be easier to answer the question if in the first term "good" we had "border line" there. I mean the second place.
- Upham: Well, change it to that. Would good bankers be deterred from making border line loans?
- Smith: That makes a different question.
- White: I think that might very well be a factor then.
- Upham: Mr. Hanes.
- Hanes: I would say "No."
- Upham: Mr. Lawres.
- Lawres: I couldn't answer that.
- Coolidge: I could only answer it from what I see. The bank examiner - his securities specifications may make him stop buying bonds, but that is not included in buying bonds.
- Brocerick: No.
- Smith: No.
- Upham: Mr. Groom.
- Groom: I am inclined to feel that if I felt the bank examiners were going to list a new loan I was going to make as slow, which would be subject somewhat to criticism, it might have some effect on my decision.
- Harrison: Well, I should think it's a question you can't answer yes or no. I think it is - there's no doubt it's true though, that some bankers, good or indifferent certainly would be influenced by a large recapitulation of the slow column, and I think as long as you have it with the significance that it's now got, they ought to be influenced.
- Upham: Well, these are the points that the bank supervisors made.
- Harrison: Well, my idea is, it's a rotten question.

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- Upham: These are the questions that grew out of a conference - the things they alleged. It is not my list of question.
- H.M.Jr: Cy, have you covered everything?
- Upham: The fifth question. Are bank directors alarmed by the slow classification practice and is it a deflationary influence?
- Those are the charges made by the minority on this point. Are bank directors alarmed and is it a deflationary practice to have this column  $\frac{1}{2}$  column number one.
- White: First off, ~~we are~~ considering column number one under a sweeter name, aren't we?
- Upham: That's right.
- White: I don't think it is.
- Hanes: I should say that probably all along probably they are alarmed, but they probably should be.
- Upham: Mr. Lawres.
- Lawres: I don't know whether the bank directors are alarmed or not, but I don't think this column would have a strong deflationary effect.
- Coolidge: I would say they are alarmed if the column is excessive - and they should be alarmed under those conditions, but a normal column - no.
- Broderick: Border line banks - yes.
- Smith: I agree with what Mr. Coolidge said. I think it's like your blood pressure. When your blood pressure gets too high you are alarmed. When it's normal you don't pay a lot of attention to it, but when it goes up you do get alarmed.
- Groom: I think they'd be governed by the trends; if the trend is more slow, I think they'd become alarmed.
- Harrison: I should think they are, no doubt, alarmed; especially by the recapitulation. If the definition were strictly in accordance with the 1934 ruling, then

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I think they ought to be alarmed, but the way it is actually done, I think there is less reason for them to be alarmed.

Upham: Those are the only .....

Hanes: Mr. Upham, may I say this? I am taking it on the basis that this slow thing is going to be liberalized.

Upham: As .....

H.M.Jr: Now before you go on, the next thing I want is a little information. Supposing we change this word "slow." See? When I say "we" I mean the Comptroller's office and the F. D. I. C., and that will include everything except state member banks. Supposing the Comptroller's office and the office of F. D. I. C., gets out new regulations on the word "slow". That takes in everything except state member banks.

Harrison: It would include state member banks, as far as F. D. I. C. is concerned.

Upham: Not members of the Federal Reserve System.

Harrison: Well, they are accepted by members.

Upham: No, I think not.

Hanes: They take the Federal examination.

Harrison: They do when they want to.

Upham: Only in a very exceptional case.

H.M.Jr: Let me put the question in another way. If we define the word "slow" - the Comptroller's office and F. D. I. C. unanimously - what banks in the United States would they not reach?

Hanes: Uninsured state banks. They are a very, very minor number.

H.M.Jr: Are there many of those?

Hanes: Very few.

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- Upham: They wouldn't reach state members or non-insured banks.
- H.M.Jr: That is what I had in mind - I'm coming back again to you (Harrison) - one of the reasons you are here.
- Harrison: To answer your question literally, it would not affect state member banks, either.
- H.M.Jr: Let me just .....
- Hanes: The state member banks are insured, so the F. D. I. C. would have control of them.
- Upham: The F. D. I. C. doesn't examine them.
- Hanes: It has a right to.
- Upham: But it doesn't.
- H.M.Jr: The F. D. I. C. and the Comptroller gets out a new ruling on the word "slow." Now who would - say we don't want to go along with a group - what group would be left outside?
- Taylor: State member banks.
- Smith: A thousand banks.
- Taylor: State member banks, plus uninsured state non-member banks.
- H.M.Jr: We can't do anything with those, I know, but am I not right, that the Federal Reserve - we don't want to change - we'll continue - have we no authority?
- Harrison: We've got authority to examine both national and state member banks. We have the same authority to examine state and national member banks.
- Broderick: The Reserve Board has the authority.
- Harrison: The Reserve Board has the authority. The Federal Reserve banks do examine state member banks, but not national banks. The tests and formulae that the Federal Reserve banks apply in their examinations of state member banks are those prescribed by the Federal Reserve Board, for the sake of uniformity

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throughout the twelve districts, and my personal concern is, as long as that is the only examination we are conducting, the best thing is to get the Federal Reserve Board in on this, as well as the other two.

H.M.Jr: They are in.

Upham: They are the minority in these first two.

H.M.Jr: In the first place they are the minority, and in the second place, I make the recommendation to the President and he says, "All right, see that it's carried out." I go to the Comptroller and to Leo Crowley and tell them, "This is what you want," and tell them, "Let's do it." See? They say, "Well, we'll do this thing." And the minority happens to be in this case, let's say, state member banks. Now you fellows rule, "No, we won't change the way - we'll continue to use the word 'slow.'"

Harrison: They could.

H.M.Jr: What?

Harrison: They could.

H.M.Jr: They could do that.

Harrison: That's right.

H.M.Jr: And then the state non-member banks could take the same position if they wanted to.

White: Yes, and the state commissioners could, if they wanted to, which would mean two tests would be applied to state member banks.

H.M.Jr: What I'd like to add is this. Let's say, again, on this one point before we put it in, would it be a sensible thing to submit it to the state commissioners and see whether they'd go along - to see whether we had one thing. Would they be more apt to submit it .....

White: It's really already been submitted to them. I have sent suggestions along this line, that's involving a change of the term of the classification "slow."

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- H.M.Jr: But supposing we define it into three new categories and say, "This is what has been decided on. We'd like to put this up to you and get your suggestions," and so forth, and so on. Have you people got an organization through which you can channelize this thing?
- White: Yes, we can.
- H.M.Jr: I mean, if something is agreed on, we can refer it to the State Bank Commissioners, would it be a matter of days or weeks or months before we could get an answer on that?
- White: I think we could employ different methods, depending on the demands of your time, and get an answer to you shortly, if necessary.
- H.M.Jr: With the Federal Reserve System we could get a thing like this almost uniform with the exception of non-insured state banks - we couldn't refer them.
- Taylor: Oh, that would cover them.
- H.M.Jr: That would cover everything? As far as I know I don't think anybody's ever tried to get everybody agreed on one thing, and if we could even get them to agree on one word, I think it would be well to do what George Harrison said - to take some of the curse off the bankers - some of the blame. How would I go about acting for the President to get the banks - state, Federal, and all these categories - to agree on one thing?
- Broderick: Mr. Chairman, I think you know Mr. White is the President of the National Association of State Bank Supervisors. He has the Executive Committees in the different parts of the country.
- H.M.Jr: Yes. That's why I invited him here - to get him, in that capacity. You, as an insurance banker - and savings banks.
- Broderick: He's my boss, now, you know.
- H.M.Jr: I think we've got everybody represented here - all kinds of banks. That's what I tried to do.

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Now, you're going to do the next one?

Upham: I think these other questions are a little easier, Mr. Secretary.

H.M.Jr: Good.

Upham: "Should the list of securities in a bank's portfolio be listed by examiners in the examination report?"

White: I say yes.

Hanes: Yes.

Lawres: Yes.

Coolidge: Yes.

Broderick: Yes.

Smith: Yes.

Groom: Yes.

Harrison: I am a little more hesitant to make answers for the record right now, because I find the minority here is my boss, but .....

H.M.Jr: How do you know?

Harrison: Well, you just told me.

H.M.Jr: Well, you're sitting here - you're here as an individual. There's nothing public here, George.

Harrison: I'll put it this way. I think that all securities should be in a report, and I am not prepared to say where they should be, but I don't think there is any question but what they should be in the examination report.

Upham: "Should all or a part of the securities' list be priced in the report?" I am going to change that to this: "Should all of the securities in the list be priced in the report?" That includes Governments and everything else.

White: You mean priced on the basis of .....

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- Upham: Market.
- White: If there be one. I think that saves the banker a little time.
- Upham: Mr. Hanes.
- Hanes: ?
- Upham: Mr. Lawres.
- Lawres: You mean at a time like the present?
- Upham: Yes, any time at all - all times.
- White: Merely of giving it on the form as of the date of the examination.
- Coolidge: Yes, with the possible qualification that they should not attempt to determine it when there is not - I've seen them offer priced, slow securities that are unsaleable, at very low prices. I don't think it's warranted, but with that exception, I agree on it.
- Broderick: Yes. I'd like to say though, in explanation, I am inclined to believe that it should be on a so-called "investment basis," as well as the market price, and it would then be by the investment basis - but to have the market price there so the directors of the bank are being fully informed as to the condition of the bank in the event they were forced to sell any of their securities.
- Smith: Yes.
- Groom: Yes.
- Harrison: Well, I - if by "price" you merely mean sticking in, for information, a market value as best you can get it - yes. But if that is to be an indication of how the item is necessarily to be treated, I would say no. I don't object to putting it in, as a matter of information.
- Upham: That's the only suggestion.
- White: That was the basis of our answer.

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- Upham: "Should all of the depreciation in securities be deducted in computing the net sound capital of a bank?" Perhaps the fourth question ought to come first, because it's .... "Should the net sound capital of the bank be computed in the report?"
- There's a very great difference of opinion there. I think it shouldn't be figured at all.
- White: Well, I .....
- Upham: Let's make it four - "Should the net sound capital of the bank be computed in the report?"
- White: Well, I think if you're going to make the examination it certainly should be.
- Upham: Mr. Hanes.
- Hanes: I don't think you have an examination without it.
- Lawres: It should be computed.
- Coolidge: It should be.
- Broderick: Yes.
- Smith: Yes.
- Groom: Yes.
- Harrison: Only if you accept my basis of computation.
- Upham: Then, the third question - there is a difference of opinion as to whether the depreciation in group two, and in the B aa's, which is the fourth group - whether the securities should be deducted. No one proposes to deduct the depreciation in Governments, municipals, or the first three grades of corporates, but as to the fourth grade of corporates - that is, group two, which is below B aa bonds - that are not eligible for purchase in banks - should the depreciation be deducted in computing the net sound capital?
- Hanes: May I ask one question? Number four of the majority agreement with respect to the appraisal of bonds says that unrealized appreciation be not allowed, and that means it be not allowed in figuring

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depreciation on one side.

Upham: That's paper profit.

Hanes: You must take the depreciation, but you're not allowed to take the appreciation.

Upham: That's right.

Hanes: I think it's altogether wrong, myself. I - if you've got your Governments and high class bonds showing an appreciation of a billion dollars, and show a depreciation on the other side, of a hundred million dollars. You throw away .....

Upham: This is only group II, and the fourth grade .....

Hanes: I said it's only unrealized appreciation that will not be allowed.

Upham: That's what it means. You can't use unrealized appreciation, but .....

Hanes: You're taking unrealized depreciation.

Upham: That's right.

Hanes: I think it's got to work both ways.

White: On this question that remains here - I would favor some middle ground between the views taken by the majority and the minority here. I don't believe the majority goes quite far enough. They recognize the principle that the market is not fair with respect to the high grade securities, but they don't carry it into the lower grades, although they are not in default. Why are we using this method on high grade securities, or are we using this method because we see that the market is not a fair basis of evaluation? I think it is the latter. I think it should be so. I think we should allow some basis different from the market even, with respect to C bonds on default. I would go with them and put them in at market, but I'd allow some write-back with respect to securities which are not in default.

This is based on the assumption that some such valuation as this is necessary under depressed business conditions to prevent bankers from becoming demoralized and giving up the ship or

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causing bank supervisors to close banks.

- Taylor: Well, Cy, isn't the first question that Mr. White asked really the important part of that? In other words, it's a type of sanction to keep them out of low grade bonds at all times. I was wondering - that was the impression I got - that it would work out.
- White: I think the point of view is wrong. I don't go along with that point of view. I think you've got to take the other into consideration too; you've got to bear in mind, here are a bunch of bank directors - perhaps they happened to get into a bunch of bonds in the B grade, and they fell into the C grade. Suddenly they began to fall off. Are we going to encourage that banker to continue, or are we going to notify - give him the benefit of this fair estimate valuation, with the result that he throws up the guns?
- Taylor: I was merely explaining what I thought the intention of the group was.
- White: Yes.
- Taylor: Rather than commenting on it.
- Upham: It's to encourage good bonds in banks. We had one bank the other day that had seventy-five per cent of its portfolio - seventy-five per cent - in group I bonds.
- Harrison: Another example of my ignorance - what is this group I and II as they use it here?
- Upham: Group I includes Governments, direct and indirect; good municipals and corporate bonds - what they call general market obligations of the first four grades, depending on the rating system of those, including B aa.
- Harrison: And II?
- Upham: And II is below B aa.
- Groom: Sub-standard.

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Harrison: Haven't you got this situation. The Comptroller of the Currency says you can buy four grades of bonds. As to the first three grades I am going to use my judgment in appraising them, and as to the others, I'm going to waive my judgment and I'm going to accept the judgment of a blackboard over here which varies, not in accordance with the worth of the obligation at all, but in accordance with purely temporary or peculiar panicky conditions. I think it doesn't make any sense. I think if he's going to authorize banks to buy bonds in four different categories he's got to treat them on the same basis of appraisal. I don't see how we can avoid that. Therefore, I think the minority report is stronger and much more consistent, and furthermore, the majority covers - you say you've got to take your depreciation in the four grades of bonds, I told you, you could buy, but I'm not going to allow you to take an appreciation in any grade.

He's interested in both the appraisal of the bonds he authorized you to buy and, second, in the treatment of the appreciation and depreciation.

Hanes: It just seems to me the whole thing is screwy. When you take the Government market today, where we have a difference of opinion. In my mind it's too high. On the other hand, you've got railroad bonds which are terribly low - way down - too low. We're not troubled with railroad bonds, but you take a tremendous appreciation in it; you must set up a depreciation of three hundred thousand dollars to take care of this other thing. It seems to be the only fair way to do it - is to take the whole and say, "Now you have your net results, which are so and so - either appreciation of so much, which you can disregard, or else you've got a depreciation.

Upham: Perhaps it would be fairer to make that third question this: "Should the only depreciation used in computing that net sound capital be the depreciation of defaulted bonds and stocks?" When you compute net sound capital, include only the depreciation on defaulted bonds and stocks.

Hanes: That would be better than what you've got now.

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- Coolidge: I'd be - I have no particular objection to the stocks and the defaulted bonds.
- Upham: There is no disagreement on that.
- Coolidge: But I would object to taking a market price, based on disturbed or panicky conditions of any paying bond, and I'd also object taking any valuation below the market price of the entire group. Now if they devise some special scheme of having a market price on a certain debenture bond that averaged over two years, or something we would have a different problem - but that's not put up to us.
- H.M.Jr: Do we approve of this?
- Upham: I'd say no to that.
- Hanes: You may be called to put up only a reasonable bond account today, and utilities and railroads may be a half million dollars of reserve - maybe six months from now the public has changed its mind about them. While I will say for the minority report on this that it is at least consistent between the matter of loans and the treatment of securities, because apparently the minority would encourage the making of long term capital loans, and at the same time, it would permit the man that makes that advance of credit to the purchase of credit bonds to continue to carry them at parity. I think it is pretty difficult to reconcile those two points of view.
- Broderick: Very difficult to reconcile them.
- White: Of encouraging these possible border line loans and at the same time putting the screws on everything but the highest grade of security, .....
- Coolidge: ..... merely a short maturity of Libbey, McNeil - unsecured, with no worries. Now, if you'll mark that bond down to sixty, why -- but it's just all wrong. That would probably be a third grade bond.

Harrison: What I am afraid of, frankly, Mr. Upham, is, as I read the report of the majority, there is too much satisfaction, as I see it, with the situation as it is, and not enough "mental itch" to see whether something can't be done to improve the situation. I think at least the minority is trying to make a step forward, which the majority doesn't want to consider at all, as I visualize these things. And I don't think any of us can be completely satisfied with the way things are; even if we only have to answer the criticism that exists, whether it is just or unjust, we've got to do something, and I don't think you can get away with doing nothing, provided there is a constructive course, different from the present, and I think there is. I think Mr. White's comments about the proposal of the majority for valuation of bonds are completely sustainable.

The attitude of the banker may be illustrated - an examiner going into a bank, for instance, and threw out a loan - a personal loan - to a man which was secured by unlisted bank stock. The banker was sore, but the examiner was insistent; the banker goes across the street to another bank and tells of the experience he's had. The second banker gets busy and goes through the whole portfolio and gets out those similar loans of his, returns the collateral, and he isn't criticized on a single loan.

H.M.Jr: Could I make a suggestion, George? I've got to stop at twelve thirty; it's now a quarter past, but I'd be more than pleased to meet with you gentlemen this afternoon, if that suits you people.

Harrison: Mr. Secretary, I think it would be helpful if you could give some of us an opportunity to mull over some of these things before being definitely committed.

H.M.Jr: I tell you what - I didn't - I didn't even tell these people - I didn't know whether this thing would run over until tomorrow. See? So I told them I wouldn't see them until Friday morning, figuring that you people, getting this for the first time, undoubtedly, would want to mull the thing over and talk it over, and this isn't one of these times where anybody's pushing me; that we've just got to do it.

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I don't want to do anything unless it's going to be constructive. What would be your pleasure, gentlemen? We've got two more questions.

Upham: Well, they can be boiled down into two more. There are several.

H.M.Jr: I don't want to rush through this. Are you so you can come back this afternoon?

Smith: I've got to leave at five-thirty. Until then I am at your service.

H.M.Jr: We can put a room at you people's disposal, and if you want to talk, be back here at three, say, or if that is too soon, four.

Hanes: Three o'clock is all right, I think, sir.

H.M.Jr: What do you think - have you got some more ball game tickets?

Harrison: No.

Smith: Mr. Secretary, I may seem a little quick on the trigger, but I live with the examiners out home, the same as Bob (Hanes) here. We are in this game, and I think we are both ready to talk at any time.

H.M.Jr: Well, I - I mean, I have to stop now, within a few minutes, and I don't want to rush anybody.

Hanes: Would two-thirty be too soon after lunch for you?

H.M.Jr: Three would be a little bit better.

Harrison: Mr. Secretary, could we all meet as a group somewhere in the Treasury at two thirty anyway and then meet with you at three?

H.M.Jr: Let's do that - Taylor, what's your room - ?

Taylor: You can use my room. That is 272.

H.M.Jr: 272. You can meet there at two o'clock if you want to.

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- White: We may get up our own majority.
- Taylor: I can give that to them right now and they can have it all afternoon. I've got a meeting in there at four.
- H.M.Jr: Well, they'll come back here at three then. Well, are you going to adjour to Taylor's room and come back here at three; is that it?
- Harrison: We'll be back here at three.
- Taylor: You can have that right now if you want it, or wait until two-thirty. Whatever you say.
- Upham: It's about lunch time now. Let's meet there at two-thirty - two if anybody gets there.
- Taylor: I'm not sure whether I'll be back by then. I've got to go back to another place. I don't think I'll be back until three.

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2:40 P. M.

(In Mr. Taylor's Office)

Broderick: I do think the word "slow" itself is like this depression; it's just like this depression - it's gaining momentum. We've heard so much about slow loans in the papers and public press, and the so-called spokesmen for bankers and business, that the bankers are scared of the word "slow." If that is so, let's change the word.

Taylor: I gathered it there was complete agreement that the word should be eliminated, Joe. So it really gets down to whether you have three columns. If you have three columns, should you have them on the same page, and should you add up column number one?

Broderick: I see. That's the whole story.

Smith: Now, on that score, I think that the bank should .....

Broderick: May I say one thing? There has to be a very clear and distinct description of what Number One means and what Number Two means, and what Number Three means.

Smith: Now then - Number one will be unsatisfactory loans; number two will be more unsatisfactory loans - loans that are more unsatisfactory than number one; and number three will be loans that are more unsatisfactory than those in the number two column. In other words, they are all unsatisfactory loans, in all of the three columns.

Broderick: No, I don't think so. Number one column may not be an unsatisfactory loan. It may be a loan upon which they are making comment.

Smith: No, if you are going to define this as an unsatisfactory loan, according to that definition .....

White: I agree with what Mr. Coolidge said - that that word "unsatisfactory" is about as bad as the word "slow."

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Coolidge: I think it's stronger. I expect them to leave off a lot if they use that.

Broderick: No. I like this term here - "Loans Listed for Information and Comment."

Smith: That don't mean anything.

Harrison: I wonder if it doesn't.

Broderick: The "For Information" comes right under that listing - the reason why it's put there. Isn't that so?

Groom: How does that differ?

Smith: I've been thinking about this thing for a good many years, and I've gone through the management of a bank - I went into a bank where we had some things to think about, and we knew every month - we had our own little "slow" column, just getting back to our own little column number one, and we have it today, and we make it up every month, and we total it, and it's been a good many years now since it's been to a point where it has given us any concern, but it did give us concern at one time. At the same time, we are making loans in connection with the R. F. C., where they participate in them, indicating that we are making a type of loans that bankers a good many years ago didn't make. I want to see that number one column, and I want to know how much it totals.

Harrison: I've made some inquiries since I last saw you gentlemen, about this, and those representing the minority have got a lot of reasons why they think the "slow" should be eliminated - that is, the term "slow" should be eliminated, and why you should not have the third column on the front page, and why it should be in a separate list, marked "Loans listed for information or comment," or whatever you want. They like the broader caption, rather than the more restrictive definition of "slow loans" used by the Comptroller, because they say there are lots of items that the examiner might want to call the examiner's attention to - such, for instance - I'll just give you a list they've given me here:

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"Loans with inadequate or uncurrent credit information."

Smith: They do that now.

Harrison: Where do they put it?

Smith: They have a column - a page - special mention. In the national bank examiner's report today a thing of that kind is referred to in that report.

Harrison: Why isn't that enough?

Smith: Because there is a loan, in the minds of men who run the bank - there is a loan that's drifting toward the doubtful column. It's a marginal loan that is getting so near the doubtful column. I tell you, if you cut that out you might just as well quit examining your banks.

Harrison: I think that is the best argument against eliminating it that I have heard.

Smith: Men who run banks - and all through this thing, I meet the examiner - I go over with our examiners every loan they classify in our banks, no matter what it is classified for - and the barometer and the experience teaching system - and we've gone back fifty years in our place - as long as they've had bank examinations, and the loans on which you have charged off as loss have come through the doubtful, and have first showed up in the slow column. It's progressive, and you just wouldn't have any bank examination if you do away with that. We don't have any differences of opinion with examiners - we haven't had any for years.

Broom: We welcome that column.

Smith: In the New York Federal Reserve Bank, you told me you had how much in loans - three hundred fifty million?

Harrison: Well, we are very much restrictive in what we can do because we are told to comply with two inconsistent tasks. One, we must make a loan which no

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other bank will make, and second, it must be a sound and reasonable loan. And to get between those two horns takes considerable ingenuity. I think we've done it pretty well. We will settle at just about the right amount of loss, I think.

- Smith: You say the slow column - let's say column number one - you say that will terrify the directors. It will, but where it terrifies the directors unduly, then the minority, big minority .....
- Harrison: Well, what I just don't get down to - I can't quite follow you because I don't know enough about it, but I am wondering whether you couldn't make a combination of that so-called number one list or slow list and these others for information.
- Smith: You don't want to do it because these others are entirely different.
- Harrison: But they are not. You get a lot of loans classified as slow that don't comply with the Comptroller's definition.
- Groom: Well, you get that .....
- Upham: Column I refers to loans or portions thereof which are of unsatisfactory quality for reasons set forth in Examiner's comments. Careful and continued attention of bank's management to assets in this classification is essential.
- White: That is tentatively - I think it would be improved to throw out the word "unsatisfactory" and say "marginal standard."
- Smith: Something like that. Take our report - get down to cases; they have their slow column - we haven't had any doubt for a loss column for four years, but then they have "special mention." Then they have loans to companies in which directors are interested, loans to directors, and have a half dozen combinations scheduled - set up - in addition to the first class, and then they have real estate mortgages, legal when purchased, but illegal now. You bought a loan at fifty or sixty per cent and reappraisal shows eighty or seventy-five per cent. They show all these classifications.

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Coolidge: In the slow column.

Smith: Not in the slow column. They have the special mention page.

Harrison: I'll read the balance of these. Just as long as we've got a record of this, I don't like to leave them out. That was A.

"B. Loans with inadequate or thin margin of collateral.

"C. Collateral loans (stock and bond collateral) with unhealthy concentrations in the collateral.

"D. Loans in connection with which there are collateral exceptions, such as defects in assignments, missing insurance policies, etc.

"E. 'Work-out' loans, i.e., loans in which loss is not anticipated but which require special attention of the management.

"F. Loans which are not being properly amortized in accordance with the agreement or sound banking practice.

"G. Loans listed for record purposes."

And their thought, I think, is that if you have the separate column - combination of column one, and these other catch-all clauses entitled "Loans Listed for Information or Comment," you could then get in all of these various categories.

Smith: They have all that now. And all those loans will be mentioned in a good examining report; if you haven't the proper assignments, they will criticize you. They have all those now, and they are shown in separate matters.

Coolidge: Of course, there is one thing certain, if you have these three columns, the first column is going to be called "slow."

