

DIARY

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June 16, 1936

Secy's Speech
PHILADELPHIA.--SECRETARY MORGENTHAU DEFENDED THE GOVERNMENT'S¹

SPENDING-LENDING PROGRAM TODAY AS NECESSARY TO ECONOMIC SECURITY AND POLITICAL STABILITY.

ASSERTING THAT THE GOVERNMENT HAD "ARRESTED THE CATASTROPHIC DECLINE" OF THE FIRST YEARS OF THE DEPRESSION, MORGENTHAU TOLD THE GRADUATING CLASS OF TEMPLE UNIVERSITY THAT THE EXPENDITURES WERE A "NECESSARY INVESTMENT" TO MAINTAIN THE PHYSICAL AND SPIRITUAL HEALTH OF THE AMERICAN PEOPLE.

"THE GOVERNMENT HAS ALREADY INCURRED THE ENMITY OF THOSE WHO, FIRM IN THE POSSESSION OF THE PREROGATIVES ARISING FROM UNBRIDLED ECONOMIC POWER, WOULD DENY TO OTHERS THE LIBERTIES WHICH IN A DEMOCRACY BELONGS TO EVERY MAN," MORGENTHAU SAID.

HE TOOK ISSUE WITH A STATEMENT YESTERDAY BY DR. JAMES ROWLAND ANGELL, FORMER PRESIDENT OF YALE UNIVERSITY AND EDUCATIONAL DIRECTOR OF THE NATIONAL BROADCASTING COMPANY, WHO ATTACKED PLANNED NATIONAL ECONOMY AS FUTILE.

"THERE ARE THOSE WHO STILL TELL US WE OUGHT NOT TO PLAN OUR FUTURE," MORGENTHAU SAID. "THAT IS A PERFECTLY COMPREHENSIBLE ATTITUDE, BUT IT IS THE DREAM-THINKING OF BEATEN MEN WHO SEEK SOLACE IN THE SURROUNDINGS AND THE ASSOCIATIONS OF A LESS TROUBLED TIME IN THE HOPE OF RECAPTURING THE PAST."

6/16--R1025A

Att

2

REB

PLAIN

London

Dated June 16, 1938

Rec'd 3 p. m.

Secretary of State,
Washington.

522, June 16, 7 p. m.

FOR TREASURY FROM BUTTERWORTH.

The demand for gold continues but the pressure has again lessened slightly. There were 422 bars at fixing and also after fixing probably less business done than yesterday. From India have come this afternoon a few forward selling orders.

The dollar has been steady to bid most of the day and although the franc has been sold the amount of sterling lost was very small.

The trade indices for May reveal no break in the downward trend. Rail traffics, bankers clearings, building plans, et cetera, as well as a counter-seasonal increase in unemployment indicate growing depression especially in the export trades. Overseas trade returns published today foreshadow further decline in industrial activity, the quantities of many important raw materials

RECEIVED

REB

2-#522, From London, June 16, 7 p.m.

received having fallen again, while further evidence of export trade losses already suffered is to be seen in the 25 per cent drop in the value of textiles and clothing exports as compared with May 1937. The fact ~~that~~ the group of exports including metal and engineering goods is maintained at about last year's level may be attributed to the time lag of deliveries of such goods, continued intensive activity in South African gold-mining, and deliveries of certain machinery orders placed by Russia under the £10 million credit of last year.

The import surplus for the first five months of 1938 was £169 million as compared with £155 million for the corresponding period of 1937.

Stock exchange prices indicate that hopes of a major stimulus from the United States in the near future are dwindling and investors are turning from industrial stocks to gilt-edged securities while speculators show increasing interest in gold-mining stocks which like gold hoarding also attract those desiring a hedge against depression and currency uncertainties.

The

REB

3-#522, From London, June 16, 7p.m.

The £80 million defence loan was well received (my 517, June 15, 6 p. m.) and allotments are reported to have been about 66 percent of applications with dealings starting today at a premium of 1/8 moving to 1/2.

The general outlook seems to be one of continued industrial decline with capital seeking liquidity and safety.

JOHNSON

CSB

01X11014
JUN 16 1946
COMMUNICATIONS SECTION
U.S. DEPARTMENT OF THE ARMY
WASHINGTON, D.C.

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: June 16, 1938, 6 p.m.

NO.: 945

FROM COCHRAN.

Paris exchange market more quiet today with only fair turnover in sterling at from 178.38 to .40. Lazard bought one and one-quarter million dollars presumably covering short position. Bank of France statement as of June 9 showed increase of over one billion francs in deposits reducing coverage from 47.13 to 46.83. Treasury account only up to 876,000,000 notwithstanding that payments on account of 5,000,000,000 franc loan were all due in by June 3. Market no longer buying Treasury bills and even trying to dispose of them to such an extent that government may shortly be obliged to raise rate thereon.

At half-past five the Bank of France telephoned me. My friend told me that the control lost a quarter million pounds this morning but this afternoon lost nothing; he had on his own initiative telephoned to the Bank of England yesterday and argued that permitting the dollar to depreciate against sterling was adding to the market belief that the dollar would be devalued, and the demand on London for gold was therefore being augmented. It had been reported that
yesterday

- 2 -

yesterday evening the American authorities had sold sterling; my friend said that he thought this had been a wise move in the interest of all of us since a real monetary panic appeared to be in the making and has given signs of letting up today.

BULLITT.

RECEIVED

JUN 14 1958

TREASURY DEPARTMENT

EA: LWW

U.S. GOVERNMENT PRINTING OFFICE: 1957 O - 300,000

7

PARAPHRASE OF TELEGRAM SENT

TO: American Embassy, Paris (France)

DATE: June 17, 1938, 11 a.m.

NO.: 377

Department asks whether it would be possible for Cochran to get an estimate in total and by individual countries of blocked balances in Germany under clearing arrangements and for other reasons. It is understood that considerable detailed material is in the hands of the Bank for International Settlements.

HULL

EA: LWW

JR

GRAY

8

London

Dated June 17, 1938

Rec'd 2 p.m.

Secretary of State,
Washington.

527, June 17, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

The demand for gold has lessened again today. Only 308 bars were dealt in at fixing and for the first time since the movement got under way the post -- fixing price was not at one-half pence premium. In fact there was at least one seller at one-half pence below fixing price. The Indian market has not traded actively. The dollar has been mostly bid. The franc has on balance been offered but in insignificant quantities.

The only noteworthy item in this week's Bank of England's statement is an increase of pounds 7,800,000 in private balances to pounds 43,200,000. In mentioning this fact the financial news states "it is known that more than one foreign central bank has been actively selling out dollar holdings against sterling during the past few days of dollar scare and it is presumed that a proportion of these sterling funds has been temporarily left on deposit at the Bank of England".

JOHNSON

WVC:CSB

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: June 17, 1938, 5 p.m.

NO.: 954

FROM COCHRAN.

In dull trading franc after opening at 178.38 improved to .25 but this afternoon moved back around .33. With talk of dollar devaluation somewhat abating there is less demand for gold on the part of the continental centers, particularly Switzerland, and India is also reported to have let up on London purchases. Local bankers understand that Bank of Canada supply of American eagles, from which European demands have been importantly met, will be exhausted before end of month. Bank of England's recent sales of sovereigns said to have been large and Swiss have been minting their own gold coins to meet European hoarding demand after Swiss supply of acceptable foreign coins was exhausted. With short covering in belga evidently completed for present this currency slightly offered today.

At five o'clock this afternoon I talked with the Bank of France. The French control had managed to purchase enough foreign exchange during the morning to meet French railway requirements. However, this evening after the market had turned it was obliged to yield almost a corresponding amount.

BULLITT.

EA:LWW

14-00000

Tell Harris I am ^{very} pleased
with this memo. *H.M.G.* 10

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE June 17, 1938

TO Secretary Morgenthau
FROM M. A. Harris

The Federal Reserve Bank receives daily from nine leading dealers reports showing their long and short position. From these reports it appears that their holdings of notes maturing within one year amounted to \$58 million on June 4, \$118 million on June 6, \$160 million on June 7, \$116 million on June 8, and \$38 million on June 9, the day after the books were closed. Also, these reports show that dealers increased their borrowings to carry their portfolios from \$139 million on June 4 to \$206 million on June 6 to \$267 million on June 7 and to \$368 million on June 8, from which point the figure held steady until June 15 when a substantial drop to \$192 million took place. These figures show heavy participation by dealers but only on a temporary basis.

As the applications for new bonds and new notes were being used in preparation for the delivery of the new bonds on June 15 it was impossible for me to look over and ascertain the amount of "rights" tendered for the bonds and notes by insurance companies, dealers, etc. However, these figures will be available in a short time.

Below is given the change in the various loans and investments of New York banks for the weeks ending June 8th and June 15th. It can be seen that the large increase in loans to brokers and dealers during the week of June 8th was for the purpose of carrying the "rights" until the new bonds were issued as the drop during the week of the 15th about

offset the previous increase. Holdings of governments increased both weeks but may be expected to decline next week due to the payment of the tax-dated bills. Also given is the holding of direct government securities by banks on June 1 and June 8 and the changes for this period.

(In millions of dollars)

	<u>Week ended June 8th</u>	<u>Week ended June 15th</u>
Loans to brokers and dealers	+ 342	- 192
Loans to banks	+ 54	- 43
Various other loans	- 16	0
Loans - Total	<u>+ 380</u>	<u>- 235</u>
Holdings of U. S. Govt. securities	+ 115	+ 64
" " Guaranteed securities	+ 31	+ 9
" " other securities	+ 39	+ 8
Total loans & investments	<u>+ 465</u>	<u>- 154</u>

Changes in direct U. S. Government security holdings of Member Banks in 101 reporting cities for week ended June 8, 1938:

(In millions of dollars)

<u>By cities:</u>	<u>June 1</u>	<u>June 8</u>	<u>Net Changes</u>
New York City	2,926	3,041	+ 115
Chicago	870	872	+ 2
All other cities	<u>4,048</u>	<u>3,978</u>	<u>- 70</u>
	7,844	7,891	+ 47

By districts:

Boston	396	387	- 9
New York	3,165	3,268	+ 103
Philadelphia	309	310	+ 1
Cleveland	733	716	- 17
Richmond	291	269	- 22
Atlanta	153	149	- 4
Chicago	1,365	1,360	- 5
St. Louis	174	189	+ 15
Minneapolis	153	152	- 1
Kansas City	223	221	- 2
Dallas	169	169	-
San Francisco	<u>713</u>	<u>701</u>	<u>- 12</u>
Total	7,844	7,891	+ 47

Dr. Burgess and Mr. Matteson were pleased with the job that dealers did in "underwriting" the new issue but are somewhat alarmed at the amount of new bonds in the hands of banks that have purchased them to re-sell. They stated that there has been very little real investment demand for the new bonds since the books closed and the rumor persisting the latter part of last week and the first part of this week as to the devaluation of the dollar kept investors on the sidelines. However, in the last few days some buying demand has been evident for the new 2 3/4s.