Upham: For several years there will be a carry-over for that term.

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- Smith: Bankers should know these things belong in one column.
- Groom: You take a good sound bank examiner that comes in - take any good practical examiner that goes in and examines a bank, and he is there with the duty of classifying that paper, and there wasn't a place he could put the so-called "slow" paper, other than this listing in the back, you would find it in the doubtful column just as sure as the world.
- Smith: They didn't mention their real estate mortgages, legal when purchased, etc. They will show a concentration as to area, or concentration in business. You know, the national bank examiner classifies the loans as to the business they are in - certain percentage on grains, certain percentage on cotton loans, certain percentage in the shoe business, etc. Now that's another schedule, and they give you all those things, but after all, when you get down to it, there are certain types of loans that are traveling toward the doubtful column, and that is where the banker wants to put in his trouble. He's watching them. Whenever you mix them up with anything else, you're breaking down the system of bank examination. Is that right, Bob?
- Hanes: I think so; I think it's something you will be watching very carefully.
- Groom: I agree one hundred per cent with that.
- Hanes: It's where your grief comes from, in the final analysis.
- Broderick: The only place you and I disagree in this thing is the fact I don't think it should be totaled and you do.
- Smith: I think it should be totaled, because the percentage of the total assets or total loans is important. You must have it, as a barometer, to see which way it is going - up or down.
- Broderick: But you're going to get the percentage yourself, aren't you?

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Smith: What's the difference?

Broderick: Your directors. A director sees the great big figure there - that's what sticks in his craw.

Smith: The good banker will total it and tell the directors what it is.

Hanes: Mr. Broderick, if the bank officer has <sup>the</sup> confidence of his Board, he can explain it to them, can't he?

Broderick: Certainly he can explain it - and why total it?

Hanes: It shows his directors where he's going before he gets there.

Broderick: The banker is not going to rely just on the figures.

Hanes: He should, yes.

Broderick: He's going to comment on the policy of the bank.

Smith: He's going to scare that Board.

Broderick: Why?

Smith: Because the "special comment" will be stronger.

Broderick: He gives the "special comment" where it is necessary.

Smith: Where it isn't necessary, the Board isn't going to be frightened.

Broderick: The Board may be frightened to see a great big figure.

Hanes: Those items under this interpretation - shouldn't they be in there? They should be looking those - the management.

Broderick: I don't disagree with that part of it.

Harrison: May I ask a question? What is the genesis of this new definition of column number one?

Upham: When Mr. Folger and Mr. Nichols agreed on giving up the word "slow" and renaming the columns I, II, and III, they agreed that on that same page there

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should be a very distinct definition of what column I meant, what kind of loans that .....

Harrison: That was the definition you've just read.

Upham: Tentatively. They haven't got the definition clearly worked out.

Harrison: I wonder if Mr. Hanes heard that.

Hanes: Yes, I heard you read it this morning.

Harrison: No, this is a new definition, one Cy just read a minute ago.

Hanes: No, I haven't heard this one.

Upham: "Column I refers to loans or portions thereof which are of unsatisfactory quality for reasons set forth in Examiner's comments. Careful and continued attention of bank's management to assets in this classification is essential."

Smith: When you've got a loan that requires careful and continued attention - when you have loans that require careful and continued attention, I think the management of the bank and the directors should know how many and should know the total of those loans. And I don't see where that hurts.

Upham: Then, they have an alternative definition which they didn't like as well as that one.

"Loans involving a substantial and unreasonable degree of risk to the bank for reasons set forth in the examiner's comment."

Groom: I think they are liberal - only classifying those as slow, such loans as that.

Broderick: Those are really doubtful loans.

Upham: Of course, the doubtful column has only got one per cent of the total loans.

Harrison: I wonder if the first definition that you read doesn't come pretty near to it.

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Upham: "I refers to loans or portions thereof which are of unsatisfactory quality for reasons set forth in Examiner's comments. Careful and continued attention of bank's management to assets in this classification is essential."

And then I also read the definition of doubtful and loss, doubtful being "Loans or portions thereof in which a substantial loss is probable but not as yet definitely determinable in amount. Should be given vigorous attention of management."

And loss: "Refers to loans or portions thereof which are estimated as losses by the Examiner. Should be charged off."

Hanes: Well, loans unsatisfactory by reason of length of time they've run--on all the facts you've got before you, you couldn't say they are doubtful or bad today, but you know if they are continued running such a time, they are going to be bad, and the bank should be watching those loans and liquidating them.

Harrison: Mr. Taylor, aren't the two questions before the Department and us, one, what can we do to avoid unnecessarily writing down bank capital or unnecessarily making deductions of assets for the purpose of determining net sound capital? That is one problem. Another problem which I put in a different category is the question of whether there is anything in these reports which is unnecessarily retarding business.

Now I think the deduction that is the discussion of this column one previously known as "slow" relates to this second question rather than the first, because under none of the examiners' reports is it required to deduct slow or column one for the purpose of determining net sound capital. Therefore, the business impact that we are now considering. There appears to be considerable difference of opinion as to how much affect that does really have on business. The only question - whether you list them under one column, or on this page or that page, to my mind, isn't very important, for the purpose of determining how much affect it has on business. I do think the only factor that might possibly have some retarding or

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deflationary influence. As to the one which Mr. Broderick refers to, whether you should have a recap of this column one, as far as I am concerned, you can do it either way. As to where column one should be - well, in fact, I'd be perfectly willing to skip the whole topic and leave it anyway that the examining authorities want to put it, provided that they do something realistic about bond depreciation, which I think is most important.

Coolidge: Isn't the effect of this new definition, which is a very liberal definition, going to take a certain number of loans away from the slow column, reduce the total slow loans and put the ones you are talking about on a sheet with the other loans where some little question has come up? And I'm not sure that isn't a good solution of the problem.

Taylor: It seems to me that it's bound to work that way, because it makes .....

Coolidge: (Interrupting.)

Taylor: Wouldn't it make the examiner really make up his mind about things which he sometimes is not inclined to do? I mean.....

Broderick: In other words, he is inclined to play safe once in a while.

Taylor: Yes. The figure will bear out the slow column is always the biggest column, whereas your loss and doubtful are very small. Therefore, if you eliminate this slow classification, whether you do it - one, two, or three - whether you put it on the same page, or not, you are asking that examiner to say that this loan is one he's damn well worried about.

Harrison: I think we have already eliminated the slow column from our New York Federal bank report. We did it on our own. We did it because we thought it wiser to do it, but we've made a very much more substantial comment column than we ever have before. We did it, I confess, more as an experiment than anything else.

Coolidge: You probably have in your two columns about what we have in three.

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- Smith: How many state member banks have you in your district?
- White: We've got about a hundred and twenty-five New York banks, and several in New Jersey.
- Harrison: I think about two fifty altogether.
- Smith: All good sized banks, aren't they?
- White: Very few small ones.
- Smith: Whenever you compute this number one column, wherein you will find the things on which the management should focus its attention - wherever you confuse that - it's more or less technical - confuse that column with other reported items, where the objection is technical, then you're - it's like pouring water on half a dozen buildings when once a fire has started - you scatter the effect, and your little banks - the big banks, it doesn't make any difference - they have their own.
- Harrison: Mr. Taylor, we're supposed to be with the Secretary at three o'clock.
- Taylor: He's going to have to be a little delayed. He had to go home, and will be a little delayed. One point I'd like to make, which is the real reason for calling this conference, and all the things that meetings have been held before for is to establish uniform practices, and the point which you have made about the New York Federal Reserve bank having eliminated the slow column, for example, in its reports, why, it is a point very much that should be discussed. You have done that in one way; various states will do it in another way - Federal Reserve banks in other districts might do it still a fourth or fifth way.
- Harrison: The New York bank will agree to any uniform rule adopted. We have had this question of examination in our minds so long we thought we'd like to make an experiment on this. I wouldn't like, yet, to put myself on record as for the retention of the column we have eliminated until we complete our experiment. It gives the examiner - emphasizes

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upon the examiner the importance of commenting on the individual loans rather than listing them automatically in column one.

Coolidge: George, your definition of doubtful, your definition - your first column, probably comes pretty close to the definition that Cy Upham just read out.

Harrison: Well, that is what I am afraid - if they put in three columns, with the definitions they have given, it is awfully hard, I think it would be hard for any mortal to differentiate very clearly between column one and two, except they revert to the old practice. While I agree with Tom Smith, there is a difference between an unsatisfactory loan and one which there can reasonably be expected to be some substantial loss. Nevertheless an unsatisfactory loan must be unsatisfactory if some loss is anticipated.

Smith: It's a strange thing, but you can sit down and make your own classification, and there, of course, getting back to "slow," we don't let it get in our doubtful column; we start hitting it. In other words, you look down on your list - your slow column - "We'd better make some charge-off on that." It means lapping over and if you don't make your charge-off you'll find in your next examination, the same loan classified as doubtful.

Harrison: Putting it differently, I feel there is much less reason to eliminate column one if you take a realistic situation on bonds. I think that is the worse position of the banks, and on the psychology of directors, both. Now, if we go in a full way, as recommended by the minority, or bond depreciation idea, I'd feel much less strongly.

Smith: All right, but .....

Harrison: So, total of the influence on the bankers' minds, and what we are trying to do is the thing you want to consider.

Smith: They want us to tell them what we think should be done in the light of its effect on recovery.

Coolidge: Suppose I put it this way. Are we largely in agreement that loans involving little doubt of

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payment shall not be put on that first page and totaled up? That leans on the question of two columns.

Harrison: I would be in favor of that.

Coolidge: That is similar to your field .....

Broderick: ..... loans, unless there is some doubt as to it.

Smith: Well, say there is.

Coolidge: Well, that is in line with Cy Upham's definition.

Smith: I'm - I'm - I agree that in light of that definition, I think that it ought to be a little broader.

Coolidge: Let's take his definition, then, and put it that loans that are not as bad as your definition will not go on the front page and be totaled up. We don't much care if there are two or three columns.

Smith: That's all right.

Taylor: I gather there is substantial agreement on that - that you can have your three columns, but as long as those three columns apply to really bad, or approachingly bad situations .....

Harrison: On which there is some doubt.

Smith: It is approaching, according to his definition, a bad situation.

Taylor: And all your other special mention stuff, where the examiner should call attention, why, that goes on another page, and that is .....

Smith: Loans with inadequate or thin margin of collateral. Of course those loans, if the collateral is inadequate, you'll get that in column one.

Hanes: Let's go to this column one again---no credit there, for you can go into the bank - these smaller banks, and they haven't got - the examiner says, "No, it's all right." I think that's a thing that should be criticized - brought to the attention of the officials.

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- Taylor: That will be on the other page, you see.
- Harrison: That should be put under a colum of special mention.
- Coolidge: I assume those are with a promissor or a good endorser.
- Smith: Should say, loans with inadequate or thin marginal collateral and no other.
- Harrison: Well, then it becomes not a loan for comment but rather a loan that would come in under .....
- Smith: Here's a type - 'work-out' loans - loans in which loss is not anticipated but which require special attention of the management.
- Taylor: Seems to me that you'd get - you'd have your three columns, which will be really criticized loans.
- Smith: That's all they put in there now.
- Taylor: And then your other page, and so on, - put everything in you want to, in there, that you want to bring to the attention of the management - technical lack of credit - for lack of insurance policies - whatever it is you want to put in there. That would just about represent the views of this group.
- Harrison: That every loan subject to criticism on the ground that there is some doubt of ultimate payment should go on the front page and should be recapitulated. I think we all agree on that, whether you put them in one, two, or three columns. That other loans not coming in that category should come in under special comment loans. Do we agree on that?
- Coolidge: We are trying to draw a line; that is all. We all agree on the principle.
- Broderick: Loans in which there is a doubt of ultimate payment.
- Smith: That's just doubtful - that's all that is.

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Coolidge: Well, that was this definition.

Smith: We've got three columns now, and the second is doubtful loans. We ought to get the loans where the tendency is where they are traveling toward the doubtful column.

Harrison: I think the doubtful column is where the examiner is sure there is going to be some loss.

Upham: "Doubtful loans, or portions thereof, in which a substantial loss is probable but not as yet definitely determinable in amount. Should be given vigorous attention of management."

Smith: Where it is reasonable, I think it is in the loss column.

White: That is as I gather it.

Smith: I couldn't agree to the elimination - to the limitation you are putting on it. It's too tight.

Broderick: How would you say it?

Harrison: That's not a fair question?

Coolidge: This whole thing is a question of phraseology.

Broderick: I don't think we are very far apart.

Smith: We're not very far apart; we're almost together.

Coolidge: I like the one Cy Upham has.

Smith: Read that again. I think that is all right.

Upham: Which?

Smith: Your definition of slow loans - loans, portions thereof, and reasons set forth in the examiner's comments.

Upham: "Column I refers to loans or portions thereof which are of unsatisfactory quality for reasons set forth in Examiner's comments. Careful and continued attention of bank's management to assets in this classification is essential."

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Someone suggested we make it marginal quality.

White: I don't like the word "unsatisfactory." I guess I have a phobia on that, but I don't like that word. Marginal is much better.

Taylor: Might say, "And on which loss may be realized unless immediate attention...." and so on.

White: Suppose you say, "Not presently doubtful, but having a tendency in that direction," or "requiring special attention."

Smith: "To avoid loss."

Broderick: "Requiring attention to avoid a loss."

Smith: That was it exactly - "having a tendency in that direction and requiring attention to avoid a loss." (To Hickman, reporter:) Did you get that?

Hickman: No sir; will you repeat it, please?

White: Toward the doubtful - not toward the loss. They've got that other intermediate step before they get to the loss. "Not presently doubtful but having a tendency in that direction."

Coolidge: How about making it simple and say, "Loans needing special attention to avoid possible loss."

Harrison: Or "probable loss," and then you have it fit in with your second definition of doubtful.

Groom: I think "Loans not presently doubtful but requiring attention to avoid loss."

Broderick: "Requiring constant attention to avoid loss."

Coolidge: Well, I think we're close.

Smith: Don't you want to put in "Having a tendency in that direction"?

Broderick: I think if you will put in "constant" you'll work that out. "Requiring constant attention."

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Smith: Either one of them is all right to me.

Taylor: How does that strike you, White?

White: I would say "But requiring constant attention to avoid being classified as doubtful."

Taylor: I don't think that's quite strong enough. I mean, it's in the minds of the .....

White: It's exactly the thought that Mr. Smith has.

Taylor: In the minds of the examiners, it would mean more than it would in the minds of bank directors, because he doesn't - he knows what your columns mean, but if it's mentioned at all, well, he'd say, "Well, it isn't as bad as I thought it was." It may just become doubtful after a while.

Broderick: "Not presently doubtful but requiring constant attention."

White: I think that's all right. After all, what we've got to do here is to compromise a little bit, and I'm afraid if we agree in putting the word "loss" in this column it would be criticized by the group that is trying to get away from the word "slow." I don't like to see the word "loss" in that column.

Groom: Is this for the purpose of .....

Smith: This is instructions to an examiner as to what to put in column one.

Upham: The definition which will appear on the page.

Broderick: Down below, Cy, I suppose.

Upham: No, I think - putting it at the top of the page.

Groom: In place of "slow."

Smith: What is your last definition?

White: Mr. Broderick has it written out - "Not presently doubtful but requiring constant attention."

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Smith: That is just exactly what it is. Here's the thing you want to watch - keep your eye on it.

Taylor: Any disagreement with that?

Smith: Now, the question is, do you want the three in a column, and should they be added? That's the next step, isn't it, George?

Harrison: Yeah.

Hanes: This sums up the three columns.

Taylor: That gives you the three columns. Now, whether you add it or not is the only question.

Harrison: I'm so interested in our present plan that I'd rather not vote on that, one way or the other. I have no great objection to it if you are going to have your third column. If you do have it, and entitle it that way, I think I would be in favor of Mr. Broderick's suggestion, that they not be recapitulated. There's some advantage in not doing so. I think if you are going to have a third column, and are going to give a definition to it, that is as good as any you can give to it. You fellows have been much closer to it than I have. I don't know how you are going to get thousands of bank examiners to make the same definitions that these three columns contemplate.

Coolidge: The same is true when you have two columns.

Harrison: Yes, but it is much easier, because there you have one with no loss and one of probable loss. However, I don't want to delay the discussion on it at all. We thought there was some advantage in not having it - not the second, but that we were right in eliminating the column, but in the wisdom of trying it, I wouldn't want to vote to reinstate it. If you do, I'll agree to this definition. In the next column, I would be in favor of not having a recapitulation.

Smith: Well, it's a strange situation when you find the bank examiner .....

Hanes: Gentlemen, the safety of your whole insurance fund depends on the type of examination fund you get.

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- Broderick: Keep them on - the examiners on their oath of office and that is going to guard them in their work. There will be no instructions from any supervisor or department - according to his oath of office. I wouldn't worry about that, Mr. Hanes.
- Coolidge: The trouble is, all loans are good in good times and turn bad in bad times.
- Hanes: I think the tendency at the top is going to sink down through the whole force. Of course, you've had a lot more experience than I have.
- Broderick: I've been through it, and we've seen it.
- Taylor: How about taking a vote on this?
- Upham: I got a vote this morning on all these things; the ones they have disagreed on. If anybody changes his mind .....
- Taylor: You've got a slight change in that there is, I gather there is agreement on three columns, with the possible exception of Governor Harrison. On the question this morning: "Is it objectionable to total the criticized loans, other than doubtful and loss, and show them on the recapitulation page?"
- White: Wouldn't it serve the purpose if this column is added up, even though it is not shown in the recap?
- Smith: I can't see any reason for adding it up.
- White: I don't think it is important; that is my frank opinion on it, but apparently there are some people who feel it is a disturbing influence on the banker, who looks at that recapitulation page first and last.
- Smith: That is the first thing he's going to do.
- Harrison: Mr. White suggested adding up the column but not to include it, the added column, in the recapitulation in the back of the report.
- White: Add the column up, but don't show that column in the recapitulation.

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- Smith: Where you get the net sound capital. Well, I don't think that's .....
- Taylor: It isn't deducted now.
- Upham: It isn't deducted - it's just shown.
- White: Well, under this scheme it would have no place in the recapitulation so far as arriving at the figures is concerned.
- Smith: They don't put that in the recapitulation.
- White: Well, you'd go along with that, Mr. Broderick, that you could add that column up - that's simply a matter of arithmetic - if you don't carry that column to the recapitulation page.
- Broderick: We are getting that definition down so that the old slow .....
- Smith: John, if the figures are big enough to cause such a concern he ought to get worried about it.
- Groom: With that definition I don't see how he could do otherwise than to include them in that recap.
- Broderick: I am not as strong for it as I was this morning, because I had the old idea.
- Smith: Loans running for a long time, although perfectly sound, being classified as slow - that is ridiculous.
- Hanes: I think that old definition is .....
- Smith: But we haven't had that in the Comptroller's office - certainly not in our district, for years.
- Groom: If they only list that type of loan in column one a certain per cent of that will eventually be loss, in my opinion, if it comes within that definition.
- Hanes: If it stays there and no attention is given to it, certainly it will be loss.

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- Broderick: Mr. Groom, I've made a number of checks on institutions, and I invariably find losses carried, first in the examiner's report, starting first in the so-called "slow" column. The good bankers, the moment a figure appears in that column, they start giving it immediate attention, or start charging off, or setting up reserves if it's not charged off. It does have a tremendously bad effect on the little fellows. They come down, just shaking like that. (Indicating.)
- Smith: Well, John, if they have - well, this definition, if it's in the bank .....
- Broderick: Now listen, Tom, I'll tell you what you're up against. You're up against the examiners playing so safe - they take no chance. I've seen almost every loan in the bank .....
- Smith: That's up to fellows like White to do that job and not tear down the system of examining banks.
- Broderick: In the meantime it's the customer that's to be reported out. I've seen instances where we've had to send other men out to have the thing redone for fear of ripping the whole thing out - reporting in.
- I'd just like to say, personally, I - I prefer not to see that put in there - this so-called slow or the so-called column I. But I raise no particular objection in case it is. The consensus is that it should be done. I prefer it the other way, but my objection to it is much less strong than it was this morning, because I think we have narrowed down this definition of column I. I also might say my particular interest on this thing is a point that Mr. Harrison makes.
- Taylor: I think we are pretty nearly ready to pass to that. Think it would be useful to have a new vote? I gather you have changed yours a little bit because you, this morning, I gather, voted pretty hard against totaling.

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- Broderick: Now, I still say I prefer not to have it totaled, but in view of the change of definition of Column I, I raise no particular objection if it's the concensus that it should be totaled.
- Taylor: The other vote against totaling was George Harrison, wasn't it?
- Coolidge: I think George Harrison didn't want to vote and I said I didn't know enough to vote.
- Harrison: I said I would prefer not to have them totaled because I would prefer for the moment to recommend not to reinstate column I at all, although I like it much better as it is now defined than I ever have before.
- Taylor: Let's say there is no vote violently opposed to totaling, if column I is newly defined.
- Harrison: That's right.
- Taylor: All right.
- Now - on the bond thing, what?
- Smith: Well, that's some progress.
- Upham: That question of yours, Mr. Taylor, refers only to totaling and not to recapitulation.
- Smith: You never did recapitulate Column I, Cy.
- Upham: Here's the recap, Mr. Smith - slow, doubtful, loss - (indicating record.) Now they don't carry this total of slow down when they figure net sound capital, but they do recapitulate it.
- Smith: I am in favor of that.
- Upham: They make a distinction between totaling and recapitulation.
- Smith: It can be shown right where you can't dodge it, but it isn't to be taken into consideration in determining the sound capital structure.

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Upham: Well, about the only thing on bond appraisal was what to do with the depreciation. I mean, we voted on that this morning.

Smith: How was the vote?

Upham: Well, you all thought that the complete list of securities should be listed in the examination report, and every one but one thought all the securities should be priced, with the market price given in the report. And every one thought that the net sound capital of the bank should be computed in the report, but we didn't get any views on what depreciation should be deducted in computing the net sound capital. The supervisors all agree that on defaulted bonds and on stocks, depreciation should be deducted in computing net sound capital. Above that, above that they differ. Some of them think that the depreciation of group two securities and B aa's ought to be deducted in computing net sound capital. None of them feel that you should deduct depreciation on the Governments, municipals, and the first three grades of corporate bonds.

Smith: Well now, you said here that the majority agreed that the group one bonds should not be priced.

Upham: Yes, they .....

White: That's right.

Smith: But we say they all should be priced.

Upham: They feel that they would prefer to price them, but in a gesture toward the minority, in attempting to get the minority to come along with them, they said, "We'll agree not to price the Governments and the three first grades."

Harrison: What's the point of not pricing them?

Upham: Well, Mr. Paulger says that an examiner's report should be a report of exceptions. You say nothing about good loans - the only ones you mention are the slow, doubtful, and loss. Why should you say anything about good bonds? Why

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not only talk about those that are in the lower grades, pricing them. You see, the minority doesn't want to price anything. He says that pricing means too much of an emphasis on market values, which mean nothing. He wants to get away completely from the market. It will train the bankers, eventually, to pay no attention to market prices. They will buy good bonds and keep them and pay no attention to what the market price is.

- Coolidge: The bank has bought, say a million of four per cent bonds; another bank has paid a hundred fifteen for them. Certainly that first bank is in a better position.
- Upham: Well, of course, the bank that paid a hundred fifteen amortizes the premium down.
- Smith: The other banks got that much more.
- Coolidge: That, evidently, is worth having, but that, you get, as a whole, when you price those high grade bonds.
- White: Why agree to price the stocks in the doubtful and defaulted securities? I wonder if the market is a thing that bankers should once and for all forget.
- Upham: I suppose it's a matter of some place to draw a line.
- Groom: You have depreciation there, deducted from your net sound capital.
- Upham: He says, "But why do that?"
- White: They ought to be out and find what the real value is, and not take the market. Certainly markets - the Governments - more than - as George Harrison pointed out, railroads did not even have a bid on certain grades.
- Upham: Some defaulted bonds are good.
- White: Sure.
- Harrison: Good for something; they may be above market.

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- White: Generally, you can see, in the defaulted classifications, the market is purely unreliable.
- Upham: They only gave up pricing those high grades in an attempt to get together. They would give them that.
- Coolidge: I think there is some excuse, under the defaulted bonds, to price them. You should mark it off, and what other standard have you got, other than the market?
- Harrison: Appraisal.
- Coolidge: Until you're prepared to take defaulted bonds into Washington - which you might want to do in an extreme case .....
- Groom: I don't think you would have any situation like that.
- White: We were pretty generally agreed, were we not, that we should price these bonds?
- Upham: Yes. List them and price them. The only question was, what depreciation would you use in your computation of net sound capital?
- White: Well, now, on that I think I said that - this is a matter of repetition, probably, but I think I said some middle ground, between the minority and the majority views should be found. In New York, on the C bonds - bonds not in default - we take a mean value between an arbitrary date of the past and the date as of which the examination is made, and allow a percentage of write back when the date of the examination is made. I am fearful that we may find that this majority view doesn't go far enough in the markets - begin to get worse, or continue to get worse. I think we ought to recognize that fact now and go as far at this time as we intend to go - as we are willing to go, and not work out a scheme now that we've got to change three months from now to meet a more - to meet another decision.
- Upham: You mean the majority deducts too much depreciation?

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White: That's right.

Upham: And the minority not enough?

White: I would much prefer to go with the minority on this point than with the majority. I think probably the minority goes a little too far. I'd be willing to make a concession to the view taken by the majority that you should place - that you should use the valuation of securities to place something of a sanction upon the bank against the purchase of these low grade securities.

Coolidge: Do you feel if a security is left out the question of stocks and defaulted bonds, that separate - if the other securities, or the various groups of bonds, total greater than the book value, would you feel there is no need of any write-off?

White: Well, that is about what we do in New York today. We do not bother to compute the fair investment value at all, unless it .....

Coolidge: I should personally feel that if the security is all of a hundred per cent that you need not have a mark-down.

White: That's a situation that is very unusual today.

Hanes: The practice in the Fifth District is that they take all the securities of whatever nature, list them, and put the market value down. Where it isn't possible to get a market value they get an appraised value. They take the mean of the three and then they have the whole thing, and if you've got an excess there's nothing said about anything. If you're under water, then, of course, it will come out. I don't see how you can take depreciation and not be allowed to take appreciation.

Taylor: We're supposed to move in to the other place now.

(Adjourned to H.M.Jr.'s office.)

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3:45 P. M.

- H.M.Jr: How's teacher?
- Upham: We had some further discussion of the slow column and we were just getting started on bond depreciation.
- H.M.Jr: Somebody take Tom Smith, did they?
- Smith: They are all after me.
- Upham: Is that enough of an explanation?
- Taylor: I think you can tell him there was substantial agreement.
- Upham: I think there was substantial agreement on what to do with the slow column - pretty substantial. Governor Harrison explained that the Federal Reserve Bank of New York, sometime ago, did give up the slow column. They took it out of their report and he'd kind of like to see that experiment continue for a while.
- Harrison: I don't want to vote to restore the third column we have eliminated and finding fairly satisfactory in the elimination. I feel very much less objection to restoring it in view of the definition that the group, as a whole, has agreed to.
- Upham: And if it goes back in they are pretty well satisfied with that definition. We were just beginning to talk about what to do with bond depreciation. How much bond depreciation should be used in computing the net sound capital of the bank. I think, Mr. Hanes, I may have misled you in saying that depreciation is the net depreciation.....
- Smith: Over the entire portfolio.
- Hanes: That's quite all right.
- Broderick: That would take in the unrealized appreciation, offsetting the other.

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- Upham: Yes. When I said they couldn't use the unrealized appreciation .....
- ? The depreciation is to be used as this net. Under this number three, that means it's to be not allowed to be written up in the books?
- Upham: That's right.
- Hanes: Everybody agrees to that.
- Upham: The present practice, I guess in all three, if there is a depreciation in defaulted bonds, or in stocks, that they deduct that when they figure how much capital the bank has, they don't count that as capital; and in group two securities, which are ones national banks can't buy, in the first place, but which they may acquire for various reasons, that depreciation is deducted when they figure the net sum of capital of the bank, and the Comptroller and the F. D. I. C. think that that should continue and that they should also include depreciation in the lowest grade of bonds that are included in the high group, with one. The minority position is not to include any of that depreciation. And they hadn't gotten any vote on that from this group. They were just beginning to discuss that.
- H.M.Jr: Did I spoil a meeting on that? I'll go out and take another walk.
- Upham: I don't know whether they're ready to say yes and no or not.
- Hanes: I'm still a little dumb on that. You are still talking about - you've got depreciation above all possible appreciation. Where you've got a net appreciation in these things, they deduct it from capital.
- Upham: That's right.
- Hanes: I think it certainly should be.
- Smith: That's the majority position.
- Upham: That's right.

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H.M.Jr: The same majority?

Upham: That's right. See, the minority feels that the schedule showing a computation of net sound capital should be eliminated. They wouldn't even have the net sound capital in the report, so ....

Harrison: Well, they are forced to that position. If you're not going to deduct any depreciation on defaulted bonds for the purpose of determining what is net sound capital, then they are afraid to make the computation of net sound capital. If the market and book are too far apart, it may give a fictitious value to net sound capital, and therefore they recommend that there be no computation of net sound capital entered in the report, and I think perhaps that is wise, if you once agree that no depreciation is to be deducted from bonds that are not defaulted - for bonds that are not defaulted.

Groom: Mr. Upham, do I understand that it will be a reversal in the high grade market and give a fair depreciation in the high grade market, including Governments, then that would be taken into consideration in figuring net sound capital?

Upham: No, it would not, unless they look at it anew.

Groom: I thought it said net depreciation.

Upham: In the securities which you carry.

Groom: All right. I just wanted to follow that closely.

Coolidge: If there should be a recession in the high grade bonds, then the bank would lose the benefit of its profits, so there would be - you'd have it off in the lower grade bonds. They wouldn't have this retraction from the loss that they now have.

Upham: The net depreciation would be much greater.

Coolidge: The net depreciation would be greater.

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- Upham: But there is no proposal to carry depreciation in Governments forward in the computation of net sound capital.
- Taylor: But it shows up there, as Jeff points out.
- Upham: Because the depreciation in the other is greater by virtue of not having that offset.
- Groom: I'm not entirely clear on it. I thought I had it all a little while ago, but getting into the minority and the majority report, I seemed to get confused. Would you restate the plan of determining net sound capital, as far as not appreciation, but depreciation in the securities is concerned?
- Upham: The majority opinion is that net depreciation in group two securities and B aa's in group one, should be deducted in computing net sound capital, plus, of course, depreciation in defaulted bonds and stocks. That the depreciation in Governments, municipals, and the first three grades of corporate bonds be disregarded in figuring net sound capital.
- Groom: What about the appreciation in determining the net sound capital between the two groups? In other words, supposing you have an appreciation in the Governments and the first three in group one, or in the qualified group for bank investment, and then you have a depreciation in the unqualified group, we'll say, and the defaulted group. Then would you determine your net depreciation or appreciation in determining your net sound capital? Do I make myself clear?
- Upham: Yes. Now you begin to make me doubtful. My understanding is that depreciation in the whole bond account is included in determining whether there is a net depreciation in the B aa's and group two, to carry forward in computing net sound capital.
- Coolidge: If you had, in group two, a hundred thousand dollar loss and in your highest grade a hundred thousand profit, there'd be no depreciation.

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- Upham: I am very confident of that, Mr. Secretary, but to make absolutely positive, I'd have to call Mr. Folger and find out.
- Taylor: I think you'd better do that.
- Upham: If you'll excuse me. (Leaves the room.)
- Harrison: You've got a messy situation though, if you're going to allow them to include appreciation in group one as an offset to depreciation in group two, and completely ignore depreciation in group one.
- Taylor: That's different there. It doesn't add up that way.
- Broderick: Well, George, if you have appreciation in group one .....
- Harrison: I know, but .....
- H.M.Jr: George, can I just stop a second? This is something terribly technical - do you mind? I want to - when we get on to this thing - I want to ask each person if he would be thinking, through his mind - maybe there's something as important as the suggestions we have, to help the whole picture. Maybe the boys here are working with this thing too close - maybe they don't see the forest for the trees. I'd like to know if there is something else as important or more important as far as bank examinations go. This is - after all these are the recommendations of bank examiners. They - it may be they've got the thing too close. I just want to drop that so you'll have it as you go along.
- Harrison: I've got a thought I'd like to give you. I'd increase, substantially, the salary of every bank examiner, beginning with the Federal Reserve Bank.
- Hanes: That is absolutely sound.
- Harrison: I think it is altogether unreasonable to expect men - junior examiners - the type we have to put in the banks - at the salaries we are forced to pay, to give appropriate judgments under these definitions.

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- Smith: And it should be made a career. That was the old system - it was changed in the last few years.
- H.M.Jr: You mean national bank examiners are not civil service?
- Smith: It isn't a career now to the extent it was before, because new men have been put in over others, which breaks down the morale of the system.
- Broderick: Mr. Chairman, may I say that in New York State, every bank examiner there is a civil service man, and every deputy is civil service. It's been a career job for years.
- H.M.Jr: How about national?
- Broderick: No, it is not.
- Smith: You asked a question - well, I know a case in the Chicago District. In this case Mr. Overworkman, who is a very fine examiner, was made an examiner one morning, and in the afternoon was put in charge of the Chicago District. It turned out very well, but that is a very dangerous thing, and it almost upset the national bank examining force. That is the outstanding case.
- H.M.Jr: Well .....
- Smith: This man - I don't mind - because he turned out, but that is what happened, and it's a bad situation. I think every examiner should be made civil service in the future.
- H.M.Jr: I'd go a step further. I think that those not civil service should - I should say they ought to be civil service at once.
- Broderick: They've started civil service substitution there, Mr. Chairman. I thought it worked out very well. They have their own civil service ideas.
- H.M.Jr: I mean, they are not a part of the Civil Service?
- Broderick: No.

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- Smith: In the last two or three years, the national banks have broken down the civil service career service.
- Hanes: That's right.
- Smith: That's the worst thing about it.
- Hanes: They have to get the O. K. of the local Ward leaders now before they can get in.
- Groom: Well, I know of a case where the Chief is now back down the line. They've had young fellows come in and have been appointed over the fellows that have been there for years. The new men appointed to Chiefs.
- H.M.Jr: I'd be tickled to death to recommend that. What about F. D. I. C.? Is that civil service?
- Upham: No.
- H.M.Jr: I might point out that Farm Credit is. Who set that up? I did, and it's still good.
- Harrison: I think that question, and the salary question are two important factors.
- H.M.Jr: With Civil Service would come a whole question of reclassification.
- Hanes: They are both very constructive suggestions - both of them.
- H.M.Jr: That's the kind of thing I'd like to have.
- Upham: (Returned to room.) That net depreciation does include - docs take into account, the depreciation in the first grade. You take your first two grades and figure the net depreciation on the whole thing and then carry forward that on the ones in the B aa. Mr. Folger says, as a matter of fact, it isn't going to work very well and it's another reason why he wants to put all the prices in. He doesn't think the minority position will work at all.
- Smith: You have to put in the prices.

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- Upham: That's what he repeated to me now.
- Groom: He means the whole bond account.
- Upham: Net depreciation on the whole bond account.
- Taylor: You can talk quite a lot on that point that has just been raised of whether that adds up or not. And if you're trying to eliminate class one - not show that depreciation, why, this formula doesn't do that.
- Upham: You pretty near have to, as this group agrees, list and price everything.
- Taylor: Unless you want to eliminate group one from any kind of depreciation.
- Upham: From any net depreciation.
- Coolidge: I do not think it's practical to do that. It's too easy - it will force them to take their profits to make up the depreciation and then they'd reinvest. I think you have to give - if there is a depreciation in the whole group - you have to give them credit for the gains, against the depreciation.
- Upham: The difference seems to be - should all depreciation above defaulted bonds be disregarded in computing net sound capital?
- Smith: All the depreciation above .....?
- Upham: All depreciation in groups one and two. Three is defaulted bonds, and four is stocks. Now, should you disregard depreciation in groups one and two in figuring net sound capital or should some of it be included, or all of it be included?
- Harrison: Well, I share Mr. Taylor's query. If by net appreciation in group one which you are going to allow as an offset against depreciation in group two, you mean only the appreciation in all the different lists in group one without considering the depreciation of certain other bonds in group one which you may have, I think you're wrong and they wouldn't balance; but if

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what you're going to do is to take everything in group one and figure out whether there is an appreciation or a depreciation, taking into account depreciation in certain bonds in group one, then I think you will come out even, but you won't unless you do that.

Coolidge: Oh, I assume he's doing that.

Harrison: I don't know whether it's worded that way or not..

White: As I understand it, what they would do is to take the book or market - whichever is higher - to figure that depreciation. Isn't that right?

Harrison: What I mean - supposing in grade one of the corporate bonds, which is in group one, you've got a hundred thousand appreciation in one list of bonds and fifty thousand depreciation in another list, in grade one. How much appreciation are you going to take from group one to apply to depreciation of group two?

White: Take it all.

Hanes: Fifty only should be taken.

Harrison: I think the way they've got it is a hundred thousand.

H.M.Jr: Would you like to have me ask Mr. Folger to come in?

Harrison: If he's available.

H.M.Jr: He's very available.

Smith: If you promise not to get me in trouble - he's my boss.

H.M.Jr: How many bosses have you got, Tom?

Smith: He's one of them.

Hanes: I think it would be fine to have him, Mr. Secretary.

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- H.M.Jr: (Over telephone:) Tell Mr. Folger to come in - right away.
- Can we go on with something else, gentlemen, while we're waiting for the expert to come in?
- Upham: The only other thing we had agreement or disagreement on is this business of impounding security sales in a reserve account against the securities account.
- Broderick: How can you do it, Cy?
- Upham: Well, Mr. Folger says you can't do it. He's against it.
- H.M.Jr: Who's for it?
- Upham: Mr. Paulger, of the Federal Reserve is for it very strongly, and Mr. Nichols went along with him.
- H.M.Jr: Well, will you ask him on those two points - or was it just the one point?
- Upham: We'll take it up with him. Well, that technical point on this depreciation on bonds.
- Coolidge: It may be that we can be in agreement on it without asking him.
- Upham: On the reserve account, on impounding bond profits?
- Coolidge: Oh, I thought you were speaking of the other.
- H.M.Jr: State the last one again, Cy.
- Upham: "Should banks be required to impound the profits on sales of securities in a reserve account against future losses in the securities account, or should all profits be treated alike and the general condition of the bank be the test as to the reserves required?"
- Smith: That is what I am figuring on. I don't see any other way you can handle it.

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- Upham: The proposal is to require the banks to use all bond profits.
- Broderick: I think you can - should urge the banks to do it and not require them.
- White: Missionary work is about as far as you can go on that.
- Coolidge: I'd put it in a general reserve.
- Upham: They feel if it is in a general reserve account it can be adjusted.
- Broderick: I think the problem of a large bank is little different from a small bank. I think you've got to urge the smaller banks to set aside their so-called profits as a cushion against probable loss on the remaining portfolio. That is where the missionary work should be done. The big banks can take care of themselves. The larger banks now have their reserve for that, and the other things - that's all right, but it's the smaller banks where you need missionary work, to make sure they are not paying out the paper profits - the former dividends. And I hope that some means can be found of urging them to adopt the suggestion. You can't require them to do it.
- Folger: (Comes in.)
- H.M.Jr: Mr. Folger, these bankers are stuck here on a very technical point.
- Upham: It's in connection with this carrying forward the net depreciation on B aa's and groups two in computing net sound capital - just what appreciation and depreciation you take into account in determining that net depreciation figure.
- Folger: The depreciation on the defaulted would be listed in the report as a loss.
- Upham: Yes.

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- Folger: And the net depreciation on all other bonds would be used to reduce the net sound capital, to reduce the sound capital, arriving at the sound capital.
- Harrison: I think what stumbled us was only one thing. You probably are not taking into consideration, for the purpose of determining net sound capital, the depreciation in group one, except B aa.
- Folger: That is not what we are doing - it's the suggestion.
- Harrison: For the purpose of determining what is net depreciation in the whole account, do you merely add in appreciation in group one or do you also deduct depreciation in other bonds in group one, above B aa?
- Folger: Above B aa the suggestion was that that be disregarded entirely - appreciation or depreciation.
- Harrison: Oh, well, that's - you mean disregard both depreciation and appreciation. That clears it.
- Smith: Not even price them?
- Hanes: Yes. That starts me all over again.
- Upham: Well, I misunderstood you on the phone just now. I thought you said take the whole net depreciation on all of one and two.
- Folger: What we are doing at present is doing just what you say.
- Coolidge: What seemed a little unfair to me was to suppose a case where you had a depreciation on your portfolio of group two and group one, and yet, due to the depreciation in group two, you mark their sound capital down.
- Folger: You would by following this suggestion; yes. If you had appreciation in your group one, and depreciation in group two .....

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- Coolidge: You'd mark them down.
- Folger: You'd be marking them down; yes.
- Coolidge: But it seems a little unfair, and it seems to me it might encourage them to sell the bonds in order to avoid that.
- Folger: I hardly think so; you're not charging off anything; it is merely a memorandum.
- Hanes: You've got some reserve - you have a hundred thousand loss, and you've got to set up a reserve for that, even though you've got a profit in your group one.
- Folger: We say "adequate reserve." That would be taken into consideration in asking that the reserve be set up.
- Smith: You'd price the bonds for your information, but not in the report?
- Folger: We know what the bonds are worth.
- Smith: Why wouldn't they be priced in the report?
- Hanes: If you're going to take - ascertain as to whether the bank has a capital impairment, if you're going to take into consideration the total bond account, that is one thing; if you're going to disregard all the prices or the profits, or whatever may be in group one, and will simply take the depreciation or appreciation in the other groups, then it is quite a different thing.
- Folger: Well, your bonds in group one, except the fourth rated bonds, would not be priced in the report.
- Hanes: But you price your other bonds below that and if there is a depreciation in those bonds you must set up a reserve to cover that depreciation, mustn't you?
- Folger: No. If you had enough appreciation in your bonds that were not priced, you wouldn't.

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- Hanes: How do you get appreciation if you don't price them?
- Folger: It depends on whether or not you think you need a reserve. If you had a hundred thousand .....
- Hanes: You have no price.
- Folger: We're talking about pricing in the report.
- Groom: Examiners will price them for their own information, Mr. Hanes, but not in the report to you. Isn't that it, Mr. Folger?
- Folger: Yes. We may price them, of course.
- Hanes: What is the idea of not pricing them in the report? You've got to price them anyhow. What's the idea of not putting those prices in the report itself?
- Folger: The thought was - we are not asking you to charge off anything in those bonds. We have never asked a bank - never in history - to charge off on Governments below par, or cost, whichever is higher.
- Hanes: Well, that being so, why price them?
- Folger: Suppose they .....
- Hanes: Price them to get a picture of your whole bond account?
- Folger: I have no objection to pricing them myself, to be frank about it. In fact, that is what we are doing.
- H.M.Jr: Mr. Folger, if you had to say this thing from your standpoint, how would you handle it, personally?
- Folger: I think I'd price them. I don't see a good deal of difference either way; I think I'd price the bonds.
- H.M.Jr: The thing that bothers me - here you fellows that are in this business - they can't understand it; how are we going to make the public understand it?

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- Folger: I think you're correct on that, Mr. Secretary.
- H.M.Jr: Isn't there a way to approach this thing which is simple, so it would accomplish the same results, so we could all understand it?
- Folger: Yes sir.
- H.M.Jr: How would you do it, that way?
- Folger: Price all of them.
- H.M.Jr: What's the matter with that?
- Folger: There isn't anything wrong with that. That's sound.
- H.M.Jr: O. K.
- Harrison: I think everybody suggested that the price should be put in the report of all of them, but everyone has not suggested that you deduct depreciation for the purpose of determining net sound capital. I mean, there are two different questions - the pricing we are all agreed to - that is just a memorandum of what the blackboard says the things are worth.
- Folger: If you are charging off, I'd say you are correct. I don't think that the capital in the report you may have depreciation - it may not affect the capital structure of the bank, but if it's too large, you want to know it. You want to know how much sound capital you have left, for they want to - may want to increase the capital. I can't see the objection to showing that.
- Harrison: The prices .....
- Folger: That doesn't mean you're asking the bank to do anything about it.
- Harrison: I think we are all agreed there's no objection to pricing the bonds in the report as a matter of information or memorandum. I think there is a difference of opinion in the depreciation of market value in the report - of the market value and the book value - whether it should be written off in determining sound capital.

Folger: Not writing it off in your - I don't believe we can call depreciation sound capital. That gets back to a matter of whether or not you are going to cut out that computation. Are you going to leave that out of your report? We think that it's been a tremendous assistance.

Harrison: You say that you should not count depreciation as net sound capital but you do count depreciation of a certain list as net sound capital.

Folger: There isn't any in a preferred list.

Harrison: You may.

Folger: No.

Harrison: In group one, with the exception of Baa's.

Folger: You have found them in that .....

Harrison: I've found some Atchison and Ford that have depreciated recently.

Folger: You will find individual issues, but on the total you'll hardly find such cases.

Groom: Some other supervising agencies have recommended some other procedure. Didn't one of the Departments suggest that they be not priced in the report?

Upham: Yes. That's right, sir. Mr. Paulger would neither list nor price any of those.

Folger: He'd neither list nor price any bond except those in default.

Groom: This group is definitely opposed to that.

Upham: That's what I gather. I don't know how much depreciation that we carry forth.

Hanes: That would be a special item - then we'd have to sit down and talk this whole thing over. You're not talking about individual issues.

Coolidge: Under present conditions you are saying that is applied to net sound capital.

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- Folger: I can see that. If a bank - it is reasonable, that if he had a large percentage of his bonds in the first grade - the first group - and he had a large appreciation, he wouldn't care for you to ignore that if you're going to take depreciation on the other bonds.
- Coolidge: It seems to me that is a fair way to do. Today if you had a case where Government bonds were selling at sixty - at eighty-five, or something, you'd have to rehash this whole thing.
- Hanes: Yes, that is an emergency; then you'd have to sit down and talk the whole thing over.
- Coolidge: I should think it would stand it on the group one and two together.
- Harrison: I don't think I quite agree with you, Jeff, if only because of the fact you have a wider spread in yields, now between B aa and triple than I think we have ever had, with the possible exception of 1931 for a short period. The spread in interest yield is over four per cent, both of which is ineligible grades for investment in a national bank, and the reason is you had a violent drop in B aa bonds in the last six months, as a group.
- Folger: Yes, I think, Governor, it is largely due to the rails and utilities.
- Coolidge: If you were running a bank wouldn't you want to see that dropped in your report?
- Harrison: I say, I think we all agree it's fair enough to list the price to enable you to see the drop. That's all right. I don't object to that at all, although I understand some do.
- Upham: The next question is, and the one I think is before us, whether we should deduct the depreciation in B aa bonds for the material purpose of determining the sound capital. Mr. Folger recommends that you should deduct it in this new program and others say you should not deduct it.

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- Folger: Others say you shouldn't deduct any.
- H.M.Jr: Well now, where are we - apart or are we together on this?
- Harrison: All in favor of listing the price without significance.
- Upham: Well, I think I have the general feeling that they are all in favor of listing all the securities and pricing them all.
- H.M.Jr: Yeah.
- Upham: And they are almost all in favor of including a computation of net sound capital in the report, but I haven't gotten any vote of how much of the depreciation should be used in computing net sound capital. That's where the supervisory agencies disagree.
- Groom: Mr. Upham, I haven't understood why they don't want to use this depreciation in determining the net sound capital. What are they advancing in showing it another way?
- Coolidge: I think the only fair answer to that would be the conditions were unusual and certain bonds were selling at values that were not sound, fair values. Wouldn't that be it, George?
- Harrison: I'm sorry - I didn't hear you.
- Coolidge: Why not take these figures and show the net sound capital with the market deductions? I think the only reason against it is that the large amount of bonds is selling under distressed prices. Offhand, I don't think enough bonds are selling on that basis to warrant changing the rules.
- White: The reason is, the current bank examinations are showing if you use a lot of impaired capital, which are highly disturbing that thing, and I know-that is, I'm not speaking alone for New York when I say that, because we have had plenty of meetings with other bank supervisors and I think it's a problem that is disturbing today to everybody.

Smith: What do you suggest, Mr. White?

White: Well, as between these views I favor the minority view. I feel - I believe however, that ordinarily progress is made through compromise, and I think that it would be advisable to take a compromise view between these two positions and not take all C-bonds at market, but to allow a write-back to some extent on C-bonds, based upon some mean value between the value as of a date a year or so ago and the present date. I would - I think that on the first three or four grades there is no need to show any depreciation, and I would permit a write-back on other securities not in default. Take stocks at market.

Upham: Sort of a convention value such as the insurance companies use.

Smith: Is that for the purpose of calculating the net sound value or for the purpose of charging off?

White: That's for the purpose of determining net sound capital.

Smith: What would you charge off?

White: I'd charge off on that basis a portion of the depreciation in the bond portfolio in the lower securities. All the defaulted and all the stocks.

Smith: That suits me all right.

Folger: And a percentage of the other depreciation at each six-months' period.

White: Yes, if that could be worked out.

Smith: Well, you really would consider that every time you examine - every six months.

Groom: You wouldn't take into consideration appreciation in the higher grades at all.

White: I don't know. I apparently misunderstood. In each of these memoranda there are statements in the majority reports and the minority reports,

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both reading identical, that unrealized depreciation is not allowed. I was going on the assumption that we were just going to forget about unrealized depreciation. I am not arguing that it should or shouldn't be; I'm not familiar with the amount of the depreciation that exists today to know how important it is.

Upham: That means there is no write-up on the books.

White: We're talking about making examinations.

Upham: Four and five probably shouldn't be there.

Coolidge: You're talking about net sound values.

White: We're talking about net sound values - in examinations, how .....

Taylor: Talking about net sound capital. That is obviously concerning net sound capital, isn't it?

White: For examination purposes - I don't know; I think that it's a little difficult for the bank examiner to say to the bank, "You must not write up your bonds here to market," and at the same time go in and examine him and allow him that depreciation for the purpose of your examination. I think the two views are inconsistent. Do you agree with that, Mr. Folger?

Folger: No, I can not. The committee doesn't think it's good policy at all for books to take unrealized appreciation, pass it into the profits account reserve, or any kind of profits account.

White: I agree on that. I say I think that is a view to which we all adhere, but it's a little difficult for us to enforce that view and at the same time go in and examine the bank and allow him the depreciation for the purpose of examination.

Folger: You're not allowing the appreciation for the purpose of examination - you're only taking the net depreciation.

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- Harrison: How do you get that?
- Folger: It would hardly be fair to take an issue of bonds that has a depreciation and say you're going to use that. It seems to me you should take the total of your bonds.
- Coolidge: That's what it seems to me. It seems to me wrong to take a bank that has a total market above book of a million dollars and say his net sound capital is less than his book value.
- Smith: You're talking about two different things. The present procedure is to calculate the net appreciation and depreciation for the entire account, and if there is a net depreciation, then you - and then you require a charge on it.
- Folger: We don't require anything in the calculation.
- Smith: You wouldn't do that, however, if there was a net appreciation in the account.
- Folger: In the defaulted?
- Harrison: You can avoid this whole discussion, can you not, by accepting the report which says you disregard appreciation and depreciation except in defaulted bonds?
- Hanes: I can't adhere to that at all, Governor. You absolutely disregard depreciation in it. I think you're getting wild when you go into that. I certainly disagree with that condition.
- Harrison: I don't see the connection in the majority report either, because the Comptroller says you can buy bonds Aaa, Aa, A, Baa - those first four grades. They say if you've made a bad debt in the first three grades that wouldn't make any difference - if you did make a bad debt in the first three grades, you wouldn't have to consider that depreciation in determining net sound capital, but if you make a bad debt in the fourth you've got to deduct that. I don't see why you pick on one grade.
- Folger: We are simply picking on the poor grades.