While I was in New York, I talked to Mr. C. J. Devine of C. J. Devine & Company, Mr. Levy of Salomon Brothers & Hutzler, Mr. Lanston of The First Boston Corporation, Mr. Morris of the Bankers Trust Company, Mr. Garner of the Guaranty Trust Company, and Mr. Mills and Mr. Repp of The Discount Corporation. Their stories as to what has taken place in the market since the terms of the refunding issues were announced are much the same and are somewhat as follows:

The story of the market that has resulted since the announcement of the terms of the refunding lies largely in the activity during the first few hours of trading on Monday, June 6. The first impression of the "street" was that the new 2 3/4s would quickly go to a premium of about 2 1/2 points and due to this belief lively bidding followed for the "rights", quickly running the premium in the first hour up to 2 1/4 points. Then dealers began to discover that they were not finding investors for the new bonds at these high levels and found themselves in a long position-- that is, loaded up with bonds. It appears that several dealers anticipated this situation and shortened their position in order to take advantage of a drop in the market. The new 2 3/4s bonds turned downward after the early

run-up and at the close on Monday were quoted 101.29/32 bid, and on Tuesday they declined 10/32nds further to 101.19/32 bid. On Wednesday the price rallied and since that time the new bonds have remained in the neighborhood of 101.24/32 bid to 102 bid. These dealers that bought heavily at top prices found themselves with bonds that stood them at a loss at those reduced levels but since Wednesday they have been able to reduce their holdings of the new bonds to a fairly low level.

Selling of 'rights' came largely from two sources. First, from speculators such as large corporations and trading banks and, second, from banks who were not interested in the long bond because of its length or in the short note because of its small return. These banks were largely outside of New York and their selling was largely on a switch basis with most banks taking intermediate bonds on the buy side of the transaction. Thus the reason for the unusually large proportion of the rights turned in in the New York district (about 75% of the total of both issues). It appears that trading banks, those banks that expect to sell their bonds at a profit later, were the large buyers of the new bonds from dealers. They stated that, due to the large proportion of bonds in the hands of potential sellers, the secondary demand by real investors has been very poor and that at the present time little demand is expected. However, they all look for a higher market in the future provided no disturbing event occurs. They all feel, though, that if the market is upset these trading banks will dump their holdings of the new 2 3/4s on the market. Estimates as to the amount in the hands of trading banks range from about \$160 million to \$300 million. Some dealers point out that the slow secondary market on the new bonds is acting as a damper on the upward rise of the market and is a good thing for

the market and further they feel that the new 2 3/4s will find good homes in the next month or two if the market continues firm. Insurance companies so far have shown little inclination to buy as it is their belief that the market on the new issue is yet too uncertain.

In summary, it might be said that those dealers and banks that made money are very pleased with the refunding while those who paid top prices for the rights and now find the new bonds selling at a price under the levels they paid for the "rights" are somewhat bitter and claim that the offering was not what investors wanted and as a result there is no secondary demand. As a matter of fact, there has been a very poor secondary market but this seems to be due to the high level that dealers placed on the new issue and investors believe that the new issue has not as yet reached a price which is attractive. Those that turned the "rights" in for the notes are very pleased and a number of dealers are sorry now that they did not turn in a larger amount for the notes.

The Guaranty Trust Company did not own any of the maturing notes but they did take about 10 million of the bonds for their trading account and still have a large portion of these. Bankers Trust Company turned in 40 million "rights" for 35 million bonds and 5 million notes for its bank account and 10 million "rights" for 8 million bonds and 2 million notes for the trading account. The trading account has disposed of all of the notes and practically all of the bonds. Discount Corporation took only 1 million of the new bonds, turning in practically all of their holdings of the "rights" for new notes. C. J. Devine turned in 50-odd million for the bonds but have disposed of practically all of them. Salomon Brothers & Hutzler took 60-odd million bonds but still have between 10 and 20 million

of them left. First of Boston Corporation has disposed of more than half of the bonds that they took.

The "Rights" Market

To me the most alarming situation in the market is the increasing speculation taking place in the "rights" market. In my talks with dealers, they freely drew my attention to what was taking place and pointed out the dangers of this speculation. The speculation, or buying up of notes maturing in the next three years, is coming largely from large institutions and from large trading banks. Many banks at the present time are selling out other governments and buying the short notes that already are selling on a "no yield" basis, as well as investing short term funds in these short notes, with the thought that if they hold them to maturity they will realize a point or more profit at the time of the refunding and are quite content to take this chance. They feel that they will make more this way than by the purchase of short term issues showing a positive yield because of the low rate that these issues provide. This means that more and more the "rights" are getting into the hands of the speculators and out of the hands of the real investors and at the time of refunding will result in undesired activity with a poor secondary market following. It means that real investors have to go into the secondary market and pay sizeable premiums to obtain the new issues. Mr. Devins told me that the American Telephone & Telegraph in the recent refunding sold \$33 million of the "rights" and that Standard Brands Corporation sold in the neighborhood of \$20 million and are using the proceeds of the sale to purchase notes maturing in the next two years. Dealers stated that they have had, in the past week, a strong demand for "rights" and that this demand is constantly shoving the "rights" premium higher, thus pulling down the yield level throughout the note market.

This situation is being further aggravated by the large maturities of short term issues in the Federal Reserve System account which have to be replaced, under the present policy, by the purchase of other short term securities.

An example of how this speculation has been increasing within the past year is shown by the following:

Last June the notes maturing one year hence were selling on a 0.50% yield basis but this June the notes maturing a year hence are selling at a 3/4-point premium above a "no yield" basis and notes maturing as far away as two years are selling on a "no yield" basis. The solution that most of them suggest to this problem is some kind of announcement stating that in the future the holders of the maturing rights may not expect 100% allotment.

I also would like to point out that this speculation in rights is compelling insurance companies to buy new issues in the market at fancy premiums because they are not permitted, under the banking laws, to buy any security that is not showing a positive yield. Therefore, unless they already have the rights, they cannot purchase them for the purpose of obtaining the new issue due to this "rights" premium. This is one reason why the percentage allotment figures on new issues of insurance companies is proportionately so small.

Dealers are not guilty of this early buying up of rights as they cannot afford to carry them for a long period of time. They usually acquire them after the terms of refunding are known. Their profit comes largely in the arbitrage operation -- that is, selling the new issue against the purchase of the "rights" and of course have to borrow for the period between the purchase of the "rights" and the delivery of the new issue.

Below is listed Treasury notes maturing within three years as of June 17, 1937 and June 17, 1938 and the yield that they provided:

<u>June 17, 1937</u>	<u>Yield</u>	<u>June 17, 1938</u>	<u>Yield</u>
3 1/4s 9/15/37 (3 mos.)	0.0	1 1/4s 12/15/38 (6 mos.)	- 1 pt. less
2 5/8s 2/1/38 (7 1/2 mos.)	0.41	1 1/2s 3/15/39 (9 mos.)	- 25/32 "
3s 3/15/38 (9 mos.)	0.38	2 1/8s 6/15/39 (1 yr.)	- 24/32 "
2 7/8s 6/15/38 (1 yr.)	0.50	1 3/8s 9/15/39 (1 1/4 yrs.)	- 20/32 "
2 1/2s 9/15/38 (1 1/4 yrs.)	0.63	1 3/8s 12/15/39 (1 1/2 yrs.)	- 11/32 "
1 1/2s 3/15/39 (1 3/4 yrs.)	1.12	1 5/8s 3/15/40 (1 3/4 yrs.)	- 6/32 "
2 1/8s 6/15/39 (2 yrs.)	1.18	1 1/2s 6/15/40 (2 yrs.)	0.0
1 3/8s 9/15/39 (2 1/4 yrs.)	1.24	1 1/2s 12/15/40 (2 1/2 yrs.)	0.19
1 3/8s 12/15/39 (2 1/2 yrs.)	1.27	1 1/2s 3/15/41 (2 3/4 yrs.)	0.31
1 5/8s 3/15/40 (2 3/4 yrs.)	1.39	1 3/8s 6/15/41 (3 yrs.)	0.43
1 1/2s 6/15/40 (3 yrs.)	1.41		

Note: I am enclosing several charts showing the member bank investments in government securities, as well as investments of insurance companies. As material on investments of insurance companies is very limited, the picture shown by these charts is not a very comprehensive one.

Jim Jr

18

Read this if you
have time. It is
what Eccles
read to us
on Friday and
represents
Board position

CU

May June 17, 1938

Classification of Loans in Bank Examinations:

1. Objectives of the Revised Procedure.

- a. To eliminate any pressure which bank examination procedure may exert towards the liquidation of sound loans.
- b. To eliminate examination procedure as a reason or excuse for a bank refraining from making sound loans.
- c. To eliminate the "slow" classification which has been a source of irritation and a cause for misunderstanding.
- d. To improve and simplify the schedules of classified loans.

Proposed Plan Regarding Classification of Loans in Reports of Examination, as Submitted by Mr. Upham:

1. Abandonment of the present caption of classified loans; namely, slow, doubtful, loss.
2. Continuation of 3 columns of classified loans, such columns to be designated by the Roman numerals II, III, IV, with the definitions of the classifications to be printed in the examination reports. In effect, in accordance with the definition submitted, this would mean 3 columns of criticized assets which might be briefly described as "Somewhat doubtful", "More doubtful", "Loss".

Board's Proposal:

1. Retention of the classifications "doubtful" and "loss".
2. Elimination of the "slow" classification.
3. Inclusion of a schedule on a separate page entitled "Loans listed for special comment", in which schedule should be listed with appropriate comment such loans as the examiner feels should be set out for the information of the directors and proper officers of the bank. Such loans should not be totaled and should not be included in any recapitulation of classified or criticized assets.

Reasons for Board's Position:

1. Inasmuch as all are apparently agreed that the "slow" classification should be eliminated, it is not considered necessary to cite reasons at this time for such elimination.
2. From the supervisory point of view, it is believed that it would be more effective to have the definitely criticized loans, i.e., "doubtful" and "estimated loss", shown on one page, and loans which are not so classified but listed for comment shown separately.
3. A logical basis for classification of loans in reports of examination is from the point of view of whether payment will be collected in full or whether some loss will be sustained. This seems to be adequately covered by classifications of "doubtful" and "estimated loss".

Objections to the Above Proposal:

1. It is inadvisable to print in the reports of examination detailed definitions of the classifications as such matters should be covered by instructions to examiners which should be changed from time to time, as they have in the past, in accordance with economic conditions.
2. The terms "doubtful" and "Loss" are readily understandable and some part of the effectiveness of such classifications may be lost through designation as Class III or Class IV.
3. The necessity of advisability of dividing the "doubtful" classification into two degrees of doubtfulness is not clear or, if such division is necessary or advisable, why two subdivisions are sufficient and not 3 or 4, such as "potentially doubtful", "tinged with doubt", "doubtful", "very doubtful". It has been contended that loans classified as "slow" are not criticized loans. The Group II loans as defined are definitely criticizeable loans. It must be expected, however, that regardless of the instructions, for a considerable time, at least, many loans which were formerly classified as "slow" will be classified as Group II. To the extent that such loans are doubtful, they should be so classified; to the extent, however, that loans so classified are not doubtful, such classification will defeat one of the purposes of the revision.

Securities:

1. Objectives of revised procedure.
 - a. Encouragement of sound investment policies with emphasis upon regularity of income and safety of principal and toward the discouragement of speculative policies based on trading profits.
 - b. To get away from fluctuating market quotations to as great an extent as possible, regardless of whether security prices be high or low, and to place the emphasis upon quality of individual issues and provision of adequate reserves.
 - c. To minimize, except where necessary, the effect of bank examination and supervisory policies as an influence for the liquidation of securities at a time when such liquidation accentuates deflationary tendencies.

2. Proposed plan for treatment of securities in reports of examination, as submitted by Mr. Upham.
 - a. Continued listing and pricing of all securities.
 - b. Classification of depreciation in Group III and Group IV securities (defaulted issues and stocks) as estimated loss.
 - c. Deduction of net depreciation in Group II securities (this includes general market obligations not in default but which are rated below the 4 highest ratings as used by the recognized rating agencies) and in the fourth grade of general market obligations (Baa, B1⁺, BBB, etc.) in computing net sound capital of the bank.
 - d. Discontinuance of showing appreciation or depreciation in Group I securities (except the fourth grade of general market obligations) and disregard of such appreciation or depreciation in computing the net sound capital of the bank.

3. Objections to above proposal.

- a. Continued emphasis of market quotations.
- b. The disregard of appreciation in Group I securities in computing net sound capital while deducting depreciation in other securities will tend to force sales in order to realize profits to provide for charge-offs of depreciation in lower grade securities.
- c. The dropping in effect of the fourth grade of general market obligations (Baa, B1 $\frac{1}{2}$, BBB, etc.) as rated by the rating agencies) from Group I to Group II. This is a restrictive measure which is proper but should be made at a time when security prices are at a higher level, i.e., a year or two ago, or after recovery has developed.

4. The Board's proposal.

- a. Classification of depreciation in defaulted bonds and stocks as estimated loss, other securities in general being allowed at amortized book value.
- b. Insistence upon provision of adequate reserves and upon the requirement that until adequate reserves against the investment account have been provided, all net profits from the sale of securities be impounded, thus preventing the treatment of such profits as regular, rather than non-recurring, income available for regular operating expenses.
- c. Insistence upon the conservation of earnings so long as the bank is faced with asset problems, whether in securities or otherwise.
- d. Elimination of the schedule listing all securities, substituting therefor a schedule of stocks and defaulted bonds and a schedule of any other securities listed as exceptions for appropriate comment.

(A complete list of all securities, however, should be attached to the report of examination sent to the supervisory authorities.)

5. Reasons for the Board's proposal.

- a. Reports of examination are not detailed inventories of all assets but to a great extent are based upon exceptions. It is inconsistent with the general scheme, therefore, to incorporate in a report of examination a detailed list of all securities, including those not subject to any adverse comment or criticism. The inclusion of such a list, especially if the bonds are priced, tends to over-emphasize the importance of fluctuating quotations.
- b. It is desirable to minimize the emphasis upon market quotations.
 1. Experience has shown that market quotations do not reflect actual prices which may be received or paid with respect to sales and purchases on a substantial scale.
 2. The sale of comparatively few bonds may result in a marked, though temporary, decline in market quotations of such issue. Quotations so established, however, even on forced sales and depressed markets, control the appraised value of all bonds of that issue held by the banks examined as of that date.
 3. It is illogical to use as a test in determining the solvency or soundness of a bank market quotations perhaps representing forced sales on distressed markets when the bank is in no need of selling its bonds, or if called upon to dispose of the bonds, has no assurance that even an

approximation of the market quotations could be obtained.

4. Emphasis on market quotations tends to stimulate trading and speculative activity.
5. Emphasis on market quotations tends to inspire sales on a declining market which in turn accelerates the extent of the decline, thus starting a vicious circle.

Net Sound Capital:

The suggested program as submitted by Mr. Upham provides for a schedule in reports of examination showing net sound capital, which is computed by deducting from total capital account all estimated losses, doubtful assets, and a certain amount of depreciation in securities. (The present reports of examination of both the Comptroller of the Currency and the F.D.I.C. include such a schedule in which all depreciation in securities is deducted.)

Board's position. The Board favors the elimination of such a schedule for the following reasons:

1. Any good which may be accomplished by not classifying depreciation in securities as estimated loss or doubtful is offset to a considerable extent, at least, by showing it as a deduction in the computation of net sound capital.
2. It is inconsistent for the computation to include as a deduction depreciation which is not shown in the recapitulation of assets, the soundness of which is questioned.
3. It focuses attention on depreciation based upon fluctuating market quotations.
4. In accordance with the purpose of minimizing depreciation in higher grade securities, the program provides that such depreciation be not deducted in computing net sound capital. It cannot be said, however, that depreciation in any securities constitutes sound capital and it is felt that such implication should be avoided.
5. The concept of "net sound capital" may have different meanings

in different circumstances. For example, an excessive investment in banking house or large holdings of other real estate, even though not classified as estimated loss or doubtful, frequently afford little protection to depositors or the F.D.I.C. and, it is suggested, do not warrant the designation of "sound capital" even by implication.

Federal Surplus Commodities Corporation
 Summary of Commodities Procured -
 July 1, 1937 to June 15, 1938

Commodity	Unit	July 1, 1937	April 28,* 1938	May 5, 1938	May 12, 1938	May 19, 1938	May 26, 1938	June 2, 1938	June 9, 1938	Total
		to April 29,* 1938	to May 4, 1938	to May 11, 1938	to May 18, 1938	to May 25, 1938	to June 1, 1938	to June 8, 1938	to June 15, 1938	to July 1, 1937 to June 15, 1938
Beans (Dried)	Pounds	14,449,700	144,000	180,000	-	-	-	-	-	14,773,700 (1)
Beans (Fresh)	Bushels	5,603,648	46,200	7,800	2,400	-	-	-	-	5,660,048 (2)
Beans (Dried)	Pounds	2,990,000	-	-	-	-	-	-	-	2,990,000 (3)
Beans (Dried)	Pounds	52,990,000	450,000	400,000	100,000	2,090,000	60,000	-	670,000	56,760,000 (4)
Beans (Snap)	Bushels	-	-	-	-	9,000	6,480	-	-	15,480 (5)
Beans	Pounds	8,320,208	918,040	753,828	513,712	663,544	1,451,152	1,734,052	886,972	15,281,508 (6)
Beans	Pounds	10,167,386	7,020,000	5,808,000	7,272,000	1,294,000	1,968,000	96,000	-	33,625,386 (7)
Beans	Crates	166,540	6,570	20,075	2,555	-	-	-	-	195,740 (8)
Beans fabric	Yards	629,536	26,279	-	92,000	400	-	237,678	-	985,893 (9)
Beans seed oil	Pounds	9,780,000	-	-	-	-	-	-	-	9,780,000 (10)
Beans (Shell)	Cases	270,164	-	-	-	-	-	-	-	270,164 (11)
Beans	Barrels	-	-	-	7,000	3,000	124,800	-	914,900	1,048,700 (12)
Beans fruit	Boxes	155,499	48,000	69,000	40,000	37,500	42,042	18,500	10,164	428,705 (13)
Beans fruit juice	Cases	-	-	40,500	4,660	-	-	-	-	45,160 (14)
Beans	Tons	7,915	-	-	-	-	-	-	-	7,915 (15)
Beans (Dry skin)	Pounds	8,642,250	-	-	-	-	7,940,000	-	-	16,582,250 (16)
Beans (Fluid)	Quarts	8,082,385	459,090	472,325	482,564	494,587	477,520	497,184	509,586	11,475,261 (17)
Beans	Pounds	3,000,000	-	-	-	-	-	-	-	3,000,000 (18)
Beans	Boxes	1,563,626	87,514	78,972	49,934	31,280	13,860	10,164	10,626	1,845,976 (19)
Beans bags	Bags	-	-	-	-	-	8,400,000	-	-	8,400,000 (20)
Beans (Dried)	Pounds	2,534,000	-	-	-	-	-	-	-	2,534,000 (21)
Beans (Fresh)	Boxes	317,982	-	-	-	-	-	-	-	317,982 (22)
Beans (Canned)	Cases	927,026	-	-	-	-	-	-	-	927,026 (23)
Beans (Dried)	Pounds	6,000,000	-	-	-	-	-	-	-	6,000,000 (24)
Beans (Sweet)	Bushels	440,304	-	-	-	-	-	-	-	440,304 (25)
Beans (White)	Bushels	4,149,756	117,325	63,365	7,337	-	-	-	2,484	4,340,267 (26)
Beans to starch & flour	Pounds	2,561,720	280,280	-	-	-	-	-	-	2,842,000 (27)
Beans (Dried)	Pounds	45,105,650	-	1,400,000	-	-	-	960,000	-	47,465,650 (28)
Beans (Milled)	Pounds	70,550,000	3,360,000	2,080,000	560,000	-	-	-	-	76,550,000 (29)
Beans	Pounds	-	-	-	-	1,000,000	-	1,600,000	-	2,600,000 (30)
Beans (Canned)	Cases	50,000	-	-	-	-	-	-	-	50,000 (31)
Beans (Fresh)	Bushels	-	-	-	-	-	-	-	66,650	66,650 (32)

June 17, 1938.

Agriculture Department, Division of Research and Statistics.

Notes shown are those reported by Federal Surplus Commodities Corporation. Annually, however, no purchases have been counted twice because of this discrepancy.