- Coolidge: I thought the bonds they picked were the ones the banks were not allowed.
- White: I'll go along with you on that point, Governor, but I don't feel we should go so far as to allow all the poor grade securities not in default on the books, because I think the problem of keeping our banks in good condition requires a stricter application of standards than that would be.
- Harrison: I think the minority recommendation that - because they say we don't want to have a computation of net sound capital, because we realize if you don't deduct all depreciation or any depreciation, then net sound capital is a fictitious one and therefore we say we won't compute that net sound capital at all, and that is a logical consequence, I think, to ignore all depreciation.
- Folger: You certainly would agree, Governor, that Aaa bonds selling below par would have better chances of coming back to par than the Bbb in the lower grades.
- Harrison: That depends upon what you think about "easy money."
- Folger: We are saying we're not as alarmed about depreciation in the higher grades as we are in the lower grades.
- Harrison: There are a lot of people think there are better chances for the higher grades.
- Coolidge: I understand the point is, you're going to take all bonds, all securities, add up the market value - but there are certain bonds you're prepared to give a fictitious value to due to present conditions, and you want some groups of examiners to get together and determine what those bonds are and what the fictitious value is. I think we're going to come to that, George, either as market for the whole thing or else as market, with certain fictitious values for certain securities.

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- Harrison: I see the danger of not deducting depreciation in the C group, or groups below that, which the Comptroller now authorizes banks to buy, and I agree with Mr. White that if you are going to adopt the form recommended by the minority, of not considering any depreciation of any bonds that when you get below group one - Baa's - or some other figures, then you ought to adopt some conventional value rather than the market value for a write-back.
- Upham: Mr. Secretary, I think we have pretty well, now, the opinions on this, of these people; if we can get a vote on one question here, I think we would just about be through.
- H.M.Jr: I don't want Tom Smith to miss his train.
- Taylor: Can I ask one question, Cy, before we get there? Suppose you took all of group one and left out your fourth classification and then applied this formula. You think that would make a difference?
- Harrison: You mean where you put in the Baa's? They are the bonds I'm interested in.
- Taylor: They're in the group one.
- Harrison: You're going to leave them there and not require a deduction in the depreciation in the Baa's. I'd go further than that and say if the bank has some other bonds below that - that are below the bonds authorized to be purchased by the Comptroller, I would adopt Mr. White's suggestion to adopt some conventional value below the Baa rather than to ignore the depreciation entirely - rather than to write it down to market.
- H.M.Jr: Well, may I say I think that what we can do is this. You people have all been very frank and told us what you thought. Upham will write this thing up; we'll present it to the heads of these agencies on Friday morning, and see if we can get a unanimous agreement on some of these things. There's no use trying to do this unless we can get a unanimous agreement from all three agencies. Then my thought would be

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whatever we can get a unanimous agreement on, we'll then take it and I'd like to present it, by Mr. White, through you, to the various state banking authorities and see what we can get from them that would be unanimous.

I hope we can get at least one thing, because I'd like to say to the President, "After having the Federal and State banking agencies look this over, here is what they've unanimously agreed to." And by starting out equally, if we agree on one thing, he'll come back and say, "Why don't you do this the way we do it?" There will come out, a sort of exchange of the state and Federal bank examinations, working toward a more uniform bank examination, and that is the objective.

White:

I think you'll find a very pleasant experience working with us on that score. I assure you we can agree and we'll cooperate in every way to facilitate a general agreement on that score. I think it's a very important thing to do; I think it doesn't matter so much what decision we make with respect to various of these problems, the important thing is that we do get together once and for all and have uniformity.

H.M.Jr:

If there is anything which is as difficult to explain as this last point, I say don't let's do that among the first things we are going to do - that can wait. I mean, you people that are devoting your lives to it, if there is as much disagreement among you, after listening, I'd say, let's let that thing wait. Let that wait. But I wouldn't put up to you people anything but the three organizations here all agree on.

And, I'll tell you this: I'm willing to recommend to the President, as far as both the F. D. I. C., and the Comptroller's office is concerned, that both organizations be put under Civil Service. I mean, it's something that should have been done a long time ago.

Mr. Folger, thanks very much - we'll need you again.

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Folger: All right. (Leaves.)

H.M.Jr: Before Tom goes - he's got fifty-seven minutes yet - is there anything else along the lines suggested - reclassification and salary and such sort of things? Somebody have any suggestions they might like to make?

White: There was one little point suggested this morning by Mr. Groom. He spoke about the fear of banks to make these so-called capital loans for fear the next examiner will classify that in some way or another. This is just a question. Could it be possible to work out some instructions which would cause the examiner to lay off a new loan for a little while and at least give it a breathing spell, and see how it's going to turn out? I think there is nothing more disheartening to a Board of Directors than to have a loan classified before it's cold. It's the first thing, I think, to be given a little opportunity to be seasoned.

Groom: I think that is very good, Mr. White. I think the examination - instructions to the examiners are so important - I was so pleased to hear the Governor suggest that salaries be raised. I think we need a higher type of examiner - I mean, men who need - they can build a career, and by their own suggested initiative go forward. It strikes me as being one of the best suggestions coming out of this meeting.

Coolidge: I felt, for some time, that if you could have the examinations divided into groups - twelve - and one examiner hitched to each Reserve Bank so that each Reserve Bank had an examiner for that district and did their examinations through that examiner, as others having the control of the currency do its examinations through the same machinery, that you would get better uniformity.

H.M.Jr: I am not sure I understand. You mean detach them - make them responsible .....

Coolidge: Make them responsible to the Reserve Bank as well as Washington, and have only one set of

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bank examiners operating in the Reserve District.

H.M.Jr: Now, we have the Comptroller, the F. D. I. C., .....

Upham: The Federal Reserve Bank, and the states.

Coolidge: You couldn't possibly escape the states on their banks. I do think some scheme could be worked out for the responsibility.

H.M.Jr: I agree with you. What I'd like to do, if you people would be willing to come back another time, after we've gotten this one going, and take up, quite frankly, this whole question of where bank examinations should be - I mean, we have all kind of ducked it - and where the F. D. I. C. should be - should it be where it is, and all that sort of thing.

Harrison: It's got to be solved some day.

H.M.Jr: Yeah, and it might just as well be solved now. We're going to decide to work it over, we all assume, with recommendations, next January. I think we'd better put our teeth into it.

Harrison: Mr. Secretary, I have one more .....

H.M.Jr: Excuse me. That would take care of that. That would be part of it. I've heard this suggestion you're making, Jeff - it isn't a new one.

Coolidge: It goes back several years.

H.M.Jr: That doesn't mean, since it isn't new, it isn't good. I personally am for as much decentralization as is possible. We are doing it here in the Treasury all the time - we're placing more authority in the field. Whether it .....

Broderick: It would work in the field, Mr. Secretary.

H.M.Jr: You think it would?

Broderick: You bet it would.

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- H.M.Jr: We're trying to decentralize - put more authority on the people in the field. If they make good, all right; if not - if they don't - fire them. At least give them a chance.
- Harrison: I have one brief other suggestion to put on the table in response to your inquiry. We hear a good deal about loans, smaller business, capital, market, and the opportunity of small business to get capital. I wonder if the Comptroller's regulations on the definition of "marketability of securities" isn't as big a stoppage in that field as we have anywhere in our whole system. It's almost impossible for a small local concern now, putting out a small bond issue, to get over the head of the S. E. C. That's bad enough, but having gotten over their heads, they can't sell a bond to a banker merely because it's so small in amount that it's not readily marketable, in the definition of the Comptroller. Yet, the Comptroller will let that bank make a concern .....
- H.M.Jr: I'm sorry - to take that up. I'd like to see that thing thrashed through once and for all, because they keep throwing it in my face all the time.
- Harrison: You study the definition of "marketable securities" and you'll find you've got an impossible situation.
- Smith: What's the limit - oh, Folger's gone.
- Upham: I put a fourth page - three questions on that. The chief difficulty seems to be it's the Congress that says such bonds must be marketable.
- Harrison: That's all right. Just quote that in the regulations.
- Upham: If the small issue isn't marketable, the Comptroller couldn't say .....
- White: The Comptroller's had that for a long time.

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- H.M.Jr: The question is which comes first, the egg or the chicken?
- Upham: That's one of the things - can the law be changed; can the regulations be changed? It's the issue of regulations, finding what is marketable.
- H.M.Jr: I'd like to go over that.
- Smith: He can just say marketable securities and oftentimes small securities are just as marketable as big issues.
- H.M.Jr: I personally think this was a very good meeting.
- Harrison: Mr. Secretary, only one last word. You said as we were concluding that you hoped we would not bring up the debatable question with which to use an hour to get nowhere. That was, the net appreciation against net depreciation. You did not mean to exclude from consideration this last topic of how depreciation in bonds for consideration of determining net sound capital, is considered, because I think that is the biggest question before the whole group.

000oo000

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May 6, 1938

ADDENDUM

George Harrison, President of the Federal Reserve Bank of New York, called on the telephone to say that he had overstated the case at the meeting in the Secretary's office on May 4th when he said that the slow column had been completely eliminated in the examination report form of the Federal Reserve Bank of New York. He said that the column is still carried and is still denominated as "slow," but the number of items placed in it by the bank examiners has been very greatly reduced. Only loans in which losses are anticipated or considered as likely to occur are classified in this column. In other words, he said the examiners of the Federal Reserve Bank of New York adhere pretty strictly to the new definition of the slow column as expressed in the instructions of the Comptroller of the Currency in 1934.

The majority agreement with respect to the classification of loans is that the three columns in the examination report now known as slow, doubtful, and loss will be continued. Their present form, and that of the instructions to examiners as to the type of loan to be included in each of the three columns, will remain the same as at present. It is proposed to label these three columns by the roman numerals I, II and III. At the top of each page upon which this tabulation occurs, there will appear the roman numeral I and following it a definition of the type of loan which is included in the column; there will also appear roman numeral II followed by the single word "doubtful"; and there will also appear the roman numeral III followed by the single word "Loss".

Where there is a recapitulation of the columns now known as slow, doubtful and loss, the same device will be used, i.e., the use of the three roman numerals as symbols with the accompanying explanation of what is included under ~~that~~ <sup>each</sup>. As now, on the recapitulation page only the totals in columns II and III will be included in figuring the net sound capital of banks.

(It should be noted that this agreement would result in the complete elimination of the word "slow" from loan classifications.)

May 2, 1938

The minority position with respect to the classification of loans in the examination report is that the column now known as "slow" should be eliminated from the pages upon which it now appears and that provision be made elsewhere in the report, under a heading "Loans Listed for Information or Comment", or other suitable heading, for listing, with appropriate comment, not totaled and not included in any recapitulation, such loans as the examiner feels should be set out for the information of the directors and proper officers of the bank, with the clear understanding that such loans are not being classified as doubtful or loss and are not necessarily to be regarded as criticized assets.

May 2, 1938

April 28, 1938

In 1934 with total loans in 5,275 national banks of \$7,740,596,000, national bank examiners classified 27 per cent in the slow column.

In the last half of 1937 with total loans in 5,267 national banks of \$8,933,216,400, national bank examiners classified only 9.81 per cent in the slow column.

<u>Year</u>	<u>Slow</u>	<u>Doubtful</u>	<u>Loss</u>
1934	27%	4%	2.9%
1935	16%	2%	.8%
First half of 1937	10.66%	1.14%	.65%
Last half of 1937	9.81%	1.06%	.49

The majority agreement with respect to the appraisal of bonds is

1. That depreciation in stock and defaulted bonds be classified as loss and that securities in these groups (III and IV) be listed and priced in the report of examination. (The minority does not disagree on this point.)
2. That depreciation on securities in group II and in the fourth grade of general market obligations in group I be deducted in the report in computing the net sound capital of the bank, and that securities in these classifications be listed and priced in the report of examination.
3. That depreciation in all group I securities except the fourth grade of general market obligations be disregarded and that these securities not be priced in the report of examination.
4. That unrealized appreciation be not allowed.
5. That a premium on bonds purchased at a premium be amortized.

May 2, 1938

The minority position with respect to the appraisal of bonds is

1. That only depreciation in stocks and defaulted bonds be classified as estimated loss, and that securities in these groups be listed and priced in the reports of examination. (This is in accordance with the views of the majority.)
2. That securities in groups I and II be not priced, and preferably be not listed, in the report of examination. A complete list of all securities, however, should be attached to the reports of examination sent to the supervisory authorities.
3. That depreciation, other than in stocks and defaulted bonds, should not be taken into consideration in computing "net sound capital." On the other hand, it can not be affirmatively stated that depreciation in any securities constitutes sound capital. Therefore, the minority feels that the schedule showing a computation of net sound capital be eliminated from the reports of examination.
4. That unrealized appreciation be not allowed.
5. That a premium on bonds purchased at a premium be amortized.

May 2, 1936

The majority agreement with respect to the treatment of net profits from the sale of securities is that until adequate reserves against the securities account have been built up, all such profits should be impounded and be unavailable for any purpose other than to take care of losses resulting from the sale of securities.

May 8, 1958

The minority position with respect to the treatment of profits from the sale of securities is that

1. Estimated losses should be charged off.
2. Banks should be required to establish and maintain adequate reserves, including reserves against the securities account.
3. Banks should not be required to earmark individual items of profit, regardless of source.
4. Speculation should be severely criticised and penalised.

May 2, 1936

*Bankers  
by*

1. Should the use of the word "slow" as a classification of loans by bank examiners be abandoned?
2. Should loans of the character described in the instructions to national bank examiners in 1934 be listed in a column parallel to the doubtful and loss columns; or would it be preferable to eliminate this column and list such loans on a separate page?
3. Is it objectionable to total the criticized loans, other than doubtful and loss, and show them on the recapitulation page?
4. Should the loans described in the 1934 instructions to national bank examiners be subjected to criticism at all?
5. Would good bankers be deterred from making good loans by the inclusion of the slow column, renamed?
6. Are bank directors alarmed by the slow classification practice and is it a deflationary influence?

May 3, 1938

1. Should the list of securities in a bank's portfolio be listed by examiners in the examination report?
2. Should all or a part of the securities' list be priced in the report?
3. Should all or a part of the depreciation in securities be deducted in computing the net sound capital of a bank?
4. Should the net sound capital of the bank be computed in the report?

May 3, 1958

1. Should banks be required to establish and maintain any particular percentage reserve against future losses in the securities account?
2. Should reserves be permitted against estimated losses in the securities account, or should such estimated losses be written off?
3. Should banks be required to impound the profits on sales of securities in a reserve account against future losses in the securities account, or should all profits be treated alike and the general condition of the bank be the test as to the reserves required?
4. Would a requirement that all profits from the sale of securities be impounded in a special reserve account
  - (a) Affect the bond market adversely?
  - (b) Discourage speculation and in-and-out trading?

May 3, 1936

1. Should the law which requires that securities purchased by national banks and state member banks of the Federal Reserve System be "marketable" be changed?
2. Should the test in the Comptroller's Regulation that securities purchased by national banks and state member banks of the Federal Reserve System be not "predominantly speculative" be changed?
3. Should the list of securities eligible for purchase be expanded or contracted?

May 3, 1938

Wednesday - 10:30  
May 4, 1938.

Jeff Coolidge

Com. Wm. R. White

- State Bank Examiner

Joseph A. Broderick

- Pres. East River Savings

Thomas J. Groom

- Bank of Commerce & Savings

Robert Hanes

Herman Wells

See M is having a meeting  
 On wed 10.30 or so when  
 time he will discuss  
 the new regulations <sup>which we are going to have</sup> see bank  
 examinations. He wants to  
 show them before you  
 advise

May 4

MD 10:30

Jeff Coolidge ok 113

Com <sup>Wm R.</sup> White?  
State Bank Examiner

Jos. A. Brodbeck - Pres  
East. Res. Savng

Thos. J. Groom - Bank of Comm. Savngs

Tom Smith + I 114  
Want you to invite  
for Wednesday.

Robert Hanes of  
Winston Salem, N.C.

and  
Herman Wells of  
Bloomington, Indiana.

---

I shall be glad to  
do it for you if  
you agree. Lynn

FORM 8846

TREASURY DEPARTMENT  
PROCUREMENT DIVISION  
PUBLIC BUILDINGS BRANCH

PROCUREMENT DIVISION  
**Treasury Department**  
TELEGRAPH OFFICE

115

36 W E 22

NEWYORK NY 124P APRIL 28 1938

1938 APR 28 PM 1 46

MRS H S KLOTZ

WASHNDC

HAVE COMMUNICATED WITH MR WHITE OVER LONG DISTANCE AND CAN ADVISE  
YOU HE WILL ATTEND THE SECRETARYS MEETING WEDNESDAY MORNING MAY FOURTH

IRVING A J LAWRES

147P

May 4, 1938

A group who had been invited by Secretary Morgenthau met with him in the morning and in the afternoon to discuss proposals looking toward the unification of certain bank examination practices and policies. Those present included:

Joseph A. Broderick of New York  
T. J. Coolidge of Boston  
Thomas J. Groom of Washington, D. C.  
Robert M. Hanes of Winston-Sales, North Carolina  
George L. Harrison of New York  
Tom K. Smith of St. Louis, Missouri  
William R. White of New York

The statements of majority agreement and minority position on the matters of loan classification, bond appraisal, and treatment of bond profits were placed before the group and the enclosed list of questions was used as a basis of determining sentiment toward the proposals now under discussion.

While there was considerable discussion and not complete unanimity of views on all the matters discussed, the consensus was

(1) That the use of the word "slow" as a classification of loans by bank examiners might well be abandoned.

- 2 -

(2) That the three parallel columns now appearing in the examination report be retained. A suggested definition for Column I was "not presently doubtful but requiring constant attention."

(3) No one was violently opposed to totaling and recapitulating the three columns if the new designation and definition of Column I are adopted. (There were some preferences expressed for Column I loans being carried separately and not totaled or recapitulated.)

(4) Good bankers would not be deterred from making border-line loans by the inclusion of Column I. (There were some dissents to this.)

(5) Bank directors are disturbed by the slow column and probably should be. (The view was expressed that regardless of the 1934 instructions as to what loans should be included in the slow column, bank examiners continue to list loans that are slow in fact even though good as to quality.)

(6) The entire list of securities in a bank's portfolio should be listed in the examination report.

(7) The entire list of securities in a bank's portfolio should be priced in the examination report.

- 3 -

(8) The net sound capital of a bank should be computed in the examiner's report.

(9) Just what depreciation in the portfolio should be deducted in computing the net sound capital of a bank was left somewhat indefinite. It was suggested by Mr. White that if the net depreciation in Group II securities, plus Baa bonds, is to be deducted in computing net sound capital (and appreciation in Group I securities, exclusive of Baa's, is to be ignored), the basis for figuring depreciation in this group should be worked out along the lines of the so-called "convention values" used by insurance companies representing, perhaps, the average price of the security over a period of a year or more past. It was suggested that if and when Group I securities show a net depreciation, perhaps the situation will have to be surveyed again. There were expressions that the inclusion of net depreciation in the lower grade securities without any benefit from appreciation in higher grade securities was a little unfair.

(10) While no definite consensus was obtained on the treatment of bond profits, I think it is fair to say that the group favored the creation of adequate reserves

- 4 -

against losses, but were doubtful about the success of enforcement of a rule that securities profits be impounded in a special reserve account.

(11) There were expressions of opinion to the effect that the definition of marketability contained in the Regulation of the Comptroller of the Currency interpretative of Section 5136 Revised Statutes should be revised.

Enclosure

1. Should the use of the word "slow" as a classification of loans by bank examiners be abandoned?
2. Should loans of the character described in the instructions to national bank examiners in 1934 be listed in a column parallel to the doubtful and loss columns; or would it be preferable to eliminate this column and list such loans on a separate page?
3. Is it objectionable to total the criticised loans, other than doubtful and loss, and show them on the recapitulation page?
4. Should the loans described in the 1934 instructions to national bank examiners be subjected to criticism at all?
5. Would good bankers be deterred from making good border line loans by the inclusion of the slow column, renamed?
6. Are bank directors alarmed by the slow classification practice and is it a deflationary influence?

May 3, 1938

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2. Should all or a part of the securities' list be priced in the report?
3. Should all or a part of the depreciation in securities be deducted in computing the net sound capital of a bank?
4. Should the net sound capital of the bank be computed in the report?

May 3, 1938

1. Should the law which requires that securities purchased by national banks and state member banks of the Federal Reserve System be "marketable" be changed?
2. Should the text in the Comptroller's Regulation that securities purchased by national banks and state member banks of the Federal Reserve System be not "predominantly speculative" be changed?
3. Should the list of securities eligible for purchase be expanded or contracted?

May 3, 1938

1. Should banks be required to establish and maintain any particular percentage reserve against future losses in the securities account?
2. Should reserves be permitted against estimated losses in the securities account, or should such estimated losses be written off?
3. Should banks be required to impound the profits on sales of securities in a reserve account against future losses in the securities account, or should all profits be treated alike and the general condition of the bank be the test as to the reserves required?
4. Would a requirement that all profits from the sale of securities be impounded in a special reserve account
  - (a) Affect the bond market adversely?
  - (b) Discourage speculation and in-and-out trading?

May 3, 1938

May 4, 1938

Col. Harrington's office telephoned the following:

Employment figures for week ending April 30 -- 2,583,196

Increase over week ending April 23rd 38,072

Wednesday  
May 4, 1938  
12:23 p.m.

125

HMJr: He's just - Butterworth is coming in now any minute on the wire.

Herbert Feis: Ah - with his reply?

HMJr: Yes.

F: Baron de Gruben, the Counselor of the Belgian Embassy...

HMJr: Yes.

F: ... after telephoning ~~is in my office~~ inquiring ...

HMJr: Well, C , he saw Taylor a few minutes ago.

F: Well, I didn't know that.

HMJr: Yeah.

F: (Speaking to the Baron: Have you seen Mr. Taylor?) He says no.

HMJr: Well then it's - then have they got a Financial Attaché?

F: (Speaking to the Baron: Have you a Financial Attaché?) No, there's some mistake.

HMJr: Because Taylor excused himself an hour ago to go out to see somebody....

F: He - ah - de Gruben said Léonard, who is one of their staff, saw Wayne but on a wholly different question.

HMJr: Oh. Uh huh.

F: Now, I wanted to know whether I could just give him an account of what happened.

HMJr: No, I wouldn't. No, I mean I wouldn't - if you don't mind.

F: Well ...

- 2 -

HMJr: Because - then we - why didn't we do it to the Swiss and why don't we do it to the Dutch. Ask him to come back this afternoon; the thing will be settled then.

F: And - would Wayne Taylor talk with him this afternoon?

HMJr: Sure. This afternoon. If you don't mind...

F: No, no. That's why I....

HMJr: I'd definitely put it off until this afternoon.

F: That's exactly why I telephoned.

HMJr: Right.

F: All right.

HMJr: And ...

F: I've got - have you got another minute?

HMJr: Sure.

F: I've got apropos of that message, the one that didn't go...

HMJr: Yes.

F: I made a rather long draft with background...

HMJr: Yes.

F: ... I think has some interest. Now I think I'll, if you're not in a rush, show it to Mr. Hull first.

HMJr: Good.

F: Before moving it over to you.

HMJr: Good.

F: Right, sir.

HMJr: Thank you.

F: Goodbye.

May 4, 1938.  
1:17 P.M.

H.M.Jr: Hello

Butterworth: Hello Mr. Secretary.

H.M.Jr: Well you've had me here on pins and needles for an hour.

B: (Laughs) I'm sorry - I've been doing the best I could - I've been trying to get a decision.

H.M.Jr: Yes.

B: And it - ah - the - the statement is alright by them.

H.M.Jr: Yes.

B: Ah - they - they think that we should both send send statements but they don't say that they have to be identical.

H.M.Jr: They think what?

B: We should both send statements.....

H.M.Jr: Send out statements?

B: That we should both send France a reply.....

H.M.Jr: Yes.

B: ....but that those replies need not be identical.

H.M.Jr: Yes.

B: Our - our reply has their approval.

H.M.Jr: Good.

B: Ah - I also have a copy of their reply, if you'd like me to read you that.

H.M.Jr: Yes I would.

B: And - ah - as soon as that is typed up they are going to hand it to the French Ambassador.

H.M.Jr: I see.

B: "His Majesty's Government.....

H.M.Jr: Wait a minute - start off - "His Majesty's Government.....

B: .....regret

H.M.Jr: Re - what's that?

B: "His Majesty's Government regretted to learn from the communication made to the Chancellor of the Exchequer by the French Ambassador on May 2d that the French Government consider it impossible to maintain the current rate of the Franc and that they felt that they had no alternative but to allow the Franc to fall to a rate in the neighborhood of one seven five.

B: Paragraph.

H.M.Jr: Yes.

B: "His Majesty's Government take due note of the intention of the French Government as explained by Monsieur Bonnet to the Chancellor of the Exchequer to achieve as the eventual result of their policy a rate corresponding to the economic condition and giving to France no competitive trade advantage. They note also the assurance given by the French Government to the United States Government on the 4th of May as to the finality of the present reduction".

B: And then is quoted a French phrase.

H.M.Jr: Then is quoted what?

B: That French phrase.