TREASURY DEPARTMENT
Office of the Secretary
Secret Service Division

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MEMORANDUM
June 17, 1938

To: Mrs. Klotz

From: Mr. Murphy

We attach letter dated June 15, 1938, from Supervising Agent Harry L. Barker, Boston, Massachusetts, with its enclosure, concerning arrangements made for the Secretary and Mrs. Morgenthau upon their arrival at Boston this afternoon.



TREASURY DEPARTMENT

UNITED STATES SECRET SERVICE

BOSTON, MASS.

OFFICE OF SUPERVISING AGENT
DISTRICT No. 1STATES OF MAINE, VERMONT,
NEW HAMPSHIRE, MASSACHUSETTS,
CONNECTICUT, AND RHODE ISLAND

June 15, 1938.



Mr. Frank J. Wilson, Chief
U. S. Secret Service,
Washington, D. C.

Sir:

Confirming instructions received by telephone this date Agent Bachelder called at the Hotel Statler, Boston, and conferred with Mr. D. B. Stanbro, Manager, relative to reservations made by Mrs. Roosevelt for Secretary and Mrs. Morgenthau starting Friday, June 17th. There is enclosed herewith a letter from Mr. Stanbro in confirmation of these arrangements.

Agent Rice will meet Secretary and Mrs. Morgenthau upon arrival at the Hotel Statler Friday afternoon, as per instructions, and will remain with the party while in this District.

Respectfully,

Supervising Agent.

Encl.
FEB/G



HOTEL STATLER, BOSTON
PRIVATE OFFICE

D. B. STANBRO
MANAGER

June 15, 1938

Frank J. Wilson, Chief of
United States Secret Service
Washington, D. C.

Dear Mr. Wilson:

We are pleased to confirm reservations made
for Mrs. F. D. Roosevelt for rooms 1284-88
for arrival on June 17th and also the
reservation for Secretary and Mrs. Morgenthau
for room 1298. This room number is tentative,
inasmuch as the room is now occupied, but it
is expected to be vacated by that time.

Very truly yours,

D. B. Stanbro
Manager

kc

FEDERAL RESERVE BANK
OF NEW YORK

June 18, 1938.

Dear Mr. Secretary:

We are now in the midst of the expected lull in new security offerings. The offerings to the stockholders of Commonwealth Edison Company and Philip Morris and Company, both of which run until next week, are still quoted at premiums. The only new issues this week were a small industrial bond issue placed privately with a life insurance company and a small offering of convertible preferred stock to stockholders of Washington Gas Light Company. Municipal bond awards totaled \$24,600,000, of which \$11,000,000 was awarded by Philadelphia to the Pennsylvania School Employees Retirement Board.

Although several large issues are expected in July, including \$85,000,000 in notes and debentures for the Standard Oil Company of New Jersey, no large corporate flotations are scheduled for the rest of this month.

Corporate financing during the first six months of 1938 has totaled \$637,000,000, a sharp decrease from the \$1,727,000,000 in the first half of 1937 and the \$2,546,000,000 in the first half of 1936, but the past quarter is well ahead of the two preceding, and the month of June is the best month since a year ago. Of the half year's financing, about \$292,000,000 was for new capital, nearly half for the United States Steel Corporation alone. The figures are shown in the accompanying chart.

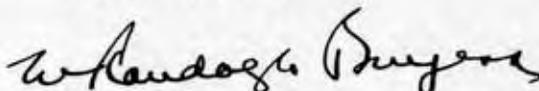
Municipal issues for new capital of \$380,000,000 in the first half of this year are about the same as in recent years. This figure is

Hon. Henry Morgenthau, Jr. 6/18/38.

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very probably less than the maturities and redemptions of municipal obligations, so that the gradual retirement of state and local government obligations is continuing.

Very truly yours,

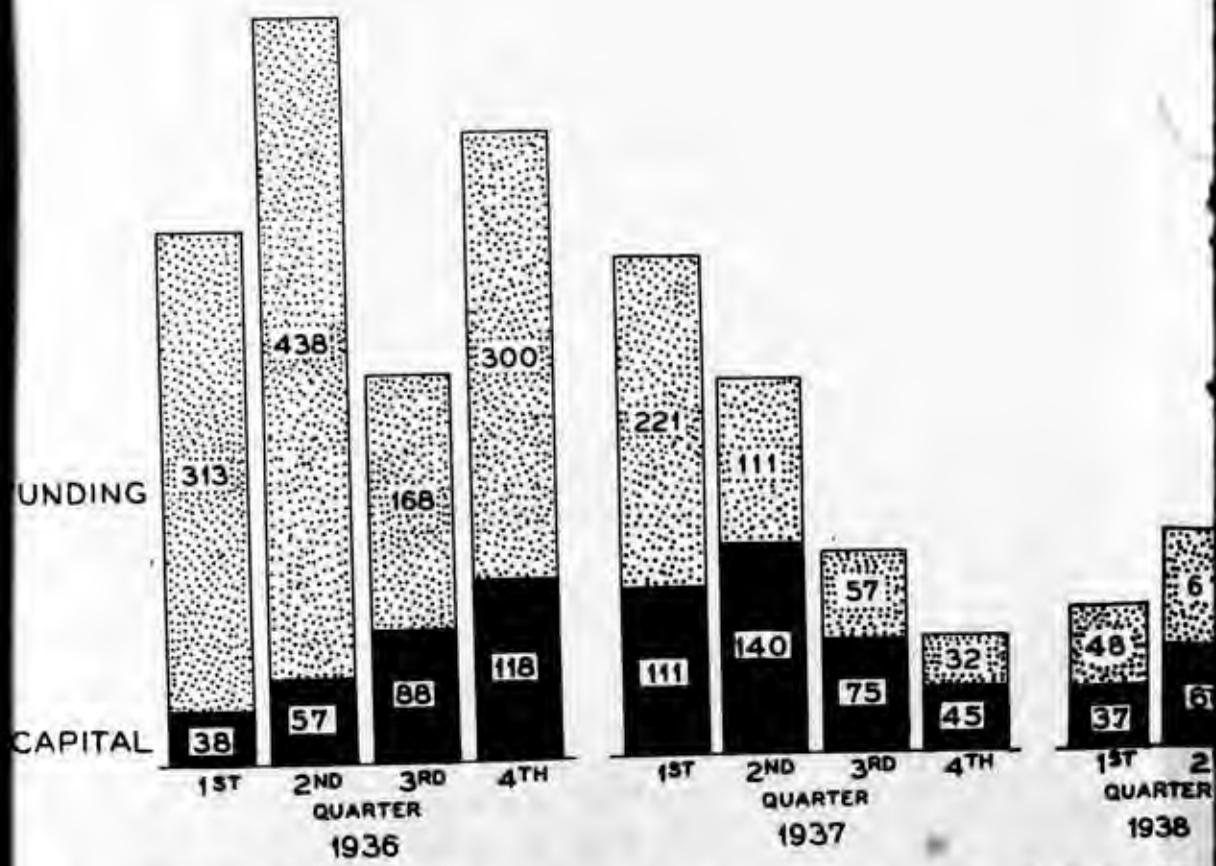


W. Randolph Burgess
Vice President

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

WRB.H

MARCH 9, 1938
3273



Average Monthly Volume of Domestic Corporate Security Issues for New Capital and for Refunding (In millions of dollars)

A Brave Speech.

Henry Morgenthau, Secretary of the Treasury, made a fine commencement address at Philadelphia's Temple University. What most impressed us was Mr. Morgenthau's courage when he touched on its topic of civil liberties.

He said that no American can afford to remain neutral in the struggle to preserve those liberties—that he who abstains from the struggle, believing his own rights not in danger, is unconsciously helping the enemy. And he added:—

"Failure to defend those liberties in one city, one county or State strikes at the liberties of all of us. When we tolerate the curtailment of constitutional rights in any place by any individual or group of individuals, no matter how close to the seat of government, we make easier an attack upon our own constitutional rights."

Does it seem strange that a public official should be praised for courage in voicing sentiments so obvious and so true? We think this speech did require courage because Mr. Morgenthau knew that his remarks would be interpreted as aimed at a man who is curtailing constitutional rights in a place very near to Philadelphia—Mayor Frank Hague of Jersey City. Indeed, Mr. Morgenthau, asked later whether he had spoken with Mayor Hague in mind, said:—"If the shoe fits, let him wear it."

Mayor Hague is "close to the seat of government." He is a vice chairman of the Democratic National Committee. And others high in the administration of which Mr. Morgenthau is a member seem to be going on the theory that discrete silence concerning Mayor Hague and his dictatorial tactics is the better part of valor.

EC

GRAY

London

Dated June 18, 1938

Rec'd 9:05 a.m.

Secretary of State,
Washington.

532, June 18, 1 p.m.

FOR TREASURY FROM BUTTERWORTH.

The buying pressure continues to lessen. Gold fixing only totaled 144 bars and subsequent dealings were proportionately small. Both the dollar and franc exchanges were steady and fairly inactive.

JOHNSON

DDM:HPD

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Berlin, Germany

DATE: June 18, 1938, 1 p.m.

NO.: 313

FOR TREASURY. FROM HEATH.

The status of German gold and foreign exchange reserves remains concealed; reserves taken over from Austria have not yet been shown as gold or foreign exchange in the monthly statements of the Reichsbank. However, there seems to be no doubt that there has been an increase in the exchange stringency as a result of the drop in demand for exports from Germany. Despite the promise in the recent speech of Minister of Economics Funk, there does not seem to be any prospect of a relaxation of exchange restrictions. I was informed yesterday by Bergemann, principal assistant to Brinkmann in the Administration of the Economics Ministry, that the relaxation of exchange restrictions which Funk mentioned had reference only to a plan for giving certain exporters a part of the foreign exchange resulting from any increase in their own shipments of goods. In view of industrial demand, he said, some stimulus was necessary for exports. However, he thought that the new scheme would probably apply only to certain large export concerns and to certain export lines.

During the next few days decision should be reached as to whether the British and Germans will be able to come to

- 2 -

to terms regarding the treatment of Austrian and German sterling bonds; this point is the only thing holding up conclusion of a new trade and payments agreement between Germany and Great Britain. An authoritative source has told me that the British did not accept the offer of the Germans to reimburse the British for any loss that might result from guarantee by the British Government of the Austrian guaranteed loans in return for British consent to interest reduction on the Dawes loan to five percent, and reduction to four percent on the Young loan. Offer was made by Germany to continue making available in foreign exchange the whole amount of the contractual interest on these loans, but the difference would be applied to sinking fund. It is understood that Great Britain held the view that Germany should provide payments for bonds of other tranches of the loans held in Great Britain, and that Germany had proposed excessive reductions in interest on the Dawes and Young loans. Early next week an answer to the British is expected from Germany.