H.M.Jr: Yes.

B: (Speaks about two lines of French)

- 3 -

H.M.Jr: Yes. All right.

B: Paragraph.

H.M.Jr: All right.

B: "In these circumstances and after consultation with the United States Government his Majesty's Government are prepared to regard the proposal as being not inconsistent with the Tri-partite Agreement which in common with the United States Government they regard as continuing in full operation. "

H.M.Jr: What's that - finis?

B: What?

H.M.Jr: That's all?

B: That's all.

H.M.Jr: Now - Butterworth.

B: Yes.

H.M.Jr: Are they going to make any statement over there publicly?

B: Now the British are not going to make any public statement tonight but there will probably be some after the House of Commons - perhaps tomorrow.

H.M.Jr: I see.

B: Now I asked Archie whether we were going to give that note out or if the French did whether we would permit them to do so.....

H.M.Jr: Yes.

B: .....but it doesn't seem to me that we can do that since it refers to a French note of May 4 which we are not in a position to give out.

H.M.Jr: Yes - well what I'm going - hello

B: Just one thing more, sir.

H.M.Jr: Yes.

- 4 -

B: The British have called over the - the French Financial Attache here.....

H.M.Jr: Yes.

B: .....,and said to him, "What is - what is Daladier going to say about this tonight?"

H.M.Jr: Yes.

B: And - and they are now scrapping with him as to that text.

H.M.Jr: I see. Well - this is what I'm going to do - you tell the British Treasury this.

B: Yes.

H.M.Jr: I've got Cochran on the other phone - I mean tied up on the French phone, see?

B: Yes.

H.M.Jr: I'm going to tell him that this message he should deliver to the French Treasury.

B: Yes.

H.M.Jr: I've got both the British and French Financial Attaches in my outer office.

B: Yes.

H.M.Jr: And I'll give them copies of this.

B: Yes.

H.M.Jr: Now - I now will tell Cochran please to ask the French Treasury what they propose to do in regard to publicity.....

B: Yes.

H.M.Jr: ....and to call me back.....

B: Yes.

H.M.Jr: ...but pending hearing what they are going to do about publicity I'm going to sit tight.

- B: Well now I can tell you what they propose - I - I just got this on the - on the other phone.
- H.M.Jr: Yes.
- B: Now this is what Daladier proposes to say on the wireless. Can you take it down? "The French Government in full agreement with his Majesty's Government and the Government of the United States of America have decided to adjust the level of the franc to a rate which will permit it to be defended victoriously.
- H.M.Jr: Victoriously.
- B: ~~Yes~~ successfully.
- B: "This decision has been taken within the framework of the Tri-partite Agreement.....
- H.M.Jr: Yes.
- B: .....to which the French Government remain safely attached".
- H.M.Jr: Ah-ha.
- B: Now Phillips has just given me this on the other telephone.....
- H.M.Jr: Yes.
- B: .....and he's with the French Financial Attache now. Phillips' instinct is - ah - that he doesn't very much
- H.M.Jr: He what?
- B: He doesn't very much like the wording of that first sentence.
- H.M.Jr: Ah-ha.
- B: What's your reaction of it?
- H.M.Jr: Well - I'll tell you - it's like (laughs) this - I - I don't think we've got time; I don't think you can do anything about it and I think we'll have to take it and like it.

- 6 -

B: I think Phillips will sort of battle that out.  
I mean he'll fight our battle as well as his own.

H.M.Jr: Well we've done a darned good job for the British  
in the last two days - hellô?

B: Yes sir.

H.M.Jr: I say I think we've done a good job for the British  
the last - as well as ourselves.

B: I think so too.

H.M.Jr: Because I think the fact that they've agreed not  
to let it go below one hundred seventy-five was -  
is distinctly a victory.

B: I think so too.

H.M.Jr: And I think we've got the best we could out of a  
very difficult situation.

B: I do too.

H.M.Jr: So - ah - I'll - I'll - I'll release it but I'm  
going to tell Cochran.....

B: Yes.

H.M.Jr: .....please to find out what they're going to do  
about publicity and let me know.

B: All right.

H.M.Jr: And then I'll tell him to call you direct and let  
you know.

B: Good. Thank you sir.

H.M.Jr: Now what else?

B: Well that's all sir. The - the only thing is the  
rumors here of this - have been worrying the  
so much - there's all sorts of rumors of general  
devaluation. I believe about one million pounds  
of gold was done out at

H.M.Jr: Well - ah - we'll see - I mean the boys here have been awful hot after us to make a statement. Of course, I'd much rather let the French make it if he makes it within a half an hour.

B: I think he'll have to make the statement in his wireless address.

H.M.Jr: Well that takes care of that.

B: Yes, because otherwise, as I say, if we make a statement it takes the cream off of them.

H.M.Jr: Well.....

B: And after all it's his show.

H.M.Jr: Well let's hope that - ah - they meet with a modern success.

B: And I hope so too, sir.

H.M.Jr: (Laughs) All right.

B: Thank you very much, sir.

H.M.Jr: Thank you - goodbye.

May 4, 1938.  
1:25 p.m.

H.M.Jr: Hello.

O: Hello

H.M.Jr: Give me Cochran on the French phone.

O: All right.

Cochran: Yes.

O: Go ahead.

H.M.Jr: Cochran.

C: Yes sir.

H.M.Jr: Ah - the British have O.K'd our statement - hello?

O: Yes.

H.M.Jr: Now - ah - ah - he - have you got it already?

C: Yes - Archie gave it to me; I read it back; I have it all down.

H.M.Jr: Fine. Now the British read their statement to us which is not quite the same but I'm not going to take the time to tell it to you over the phone.

C: Oh no, certainly not.

H.M.Jr: See?

C: Yes.

H.M.Jr: So - ah - you let them know because Daladier is going on the radio, isn't he in 30 minutes?

C: Yes, I just have that statement now.

H.M.Jr. Now.

C: And he goes on at 8.

H.M.Jr: All right. Now you tell them that - now - that - please find out what they're going to do about our statement - if they're going to do anything on publicity. I mean are they going to release our statement on the other side or what are they going to do?

- 2 -

- C: Just what are they going to do with this statement which I give them?
- H.M.Jr: That's right.
- C: What are they going to do with that?
- H.M.Jr: That's right.
- C: All right and - ah - are you people going to listen in to Daladier's statement?
- H.M.Jr: What's that?
- C: Did you ever try to listen in to the broadcast statements from over here?
- H.M.Jr: Ah - Butterworth read to me what he's going to say.
- C: Monnick had it over there.
- H.M.Jr: Well he's read it and they asked me how I felt about it and I said, "Well what's the difference. He won't change it in the next 30 minutes anyway".
- C: Yes - yes.
- H.M.Jr: See?
- C: Yes.
- H.M.Jr: And so I - I think - I don't know how you feel - but I think we did - we distinctly got something in the last two days.
- C: There's no - no question about it and I think if we ever have any other negotiations we'll be a little more careful about the time we start.
- H.M.Jr: I think so.
- C: Yes - yes.
- H.M.Jr: Well - cherrio.
- C: I'll get in touch with them right now, I'll go right over.

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H.M.Jr: Yes you better because I imagine they're all sweat on account of Daladier going on the phone in 30 minutes.

C: And then I'll call you back or - I'd better call you back in regard to the publicity.

H.M.Jr: If you please.

C: All right.

H.M.Jr: If you please.

C: Fine, and I won't report Daladier's speech, unless I hear it by radio.

H.M.Jr: All right.

C: It will all be out in the morning but if I - if I get anything more on it yet to-night I'll tell you when I call you back.

H.M.Jr: Well personally I'm going to listen to Hoopnagle.

C: (Laughs) I see.

H.M.Jr: (Hearty laughter)

C: I'll go over to the Treasury right now then.

H.M.Jr: All right (still laughing) Goodbye.

Thursday  
May 5, 1938  
9:06 am

H. Merle Cochran: But I wanted to give you a summary up to date.

HMJr: Yeah.

C: This morning the Guaranty told me at ten o'clock that sterling had opened with the bank a buyer of sterling at one seven eight ninety and a seller at one seven nine.

HMJr: Yeah.

C: And at ten-thirty it was going about the same and the franc premium had been lowered three quarters on forward rates without any discount.

HMJr: Yeah.

C: Then I went out to the Bank of France and by eleven thirty they had taken in fourteen million pounds sterling.

HMJr: Fourteen million pounds!?

C: Fourteen million pounds.

HMJr: For heavens sakes!!

C: At eleven thirty.

HMJr: What?

C: I also got figures in regard to the contest last night..

HMJr: To the what?

C:

HMJr: To the what?

C: How much they had in their control last night.

HMJr: Yes.

C: I mean after close of business. I've cabled that unless you want it now.

HMJr: Well I want it now.

- C: They had gold in foreign exchange at close of business last night two billion four hundred eighty-one million francs.
- HMJr: Well, and now on top of that they've got what they picked up today.
- C: Yes. And they have in French francs eleven billion two eighty-nine.
- HMJr: Uh huh.
- C: But I spoke with my friend again at two-fifty; it's now three-ten.
- HMJr: Yes.
- C: I spoke with him down at the Bourse and by that time they had taken in twenty-five million pounds altogether.
- HMJr: You don't mean twenty-five million pounds!?
- C: Twenty-five million pounds, yes. And they had taken in about ten million dollars through the Chase; the Chase is operating here for them.
- HMJr: Now wait a minute. These figures don't seem possible.
- C: Well, now those are the figures. No, it's a tremendous and they're paying about thirty-five eighty-five for the dollar.
- HMJr: They've taken in today twenty-five million pounds!?
- C: Pounds. Yes, sir. It was fourteen million when I was out there at half past eleven.
- HMJr: Uh huh.
- C: I mean after all my friend definitely gives you some idea of the position against the franc decision that was made the last few days.
- HMJr: Well, as I told you before and you tried to take it personal, it must be nice to know that - that to buy at a hundred and sixty and sell at a hundred and seventy-five.

C: Yes. Yes.

HMJr: As the Chinese say, there's a nice "squeeze" in that.

C: I should say so. And the franc is now at a premium of one quarter franc against sterling and dollars silver.

HMJr: What?

C: I say the forward franc is at a premium against both sterling and dollars.

HMJr: Yes.

C: And when I went to see my friend this morning and he said the rate was about one seven nine; and I said, "Well, didn't your people say anything to you about a one seven five rate?"

HMJr: Yeah.

C: Hello.

HMJr: Yes, I'm here.

C: And he said they just mentioned one seven nine. So then I called over at the Ministry.

HMJr: Yes.

C: Then I saw Rueff and I said, "Well, just what's the idea here? - I suggest another rate." And he said, "Well, you said around that." He said that they opened up here to get the benefit of a decline.

HMJr: Well, of course, I'm not going to lose my temper, but I have a message in writing from the French Cabinet saying they would not ..... (Secretary starts conversing with group in his office.)

C: Well, I don't hear. Hello. Hello.

Operator: Just one moment, please.

HMJr: Hello.  
(Speaking to men in his office: I thought they did - I thought they had put it in.)

O: Just one moment, Please. Hello.

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HMJr:

Yes.

O:

Just one moment. We're having some trouble; we'll try to call you in just a minute.

(Pause while Secretary talks to group in his office: it was Well you told me/a hundred and seventy-five. \* \* \* Well, we all sat around here. I mean what's the use of having us all sit around here. I've said again and again you fellows get time to read those things - you said one seventy-five and Harry White said one seventy-five - you all seem to sit around here; you let me work on this thing - Where is Harry White? I sent for him ten minutes ago. What's the use of having people all sit around. The purpose is here to check me. White, what did you think that they said was the final figure that they would depreciate at? There we are; you all say a hundred and seventy-five. Now, Archie walks in and doesn't....)

O:

Hello. Hello, Mr. Morgenthau.

HMJr:

Yes.

O:

Go ahead, please.

HMJr:

All right.

Secretary continues to speak to group in his office: I mean we all sit around here. It's like that other time we all sat around - the night we overlooked this...

O:

Go ahead, please.

HMJr:

...on the gold thing - (Still speaking to group in his office.)

HMJr:

Hello.

C:

Hello.

HMJr:

I say, what is the sense of the French making any statement to me that it's going to be the last devaluation? They left me under the impression that it was going to be a hundred and seventy-five and now it's a hundred and seventy-nine.

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- C: That's just why I went over there, Mr. Secretary. When I saw Rueff I said, "What the hell rate have we been talking about here for three days?" And he said, "Oh, you're protesting?" I said, "I have no instructions whatever but I certainly protest...." (Conversation breaks off)
- HMJr: Hello.
- C: Hello.
- HMJr: Well, you can tell them for me that I'm very much disturbed, see?
- C: Yes.
- HMJr: Now I was under the distinct impression that they said a hundred and seventy-five would be the last.
- C: Yes.
- HMJr: And ...
- C: I said to him, I said, "That's what I understood last night," and I said, I must call you as soon as possible - concerning time - to explain this. And Rueff said, "Well, the Minister will want to see you if you're annoyed over this."
- HMJr: Well, I - what the hell difference is there in being tied up with a man who is a private speculator or a government that's just a speculator?
- C: Yeah. Well anyway, I went in to see the Minister then. Hello.
- HMJr: Yeah.
- C: I saw him just before one o'clock; he had just been making a declaration to the press. He said, "Well Rueff said you were annoyed - you, Cochran, are annoyed over our opening at one seven nine." I said, "You didn't mention any margin of maneuvering - anything of the sort." I said, "You didn't tell me one seventy-nine and," I said, "you didn't tell me anything last night except that." He said, "Well, we didn't make a decision until this morning." I said, "Well, we made a decision about one seventy-five in the past three days." And he said, "Well, my experts told me this morning that I should open up as high as one eighty-one." And he said, "I told him

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that that was too far so he agreed at one seven nine."

HMJr: Well, who was this you were talking to?

C: The Minister himself. I saw him at ten minutes to one.

HMJr: Well, they certainly left me under the impression that it was not going below a hundred and seventy-five and everybody in the Treasury was under the same impression.

C: Well, I was so strongly under it that I went there this morning without any instructions as I thought I could get a story from them and see what explanation I'd have to give to you as soon as I could get in touch with you.

HMJr: Well I make the point - there isn't a God-damned bit of difference between doing business with an individual speculator than this French Government!

C: Yes. Yes.

HMJr: And I mean, if all they're interested in is in speculating in the franc I don't want to do business with them.

C: Yeah. Well, I told him, I said, "We talked a hundred and seventy-five," and I said, "now you forget." And he said, "Yes, we wanted to get a good start." I said, "When you get a good start this way it just means that your French business people who have been holding foreign currency now sell it at a rate of more - above the rate which we agreed upon and have that much advantage against our merchants, against the British merchants, and

HMJr: Well I think it's an outrage.

C: And he and he said, "I expect to bring it beyond one seventy-five."

HMJr: Well, they'd better! Because, ah - as I say, I'm sick and tired of doing business with them. I'm just sick and tired.

C: Well, this is the first time I've ever talked to them the way I did this morning.

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HMJr: Well, it's the first time I've talked this way.

C: I had no instructions or authority. I said, "No, but I take the responsibility myself."

HMJr: Well, you can tell them you've talked to me and I - I'm simply amazed!

C: All right, sir.

HMJr: I'm simply amazed. Now, just wait a minute.

(Long pause while conversation goes on in Secretary's office.)

HMJr: Hello. Hello.

C: Yes. Hello.

HMJr: Now Cochran.

C: Yes, sir.

HMJr: After all, the cable that you sent me on Monday said one seventy-five.

C: Yes.

HMJr: Then the French Ambassador here brings in a note on Wednesday morning and says, "This will be the limit."

C: Yes. That's right.

HMJr: Now, we have certainly every reason to believe that what they were referring to was their previous message.

C: Yes. Yes.

HMJr: Because first they say to us, "We will depreciate to one seventy-five." They say that on Monday - Monday at one o'clock in the morning they say, "We'll postpone it." Then they come in Wednesday morning and say, "Well, this will be the limit." Well, if they weren't referring to one-seventy-five what the hell were they referring to?

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- C: Well, I made that point and they said, "Oh, we said around one seventy-five."
- HMJr: No, they did not.
- C: Well, that's in the message then. But I said, "Even if you said around one seventy five," I said, "you're taking an unfair advantage there." I said, "One seventy-nine isn't around one seventy-five even."
- HMJr: Now, wait a minute, Archie is saying something.  
(Short pause)
- HMJr: Hello.
- C: Yes.
- HMJr: Cariguel's instructions last night - now get this - to the Federal Reserve were: Don't let the franc go one fraction below one seventy-five.
- C: Absolutely. I brought that up; I didn't know that instruction but I told ...
- HMJr: Well, now you know it.
- C: Yes.
- HMJr: That the instructions were - not one fraction below one seventy-five.
- C: Well I said to Rueff, I said, "We've submitted this and stood by this rapid depreciation." And I said, "We - I know that the rates have stopped at New York last night a little below thirty-five to the dollar or one seventy-five to the pound." And I said, "This morning you do deliberately just what we'd avoided giving our own country - of making a purposeful drop in the franc."
- HMJr: Well, as far as I'm concerned, as I say, I can't be too emphatic in my disgust and - ah - as far as I'm concerned it's the last time I take their word on anything financial.
- C: Yes. Yes.

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HMJr: Now I should think that the friendship of the United States would be worth something to them and they keep coming in here and making pretty statements and all that but they don't keep their word.

C: No, no. No, they're

HMJr: And - ah - to let those inside crowds clean up a lot of money it's just - it's just an outrage.

C: Yes, yes.

HMJr: And they'd better tonight bring that down to one seventy-five if they know what's good for them.

C: Do you want me to intimate that?

HMJr: I - absolutely!

C: Fine. I just wanted to be sure because ....

HMJr: You tell them that there isn't any - the slightest doubt in my mind that one seventy-five is the limit and if they don't bring the franc down to one seventy-five or just under that I consider that the French Government has broken their word.

C: To bring it down today?

HMJr: Today!

C: All right, sir.

HMJr: Today! And if they don't do it I consider they've absolutely broken their word.

C: All right, sir.

HMJr: Now don't hesitate to call me. And I don't care how strong you put it.

C: All right. I'll go right over - they ought to be in now. I'll try to see them right away.

HMJr: Today. I want it down to one seventy-five and if they've taken in over a hundred million dollars they can use it.

C: Yes. Absolutely.

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- HMJr: Now I'm very very much annoyed.
- C: Because every Frenchman who has been acquiring francs at that rate has that much advantage over our traders.
- HMJr: Well, that is true, but the whole purpose of this - I mean the whole spirit of this Tri-partite is that I can believe the word of the Council of Ministers!
- C: Yes.
- HMJr: Now, if the word of the Council of Ministers isn't worth the paper it's written on why I'm not going to do business with them!
- C: No. That statement I'm reading over again - ah - the one that I turned in and which you also got where it said, "The rate at which the French Government has decided to stop is around one seventy-five francs to one pound with the will to lower progressively this figure in correlation with the economic improvements which it expects from this decree."
- HMJr: Yes.
- C: And either to start back from a hundred and seventy-five and not from a hundred and seventy-nine.
- HMJr: Well, you go over there and you can put everything you got into it and I'm backing you a thousand percent.
- C: Thanks a lot. I'll enjoy it.
- HMJr: All right.

## GROUP MEETING

May 5, 1938.  
9:30 A. M.

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

H.M.Jr: I thought we might get re-acquainted. Thought we'd have a nice quiet morning, but our dear friends, the French, after agreeing that they would not let the franc go beyond 175 francs a pound, opened it up to 179. In other words, their word is just that (snaps fingers).

I've got different memoranda from you, but you'll just have to keep after me to do them. I thought I'd be able to do it - I thought I'd have a nice quiet morning this morning. Instead of that, we're right back where we were.

I've talked over-seas, in the last three days, seventeen times. Seventeen times we've talked over-seas.

Magill: Have you talked to Manilla?

H.M.Jr: No.

Magill: That's the cachet of success when you talk to Manilla.

H.M.Jr: The thing that's got me upset so is that Mr. Roper said certain things that in the New York Times are credited to me. I just can't take it, Herbert.

Gaston: We'll put out a statement that you don't believe in .....

Oliphant: Is that a misquote?

H.M.Jr: In the New York Times, yes. I'm going to - Gaston, I tell you - wait and try to get it in the Wall Street Journal, the way they did that time. You want an accurate report in the Wall Street Journal.

Gaston: Yes, but they wouldn't do it.

H.M.Jr: You sure?

Gaston: Yes.

H.M.Jr: O. K. Too business-like.

Magill: ~~The~~ revenue bill is about done. I imagine they will get it enacted early next week.

H.M.Jr: Is it a soft-boiled egg or four minutes?

Magill: Well, it's kind of soft on both ends and hard in the middle, I should say.

H.M.Jr: What else?

Magill: I think that's about all.

H.M.Jr: Does she smell?

Magill: No, I don't think she smells.

Klotz: (Inaudible.)

McReynolds: May have a little bit of taste?

Magill: That's right. Sort of a duck egg.

Klotz: You're really good.

H.M.Jr: Well, let's hear from .....

Magill: I was talking to your friend, Mr. Blough.

H.M.Jr: He's supposed to come in at a quarter of twelve. What else?

Magill: That's all.

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H.M.Jr: He's my friend?

Magill: (Nods "Yes.")

H.M.Jr: O. K. Herman?

Oliphant: The only official thing I have to report is when La Guardia went through the sculpture exhibit yesterday afternoon, of an exhibit he said, "If that thing's a bird, I'm Hitler." Of Greenbaums's "Study of a Boy," he said, "That's good."

H.M.Jr: (Inaudible - something about Ringling Brothers.)

Oliphant: I looked into that Los Angeles matter. It doesn't - the Los Angeles Exposé - that forty thousand dollar additional fund. I have a report on it. There's nothing there of any importance.

H.M.Jr: Well, you .....

Oliphant: You saw the outcome.

H.M.Jr: They are not in jail yet. All right.

Magill: That Ringling Brothers story is just incredible.

H.M.Jr: What's a good elephant worth anyway?

Magill: I don't know - I haven't bought any lately.

H.M.Jr: They have. How does one go "short" on elephants?

Magill: Ask Mr. Kelley, of the Counsel for Ringling Brothers.

H.M.Jr: Somebody suggested that the Treasury go to the circus when they came yesterday.

Lochhead: There's nothing new on the exchanges. Feis is sending that over to you in an envelope, all ready in cable form, and he'll be at your disposal up to one o'clock if you want to speak to him.

H.M.Jr: (Side conversation with Mrs. Klotz.)

Oliphant: I'm ready to report to you on that Jackson matter.

H.M.Jr: Right after this meeting.

I just want you to know that if you want anybody to lose money on a horse race get Herman Oliphant to do it, because the horse almost wins - by eleventh.

Oliphant: Did you hear how I came out?

H.M.Jr: No.

Oliphant: I'm rich, about fifteen cents. I won a quarter and spent a dime for a hamburger.

H.M.Jr: When you go to the next one I want to put up a quarter.

You stay after. Mr. Gaston.

Gaston: I got ahold of Bob Kintner yesterday, and had Harold Graves in and gave them quite a story on the Los Angeles situation. I thought it was desirable to get something out, and I was afraid we wouldn't get very good results in the general press conference.

H.M.Jr: Aren't you slipping - giving these on the side?

Gaston: It's not a story - just a chance to write a column - "syndicated by."

H.M.Jr: (To Mr. Upham:) Tell them the story, off the record, about Carter Glass.

Upham: He told the boys on the Hill day before yesterday that he had heard a good deal about himself, it being said he was getting old and was slipping. He said, "You don't have to get old to slip - look at Eccles."

Magill: Who said that?

Upham: Carter Glass.

H.M.Jr: Incidentally, who's going to call up Doughton and ask him when he's going to get that bill through for me on bonds?

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- Magill: Think they'll write, saying they should wait until the tax bill is out of the way.
- H.M.Jr: Are you talking to him?
- Magill: I haven't seen him in the last few days.
- Bell: That was the agreement.
- H.M.Jr: (Over telephone:) Congressman Robert Doughton.
- Gaston: I notice Mr. Hopkins made public this morning the text of a letter he's sending out in the pay envelopes of W. P. A. workers.
- H.M.Jr: I saw that.
- Gaston: I just wanted to get confirmation of the fact that it's getting in the pay envelope.
- Bell: Yes, it's going out in them.
- Gaston: Really, it was a good letter, urging them to use their own conscience in voting and contributing to campaigns.
- McReynolds: He promised not to take anybody off the rolls.....
- H.M.Jr: My very good wife - she thought it was a tragedy that Harry had to say anything to them; that they could vote or act how they please. Why should anybody in the Government have to say anything. I mean, the very fact that he has to say something like that shows there is something wrong. It's like somebody said in the Treasury - "Tell your people that they can't speculate." I said, "No, I wouldn't insult them by getting out instructions like that." - Except in horse races, but, then, that's not speculating.
- Oliphant: No, that's a certain loss.
- (Telephone conversation with Mr. Butterworth at 9:39 a. m. filed in Stabilization Diary.)

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- H.M.Jr: That's the eighteenth time. Nice people.
- All right. George, I haven't had a chance to read your business thing yet - but, how are you on business? How's business?
- Haas: I think I feel a little better than most people do, but I may be wrong.
- H.M.Jr: You're looking wonderful, George. The funniest thing is, poor Harry (White) looks a little yellow around the gills, a little worn out, and you look quite healthy.
- Haas: I wonder why that is.
- (Telephone conversation with Congressman Robert Doughton at 9:45 a. m. is attached.)

Thursday  
May 5, 1938  
9:45 a.m.

Congressman

Robert L.

Doughton: How are you feeling?

HMJr: Oh, wonderful!

D: Well....

HMJr: Everything's fine.

D: All right.

HMJr: I don't where, but it's fine.

D: Well, I'm glad to hear you say that because I wish I could feel that way.

HMJr: Yeah. Well...

D: But I'd like to know how you made that speech in New York

HMJr: I think so.

D: Yes.

HMJr: I think so. Bob, you're not forgetting about my little bill to fix me up with some bonds?

D: No. I'm going to take - call a committee together on that just as soon as we - I adopt this cotton report. If you're in a hurry about it I'll call it before. I want you to come up, you know, or send somebody to ...

HMJr: Well...

D: ...explain it to the full committee.

HMJr: Yeah. Well I just wondered - are you fellows busy up there now?

D: Well, not especially. We have to wait on the drafting service.

HMJr: Well, I don't what's the best tactics as far as the House is concerned - I mean....

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D: I probably could call the committee together tomorrow on that.

HMJr: Yeah.

D: It'd suit you, would it?

HMJr: Yeah, unless - what do you think?

D: Well, I'll talk to - I want to talk to Frank and one or two of the boys about it. It'd suit me exactly.

HMJr: Well...

D: I'll call you up tomorrow.

HMJr: All right. I'm ready or somebody's ready here anyway.

D: Let me ask you this. I sent you down this morning or last night a copy of this resolution about this floor tax on liquor stocks.

HMJr: Yeah.

D: I want you to look into that and see what you think about it. It looks like if we don't have some of that kind that they'll stock up with liquor - enough to do them for two or three years - before the tax goes on.

HMJr: Well, Magill's my liquor expert. I'll find out what he's got to say.

D: All right. All right.

HMJr: All right.

D: I'll see you up here on the Hill.

HMJr: All right.

D: All right. Thank you - I'll let you know about that as soon as I can.

HMJr: All right.

D: Thank you very much.

HMJr: Goodbye.

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- Magill: Well, Gene Tunney is bigger. (Laughter.)
- H.M.Jr: Very good - that's all right.
- Klotz: You're marvelous.
- H.M.Jr: Isn't that funny - look at Haas, and see how well he is, and Harry White is kind of yellow around the gills; Harry kind of yellow around the gills, and Haas looks happy - has on a new shirt and tie, suit pressed, a good shine ..... Well, I'll read your business report.
- Haas: Fine. This is a far cry from the French franc, but Blaisdell's committee has a report ready and when you get around to it he'd like to see you.
- H.M.Jr: On the French franc?
- Haas: No, this is a far cry from the French franc.
- H.M.Jr: The French franc is no national resource.
- Oliphant: Maybe in that connection, maybe I should report to you we once had a practice to enforce so far as tie bids are concerned ..... I had a letter from the Attorney General yesterday, saying that is all fine; he's ready to do it.
- H.M.Jr: Wonderful. Did he have special counsel on that?
- Oliphant: I don't know. Maybe Thurman Arnold.
- Taylor: Yesterday afternoon Mr. Parker, of Standard Statistics called on me and said that at one time or another they had done work for the Bureau - I guess it's here - valuation work. He said that they had been informed that the Bureau's budget was limited. On account of the fact that their cost might be a little high he wanted to tell me to convey the information to the proper authorities that they would be more than glad to do any work at absolute cost - simply the pay of the men who are on the job, and the case that they particularly had in mind was Associated Gas and Electric; that they would like to appear on the other side of the Associated Gas and Electric - on the Government's side.

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They have done quite a bit of work on it, and have a personal interest in standing on the right side on that one.

H.M.Jr: All right. Anything else?

Taylor: (Nods "No.")

H.M.Jr: Archie.

Lochhead: The rates haven't changed yet.

H.M.Jr: Harry.

White: (Nods "No.") Could give you a story that might explain my looking yellow.

H.M.Jr: Go ahead.

White: There was a colored woman who lost her husband, who had been in the hospital for some time, and a friend asked her what he died of. She said she didn't know; that every day she came to the hospital and the doctor said the husband was improving. She said, "I done spose he died of improvement." (Laughter)

H.M.Jr: That's all right. I'll use that on Monday for the President. Thank you.

McReynolds: It's a good story, Harry, but you've got to watch Harry's stories.

White: I'll stop there.

H.M.Jr: Dan.

Bell: I thought maybe it was the French gold that made him yellow.

H.M.Jr: Cy, what do you know?

Upham: I'm writing a report on that Pennsylvania bank attorney. Did you see it? It was sent to me.

H.M.Jr: No.

Upham: Some political difficulties.

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H.M.Jr: I don't want to make Cy blush, but I want to say that the presentation of that bank thing yesterday was one of the nicest presentations I've had since I've been in the Treasury.

Upham: Thank you, sir.

H.M.Jr: I think we're going to get something.

Mr. Bell:

Bell: I don't know whether the Greek Minister has called up or not, but I think he's going to. They are paying a hundred seventy-four thousand dollars, and I think they'd like to make an international event of it.

H.M.Jr: Have you heard anything, Taylor?

Taylor: (Nods "No.")

H.M.Jr: I don't like Greek wine.

Bell: Ordinarily they would pay it through the Federal Reserve Bank of New York, but they've asked the Federal Reserve Bank of New York to send it to the Greek Minister in Washington, and I've an idea he will call you for an appointment, and he'd like to have his picture taken, etc. That would bring a little pressure on the other bond holders to accept the forty per cent and interest.

H.M.Jr: Well, I'm open to a proposition.

Taylor: It ought to make the front page.

H.M.Jr: We ought to get a special edition.

Magill: Dancing in the streets.

H.M.Jr: What else?

Bell: That's all.

H.M.Jr: The money - relief money, goes to half the agencies or does Jimmy Roosevelt get it?

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Bell: Well, I think he might combine them.

Gibbons: I'd like to see that letter Hopkins is sending out. The only reason they are making a furor of it, it came to the surface in Pennsylvania that they'd been collecting campaign funds from W. P. A. workers. They've been doing it in Chicago all the time.

Upham: In New York they took ten per cent from a woman who was getting seventy-eight dollars a month - on the state pay roll. Just as long as this money is distributed to the state authorities you're going to have that - taking the money of the people on their pay roll.

H.M.Jr: You mean - the Federal people don't do that?

Gibbons: As I understand it, it's being put under each state.

H.M.Jr: Steve, excuse me. The point is - the point is, this money being drawn - all the money being given to the President and he allocates it instead of it going - giving it directly to the agencies. Now, instead of giving it to the President - give it to the Director.

Gibbons: I am speaking of what they did in the past.

Bell: The draft of the bill that will go to the Committee tomorrow morning, unless the Democratic huddle this morning changes it, will appropriate the money directly to the agencies. Woodrum got word - how, I don't know - supposedly directly from the President, that he wanted nothing to do with the approval of projects or the allocating of the money.

H.M.Jr: The President?

Bell: Yes. Which is absolutely contrary to what he told me at four thirty Friday evening, and he laid a great deal of emphasis on the statement to me that he didn't want Harry Hopkins to have the money and he didn't want Harry Hopkins to approve the projects. He said, "It doesn't take much of my time and I still want to pass on them, and I still want the Bureau of the

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Budget to take care of the accounting." Cliff asked me what I thought about it and I said, "You received your instructions, and I'm out of the picture, so far as the bill itself is concerned.

H.M.Jr: It takes the accounting away from you?

Bell: Yes. Naturally, it would, unless they wrote a provision in the bill that the Treasury would do the accounting.

McReynolds: Wouldn't be hampered by our requiring them to limit their budget to the amount of money they've got to operate on.

H.M.Jr: Is that the way it is?

Bell: We've got a control over the projects.

H.M.Jr: Has that been settled up there?

Bell: Unless - I think that's so.

McReynolds: If they appropriate directly you wouldn't have any hold on it. You see, it will break down any state offices entirely - the Treasury having nothing to do with it. They do their own accounting and use their own conscience with respect to the amount of obligations they create against it.

H.M.Jr: Doesn't it go to the Senate?

Bell: Yes, surely.

H.M.Jr: I'll tell you what you do, Dan. You go up stairs and write a cable to the President which you and I will sign, pointing out that this is what's happening and that we feel that it's most important, from the standpoint of sound finance, that the accounting be in the Treasury, and that these things should continue in the Budget. Let's put ourselves on record. Will you? If you don't want to sign it, I'll sign it.

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- Bell: I've talked to him so many times about it, and have gotten the same answer every time. I feel that influence is being brought.
- H.M.Jr: Let me sign it. I want to point out, before it's too late, I want to point out to him today, that by giving up the thing - just make it - it doesn't have to - I'd like it just very quiet: "My dear Mr. President: I feel it is my duty to point out to you the dangers involved through use of fiscal control of ....." what they have if this thing is changed, "... and I urge you to continue it as it has been before."
- Bell: You want to recommend no change?
- H.M.Jr: Yes, and if you could do it right away I'll sign it.
- Bell: I think I'll have to get that changed in the Senate.
- H.M.Jr: Will you do it right away? You and Mac do it.
- McReynolds: Dan talked to me about it. He said he'd be delighted to be rid of it. I said, "The Secretary would like to too, but he doesn't think it would be to the interest of the Administration to do it.
- H.M.Jr: How long will it take you?
- Bell: I have an appointment with General Reynolds, but I'll have it down here about eleven thirty.
- H.M.Jr: You want to make an appointment or you want to come in right after lunch, so it will give you a chance to polish it? Let Gaston take a look at it. Why don't you people come in at two fifteen? Gaston, McReynolds, and Bell.
- Bell: It's all right with me.
- McReynolds: I don't think you could give them ..... (inaudible)
- Bell: It's been a headache long enough for me.

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- H.M.Jr: I'd just as soon ..... - but you know whether that's the fact. You mind if I ask?
- Bell: Oh, I don't know whether it's the fact.
- H.M.Jr: (Over telephone:) Congressman Woodrum, please.
- Bell: The agreement was, on day before yesterday, that he would send the telegram to the President personally and yesterday he had the message from some place that the President didn't want anything to do with it.
- H.M.Jr: Well, if you fellows come down here at two fifteen, that gives you a chance to polish it. I mean, I'd like to point out to him what's involved, you see?
- Bell: Of course, you have no consolidated report item going to Congress in January. Each agency will make its own report.
- H.M.Jr: Well, point that all out.
- Bell: That will have to be pointed out.
- McReynolds: The thing that's done more to keep it straight so far .....
- H.M.Jr: Does it take the purchasing away too?
- Bell: No, it doesn't take that, or the disbursing. That is law. They would have to write a provision into the Act.
- H.M.Jr: (To Mr. Lochhead:) You've got time to take a fresh look at the franc.
- Lochhead: That's right. Feis said he'd be at your disposal until one o'clock. (Goes out.)
- Gaston: Did you know the Herald-Tribune attributed directly to Daladier that they expected to open it at 179 or 180?
- H.M.Jr: Hello. (Telephone conversation with Congressman Woodrum at 10:01 a. m. attached.)

Thursday  
May 5, 1938  
10:01 a.m.

HMJr: Hello.

Operator: Congressman Woodrum. Go ahead.

HMJr: Hello.

Clifton A.  
Woodrum: Good morning, Mr. Secretary.

HMJr: How are you?

W: Fine, thank you.

HMJr: Woodrum, Bell and I have just been talking over this relief bill and I'd like to ask you a question, if you don't mind.

W: Yes.

HMJr: Bell is under the impression that the method of handling the finances and accounting is going to be changed, I mean, up to now all of these appropriations and allocations go through the Bureau of the Budget and through the President and we do the accounting.

W: then  
Yeah.

HMJr: Now, is that going to continue or is that going to be changed?

W: Well, I - the question has arisen now as to whether the appropriation should be made direct to Hopkins and his agencies or to the President and to be allocated by him.

HMJr: Yeah.

W: And I think he would like to have it made direct to the agencies.

HMJr: Are you sure of that?

W: Well, I - yes. I'll just tell you what happened about it.

HMJr: Please.

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W: Aubrey Williams brought us word that the President had told Mr. Hopkins he'd like to have that done. The next day Dan Bell told us that the President told him he didn't want that done.

HMJr: Yeah.

W: So I called Jimmy Roosevelt and I talked to him and he communicated with the President and the President sent back the message that he didn't care anything about it - he'd leave it to Sam Rayburn and myself. But then I talked to Jimmy Roosevelt and I got the impression from him that perhaps the President would like to have it changed. Now, that's the way the thing's developed. I don't ....

HMJr: Well, I, as Secretary of the Treasury, feel very very firmly about it. I think it's a mistake - ah - it's - there's been - everything has been on the level - ah - these allocations - ah - they've stayed within their money, they've stayed within the Woodrum Amendment.

W: Yes.

HMJr: Ah - the only way - after all, the Treasury people are financially minded and we are bookkeeper minded; that's what we're hired for.

W: Yes.

HMJr: And a lot of these things that go over to the President the President turns down because he doesn't think they're practical. Ah - it gives us some chance to see that they keep within their appropriation.

W: Well, I cede all that. I...

HMJr: And I'm so disturbed about it I'm going to get off a radio to the President as Secretary of the Treasury.

W: Well, you go ahead and do that and let me know what you hear from him.

HMJr: Because, if they're going to do the other thing - ah - I don't know any business that doesn't have some

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- W: Well, the President has evidently committed himself to Hopkins to let the appropriation be made direct. It looks like that's what he's done.
- HMJr: Uh huh. Well....
- W: And - now, I just don't know what to do. What we're trying to do is to fix it the way he wanted it.
- HMJr: Well, I've asked Dan to fix me up a cable giving me the facts and pointing out the dangers to the President.
- W: Yeah.
- HMJr: And aside from everything else, towards the public, I mean it looks as though Congress says, "Well, we don't trust the President but we trust Hopkins and we trust Farm Security and we trust these people but we don't trust the President."
- W: Well, I - of course, there's something to that construction. Then, on the other hand, the President gets out from under some of this fire and hell-raising that there's been over this program, you know.
- HMJr: Perfectly true. But....
- W: And he'll still have control over it literally because whatever he'll tell Harry Hopkins to do he'll do it.
- HMJr: I know, but he can't follow it the way the Treasury and the Budget does for him in every State with officers and accountants and careful disposition of the money.
- W: Yeah.
- HMJr: And....
- W: Well, see what you get on that, Mr. Secretary. And will you let me know as soon as you hear?
- HMJr: I'll let you know the second I hear.
- W: Thank you, sir.
- HMJr: Thank you.

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- H.M.Jr: He's a square-shooter.
- Bell: Well, he didn't tell me that. He said he had word from the President - I assumed it was through Jimmy but I didn't know.
- H.M.Jr: Incidentally, include in that, please, that the reaction of the people will be that the Congress doesn't trust the President of the United States - won't let him do it, but they'll let these people do it. That's my reaction.
- Bell: The President told me that he never told Harry Hopkins that. I told him the Committee had two different versions of it.
- H.M.Jr: If you ~~can~~ can get it before two o'clock, I'd get it, and this will go through.
- White: The rate of expenditure has nothing to do with this?
- H.M.Jr: Look, Harry, all this has nothing to do with this. It's a billion dollars, but it's just a question of whether spending agencies should be their own bookkeepers.
- White: I have in mind something Danny said. It may be irrevelent. He said something about controlling in his hands - being such he could delay or speed up at a certain time. That doesn't bear on that problem.
- H.M.Jr: As a matter of fact he doesn't do that; he's never done that. Douglas did do that. Dan Bell never has.
- Bell: I think that the President and .....
- White: Let's get an understanding on it. In other words, there is no control within the budget director's office - being able to delay expenditures or speed them up?
- H.M.Jr: He could, but he hasn't.
- White: I didn't mean to imply he would.
- Bell: I don't think I made that statement. I think if the President gave me instructions to slow

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up his program, I certainly could do it.

White: I merely say there is a leeway there. That may be the burden of the discussion.

H.M.Jr: No, it's - it's all right.

McKeynolds: Harry's been trying to get the control out of the Treasury a long time.

H.M.Jr: They could run two or three hundred million dollars over by starting projects. It just-- all this question - loose bookkeeping - loose finance. It's just - I mean .....

Bell: C. W. A. is a typical example. We never have yet had a complete report from C. W. A.

H.M.Jr: (Telephone.) Hello. All right.

Well, why not put that in it as an example? Put that in as an example.

(Looks at note handed him by Mr. Lochhead who just returns to room.)

All right.

Well, I want a good cable on this. And use that as an example.

Gibbons: If I might suggest White's answer - that they could slow it up or speed it up according to which way they wanted an election to go.

H.M.Jr: Nobody knows any more about this end of it than I do. Nobody. I've sat in and spent hours on the thing, and on this last thing here, we were trying to help them get up to two and a half million people, and they couldn't do it. We leave all the restrictions off; all projects went through the same day, and all restrictions were lifted. Now there have been times when the President wanted to slow it up, and, true, as a matter of history, both December of this year and December a year ago when they were slowing the thing up and not putting it out, Bell and I are entirely and solely responsible for putting more people

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to work. It's our sole responsibility - we did it, and we got it in right, and there have been times when Hopkins wanted to lay people off, for various reasons, but the thing here is regularly done, and it isn't a question of slowing it up and speeding it up; it's a question of spending a couple of million dollars and letting the fellow who spent it keep his own books and all that. No fellow in business would even think of doing it. You might as well say, "What's the use of having Certified Public Accountants? Let the Advertising Manager be the bookkeeper," and that's just what they are talking about wanting to do, and what I'm trying to do is keep a little sanity in sound finance in the Government.

Gibbons: It's always - never been any slowing up.

H.M.Jr: Let the Advertising Manager be the comptroller of the business.

Bell: By the way, John Eddy, who is the City Manager of Toledo, formerly Assistant Manager of the Budget will be in town at eleven-twenty. Would you like to see him? He's got some angles on the matter. Would you like to see him?

H.M.Jr: Yes.

White: If the statement you have just made could be weaved in, in your statement, I think it would help considerably.

H.M.Jr: Harry, I know. I've lived with them. I've known Hopkins for three years in New York and I've known him five years here.

(Telephone conversation with Mr. Butterworth at 10:12 A. M. filed in Stabilization Diary.)

(After Butterworth conversation)

H.M.Jr: Well, you people have a little .....

Upham: Nineteenth.

H.M.Jr: Yeah.

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Thursday  
May 5, 1938  
9:39 am

HMJr: Hello.  
Wm. Walton  
Butter-  
worth, Jr: Yes, Mr. Secretary.

HMJr: Butterworth...

B: Yes, sir.

HMJr: I wanted to tell you about my conversation that I just had with Cochran.

B: Yes.

HMJr: Now, they've opened up the franc at around a hundred and seventy-eight - a hundred and seventy-nine.

B: Yes.

HMJr: Now everything that we had here - ah - we had very very good reason to believe that it would be a hundred and seventy-five or less. And, after all ...

B: I didn't hear that, sir.

HMJr: We had every reason to believe that it would be a hundred and seventy-five or less.

B: Yes.

HMJr: Now, I consider that the message that I got yesterday was from the combined French Cabinet.

B: Yes.

HMJr: And - ah - I have told Cochran to go over and see Marchandean and tell him that I am very much surprised and very much disgusted.

B: Yes.

HMJr: And - ah - to put it just as strongly as possible.

B: Yes.

HMJr: Now the fact that they have gained a hundred and twenty-five million dollars today is very nice for the French speculator.

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B: Yes.

HMJr: But they just haven't kept faith with me.

B: Yes.

HMJr: And I'm having Cochran put it just as strongly as he can.

B: Hello.

HMJr: Hello.

B: Hello. I couldn't hear that sir.

HMJr: I'm having Cochran tell Marchandean just how strongly I feel about it.

B: Yes, sir.

HMJr: And I've told him that they must close the franc at a hundred and seventy-five or less or otherwise I will consider that they've broken their word to me.

B: Yes.

HMJr: Now, I wish you'd get that to Sir Frederick Phillips as quickly as possible.

B: Yes, sir. I will.

HMJr: And, I mean, the whole thing is a question of a gentlemen's agreement which means that you keep your word.

B: Yes, sir.

HMJr: And we were distinctly told a hundred and seventy-five was the limit.

B: Yes, sir. Well, in the text of the note that the British got it said "around a hundred and seventy-five."

HMJr: Well....

B: It didn't say precisely at a hundred and seventy-five. And I think you'll see the French text does say that.

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- HMJr: Well, but what they sent us Monday - the first one on Monday said "a hundred and seventy-five."
- B: Because I have a copy of Cochran's telegram and I just looked it up as you were talking - telegram number 683 of May 2 - and it says there, "...around a hundred and seventy-five francs for one pound."
- HMJr: Well, what does "...around a hundred and seventy-five..." mean?
- B: Well, I should think that it would mean - that they probably will say that as long as it's within two percent of a hundred and seventy-five that they don't feel that they will contradict what they said in their written communication.
- HMJr: Well, I want you to - but we have every reason to believe a hundred and seventy-five and - ah - I told him that I can't see very much difference between an individual private speculator and a government as a speculator.
- B: Well I sent two - but I think what Phillips will say is that they took that into consideration. I don't think the British like the franc opening at a hundred and seventy-nine this morning but ....
- HMJr: Well...
- B: ...in the statement which I sent you - have you gotten that telegram of this morning?
- HMJr: No.
- B: giving you the statement which Sir John Simon is making in the House of Commons.
- HMJr: Well, I told them that I consider in order for them to keep their word with me it must close at a hundred and seventy-five.
- B: I see.
- HMJr: Now, furthermore, to show you that that is what they thought last night - Cariguel gave distinct positive instructions to the Federal Reserve last night that the franc should not be permitted to go one fraction above a hundred and seventy-five.

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B: Uh huh.

HMJr: Those were his instructions last night.

B: Yes.

HMJr: Now that's what the Bank of France thought.

B: Yes.

HMJr: And - so we have - everything that we have around here was a hundred and seventy-five or less.

B: Yes.

HMJr: Or less. And certainly the Bank of France felt last night - because they were very very positive in their instruction that it not be a - not a fraction above a hundred and seventy-five.

B: Right, sir. Well, I shall get in touch with Sir Frederick Phillips immediately.

HMJr: What?

B: And give this message to him.

HMJr: And after you've gotten his reaction I wish you'd call me back.

B: All right. I will.

HMJr: Thank you.

B: Goodbye, sir.

## PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: May 4, 1938, 9 a.m.

NO.: 700

FROM COCHRAN.

As instructed over the telephone at 10 p.m. last night by the Secretary of the Treasury, I called on Rueff at the Ministry of Finance at 11 p.m. and said -

First. On Wednesday the United States monetary authorities would keep on doing business with and in behalf of the French authorities.

Second. The whole question was being given very serious consideration by the Secretary of the Treasury, but in order to reach a decision he would need at least one more day.

Third. Caution should be exercised by the French authorities to avoid official leaks, particularly of such a nature as would reflect criticism on any party to the negotiations now going on. It had been noted that yesterday afternoon an American news ticker carried an item to the effect that, pending a reply from Washington, the French were holding up decision on a monetary matter.

Fourth. On Tuesday the Federal (omission) had bought only one and one-quarter million francs in New York.

END SECTION ONE.

WILSON.

PARAPHRASE OF SECTION TWO, TELEGRAM No. 700  
of May 4, 1938, 9 a.m., from Paris.

These points were taken down by Rueff, who took the memorandum to Marchandean, who was conferring with Fournier and Rueff. I was asked to await the Minister's reaction. Rueff told me at half-past eleven that a telephone call was just coming in from the French Embassy in Washington to the Ministry for Foreign Affairs here. I was asked to wait until the results thereof were known to Marchandean, as some news of common interest might be forthcoming.

While we waited, I had a chat with Fournier, who told me that last evening telegraphic press reports had been received here of conferences on the French monetary situation held at the American Treasury. Fournier said he feared that there would be increased pressure on the franc because of these reports and rumors; he felt that he had had fairly severe exchange losses yesterday. Fournier is afraid that each day that uncertainty exists the control will have to give ground, and that in the end 175 may be reached even despite the attempt to resist depreciation. The control would lose all opportunity for maneuvering if there is gradual decline, and would have to sacrifice an important sum of gold and foreign exchange. At half-past twelve Fournier left, being very tired - he said he could not confer in the Treasury all night and run the Bank of France during the day.

END SECTION TWO.

WILSON.

EA: LWW

PARAPHRASE OF SECTION THREE, NO. 700 of  
May 4, 1938, from Paris.

Rueff had a telephone conversation with the French Financial Attaché in Washington at one o'clock. Rueff gave him a reply to the message which was transmitted earlier in the night by St. Quentin to Bonnet, which latter message was the same as the one I delivered as reported above. I was asked by Rueff to try to get the French reply directly to Secretary Morgenthau during the night lest Leroy Beaulieu might not be successful in delivering his message.

I give below <sup>the substance of</sup> an English translation of the reply given over the telephone to the Financial Attaché by Rueff, and which I noted for communication to the Secretary of the Treasury:

It had been our expectation that the reply which had been asked in our communication of four o'clock yesterday afternoon, through Cochran, would be given tonight during the appointment which the Secretary of the Treasury gave our Ambassador in Washington. The Council of Ministers therefore had been summoned for half-past eight Wednesday morning to take a final decision before the Paris market opened. It is feared that the market pressure will be stronger than on preceding days, in view of the fact that Mr. Morgenthau's communication (just given to us by Cochran) confirms the rumors current this past evening

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ing in Paris with respect to a news item being published by American tickers in New York on the exchange question. It appears to be very necessary that before the Council of Ministers meets a reply be given.

I reached Mr. Lochhead of the Treasury by telephone from the Embassy at two-forty this morning. I gave the foregoing information and message to him. I telephoned to Rueff at three o'clock this morning, I reiterated that he should not expect a reply from the Secretary of the Treasury before the meeting this morning of the Council of Ministers.

END MESSAGE.

WILSON.