During our conversation Bergemann referred to the recent circular order which prohibits Jewish emigrants whose property is worth more than five thousand marks from selling emigrants' blocked marks against foreign exchange. He said that this was only a temporary restriction, but admitted that

it

- 3 -

it was designed to keep Jewish people from escaping the provisions of the Jewish property registration decree through selling their property and placing the proceeds in blocked accounts to be sold to foreigners. Bergemann told me that in a month or two Jewish emigrants would again be allowed to sell their blocked marks against foreign exchange, once the registration had been finished.

Bergemann asserted that Germany did not intend permanently further to limit the already reduced amount of money it is permissible for Jewish emigrants to take with them because that would tend to defeat the German policy of encouraging the emigration of these people.

WILSON.

REC'D
JUN 11 1951
EA:LWW
FEDERAL BUREAU OF INVESTIGATION
U. S. DEPARTMENT OF JUSTICE

EG

GRAY

London

Dated June 19, 1938

Rec'd 8:13 a.m.

Secretary of State,
Washington.

534, June 19, noon.

FOR TREASURY FROM BUTTERWORTH.

The following excerpt from yesterday's STATIST
may be of interest:

"It is believed that one hundred and forty thousand kilos gross of Spanish silver coins have recently been deposited with an important firm of bullion refiners in Paris. They are being refined there and should produce between three million five hundred thousand and four million fine ounces of silver which will appear in the market in the form of fine bars bearing the stamp of a recognized firm of refiners and will have no apparent connection whatever with Spain. Legal complications of the most serious character might arise if in the event of the Spanish insurgents winning the civil war the new authorities were to dispute the title of those who had bought silver from the former government. Consequently it is unlikely that such silver will be bought without

-2- #534, June 19, noon, from London

without some intermediary of substance to whom recourse could be made in the event of trouble. The evident link will presumably be broken if the metal is refined and appears in the market in the form of bars of good delivery and bearing the stamp of a recognized refiner. Even so, ^{substantial} ~~subsidy~~ purchases by the London market are unlikely, as there is as yet no inclination to ship silver to the United States except on a covered basis. Such covered arbitrage is actually occurring when the spot price dips below the American parity and the American trade buying, which is largely overrated for such covered operations, has recently provided the bulk of the support which the market here has received."

JOHNSON

EDA:RGC

JR

GRAY

London

Dated June 20, 1938

Rec'd 1:30 p.m.

Secretary of State,
Washington.

538, June 20, 6 p.m.

FOR TREASURY FROM BUTTERWORTH.

The buying pressure for gold almost reached normal proportions today. Only 124 bars were dealt in at fixing and there was little demand after fixing.

Both the dollar and the franc were strong in terms of sterling.

JOHNSON

DDM:CSB

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: June 20, 1938, 5 p.m.

NO.: 986

FROM COCHRAN.

Paris exchange market quiet. Spot franc improved from 178.35 to .21 and control was endeavoring to pick up a little sterling around latter rate late this afternoon. Rentes better with Parliament having adjourned until at least latter half of October, with City of Paris billion franc loan subscribed and following President Lebrun's public plea for regular, productive and prolonged work by all Frenchmen.

This afternoon I was visited by Robert Lovett of Brown Brothers Harriman. He gave me his impressions from his annual trip to Europe.

First. Practically all of the Swiss bankers, he said, were nervous lest the dollar be devalued to fifty cents by the President in order to obtain a price pickup in the Fall.

Second. Mr. Lovett thought that our denials of dollar devaluation would be more effective if they were made more formally, in view of the remarkable susceptibility of Europe to rumors regarding our currency.

Third. European central and private bankers, he found, were generally convinced that there would not be much help for the American situation by further devaluing the dollar

by

- 2 -

by 16 percent. They felt that it would be followed by at least corresponding depreciation in currencies of all important countries.

Fourth. Much doubt was expressed as to the finality of the French franc rate being 179.

Fifth. Mr. Lovett believes that the United States should resort to some sort of control of German capital movements into our country such as those for propaganda purposes, as well as those out of our country to Germany such as immigrant remittances and securities repatriation in an effort to collect part of what is owed to us.

Sixth. He does not feel that superior judgment is at present being exercised by financiers of Great Britain. He shared my belief that such funds as are now being sent to Danubian countries by Great Britain in an effort to hold British trade are very likely to be applied to purchasing from the Germans instead.

Seventh. If real world recovery does not set in to take the place of armament activity, he will be concerned about the basic economic situation.

Eighth. This year he does not expect a general European war. He believes that without conflict the Sudetens will be absorbed by Germany.

BULLITT.

EA: LWW

June 20, 1938

The Secretary telephoned to the President at 2 o'clock today at Hyde Park and said to him, "The stock market went up five points today. I told my son, Henry, my rain drop story and his remark was 'Daddy, be sure it is not a bird in the tree'. Both the President and the Secretary laughed very heartily.

HM, Jr then said to the President, "The other thing is, I would like to take the liberty of suggesting if you could that you sign the Recovery and Relief Bill right away." The President replied, "I would if I had the bill, but I haven't got it." The Secretary then said, "Do you mind if I speak to Forster about it? I will find out where it is and, if necessary, I will send a Secret Service man up with it tonight."

He then said to the President, "The third thing I would like to ask is if you could would you save a little time for me either Thursday or Friday. I would appreciate it."

After he had talked to the President, HM, Jr telephoned to Forster and spoke to his assistant and was informed that they had the Relief Bill and would send it to the President immediately. HM, Jr asked him to send a telegram to the President letting him know that the bill was being sent to him. Forster's assistant informed Mr. Morgenthau that they had just gotten the bill back from Budget this morning.

THE WHITE HOUSE
WASHINGTON

60-418

My dear Mr. Secretary:

Under the provisions of H. J. Res. 679, funds for administrative accounting are included in the amount appropriated to the Treasury Department for administrative expenses.

In order that I may obtain a clear picture of the use of the funds provided by Title I of that Joint Resolution, particularly with reference to Federal activities, if possible, I wish you would indicate in your monthly reports, not only the amounts obligated directly by Federal departments (by bureaus), establishments and agencies, but also the amounts obligated in connection with projects sponsored by such departments, establishments and agencies.

Sincerely yours,

The Honorable,



The Secretary of the Treasury.

RE BANK EXAMINATIONS

June 20, 1938.
2:00 p.m.

Present: Mr. Gaston
Mr. Upham
Mr. Crowley
Mr. Diggs
Mr. Smyth

H.M.Jr: The reason I asked you gentlemen to come in here is because it looks to me that, as to brother Eccles, it's going to be kind of a public relations fight, and I thought if we hard-boiled bank examiners got together and kind of talked things together and planned to act together, why, maybe we could take him on and roll him up and tie him up in big ribbons. But I think we'll have to - as far as I know, I think we're all in the same boat, and if we all decide on what we're going to do and kind of talk together, why - I mean - then I have this 3 o'clock press conference and I want to get you fellows' advice and see what you had to say.

Crowley: Well, here, Mr. Secretary, is what Marriner's done. He's left the impression publicly that we're all conservative, reactionary fellows not interested in credit expansion and that he's the only fellow that has a program to cure this thing at all.

Now, as a matter of fact - I think Marshall and Cy would bear me out on this, that Saturday - Friday afternoon we spent four hours and really you couldn't get head or tail of what Marriner was talking about. He talked in circles on the thing. We had presented them a majority report here, and the Federal Reserve just haven't given it the thought that the Comptroller's office and the Federal Deposit have given it.

Now he writes this letter to Vandenberg, which is very embarrassing.

H.M.Jr: What's the date?

Upham: Tuesday.

Crowley: It went up there Tuesday afternoon.

H.M.Jr: Wasn't that the day we had the lunch?

Upham: That's right.

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- Crowley: And in that letter to Vandenberg he practically put the responsibility for the depression on bank examinations.
- H.M.Jr: Yes.
- Crowley: Now, I've prepared a little bit of a memorandum that I thought set forth our views, and don't know whether it's worth a damn or not. Cy, would you mind, or - it may be too much for you to read, Mr. Secretary.
- H.M.Jr: No. Do you mind - have you (Diggs) seen it?
- Diggs: No, I have not.
- H.M.Jr: Well, read it out loud, Cy.
- Upham: "The Comptroller of the Currency and the Federal Deposit Insurance Corporation, together with the Executive Committee of the State Bank Supervisors, agreed more than a month ago on a program of uniform standards in connection with the appraisal and classification of loans and securities in bank examinations. These standards have been adopted with a view to promoting a wholesome recovery and providing permanent high standards in bank examinations and bank supervision.
- "Inasmuch as all of the nation's banks are examined by one or the other of the above authorities, a high degree of uniformity will exist in future examinations of banks of all classes. A better coordination of bank supervision is therefore assured.
- "An important aspect of our program is the proposed abandonment of the term 'slow' in connection with the classification of loans in bank examinations. The confusing nature of the term 'slow' is evidenced by the requirement of the Federal agencies that a loan should not be so classified if its ultimate repayment is reasonably assured, even though the loan is slow in a literal sense.
- "The adoption of numerical captions for the classification units, with each classification uniformly and unequivocally defined, should do much to eliminate

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this confusion. The definitions preclude, and examiners will be emphatically instructed to exclude from classification, any loan the ultimate orderly repayment of which is reasonably assured.

"It has long been recognized by all that the lending of funds to sound and solvent borrowers, small and large, for reasonable periods, is a legitimate function of a bank, provided there is proper provision for the orderly payment of such loans. Bankers should be willing to assume reasonable risks, and it is far from anybody's intention that they should be criticized for so doing. To state the matter concisely, the principle that banks should make exclusively self-liquidating seasonal loans is being abandoned as a basis for classifying loans in bank examinations. In my opinion, all of these steps add up to more reliable and trustworthy bank examinations.

"The abandonment of quoted market prices and the adoption of cost as a basis for valuing securities of investment quality is another constructive aspect of the program. The use of market values has not proved satisfactory as a method of appraising high-grade securities. Also, cost valuation will result in an accurate and uniform appraisal procedure through periods both of depression and business upswing. Something over 80 percent of the securities presently held by banks are of investment quality, and appraisal at cost will give recognition to the principle that such securities are investments and are not intended to be continually turned over in the market.