## CONFIDENTIAL

May 4, 1938

(CONFIDENTIAL CABLE FOR AMBASSADOR BULLITT)

*M. Wilson*

STRICTLY CONFIDENTIAL FOR AMBASSADOR BULLITT AND  
MR COCHRAN FOR THEIR GUIDANCE FOLLOWING MESSAGE  
FROM THE PRESIDENT OF THE UNITED STATES TO THE  
SECRETARY OF THE TREASURY QUOTE AS FAR AS I CAN  
MAKE OUT THE ACTION PROPOSED ~~BY FRANCE~~ IS WEAK AND  
GETS NO WHERE IN THE LONG RUN PERIOD I AGREE WITH  
YOUR LINE OF THOUGHT PERIOD OFFHAND IT SEEMS TO  
ME THAT SUPERVISION OF CAPITAL MOVEMENTS AND GOLD  
CONTROL SIMILAR TO OURS WOULD OFFER A MUCH MORE  
PERMANENT SOLUTION PERIOD AND IF THAT FAILS THEN  
A MORE DRASTIC FORM OF EXCHANGE CONTROL END QUOTE

CONFIDENTIAL

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May 4, 1938

(CONFIDENTIAL CABLE FOR AMBASSADOR BULLITT)

*Mr Wilson*

STRICTLY CONFIDENTIAL FOR AMBASSADOR BULLITT AND  
MR COCHRAN FOR THEIR GUIDANCE FOLLOWING MESSAGE  
FROM THE PRESIDENT OF THE UNITED STATES TO THE  
SECRETARY OF THE TREASURY QUOTE AS FAR AS I CAN  
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CONTROL SIMILAR TO OURS WOULD OFFER A MUCH MORE  
PERMANENT SOLUTION PERIOD AND IF THAT FAILS THEN  
A MORE DRASTIC FORM OF EXCHANGE CONTROL END QUOTE

May 4, 1938

My dear Cordell:

For your own confidential information, I am forwarding herewith a copy of the message which I have received from the President of the United States.

Yours sincerely,

The Honorable  
The Secretary of State.

CONFIDENTIAL

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May 4, 1938

(STRICTLY CONFIDENTIAL CABLE FOR AMBASSADOR KENNEDY)

STRICTLY CONFIDENTIAL FOR AMBASSADOR KENNEDY AND  
BUTTERWORTH FOR THEIR GUIDANCE FOLLOWING MESSAGE FROM  
THE PRESIDENT OF THE UNITED STATES TO THE SECRETARY  
OF THE TREASURY QUOTE AS FAR AS I CAN MAKE OUT THE  
ACTION PROPOSED BY FRANCE IS WEAK AND GETS NO WHERE  
IN THE LONG RUN PERIOD I AGREE WITH YOUR LINE OF  
THOUGHT PERIOD OFFHAND IT SEEMS TO ME THAT SUPERVISION  
OF CAPITAL MOVEMENTS AND GOLD CONTROL SIMILAR TO OURS  
WOULD OFFER A MUCH MORE PERMANENT SOLUTION PERIOD  
AND IF THAT FAILS THEN A MORE DRASTIC FORM OF EXCHANGE  
CONTROL PERIOD END QUOTE

CONFIDENTIAL

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May 4, 1938

(STRICTLY CONFIDENTIAL CABLE FOR AMBASSADOR KENNEDY)

STRICTLY CONFIDENTIAL FOR AMBASSADOR KENNEDY AND  
BUTTERWORTH FOR THEIR GUIDANCE FOLLOWING MESSAGE FROM  
THE PRESIDENT OF THE UNITED STATES TO THE SECRETARY  
OF THE TREASURY QUOTE AS FAR AS I CAN MAKE OUT THE  
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OF CAPITAL MOVEMENTS AND GOLD CONTROL SIMILAR TO OURS  
WOULD OFFER A MUCH MORE PERMANENT SOLUTION PERIOD  
AND IF THAT FAILS THEN A MORE DRASTIC FORM OF EXCHANGE  
CONTROL PERIOD END QUOTE

May 4, 1938.  
9:17 A. M.

H.M.Jr: Hello.

H. Merle  
Cochran: Hello.

H.M.Jr: Go ahead, Cochran.

C: I sent you two - two telegrams today, one  
confirming the conversations of last night.

H.M.Jr: Yeah.

C: And a second one at eleven o'clock giving the  
developments up until that hour.

H.M.Jr: Yeah.

C: Have you received the second one?

H.M.Jr: I haven't received anything. - from you.

C: Hello.

H.M.Jr: I have not received anything.

C: I say, well then, I'll tell you, in summary, what  
I said in the second one.

H.M.Jr: Go ahead.

C: Ah - the market opened, ah, with pressure on the  
franc at a hundred and sixty-five and a half.

H.M.Jr: Yeah.

C: And by, ah, twelve o'clock it had gone to one  
hundred and sixty-eight and five-sixteenths.

H.M.Jr: Yeah.

C: The control had sold one hundred sixty thousand  
pounds.

H.M.Jr: Yeah.

C: That was at noon, and at two forty-five - that's,  
ah, twenty minutes ago.

- 2 -

H.M.Jr: Wait a minute - one hundred sixty thousand pounds by noon.

C: That's right.

H.M.Jr: Yes - ah - go ahead.

C: And, ah, at two forty-five the rate was one sixty nine and one-quarter.

H.M.Jr: Yeah.

C: It had touched one hundred seventy.

H.M.Jr: Yeah.

C: That much evidence of the control operating at this rate.

H.M.Jr: Yeah.

C: Rueff called me to the Ministry of Finance at, ah, ten o'clock this morning.

H.M.Jr: Yeah.

C: He told me of the Leroy-Beaulieu conversation with you which was, ah, telephoned on at six o'clock this morning.

H.M.Jr: Yeah.

C: Then he asked me to communicate to you, a message which he wanted you to receive.....

H.M.Jr: Yeah.

C: ..... before the French Ambassador came.

H.M.Jr: Yeah.

C: Ah, have you received that message through the Ambassador?

H.M.Jr: Ah, aah - today?

C: Yes.

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- H.M.Jr: I haven't seen or heard from anybody today.
- C: Because the French Ambassador, according to Rueff, was to call on you at nine o'clock.
- H.M.Jr: Well, they were supposed to be here this - there's - there's no sign of any Frenchmen here.
- C: Well this - this is the message which he wanted communicated to you.
- H.M.Jr: Yes.
- C: Ah, quote: "Upon the specific request of Mr. Morgenthau ....."
- H.M.Jr: Yeah.
- C: ...."the French Government has decided to wait - to await...."
- H.M.Jr: Yeah.
- C: ...."the reply of the American Government."
- H.M.Jr: Yeah.
- C: "This becomes, from hour to hour, more urgent,...."
- H.M.Jr: Yeah.
- C: ...." and we request, urgently, that Mr. Morgenthau make known his reply at the interview which he is kindly giving to our Ambassador today,....."
- H.M.Jr: Uh.
- C: ...."May 4, at nine A. M., Washington time. In the meantime, we continue, as we have been requested, to protect the currency against the very strong pressure which can only grow."
- H.M.Jr: Yeah.
- C: "It is necessary for us to have, as soon as possible, an adherence to our request."
- H.M.Jr: Yeah.

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C: Then there follows, a phrase which, ah, ah, we didn't agree on a translation.

H.M.Jr: Yeah.

C: This is about the sense of it: "And we give the assurance that the Government is determined, upon the contemplated fall as the last one."

H.M.Jr: Now I asked Rueff, ah, ah, if they definitely pledged that the present Government, ah, ah - would make no depreciation beyond one seventy-five.

H.M.Jr: Yeah.

C: And Rueff said that he couldn't take the responsibility for the translation.

H.M.Jr: Yeah.

C: He said that in this way .....

H.M.Jr: Yeah.

C: .....and, but he said the words used certainly indicated .....

H.M.Jr: Yeah.

C: .... the Government is determined to stop definitely at one seventy-five.

H.M.Jr: Well .....

C: But in the cablegram I quoted the French words for just that last, ah, phrase.

H.M.Jr: I see.

C: See?

H.M.Jr: Now - is that all?

C: Yes.

H.M.Jr: Hello.

C: Hello.

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H.M.Jr: Now, I'll tell you what I'm going to do - I'm going to turn you over to Lochhead - you can repeat this to him, because I'm alone here, see?

C: You - you're alone now.

H.M.Jr: Ah, just a minute.

C: All right.

H.M.Jr: I'll let the girl transfer you to Lochhead, and he can have it. See?

C: All right.

H.M.Jr: Will you hold on?

C: Surely.

Operator: Operator.

H.M.Jr: I want Mr. Cochran to talk to Lochhead, please.

Operator: Right.

H.M.Jr: And now don't call me until after goes.

Operator: All right.

H.M.Jr: Thank you.

## RE FRENCH MONETARY SITUATION

May 4, 1938.  
9:30 a.m.

Present: Mr. Taylor  
Mr. Lochhead  
Mr. White  
Mr. Feis  
Mr. Harrison

Mr. Bewley (For brief period)  
Mr. Beaulieu (For brief period)

Lochhead: "From the President of the United States to the Secretary of the Treasury.

"As far as I can make out, the action proposed by France is weak and gets nowhere in the long run. I agree with your line of thought. Offhand it seems to me that supervision of capital movements and gold control similar to ours would offer a much more permanent solution, and if that fails then a more drastic form of exchange control.

"I hope Simon and you will have a pleasant telephone conversation."

Harrison: It's doing him good.

H.M.Jr: What?

Harrison: That stuff's doing him good.

H.M.Jr: (To Kieley) Will you show Mr. Leroy Beaulieu in, please.

(Beaulieu comes in)

H.M.Jr: Good morning.

Beaulieu: Good morning, Mr. Secretary.

H.M.Jr: I understand you've got a message for me.

Beaulieu: It's in French. If you want me to translate it ....  
It's the same as Mr. Cochran .....

H.M.Jr: Just a question of words. Go ahead.

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Beaulieu: "At the meeting of the Council of Ministers held on the 4th of May at 8:30 French time, it was decided to address to the American Government a message of which the text has been given to Mr. Cochran by Mr. Rueff and phoned by this one to the French Ambassador in Washington, who has been asked to assure its transmission to the Secretary of the Treasury.

"'On the express demand'" - so this is the effect of the message - "'On the express demand of Mr. Morgenthau the French Government has decided to wait for the answer of the American Government.

"'This answer becomes from hour to hour more urgent'" - I have translated it freely; if you will try - don't know whether my English is very good - "'and we ask - we pray instantly Mr. Morgenthau to let us know when he receives the French financial attache this morning at 9 o'clock American hour. Meanwhile, we shall go on as we were asked, defending the French exchange against extremely hard pressure which can only accentuate - grow worse. It is indispensable to have as soon as possible agreement to our demand.

"'We give the assurance that the French Government has fixed to itself the new fall in the value of the franc as the last.'"

H.M.Jr: Just let me get that. What's that last sentence? Say that again please.

Beaulieu: "We give the assurance that the French Government has fixed to itself ....." "

H.M.Jr: Wait, I want to write it.

Beaulieu: "We give the assurance ...."

H.M.Jr: "We give the assurance ...."

Beaulieu: "...that the French Government..."

H.M.Jr: "...that the French Government..." Yes.

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Beaulieu: " ... has fixed to itself ...."

H.M.Jr: "....has fixed to itself.... "

Beaulieu: Oh - yes. Well, I'm trying to confine the English version to a mutual one.

"... has fixed to itself the fall ..." - how would you say ....

H.M.Jr: "The fall"... what?

Beaulieu: "... the envisaged fall as the last one."

H.M.Jr: "We give assurance that the French Government has fixed to itself the envisaged fall as the last one."

Beaulieu: Yes, I think this would be the exact .... Perhaps "fixes to itself."

Lochhead: I think "fixes to itself."

Beaulieu: ".... the French Government fixes to itself..."

H.M.Jr: Well, I understand the meaning. I mean they guarantee ... Now, naturally, the question I ask is, "All right, ...."

Beaulieu: I can leave you this (note in French).

H.M.Jr: I'd like to have it. "...well, they guarantee it won't go below 175?"

Beaulieu: Well, I suppose that's it.

Harrison: That's the interpretation you got.

H.M.Jr: And then what? Well, I can't - now, I tell you what I'll do. I can't give you an answer much before noon. But can you be at the Embassy?

Beaulieu: Yes, I'll make sure of it.

H.M.Jr: Well, I think the easiest thing would be if you go back to the Embassy, because after all you can come down in 15 minutes.

Beaulieu: Oh yes, easily. If you want to ask me any questions,

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if there is something in this text which isn't very clear.....

- H.M.Jr: No; just leave that with me, please, and if you'll go back to the Embassy .... Thank you.
- Beaulieu: And remember, when I gave you the message I insisted on having the answer as soon as possible because of the extreme pressure.
- H.M.Jr: I understand. We'll do it just as fast as we can. I'm trying to get Dr. Feis now.
- Beaulieu: Thank you very much. (Leaves)
- H.M.Jr: It seems to me the thing to do is go along with these babies. We've gotten a guaranty out of them.
- Harrison: I would urgently recommend that you do, Henry, because, whether rightly or wrongly, or whosever fault it is, all the press publicity now about 175 makes that the inevitable mark to which the franc will go, and the difference is so slight ....

(Feis comes in)

- Feis: Gentlemen.
- Harrison: ... as compared with the risks to us of a refusal to go along, that I think you can make a very stiff statement to them that you don't like the way it's been done, that you haven't had free opportunity for consultation in advance, that because of leaks or publicity you haven't been given a free choice, and that you reluctantly accede to their request, with the definite understanding, as conveyed in this letter, that this is the last drop.
- H.M.Jr: Of course, there is another way to do it, which simply would be to say nothing and simply say, "All right, go ahead."
- Harrison: Well then, they come back and say, "Are we in the tripartite or are we not?"
- H.M.Jr: Well, we just say, "Go ahead, and we consider you're in."

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Taylor: I think you have to go a little further than that.  
H.M.Jr: All right. It's all right with me.  
I wish you could excuse me one second while Herbert Feis is reading that. I want to put in one call.

(H.M.Jr goes out)

Harrison: Good morning, Dr. Feis.  
Feis: Gentlemen. On the basis of this last sentence here, I'm in favor of writing in a little ..... - "l'esperance que le Gouvernement Francais..."  
Harrison: Well, that's "l'assurance," not "l'esperance."  
Feis: Oh, that makes a lot of difference.  
Taylor: You're damn right.  
Feis: That's as far as they can go. Oh, that makes a lot of difference.  
Taylor: A hell of a lot of difference.  
Harrison: You worried me when you said that.  
Taylor: I read it that same way, but he (Beaulieu) translated it right, and it is "l'assurance."  
Feis: Well, I wish - I wish he'd write that double "s" so that ....  
Taylor: I'm writing it "assurance" in here.  
White: "l'assurance."  
Feis: Yes, but you can see how you can read it "esperance." Wayne, it wouldn't be "esperance" anyway; it would be "espe."

(H.M.Jr returns)

H.M.Jr: Herbert, I'm kind of pressed for time. I mean I got 40 minutes, and what I want - I mean what I'm going

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to do is, I go into a meeting at 10:30 and by 12 I'll be free again. See what I mean?

Feis: Yes, sir.

H.M.Jr: And I thought between 10:30 and 12 we can kind of write this thing out. Now, I've got a call in for Butterworth and I'll let you read the letter to him in French, see? No other person. You can read it to him.

Feis: Yes, I can read it to him.

H.M.Jr: He can get that to Phillips, and say, "Now we've got this thing and, based on this, we are now drafting a reply in which we will go along. As soon as we have it ...."

Feis: As soon as we have what?

H.M.Jr: "As soon as we draft an answer, we'll phone you again. But in the meantime we want the British Treasury to know what we've got."

Harrison: "And what we plan."

Feis: It's a trial balloon to me. Have to translate it from French.

H.M.Jr: (To Kieley) Tell Mr. Bewley to come down to the Treasury.

I'd read it to them in French. I'd read it to them in French.

White: Particularly that last sentence, because that last sentence - best translation would be that the French Government sets for itself, not fixes.

Feis: "We give assurance that the ...."

Taylor: No, "fixes" - "fixe."

White: "Fixe" means "sets."

Harrison: "Fixe" means "establish" or "determine." That's really the right translation - "fix."

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Feis: "... as the final one."

Lochhead: You'll be interested to know the franc this morning is about 170 to the pound, from 166 yesterday. They gave it spasmodic support, not to any great extent; just enough, I think, to carry out the technical angles of the tripartite, that they were ....

White: How much did they lose?

Lochhead: They had lost this morning up till - or rather this afternoon in Paris about 160,000 pounds; now, of course, probably they have lost more at London, because yesterday, remember, they only lost 50,000 in Paris, but they lost a total of six or seven hundred thousand pounds for the day. But still, it's a moderate loss. They're not making any serious attempt to do anything more than to ease the fall gradually.

Feis: You're not going to see Leroy Beaulieu today?

H.M.Jr: Oh yes, I told him by noon I'd have something. But I'm giving the letter to Cochran, and we'll give it direct to Butterworth, and let them handle it. And I'll let Leroy Beaulieu know what we're doing.

Did - Christ! I can't tell you what happened; did Messersmith tell you what happened last night at the Embassy? I was there for dinner. They get me in the corner, the two of them. I asked Messersmith, "Would you mind sitting next to me?" which he did. But I didn't want those two fellows - and as usual ....

Feis: Who were the two?

H.M.Jr: The Ambassador and Leroy Beaulieu. So I made Messersmith sit right next to me, just listen, you know. But for one hour after dinner they let everybody wait while they pounded me and said they must have an answer by 8:30 this morning, or 3:30 our time, in the morning - they must have an answer. I said, "Well, gentlemen, I'm very sorry." I said, "You've had two weeks to make up your mind."

Then they tried to pin this leak on us and Beaulieu said, "Well, I'm quite sure that if the leak came from

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anywhere, it came from Paris."

Feis: I haven't had time to see the papers yet this morning. Is it in the New York papers?

H.M.Jr: They treated it very well here. I kind of got a manifesto from four newspaper men, so I walked out and told them, "I'm not going to see the press, I've never seen the press, but if you write the story this is the way I'd write it. But you've never seen me." The Times and Associated Press - they wrote it just the way I told them.

Feis: That was when?

H.M.Jr: Oh, about half past four. Well, half past five. "You can't credit it to anybody. You can't use it. Never seen me." But they were going to write a big headline story that the tripartite was busted and we were letting the French down. "Now, you've never seen me, but you fellows have treated me beautifully, and in return for that here's the thing." So they wrote it just the way I asked them. And, as I said, couldn't have been better. Don't you think so?

Lochhead: Very well. The story that they are referring to about putting pressure on the franc was a story that came out of Paris, in which it was reported that the French Treasury had announced they were waiting on a decision of the British and American Treasuries to stabilize at a lower level; as soon as that came out, the franc was absolutely under pressure. So then when they came back last night with this and said the trouble was caused by news from here, we had ....

Feis: No news came from here at all.

Lochhead: No news came from here.

H.M.Jr: This is what I pointed out to the Ambassador. "Mr. Ambassador, Monday afternoon you sent word to me that the Minister of Finance - he sent word to me in a cable sent off Monday afternoon that you were going to let the franc go to 175. Now, he must have issued orders before he went to bed. One o'clock in the morning he changes his mind and says he isn't going to do that. Now, those orders were undoubtedly

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out Monday afternoon before Marchandean went to bed, and if there was any leak it was that the orders went out and at one o'clock in the morning he recalled them." You can't tell me that he didn't give the orders before he went to bed; and then one o'clock in the morning he recalled them. If there was any leak, it was on the other side.

Then I pounded him on this. I said, "I can't help it if speculators in international exchange for two weeks have known that it is going to be 175." So Leroy said, "That's right." He said, "I got so excited, I called up and spoke to Rueff on my own account. On my own I called up the Treasury and it was the same thing."

Leroy is with us, but that Ambassador is just one jack-ass.

Feis: In some ways.

White: There's a little trouble, Mr. Secretary, about saying anything in writing, because if your statement indicates that you're willing to go along because of the assurance that this is the last, and if that gets out, it may tie your hands on the one hand in the future, and on the other hand makes the world a lot more nervous about the franc and its prospects than probably we'd like to see. If, on the other hand, you graciously accede without indicating that the reason you're doing it is because they've given you this assurance, it may make it appear that anything goes for the time being. So that from the point of view of the public I'm wondering whether it may not be better ....

Harrison: Well, but ....

H.M.Jr: Let him finish his sentence.

Harrison: Excuse me.

White: I was wondering whether it would be better or not to follow your first inclination, which is to go ahead on a 24-hour basis; that is, not on a 24-hour basis in the sense you're going to let them know every day,

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but go ahead without giving your acquiescence or your disapproval.

H.M.Jr: Well, that's the point - I mean that I want advice on.

White: See, what I have in mind, what I am afraid of - if you say that "in the light of the assurances which you have given us," so on, so on, see what that would mean.

Harrison: Dr. White, what would you think of something ....

H.M.Jr: That's the point that should be settled.

Harrison: Not these words necessarily, but I wonder if this answers what you have in mind: "The American Treasury, without commenting on the wisdom or unwisdom of the envisaged plans of the French Treasury regarding the future of the franc, is pleased to accede to the request of the French Treasury that its action be accepted without prejudice to its position in the tripartite agreement. This position of the American Treasury is taken in view of the assurance of the French Government that ...." - and so on.

White: Well, that's the part that gives me a little pause.

Taylor: Well, here's the point.

H.M.Jr: Is there such a word as "unwisdom"?

Harrison: Yes, it's a very good word.

Taylor: Here's the point: if we have scared the life out of these people at this time, if they know without any question in their minds that they are out if they go below 175, these fellows are going to behave.

White: Well, that assumes that they have control over the situation.

Taylor: And if they don't behave, why, they're out anyhow.

Harrison: I like putting in that last sentence - "in view of their assurance" - because then you are forewarning them that that is the last ....

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White: Very thing I should like to avoid.

Feis: I agree with you.

Taylor: The one way of stopping all this speculation in the franc.

H.M.Jr: Do you want to put me in that position?

White: Definitely not.

Lochhead: I would rather say we were doing it ....

H.M.Jr: Listen, I told - when these fellows got terribly excited last night and were pushing me, they said, "Well, Mr. Rueff says he can't understand the Secretary of the Treasury; he's seen the franc go from 110 to 165 and he hasn't said anything. Now, suddenly when it wants to go to 175, he gets so excited."

So I said, "Well, Mr. Ambassador, I'll tell you the answer to that." I said, "I know I've lost my virtue, but I don't want to become a professional." And they just howled. You (reporter) put that in the record; that's all right. They just howled. And that's exactly - but I then told them - and Messersmith loved it - but I said, "Don't forget, Mr. Ambassador, all of us have done things in the last six months that we're not very proud of."

And I don't want to be put in the position of saying, "Over 175, you go out," because you fellows might be back here on your bended knee, Herbert Feis with the tears rolling down his face, saying that "General Goering today is in England and, my God, with General Goering in England you're not going to at this time kick out the French." And with the tears rolling down his cheeks, I would graciously accede. I mean I've just got to be careful.

Harrison: I agree that you shouldn't put yourself in that position. But my last sentence was merely to indicate that you're taking this position. We can say, "In view of," but that may be a little strong. "In the light of the French Government's assurance

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that" - no, that doesn't say ....

White: Quite the same.

H.M.Jr: What?

White: It's almost the same.

Let me ask this question. What is to be gained by making any statement beyond the fact, which can be given by a simple statement, that they are not out? What is there to be gained? They don't need any more confidence. All they're worrying about is that some action will be taken here which will throw them out.

Harrison: Oh, I'm perfectly agreeable to eliminating the last sentence. I thought that was going to protect the Treasury position rather than prejudice it.

White: I would eliminate it - not only the last, but I think the earlier as well.

Feis: Suppose ...

Lochhead: I think ...

Feis: "1. The Secretary of the Treasury states you are not out of the tripartite agreement.

"2. The Treasury is very glad to have the clear assurances of the French Government."

Just two very ....

H.M.Jr: May I change it, take an entirely different angle? Your statement, I mean, reminds me of the story about beating your wife. I haven't got the tripartite here, but I would paraphrase the tripartite - the thing about consultation, and restate it and say that we appreciate the fact that the French Treasury has consulted with us about their action, and in view of this consultation we consider - we are glad to continue.

White: "There is no change in the status quo."

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Feis: "We are glad to continue. No change."

H.M.Jr: And that's all. See? In other words ....

White: I'll get the tripartite wording.

Feis: I think that's fine.

H.M.Jr: I mean just paraphrase ....

White: Shall I get it?

H.M.Jr: Yes. You see, we say that under the tripartite agreement we considered that we have been consulted, and in view of that the agreement is still in force.

Harrison: I think that's quite all right.

Feis: That's good, but what about adding one sentence referring to these assurances?

Taylor: I think that ought to be in there.

Lochhead: You could refer to this message in answering - refer to the message and the assurances given in the message, without specifying what they are.

Harrison: "American Treasury appreciates the assurance."

H.M.Jr: Which come under - I mean bring in the word "consultation." Something like that. You can start off, "We acknowledge receipt of this message and we are glad of the opportunity to confer with the French Treasury over their proposed move. We beg to advise you that we consider that you have lived up to the spirit of the tripartite agreement." Something like that.

Harrison: I think that's fine.

H.M.Jr: See? Herbert?

Feis: That's the way to handle it.

H.M.Jr: Is that the way to handle it?

Feis: Yes.

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Harrison: That's very good.

Lochhead: Leaves you free at any time in the future.

H.M.Jr: After all, you can't disregard this message from the President of the United States. Did you read that?

Feis: As I say, I read it - ordinarily, I sign these Treasury cables. But I wasn't going to sign this one; that was going to be from Mr. Hull.

H.M.Jr: Well, you know my purpose in sending that. I used the word "for their guidance" because both Kennedy and Wilson are advising the Government that they think it's a mistake, more or less. Kennedy, very definitely - very definitely.

Feis: You mean the consideration of control is a mistake?

H.M.Jr: Yes.

Feis: Kennedy may. I'm sure I know Wilson well enough to know that he would not be giving a single sign that he's sent us his opinion; but he's not, I'm sure.

H.M.Jr: Well, I have a very definite reason. I don't want to go over it now, but you can when you go back.

Feis: I'm glad to be able to explain that to Mr. Hull.

H.M.Jr: Well, tell Mr. Hull that Kennedy put up the darndest argument to me at five o'clock yesterday morning, trying to stop me from doing that - definitely putting it up then. But after this - this has just come in now. You put this in your pocket, and this is only for Hull and you. Only for Hull and you. Nobody's seen it yet, and - which makes it all the more reason that he should know where the President stood. See? Also, I know my President.

Now, can somebody - can somebody ....

Taylor: I've got something for a start here.

Lochhead: Harry had something.

Taylor: You can fill in the language about the cooperation here. See how this sounds. And it goes back to their original message a little bit.

"The Secretary of the Treasury appreciates the severe strain which has been placed on the assets of the French equalization fund during recent months. In view of all the circumstances which have contributed to this situation, the Secretary of the Treasury hopes that the program which has been adopted by the Government of France will foster economic conditions in France which will enable her to fully utilize her productive capacity."

H.M.Jr: No, don't want any of that.

Taylor: "The Secretary of the Treasury appreciates the assurances which the French Government has given to the Treasury of the United States and appreciates the opportunity to consult," and so on.

H.M.Jr: No, I'm sorry.

Taylor: All right.

"On the basis of these assurances, the Treasury of the United States will continue to cooperate fully with the French Treasury under the terms of the tripartite accord."

H.M.Jr: No, we'll - no - no, I - something very simple, Herbert. If you could take a couple minutes. I mean very, very simple - and simply say that "I acknowledge receipt of this message delivered to me by the French Ambassador - message from Minister Marchandeau, and ... "

Lochhead: Is that the Minister or the whole Council of Ministers that sent that?

H.M.Jr: Well, whatever it is. And that I consider that the French during the past two days have lived up to the spirit of the tripartite agreement, and in view of this the United States Treasury is glad to continue. I mean you can polish that up.

Feis: I think I can make ...

- H.M.Jr: Just as short and terse ...
- Feis: Would you visualize that the Council of Ministers might give this out?
- H.M.Jr: True.
- White: That's why I don't think - if that's the case, it ought to be just ....
- Lochhead: They'll give out the point that they have a note from the United States.
- Feis: Secretary's message, without giving anything else out. But I think that's an additional reason for keeping the thing short and simple.
- White: One sentence, if possible. One, possibly two brief sentences.
- Feis: Well, the Secretary's approach, by referring back to the tripartite agreement ....
- White: I think we can get a phrase out of there.
- Feis: And then possibly a concluding sentence - "takes note with the greatest of interest of the assurances given in this note."
- H.M.Jr: Have you got something there, Harry?
- White: Here it is.
- H.M.Jr: When these gentlemen come in at 10:30, would you (Kieley) tell them that I've got a bad throat and I would appreciate it if they would not smoke in here today - not smoke at all here today.
- (White hands copy of tripartite agreement to Secretary)
- H.M.Jr: Here's the thing. You better not come too close, but it's in here - right in there, Herbert.
- Tell you what you could do ....
- (On phone) What about Butterworth?

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- H.M.Jr: Herbert, I think if you wrote it all by yourself we could get somewhere better. Do you want to go down to the room downstairs by yourself? Don't you think so?
- Feis: Yes. Could I ....
- H.M.Jr: I'll send a messenger down with you.
- Feis: Could you ask White to go down with me?
- H.M.Jr: Sure, I'll send you down by yourselves.  
(To messenger) Take Dr. Feis into my dining room downstairs. You (White) go with him.
- Harrison: I've got another good one.
- H.M.Jr: I think let him go downstairs.
- Harrison: Want to try this one? No, that's all right.
- H.M.Jr: Oh, all right, go ahead.
- Harrison: "The American Treasury begs to acknowledge the receipt of the message of the French Government giving its assurance that the envisaged depreciation of the French franc is a final one.  
  
"In view of the fact that the French Treasury has been good enough to consult with the American Treasury (tongue in your cheek) concerning its present plans to devalue the franc, it begs to advise the French Treasury that it accedes to its request that its proposed action be regarded as coming within the spirit of the tripartite agreement."  
  
End of message.
- H.M.Jr: Well, supposing I send it down to the boys. How's that?
- Taylor: That ties a little too closely to the fact that they have consulted.
- H.M.Jr: Let me send it down to them.  
  
(On phone) Hello. (Conversation with Butterworth follows:)

Wednesday  
May 4, 1938  
10:17 a.m.

Wm. Walton

Butterworth: Yes, sir.

HMJr: Hello, Butterworth.

B: Yes, Mr. Secretary.

HMJr: Can you hear me?

B: Yes, I can.

HMJr: Now, ah - we've got a message.

B: I beg pardon.

HMJr: Just a minute. I've got a message from the French.  
Hello?

B: Yes.

HMJr: Can you hear me?

B: Yes.

H.M.Jr: Ah - which they delivered to me this morning at nine  
o'clock. Now, a literal translation of the last part  
of it is something like this - have you got a pencil?

B: Yes.

HMJr: "We give the assurance that the French Government ...."  
Hello.

B: Yes.

HMJr: "... has fixed to itself the envisaged fall as the  
last one." I'll repeat it. "We give the assurance  
that the French Government has fixed to itself the  
envisaged fall as the last one."

B: Right.

HMJr: Now - this comes from the Council of Ministers.

B: Yes.

HMJr: I don't know whether the British Government has  
got anything like this or not.

B: I don't either. I can find out, though.

- 2 -

HMJr: Well. Now what we're doing now, we're drafting an answer which will be very short and will be along something - this line - "We refer to the Tri-partite Agreement..."

B: Yes.

HMJr: We will say that we consider that they have consulted us.

B: That - we will say what?

HMJr: That we consider that they have consulted us.

B: I see. Uh huh. That's good.

HMJr: And that in view of this assurance we'd be willing to go along with them. You see?

B: Yes.

HMJr: Now that is very roughly what we're trying to put into a note.

B: Yeah.

HMJr: As soon as we have the note drafted...

B: Yes.

HMJr: ...we will phone it to you.

B: Yes, sir.

HMJr: We will give you a chance to show it to the British Treasury.

B: Right.

HMJr: And we will wait until we hear from them.

B: Right.

HMJr: We will do nothing until we hear from them.

B: Right.

HMJr: But you might tell them that that's the way it stands now.

- 3 -

B: Yes. I will tell them.

HMJr: And just as soon as we see the note I will phone it to you.

B: Right, sir.

HMJr: And - but, in view of this assurance and in view of the fact that they have postponed action for two days...

B: Yes.

HMJr: ...in order to consult us...

B: Yes.

HMJr: ...why we feel that we ought to go along with them.

B: Yes, that's changed the picture.

HMJr: Pardon me?

B: I say that's changed the picture.

HMJr: Yes. Yes. And - ah - I say the State Department is working with us now on a draft.

B: Yes, sir.

HMJr: Now, it will be another couple of hours. Hello.

B: Yes.

HMJr: I say it will be at least a couple of hours.

B: Right, sir.

HMJr: All right?

B: All right, sir.

HMJr: What have you got, anything?

B: Nothing very much. The franc is about a hundred and seventy and a fraction and the French control has come in and they're steady.

HMJr: That's right. Well, ah - wait a minute.

- 4 -

(Short pause)

HMJr: Hello.

B: Yes.

HMJr: Just a minute until we have it - ah - we'll phone it over to you and - of course you appreciate that the French are putting terrific pressure on us now.

B: Oh I understand.

HMJr: And so once we get the draft I would appreciate a yes or no as quickly as possible.

B: All right, sir.

HMJr: And Lochhead just pointed out to me that Daladier goes on the radio at eight o'clock French time tonight.

B: Yeah.

HMJr: And, as I say, the French - ah - they tried everything they could to get me to change last night but I wouldn't.

B: Yes.

HMJr: And - so once we do get it over there why the sooner we get an answer the happier everybody will be and that's that.

B: Right, sir.

HMJr: Thank you.

B: And we'll try to get this answer before eight o'clock tonight if possible.

HMJr: Oh - ah - yes, yes.

B: Goodbye, sir. Thank you very much.

HMJr: Thank you. All right.

-18-

H.M.Jr: Now, I want five minutes to catch my breath. Archie, just give them this thing that Mr. Harrison wrote and tell them this, that when they're ready I'll come downstairs, I'll leave this meeting and come downstairs. And then you can arrange for Mr. Hull to see it.

Lochhead: Do you want us to go downstairs with them?

H.M.Jr: Well, they'll be here - the three of us can come downstairs.

Lochhead: Well, I'll let them know.

Harrison: That's just nothing but a suggestion for those fellows.

H.M.Jr: (To Kieley) All right, tell them to come in, please.

(Bewley comes in)

Hello, Bewley, how are you?

Bewley: Good morning.

H.M.Jr: This is what I have done. Then you can go in there and read this. We have a message from the French Ministers' Council in which the point of it is that they guarantee to us now they won't go below 175. I've phoned this just now to Butterworth, told Butterworth that based on this we're drafting a note to the French in which we now say we've been consulted and in view of this thing we're going to go along. But when it's drafted I'm going to phone it to Butterworth so he can take it right over to the British Treasury. We are doing nothing until we have given it to the British Treasury. I couldn't give this to Butterworth, but if you would copy this - I think if you would phone it over, cable it over once to your people, it would help. But just as soon as we have this note, I'll phone it and give you a copy of it. And Daladier goes on the radio at 8 tonight French time; if we can't clear this all up - do all we can. But this is quite a remarkable note. So I do think that, having waited a few days, we've got something.

-19-

Bewley:

Yes.

H.M.Jr:

We have distinctly got something. They say, "We give the assurance that the French Government has fixed to itself the envisaged fall as the last one." So I would say that is a definite accomplishment.

If you two gentlemen would tell them downstairs that as soon as they're ready ...

The thought underlying the draft reply to the French Government proposed by His Majesty's Government was as follows:

(1) They thought that any decision which led to France leaving or being expelled from the Tripartite Agreement might bring about a government by the large party in France which wants exchange control and would in any case be a heavy blow to the present French Government. They thought that exchange control could not be satisfactorily worked in France, that it would seriously hamper legitimate trade and business but would probably fail to stop illegitimate activity, and further that the effect would spread to other countries. Moreover, they did not think that exchange control would in fact prove an alternative to a lower value of the franc but would be in addition.

(2) A breakup of the Tripartite arrangement would be hailed everywhere by advocates of autocracy as a disaster for liberal ideas in international finance and business.

(3) On the technical question the British view was that until recently there was no reason to suppose that it would be harder to hold the exchange at say 160 or so than it would be to hold it at 175 but an entirely fresh situation was created when there were leakages by which important parts of the market learned that some members of the French Cabinet favoured a rate of 175. Thus the damage has to this degree already been done and it would seem that the French franc would be liable

to considerable weakness whenever it stood above that point.

(4) The fundamental weakness of the franc is due to internal causes no less than to capital movements and the foreign trade position. That is to say, the franc might be supported on a basis of increase of production, improvement in volume of business, avoidance of undue concessions in respect of wages and labour conditions. The decrees recently issued though not themselves adequate at least indicate a real effort to face the situation and it is also possible that if things do not seriously deteriorate the present government might be replaced before long by a real national government which could deal successfully with the situation.

(5) For these reasons, while the situation is certainly unsatisfactory (and indeed is likely as concerns tariff changes etc. to be at least as harmful to Great Britain as to the United States if not more so) it was felt that it would be the wrong policy to take any step which would result in France leaving the currency club.

7

Thursday  
May 5, 1938  
10:12 a.m.

Operator: Go ahead.

RMJr: Hello.  
Wm. Walton  
Butter-  
worth, Jr: Hello, Mr. Secretary.

RMJr: Hello, Butterworth.

B: Hello.

RMJr: Hello, Butterworth.

B: Yes, Mr. Secretary.

RMJr: Go ahead.

B: Ah - I passed on your message to Phillips.

RMJr: Yes.

B: And he said that he also thought it was very bad behavior on the part of the French....

RMJr: Yes.

B: ...to have opened the rate as low as a hundred and seventy-nine.

RMJr: Yeah.

B: He said however that he did not feel that a hundred and seventy-five was the absolute top limit.

RMJr: I see.

B: For the note which the French Government had sent here to them had used the phrase, "in the neighborhood of" and that same phrase had been repeated in the British note.

RMJr: Oh.

B: ... yesterday evening.

RMJr: I see.

- 2 -

B: Phillips said that he is however in absolute agreement with you...

HMJr: Yeah.

B: that before the day is over the French should push the rate up to a hundred and seventy-five.

HMJr: Yeah.

B: And that he will see what he can do on his side to help you with that.

HMJr: Fine. Now wait a minute, Archie is - Archie wants to say something.

(Pause)

HMJr: Hello.

B: Yes, sir.

HMJr: This is a message from Bolton of the Bank of England. Hello.

B: Yes.

HMJr: Bolton told Knoke that he understood that it was to be a hundred and seventy-five.

B: Yes.

HMJr: That was his understanding.

B: Yes.

HMJr: And - a "gentlemen's agreement".

B: Yes.

HMJr: And that the extra three or four percent is going to make it particularly difficult for Belgium and Holland.

B: Yes.

HMJr: And Bolton went on to say, "Well, at least it'll be a great day for France for one day."

- 3 -

B: It'll be a great day for France for one day?

HMJr: Yeah.

B: Yes. (Laughs)

HMJr: So Bolton thought it was a hundred and seventy-five; we thought it was a hundred and seventy-five; Cariguel thought it was a hundred and seventy-five.

B: Yeah.

HMJr: Federal Reserve in New York thought it was a hundred and seventy-five.

B: Yeah.

HMJr: Ah ....

B: Phillips says that he is in absolute agreement with you....

HMJr: Fine.

B: ...that before the day is over the French should try to push it much nearer that.

HMJr: All right. Now I didn't give them any ultimatum but I went as far as I could in letting them know how displeased I was.

B: Right. And he appreciated very much - he asked me to express his appreciation for your

HMJr: Right. And the same to him and many of them.

B: Yes, sir.

HMJr: Hello.

B: Yes, sir.

HMJr: What was the name of the hotel that you went to with your wife on - at Antibes?

B: Hotel Ducap.

HMJr: Well that's the one that I'm thinking of going to. That's the one you recommended, wasn't it? Hello?

- 4 -

B: Hello.

HMJr: That's the one you recommended so highly?

B: Yes, I think it's a grand place.

HMJr: That's what I - well, I have hopes.

B: Oh. Good.

HMJr: For August.

B: For August?

HMJr: Yes.

B: I see, sir.

HMJr: Yeah.

B: Well, that's grand.

HMJr: What's that?

B: I say that's fine, I'll look forward to it.

HMJr: I have hopes.

B: Good.

HMJr: And - ah - possibly I - we could - ah - some of the people in the British Treasury might be in that neighborhood at that time or they might - when I get - after having a couple of weeks possibly we could get together somewhere.

B: I should think so.

HMJr: Well you might sort of pass that along.

B: Right.

HMJr: Sort of casually. I wouldn't make a great point of it.

B: Right. What about this country?

HMJr: Well, I haven't thought it through; the whole thing is very vague.

- 5 -

B: All right, sir.

HMJr: Very vague.

B: Right. Well, I'll pass that along very casually to Phillips.

HMJr: Fine. Thank you.

B: Thank you very much, sir. Goodbye.

## PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: May 4, 1938, 11 a.m.

NO.: 701

RUSH FROM COCHRAN.

At five minutes after ten this morning the Bank of France telephoned to report that at 165 1/2 trading had opened, and by the time they telephoned the rate had moved to 166-3/4 in spite of the fact that 1,000 pounds were yielded by the control. It is believed that the strong demand for sterling is due partly to a detailed report in AGENCE ECONOMIQUE cabled from New York with regard to monetary conferences being held in Washington among French, British and American representatives. According to my friend it would be very difficult to check this movement.

At 10:50 I was received by Rueff at his request. He told me that Leroy Beaulieu had telephoned him at 6 o'clock this morning a report of his conversation with Secretary Morgenthau last night. Rueff then said that following the meeting of the Council of Ministers which was held at 8:30 this morning Marchandau desired that the following message be promptly communicated to Secretary Morgenthau:

"Under the specific request of Mr. Morgenthau the French Government has decided to await the reply of the

MISS CHAUNCEY

217

Correction on Cable #701, Paris, May 4/38  
last word (omission) should be very

American Government but this reply becomes from hour to hour more urgent and we request urgently that Mr. Morgenthau make known his reply at the interview which he is kindly giving to our Ambassador today, May 4, at nine a.m., Washington time. In the meantime we continue as we have been requested to protect the currency against a (omission).

END SECTION ONE.

WILSON.

EA: LWW

02118523  
REC'D  
TREASURY DEPT  
MAY 4 1938

JR

SPECIAL GRAY

Paris

Dated May 4, 1938

Rec'd 10:05 a.m.

Secretary of State,  
Washington.

RUSH.

701, May 4, 11 a.m. (SECTION TWO).

strong pressure which can only grow. It is necessary for us to have as soon as possible an adherence to our request "et nous donnons l'assurance que le gouvernement se fixe la chute envisagee comme la derniere".

Rueff and I could not agree on a translation of the final phrase above quoted in French. I asked if this meant that the present Government definitely pledged that no depreciation beyond 175 shall take place. Rueff said that he could not take the responsibility for a translation but thought that the words used indicated clearly the Government's determination to stop definitely at 175.

Rueff asked me if we had taken any action vis a vis the three countries which subsequently adhered to the original tripartite accord. I told him that I had not been in touch with the Belgian, Dutch or Swiss officials and was not aware of any consultation between Washington officials

-2- #701, May 4, 11 a.m. (SECTION TWO) from Paris.

officials and those of the three countries mentioned. I remarked that the proposition under discussion had originated with the French. Rueff said he asked the question because his Financial Attache in Washington had reported Secretary Morgenthau's concern as to whether the contemplated French depreciation might hurt the other three currencies.

While I was with Rueff he telephoned the Bank of France and learned that the rate was 167-5/8. Since preparing above message I have again talked with Bank of France at 11:50 a.m. Rate was then 168-5/16 on a one way market and control had yielded 160,000 pounds. (END OF MESSAGE).

WILSON

HPD

May 4, 1938

FOR THE PRESIDENT OF THE UNITED STATES  
STRICTLY CONFIDENTIAL

THIS MORNING I RECEIVED A NOTE IN FRENCH FROM MARCHANDEAU,  
A TRANSLATION OF WHICH FOLLOWS:

"AT THE SPECIFIC REQUEST OF MR. MORGENTHAU THE  
FRENCH GOVERNMENT HAS DECIDED TO AWAIT THE  
REPLY OF THE AMERICAN GOVERNMENT.

"THIS RESPONSE BECOMES FROM HOUR TO HOUR MORE  
URGENT AND WE URGENTLY REQUEST MR. MORGENTHAU  
TO MAKE KNOWN HIS REPLY IN AN INTERVIEW WHICH  
HE IS KINDLY GIVING OUR FINANCIAL ATTACHE TODAY,  
MAY 4TH, AT 9 O'CLOCK WASHINGTON TIME. IN THE  
MEANTIME WE CONTINUE, AS WE HAVE BEEN REQUESTED,  
TO DEFEND OUR CURRENCY AGAINST THE EXTREMELY  
STRONG PRESSURE WHICH CAN ONLY GROW. IT IS  
NECESSARY FOR US TO HAVE AS SOON AS POSSIBLE AN  
ADHERENCE TO OUR REQUEST.

"WE GIVE THE ASSURANCE THAT THE FRENCH GOVERNMENT  
ESTABLISHES FOR ITSELF THE CONTEMPLATED DROP AS  
THE LAST."

AFTER RECEIVING THIS MESSAGE CORDELL HULL AND I AGREED THAT  
WE SHOULD ACCEPT THE WISHES OF THE FRENCH IN RESPECT TO THEIR  
CURRENCY. WE FORWARDED TO THE FRENCH THE FOLLOWING MESSAGE  
AFTER HAVING FIRST SUBMITTED IT TO THE BRITISH:

"CONSEQUENT UPON THE CONSULTATION WHICH THE FRENCH  
GOVERNMENT HAS CARRIED ON WITH THE AMERICAN AND  
BRITISH GOVERNMENTS, AS PROVIDED BY THE TRIPARTITE  
ACCORD, HIS GOVERNMENT REGARDS THE ACCORD AS  
CONTINUING IN FULL OPERATION.

"THE ASSURANCES IN THE NOTE OF MAY 4, 1938, GIVEN  
BY THE FRENCH GOVERNMENT WITH RESPECT TO CARRYING  
OUT THE LETTER AND SPIRIT OF THE ACCORD ARE NOTED  
WITH THE GREATEST OF INTEREST."

Henry Morgenthau, Jr.

AMBASSADE DE FRANCE  
AUX ETATS-UNIS.

Le 4 mai 1938

Le Conseil des Ministres, qui s'est tenu le 4 mai à 8 heures 30 (heure française) a décidé d'adresser au Gouvernement des Etats-Unis le message suivant dont le texte a été communiqué à Mr. Cochrane par M. Ruoff et téléphoné par ce dernier à l'Ambassadeur de France à Washington qui a été pris d'en assurer la transmission au Secrétaire de la Trésorerie :

« Sur la demande appuyée de

Mr. Morgenthau, le Gouvernement  
Français a décidé d'attendre la réponse  
du Gouvernement Américain.

« Cette réponse devient d'heure  
en heure plus urgente et nous prions  
instamment Mr. Morgenthau de  
vouloir bien la faire connaître au  
cours de l'audience qu'il doit  
accorder à notre Attaché Financier  
aujourd'hui 4 mai à 9 heures  
(heure Américain).

« En attendant, nous continuons,  
ainsi que cela nous a été demandé,  
à défendre la monnaie contre des

prejouis extrêmement vivés qui ne  
peuvent que s'accroître. Il vous est  
indispensable d'avoir au plus tôt une  
adhésion à notre demande.

« Nous donnons l'assurance que  
le Gouvernement Français se fera  
la chute envisagée comme la  
dernière » / JH

COPYCOPY

Ambassade de France  
Aux Etats - Unis

Le 4 Mai 1938

Le Conseil des Ministres, qui s'est levee le 4 mai a 8 heures 30 (heure Francaise) a decide d'adresser au Gouvernement des Etats-Unis le message suivant dont le texte a ete communique a Mr. Cochrane par M. Rueff et telephone par ce dernier a l'Ambassadeur de France a Washington qui a ete prie d'en assurer la transmission au Secretaire de la Tresorerie.

"Sur la demande expresse de Mr. Morgenthau, le Gouvernement Francais a decide d'attendre la reponse du Gouvernement Americain.

"Cette reponse devient d'Heure en heure plus urgente et nous prions instamment Mr. Morgenthau de vouloir bien la faire connaitre au cours de l'audience qu'il doit accorder a notre Attache Financier aujourd'hui 4 mai a 9 heures (heure Americaine).

"En attendant, nous continuons, ainsi que cela nous a ete demande, a defendre la monnaie contre des pressions extremement vivies qui ne peuvent que s'accentuer. Il nous est indispensable d'avoir au plus tot une adhesion a notre demande.

"Nous donnons l'assurance que le Gouvernement Francais se fixe la chute envisagee comme la derniere."

(signed by initials indecipherable)

May 4, 1938  
Wednesday

At 11:15 today telephoned Butterworth at the American Embassy, London, and dictated the text of the attached note, explaining to him that we were not sending this note to the French until he had shown it to the British Treasury and secured their approval. He assured me he would do this immediately and telephone as soon as he received their reply.

Butterworth brought up the point that Daladier was making a radio address this evening at 8 o'clock, Paris time, and might possibly wish to use the text of our note. Told Butterworth that the text of our note was drawn up with the thought that if it became public we would have no objection.

A.L.

May 4, 1938

Consequent upon the consultation which the French Government has carried on with the American and British Governments, as provided by the Tri-Partite Accord, this Government regards the Accord as continuing in full operation.

The assurances in the note of May 4, 1938 given by the French Government with respect to carrying out the letter and spirit of the Accord are noted with the greatest of interest.

May 4, 1938

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The assurances in the note of May 4, 1938 given by the French Government with respect to carrying out the letter and spirit of the Accord are noted with the greatest of interest.

*Handwritten notes:*  
W. A. ...  
K. ...  
8-5-1  
... ..

Consequent upon the consultation which the French government has carried on with the American and British governments, as provided by the Tripartite Accord, this government regards the Accord as continuing in full operation.

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<sup>in the note. 7 May 1942</sup>  
The assurances given by the French government with respect to carrying out the letter and spirit of the Accord are noted with the greatest of interest.

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May 4, 1938

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FEDERAL RESERVE BANK  
OF NEW YORK

OFFICE CORRESPONDENCE

DATE May 4, 1938.TO CONFIDENTIAL FILESSUBJECT: TELEPHONE CONVERSATION WITH  
BANK OF FRANCE.FROM L. W. Knoke

I called Mr. Cariguel at 2:56 to inquire whether in view of the fact that the American note expressing itself in accord as continuing in full operation the Tripartite Accord, had just been delivered in Paris, he still wanted to hold the franc around the 170 level. Before I had a chance to state the purpose of my call Cariguel asked that against his second buying order (at 170.88) we take in only 10,000,000 and then let the rate go up to 175 and hold it there, operating both ways. I assured him that we would do our best to comply with his new instructions.

LWK:KW