"Securities not of high-grade investment quality, although not default, represent about 10 percent of bank holdings. The appraisal of net market depreciation in these issues as 'doubtful' is, to my mind, fair. The appraisal procedure with respect to these issues must give consideration to the risks involved in securities of this quality. Classification as 'doubtful,' however, does not as a general rule involve a required alteration in a bank's carrying value of issues so classified, or the charge-off of such classifications. Defaulted bonds and stocks are

-4-

approximately 5 percent of total securities, and everyone agrees that net depreciation in these securities is an estimated loss which should be charged off.

"Another important angle of the program relates to the treatment of profits from the sale of securities. Until losses in securities have been written off and adequate valuation reserves established, security profits are to be available only for the establishment of such reserves.

"This treatment of profits is a sound procedure which many well-run banks have been following for some time past. It will tend to, in some measure, discourage speculative in-and-out trading in the bond market. Too many bankers have been viewing their bond holdings not as investments but with a view to obtaining speculative profits from turnover, and this condition has contributed to the instability of the bond market. Furthermore, the so-called profits from security sales are in many instances not actual profits but merely write-ups in book value. This results from the fact that a banker, in disposing of securities at a profit, frequently reinvests at approximately the same price levels.

"In connection with the Comptroller's regulation, we understand that there is general agreement that member banks will in the future be permitted to purchase small and local issues provided they are of high credit quality and there are proper amortization provisions, and provided further that such issues are not held in excessive amounts. This Corporation has never criticized or objected to such purchases by insured state banks, not members of the Federal Reserve System.

"The Corporation does not view the above program as either lenient or liberal. We regard it as sound and realistic. Bank supervision loses its entire meaning if it is viewed as other than for the protection of depositors.

"Moreover, it would be unfortunate if the program were to be considered as a whitewashing process by either bankers or the depositing public. We feel

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confident it is not. More would be lost psychologically, however, if it were so considered, than could be gained by the program. The deserved confidence which the general public has in the banking system is a strong plus factor in the present situation, and nothing should be done through the press or otherwise which will impair this merited confidence.

"Bank examinations must continue to be accurate and reliable. Unless they are, bank examiners will not continue to hold the respect of sound bankers. Correction of adverse trends in poorly managed institutions will correspondingly become the more difficult."

H.M. Jr:

"Now, it's an excellent letter, but I'm going to be very frank, see? You (Diggs), you (Crowley), Eccles and I were given a job by the President. We're supposed to report to the President. Now, this burns me up just as much as it does you, but I'm going to keep my mouth shut, and I have a press conference - unless Herbert thinks I'm wrong - at 3 o'clock, and I'm asking everybody to say his piece. And my thought was if they went after me, all I was going to say was this: "We have been waiting now for about a month. We have been ready. We have been waiting a long time for the Federal Reserve Board to get down to business, and I am reliably informed that last Monday was the first time that the Board took a look at this thing." I may not even say that, but - "Now, the Board has been looking at this thing for a week. We've been looking at this thing continuously. And I think from the conversations that I have had with Mr. Crowley and Mr. Diggs - I think that we're all in agreement that our first interest is the interest of the depositor."

Crowley: That's right.

H.M. Jr: "That's our first interest." And if they push me a little hard, I thought I might say, "And we're not sitting up all through the night trying to find easy ways to lend depositors' money."

Crowley: That's right, that will help us.

H.M. Jr: See?

Crowley: That will help us. That's what we need.

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- H.M.Jr: See? That we're not sitting up all night trying to find - and furthermore, maybe I feel this so strongly because I have never been in the business of lending other people's money. "But our job is to make a report to the President and while we're studying this thing we don't write any letters."
- Crowley: Well, you understand I've just given
- H.M.Jr: No, I'm talking
- Crowley: I get you.
- H.M.Jr: "We don't write any letters." And I'm willing to say off the record that I think presidential appointees ought to work together and this idea of one of them going out and doing this thing as an individual - because I've checked up; I called up Ransom and asked, "Is it a Board action?" He says, "It is not." So Marriner's out on the end of a limb, and I thought that - to announce Thursday - hell, they'll either come on board and do it our way or I'll send the thing - do it the way you fellows want; now, I won't fool with this one bit more after midnight Wednesday night.
- Crowley: Fine.
- H.M.Jr: But in the meantime - I'm talking positive because I feel positive, and if you fellows don't agree with me I'll go around the room - in the meantime I think the lid should be on, see, and sit tight and not make it more difficult for the President. And I think it is very easy to twist this thing around - that we're not going to wash our dirty linen, and we've been sitting back here waiting.
- Crowley: That's right.
- H.M.Jr: But if we agree - I mean I'll give strict orders in the Treasury that there should be no leaks, if you fellows agree - that this fellow and that fellow shouldn't be slipping something - I mean somebody got a whole copy of these rules.
- Now, if you fellows think we should make a blast and answer him prior to giving the President a report

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Crowley: No, I think that's right.

Gaston: I think your attitude is just right. I think that the less you say - point it directly at Eccles in the present contingency, the better. I think it's simply best to say, "The President gave us a job. Now we've got to the point where we have something prepared. We understand that the Federal Reserve Board as a board began consideration of this only a few days ago, has not completed it. I'm not going to make any statement, I'm not going to argue for this proposition or that proposition. My business is to report to the President, and that I'm going to do."

H.M.Jr: But Herbert, you've got to let me say that the attitude - our attitude, our consideration, is the consideration of protection of the depositors.

Gaston: "We must have as our first consideration the protection of the interest of the depositor. That doesn't mean that we're"

H.M.Jr: All right. No.

Gaston: And so on - absolutely.

H.M.Jr: All right. I won't say anything on the

Gaston: As to the handling of this thing, I think it's perfectly clear. The report itself has to go to the President; when it comes back from the President and he approves it, then we put out a release in which we say that "the Secretary of the Treasury, after consultation with the Acting Comptroller of the Currency and with the Board of the Federal Deposit Insurance Corporation, announces that the following new regulations" - or rules, or whatever they are - "will be put into effect." Then we'll take them 1, 2, 3, 4, 5. Then we start in on Number One and explain the basis of the action, what it means; Number Two, the basis of the action, what it means, so on.

H.M.Jr: Well now, let's see whether this is agreeable to these people.

Crowley: Well, that's perfectly agreeable, because I think you put us in a strong position.

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- H.M.Jr: Pardon me?
- Crowley: You put us in a strong position by the statement that bank examination is for the protection of depositors. Now, Marriner is leaving the impression that bank examination is supposed to be mixed up with some other things.
- H.M.Jr: Well, who the hell's money is it?
- Crowley: That's right, and
- H.M.Jr: Who the hell's money is it? It's the depositors' money. And he sits up all night trying to find sloppy ways in order to loan this money. And it's other people's money.
- Crowley: That's right.
- H.M.Jr: It isn't his money. *nd as a matter of fact, what the hell's the Federal Reserve board got to do with this thing? You know, if they want to start - those fellows are just a bunch of mollusks. They got two things that they live off. One is the interest on the United States Government bonds and Two is the four million dollars that I pay them for service fees, and you take that away from them and I don't have to use them as fiscal agents. I can appoint the First National Bank of Podunk as my fiscal agent tomorrow.
- Crowley: That's right.
- H.M.Jr: And with it goes four million dollars. I can appoint tomorrow the First National Bank of Podunk as a fiscal agency of the Treasury. I can appoint the Federal Land Bank. I think I'm right, am I not?
- Upham: Yes.
- Gaston: And I don't think there is anything in law to prevent you from establishing a Sub-treasury office in New York.
- H.M.Jr: If this fellow just wants to push me, he's just going to go a little bit too far. But I've said and I want

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you fellows to know that I think the worst thing that could happen for this country is for the Federal Reserve and the Treasury to have an open break.

Crowley: That's right.

H.M.Jr: And I've sat here and worn out pants after pants listening to Marriner Eccles philosophize and just talk in circles. But I think doing it - and it's damn hard to do it - I think the country's better off. And I'm willing to wait until midnight Wednesday night. But after midnight Wednesday night I won't wait one minute.

Crowley: That's right.

H.M.Jr: See?

Crowley: Let me make

H.M.Jr: Now, if these fellows want a fight, they can have it. And this thing - what the hell is the Federal Reserve Board? Christ, their set-up - put them alongside the Farm Credit. I want a comparison of the business that Farm Credit does as compared to the business of the Federal Reserve. Why, it's just nothing. They don't do anything - any discounts. Do they do any discount business?

Upham: Almost none.

H.M.Jr: I mean, Herbert, I just want to set Farm Credit alongside of the Federal Reserve and - why, if we ever start to unmask the Federal Reserve, it's just a joke.

Gaston: The whole system. Uh-huh.

H.M.Jr: The whole system. It's the whole system. It's a lot of marble palaces scattered all over the country - empty shells - and they exist because the Secretary of the Treasury lets them exist.

Crowley: That's right.

H.M.Jr: But if they're going to push, not me, but the

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President, hard, I got all the cards, provided you - we stick together.

Crowley: Well, we won't move from our position. Now, Marriner stopped down at the hotel last night.

H.M.Jr: I haven't started this, and I'll be very quiet at my press conference. But I've had a lot of time to think this thing over, and I got all the cards.

Diggs: You've got more cards than maybe you realize, from the facts Mr. Crowley has and the facts we have dug up here on this lending business. Tell him those figures, Leo.

Crowley: For instance, your national banks and your state non-member banks have had an increase of from about 4½ to 3 percent in loans. The large metropolitan state member bank has had a decrease in loans of 1.2 percent. Marriner admitted to us Friday afternoon that he has no uniformity of examination in his twelve Federal Reserve banks, that he doesn't know what kind of examinations they are making.

H.M.Jr: Really?

Crowley: And then he's talking to us about the weaknesses in our program.

H.M.Jr: All right. Unless I'm kidding myself - and I don't think we are - we got all the cards. And just let this fellow - give him a little bit more rope. But if I attacked him today or any of you fellows attacked him, then the Federal Reserve Board would get together and defend him. But if I make it general - as I understand, the Federal is sore as hell.

Now, Jesse wrote me a very nice letter that he was with Marshall Diggs, so forth and so on. Then he sent me over a couple of suggestions that he made, see?

Upham: He called me over Saturday morning.

H.M.Jr: Well, he's got them all. Jesse wants me to - he always plays ball, tells me what he's doing. He's got two little suggestions: that 25 percent business, and he's got another one - he wants to call it "an

established business enterprise" instead of "commercial, mercantile, or manufacturing."

Now, what I'm ready to do is this - if I'm going too fast, just stop me.

Upham: Can I stop you there?

H.M.Jr: Just one second. I've saved tonight, see, and then I thought by tonight the three of us ought to be together. And then let's call in the Federal Reserve tomorrow afternoon and say, "Now, here's where you are. What are you going to do about it?"

Crowley: Well, we're all together except him getting his regulations, and I don't think you and I are apart on that much, Marshall.

H.M.Jr: No, if Jesse thinks - I think if we can get Jesse playing with us, there's another very strong factor, because he owns a lot of stock; if Jesse's with us, there's such a thing as being out of step with the world.

Gaston: Did you read this editorial in the Wall Street Journal this morning - "Those Who Are Insured." They're taking him apart.

H.M.Jr: They're taking his part?

Upham: Taking him apart.

Gaston: Taking him apart, telling him he's all wrong.

H.M.Jr: Fine. If I can, I want to get Jesse in our camp.

Diggs: Well, he's with us now.

H.M.Jr: Well, he's made two suggestions.

Diggs: One of those we think we can do. The other, we don't know - we're afraid that brings in hotels and apartments.

H.M.Jr: Now, Jesse's in town, and after you fellows leave, if you can put on the high pressure - I'm free from

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8:30 tonight on at my house, see?

Crowley: Well, could we get hold of Jesse and meet with you?

H.M.Jr: Yes. He's coming here at quarter to four, but he wants to see me on something else. But he won't be here but about 15 minutes.

Crowley: Why can't we have him go to your (Diggs) office?

Diggs: All right.

H.M.Jr: How's that?

Diggs: That'll be around 4:30.

H.M.Jr: Won't be here more than 15, 20 minutes.

Crowley: Here's the position we want you to be in. They know they're on the spot. They want to join the hundred percent agreement. They want something from us, see? Now, all I say is, let's not lose the position we're in. Whatever you finally want us to do, after we in this room agree with it, we'll go with you, see? But that may come from you

H.M.Jr: No, that isn't - no, I've been absolutely impartial up to now. I've been an impartial chairman. I haven't made any suggestions.

Upham: I was impartial up to Friday.

H.M.Jr: Well, I haven't made any. And what you fellows have done up to now - I think by waiting this long we've got a few suggestions which have been very helpful.

Crowley: Well, here's what Eccles wants, Mr. Secretary. Eccles knows now he's in a jam on the Vandenberg letter. He knows he's in a jam with his Board. John McKee is mad as the devil at him.

(At this point the Stenotype machine began to function very imperfectly, and the rest of the transcript is fragmentary)

H.M.Jr: Now look, I can see you fellows at 8:30 tonight.

Crowley: I think if we could see the Board tomorrow, Cy, ...

H.M.Jr: Make it 2:30 tomorrow afternoon. That'll give them the time necessary

Upham: Just Eccles?

H.M.Jr: No, I want Ransom, I want those other two fellows who are on the committee.

Upham: McKee and Davis.

H.M.Jr: There's four.

Upham: How about lunch tomorrow?

H.M.Jr: No. Can't stomach it.

Upham: Eccles thinks he holds one card which is very important. I don't know whether you know about it or not. If I had, I would have conducted myself differently. He said that when he agreed to serve on the committee, the President promised him that he would get a coordination of the banking agencies to make effective the Administration's cheap money policy. He says that you knew that.

H.M.Jr: That isn't true.

Upham: That we were to do something which would make effective the Administration's easy money policy.

H.M.Jr: That isn't true.

Upham: Right. That's the card which he thinks he holds.

H.M.Jr: The President said that we did not want bank coordination, we did want bank unification. And the President changed it, in writing.

Upham: "Coordination" is the word he used.

H.M.Jr: And I'll stand on what the President said in writing.

Upham: Right.

H.M.Jr: And Mr. Eccles - he wants to mix up bank examinations

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with money management, and I'm opposed to that.

Upham: That's right. You told him so.

H.M.Jr: I'm opposed to it. And Mr. Eccles has no card, except a joker.

Upham: A two-spot.

H.M.Jr: And we're leaving all jokers out.

And I sat there with Danny Bell at my side, and I said, "No, Mr. President, we do not want that." Now, I have no doubt Eccles said it, but I'm sure the President didn't agree.

Diggs: He made that statement over at luncheon the other day.

H.M.Jr: And if Mr. Eccles - as all the children say, "Nuts!"

Crowley: Marriner's got in the back of his mind - he wants a branch banking system.

Upham: He also wants the country banks to put their reserves in the Reserve Banks.

H.M.Jr: But I think it's just as well this has happened, because now it's out in the open, and instead of going along until the first of January, with Mr. Eccles have seven or eight months to work under cover, we make him come right out in the open.

Now, my record is - damned if you can find anything that I have ever said about bank examination. I haven't opened my mouth on it.

Upham: Ronald Ransom spoke to me on this and again said that he himself feels that we can get together.

H.M.Jr: I talked to Ronald Ransom at five minutes of one, and that's the way he talked. But Ronald Ransom is just - he's like I am; he's a born optimist. I hope he's right, what he says is true, and so on. But Wednesday midnight is the line. I won't wait one minute longer.

Now, I asked Ransom to come over here because he'd been so helpful as a balance wheel, which he has been.

Now, Mr. Eccles - if he wants to take - what do you

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say in Texas when you give a man rope and

Smyth: "Give him enough rope and he'll choke himself.

Upham: Of course, it's possible that he will go to the White House and bring it right to the President.

H.M.Jr: How can he?

Upham: Isn't the President here?

H.M.Jr: No. I just talked to the President a little while ago.

Upham: I'm sorry.

H.M.Jr: Do you (Smyth) think I'm

Smyth: Oh, absolutely.

H.M.Jr: I got a very interesting cable that came in - just to show you. Every month they have the meeting of the Bank for International Settlements at Basle, and these central banks get together, and somehow they remarked that we were the only country where the head of the central bank was the fellow that wanted to spend the money and the Treasury is holding him back, and in every other country it's the reverse.

Crowley: Thank you. We'll see you at 8:30.

June 20, 1938.
12:50 p.m.

H.M.Jr: Hello.

Operator: Jones. Go ahead.

H.M.Jr: Hello.

Jesse Jones: Hello.

H.M.Jr: How are you, Jesse?

J: Pretty good, how are you?

H.M.Jr: I'm better.

J: I sent you a little note over there.

H.M.Jr: Well, I just got in and I haven't got my mail yet.

J: And I wanted - it's about these - I met with a crowd of other bankers over at Marshall's office Friday.

H.M.Jr: Yes. Marshall Diggs.

J: Yes.

H.M.Jr: Yes.

J: Discussing these regulations and things.

H.M.Jr: Yes.

J: And I wanted to talk with you before you reached your conclusions.

H.M.Jr: Well, you'll have to talk awful fast.

J: How fast? What time can I come?

H.M.Jr: Well, I've asked Diggs and Crowley to come at two.

J: At two?

H.M.Jr: Yes. And - but I won't come to any conclusions then, but I was going to tomorrow.

J: Well, I'd like to talk to you this afternoon.

H.M.Jr: Well, how about a quarter of four?

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J: Quarter to four. I'll be there.

H.M.Jr: Yes. And ...

J: Thank you, Henry.

H.M.Jr: Now wait a minute.

J: Yep.

H.M.Jr: Wait a second. Just give me an inkling, will you? You ...

J: Tell you what I'll do.

H.M.Jr: Yes.

J: I sent you a little note. I'll send you over a memorandum of what I think it ought to be.

H.M.Jr: Will you?

J: And it's - I went over - I showed it to - to Upham Saturday.

H.M.Jr: Oh, good.

J: I asked him to come over here. And there's - I have just a few modifications.

H.M.Jr: Yes.

J: And the thing that - but it's - I think it's quite essential and I'd like to - and I'll send that over to you now if I may.

H.M.Jr: Would you do that?

J: I will do it right now.

H.M.Jr: Yes. Now, let me - let me talk to you a minute.

J: Yes.

H.M.Jr: You're not going to be here tomorrow?

J: I may or may not.

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H.M.Jr: Well, when - will you know at a quarter of four?

J: Yes, sir.

H.M.Jr: Now, I - I - when you come over, I'd like to talk to you a little bit about lending possibly to some railroads.

J: Yes.

H.M.Jr: And you know - I take it you know what you've done up to date on that. I mean if anything.

J: Yes.

H.M.Jr: I mean in the way of equipment.

J: Huh?

H.M.Jr: In the way of ...

J: Yes.

H.M.Jr: In the way of equipment.

J: Yes.

H.M.Jr: See?

J: Yes.

H.M.Jr: So we can talk a little bit then.

Now look, another thing while I've got you. What's your reaction on what Eccles did in that Vandenberg letter?

J: Well, I think he disturbed the boys more than anything else.

H.M.Jr: Yes. See, I'm seeing the press at three.

J: No, I haven't.

H.M.Jr: No, I'm going to see the press at three.

J: How's that?

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H.M.Jr: I'm going to see the newspapers at three.

J: Oh, you are.

H.M.Jr: But I'm not going to say anything.

J: I don't believe I would if I were you. I think you're right.

H.M.Jr: Well, I've got further with the President by not washing our dirty linen in public.

J: That's right.

H.M.Jr: I never have. I don't - I never did think that that's more difficult for him.

J: (Garbled.)

H.M.Jr: Yes. Go on.

J: (Garbled.)

H.M.Jr: But I'd be tickled to death to see you and I'll be glad to get what you have out.

J: Thank you.

H.M.Jr: Thanks.

J: Yes sir.

H.M.Jr: Starting in tomorrow morning.

June 20, 1938.
12:55 P. M.

H. M. Jr.: Hello

Operator: Ronald Ransom

Ronald
Ransom: Good Morning.

H.M.Jr.: How are you?

R: Fine. I hope you're well.

H.M.Jr.: I'm fine.

R: That's good.

H.M.Jr.: I'd just like to ask you a question if you can answer it.

R: All right.

H.M.Jr.: The letter of which Chairman Eccles sent to Vendenberg. Is that the opinion of the Board? Is that - is it a Board action?

R: No. That's a purely personal matter.

H.M.Jr.: It's not a Board action?

R: No. That is not Board action.

H.M.Jr.: I see.

R: But I had rather you would treat that as an off-the-record answer, if you will.

H.M.Jr.: Well, I just wanted to know because it disturbed me considerably.

R: No. I think that you're going to find that this thing is going to work itself out to a satisfactory conclusion.

H.M.Jr.: Uh huh.

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- R: I think it's going to do it for the reason that as a result of the suggestion you made last Tuesday with Mr. Eccles, Mr. Crowley and Mr. Diggs have been together - have been working on it and have been exchanging ideas, and that I believe there's enough elasticity all the way around to produce a result which would be mutually satisfactory and if I'm too optimistic, why, I regret it. I hope that I'm not.
- H.M.Jr: Well, now - well I haven't seen Upham so I don't know what we're supposed to --
- R: Well, he's - he's not on the crypt of optimism if he correctly reports his own feeling to me. Because he called me last evening and I did not have a chance to call him back until this morning. He expressed a rather pessimistic view. I don't know whether it was for the purpose of developing my own thought but I didn't hesitate to tell him that I didn't feel nearly as pessimistic about it as he does.
- H.M.Jr: O. K.
- R: Now let's take time off and view this. Here's the situation.
- H.M.Jr: Yes.
- R: For the first time I believe Mr. Crowley, Mr. Diggs, and Mr. Upham are having the chance to really get a point of view.
- H.M.Jr: Yes.
- R: And that there can be some compromises along the line on both sides that would result in a much better agreement that otherwise would be the case. And I just hope I'm right.
- H.M.Jr: I hope so. God knows I've waited long enough for a compromise.
- R: Well, you've been very patient. But these dead lines do bring things, you know, to a conclusion.

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- R: Now let me tell you one other thing I heard last week that I called you up to tell you at the time but you were out of town.
- H.M.Jr: Well, the message I got was that you would call me later. They said you were not in your office.
- R: Well, when I called you - when I got a chance to call you later, you had left.
- H.M.Jr: Oh, I'm sorry.
- R: Now, it wasn't very important. If one banker doesn't like to swallow he doesn't make a stumble but when one banker commences to get an idea sometimes it does boil and I'm just giving you this as a reporter.
- H.M.Jr: Right.
- R: There was a very conservative banker in the Southwest who had commenced to survey his own Government bond account with the idea that he better take his profits because he believed all this newspaper talk about devaluation must have some background.
- H.M.Jr: Yes.
- R: And I was very disturbed because he is the conservative type.
- H.M.Jr: Yes.
- R: And if one of them thinks that maybe others will.
- H.M.Jr: Well, I just can't help the doctor.
- R: I know you can't.
- H.M.Jr: Last year it was the other way. We talked our heads off trying to convince them that we were not going to lower the price of gold.
- R: Well, I'm merely telling you this simply as a repertorial item for what it might be worth to you.
- H.M.Jr: Yes. Well - then, are we to see you tomorrow?
- R: Yes.

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H.M.Jr: That's your program?

R: That's my program.

H.M.Jr: After I've seen Eccles I'll find out what's what.

R: I mean, what time will I see you?

H.M.Jr: I'll call you back after lunch.

R: Well, I'll tell you what you do. I've stayed away from the active participation in this thing in print but it stayed on the sidelines. So if you should plan to see us tomorrow you just call the chairman and I'll come over with him. Is that --

H.M.Jr: Well, I very definitely want you because I need you as a balance wheel. I mean I - no, I - I --

R: Thanks for the compliment --

H.M.Jr: But I feel - I feel quite hurt over what Eccles has done. I feel very much hurt over this Vandenberg letter. And for him to sit there and have lunch with us - I haven't seen the date of it - but he must have written it when we had that heart-to-heart talk -- last Tuesday.

R: Well, of that I don't know - I'm unable to answer. I just don't know that.

H.M.Jr: I'm going to find out what the date was on the Vandenberg letter.

R: Yes.

H.M.Jr: But if he wrote that letter after we had that talk and put all our cards on the table, I think - I do think he should have mentioned it.

R: Well, now I'm unable to express an opinion because I frankly don't know.

H.M.Jr: All right.

R: And --

H.M.Jr: But I'm going to call you later on during the day and we'll see if we can all get together.

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R: O. K.
H.M. Jr: Fine.
R: Thanks.
H. M. Jr: Goodbye.

June 20, 1938.
4:00 P. M.

Operator: Secretary Wallace for you.

H. M. Jr: Hello.

W.'sSecy: Secretary Morgenthau?

H. M. Jr: Yes.

W.'sSecy: Just a second.

H. M. Jr: Yes.

Henry
Wallace: Hello.

H. M. Jr: Hello.

W: Hello, Henry?

H. M. Jr: How are you?

W: Where are you Henry?

H. M. Jr: I'm here in the Treasury.

W: Fine. Why, Henry, I've got a couple of ^{rather} indirect approaches from people indicating that -- one is from a newspaper man - a French newspaper man indicating that - this French gran firm of Dreyfus.

H.M. Jr: Yes.

W: -- Has heard the rumor that we're interested in -- in exports of wheat to China.

H. M. Jr: Yes.

W: And indicating that they have considerable facilities in China, especially Indo-China, and they'd like to be of service. I'm just passing on the rumor, that's all.

H. M. Jr: Well --

W: They haven't got in touch direct with me in any way, but I --

H. M. Jr: They wouldn't get it out of this shop.

W: How's that?

H. M. Jr: I say, they wouldn't get it out of here.

W: Yes.

H. M. Jr: Of course, if we did --

W: Well, I'm not - I'm not speaking about it to indicate -- but merely because I thought you might be interested.

H. M. Jr: I see. All right. - - - Had a nice market today.

W: How's that?

H. M. Jr: The market acted very well today.

W: I see.

H. M. Jr: Yes.

W: Is there - is there any progress on that front that --

H. M. Jr: That which?

W: That you and State and we were interested in?

H. M. Jr: No. I haven't heard a thing. I understand that the State Department is working on it.

W: Who's working on it?

H. M. Jr: The State Department.

W: I see.

H. M. Jr: And I'm waiting to hear from them.

W: Yes.

H. M. Jr: But if I have anything I'll get in touch with you.

W: Yes.

H. M. Jr: Thank you for calling.

W: Yes. All right then.

H. M. Jr: Goodbye.

June 20, 1938.
4:30 P. M.

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H. M. Jr: Hello

Operator: Go ahead.

H. M. Jr: Hello

Operator: Go ahead.

H. M. Jr: Hello.

Gordon

Rentschler: Hello Henry, how are you?

H. M. Jr: I'm all right.

R: Got over the wedding, did you?

H. M. Jr: What's that?

R: Did you get over the wedding?

H. M. Jr: Oh yes.

R: Well, that's all right then.

H. M. Jr: I've got Jesse Jones sitting here with me and he can listen, see?

R: Yes. All right.

H. M. Jr: And what I wanted to know was whether you've been able to make any headway on this idea of some railway equipment.

R: Yes. We got - American Car and Foundry are going to bring us in tomorrow morning a list of the constructive sales that they think they could make to the railroads.

H. M. Jr: Yes.

R: And Walt Dickerman of the American Locomotive is out of town -- was out of town Saturday and today but is expected back too, tomorrow morning.

H. M. Jr: Fine.

- 2 -

- R: And we're going to start with those two fellows first.
- H. M. Jr: Yes.
- R: Now, Charlie Hardy has a week or so ago - he's the American Car and Foundry -
- H. M. Jr: Yes.
- R: --Has had some talks with Jesse's man, Frank Wright.
- H. M. Jr: Uh huh.
- R: And I don't know how far they got.
- H. M. Jr: Uh huh.
- R: But you can call Jesse. We'll be careful not to cross wires anywhere along the line. As soon as we get the information we'll see that they get it too.
- H. M. Jr: Yes.
- R: I think that we'll have something definite to say to you in the morning, Henry, or sometime tomorrow.
- H. M. Jr: All right. Now just a minute. Let me ask whether Jesse wants to say anything. Jesse says he'll be in New York Wednesday.
- R: On Wednesday.
- H. M. Jr: And he'd like to see you and discuss this very particular thing we're talking about.
- R: Fine.. You tell him we'll get all the stuff together we can and I'll give you a ring tomorrow.
- H. M. Jr: Do that.
- R: And then you tell Jesse that I'll pick him up Wednesday any time that suits his convenience.
- H. M. Jr: Fine. Jesse is very much interested in this.

R: Yes. Well I think that something can be done with it.

H. M. Jr: Fine.

R: All right, Henry, I'll give you a ring tomorrow.

H. M. Jr: All right. I had to pay a terrific rate for my bills today.

R: What did you pay, .00?

H. M. Jr: Just a fraction of that.

R: Just 1 at the bottom, eh?

H. M. Jr: 1 - 1 $\frac{1}{2}$

R: Well, I quit that. I keep betting that 7 will win, hoping that some day something might happen, you see?

H. M. Jr: I see. Well -

R: Never get any.

H. M. Jr: All right.

R: But I'd be ashamed to tell you what I paid for September 1940 today.

H. M. Jr: Don't - don't tell me. I might cry.

R: I don't want to tell you because you'll feel so badly you'll hold it agin me.

H. M. Jr: All right.

R: All right.

H. M. Jr: All right. Bye Bye.

R: Good bye.

June 21, 1938.
10:39

William C.

Bullitt: Hello, Henry.

H. M. Jr: How are you?

B: Fine. How are you, boy?

H. M. Jr: I'm all right.

B: Let's see. I hope your coming over has been settled.

H. M. Jr: Yes. I got your very fancy cable and I thought the easiest way was to talk to you about it, see?

B: Fine.

H. M. Jr: Here's the point. I found out from the boat company that we're coming on the Statendam.

B: Yes.

H. M. Jr: Which would land us ⁱⁿ Paris between 10 and 11 the night of July 23.

B: You'll arrive the night of July 23 at Paris.

H. M. Jr: Yes. We're coming over on the Statendam.

B: Yes, that's fine.

H. M. Jr: But now, what I want to do is, I want to get my vacation first.

B: Yes.

H. M. Jr: And go right down to Antibes, you see?

B: Yes.

H. M. Jr: Hello.

B: Hello. Yes, all right.

H. M. Jr: And then I'd come back up and I want to stay there between two and three weeks.

B: Yes.

H. M. Jr: And I'm going to stay put. The family is going to travel around, but I'm just going to stay there and just sit in the sun and swim.

- 2 -

Yes.

H. M. Jr: Now, then when I came up if anybody wanted to see me why, I'd be at your disposal.

Fine Henry. But, what I'm anxious about, what about those rooms? Do you want those rooms?

H. M. Jr: Yes, we'd like to have them.

All right. I'll engage those rooms from the 24th, then.

H. M. Jr: Yes.

From the 24th on for three weeks.

H. M. Jr: Right.

If you want to give up some of them, you won't have any trouble in giving them up because there are at least a hundred people fighting for every room.

H. M. Jr: I see. Well, now, Bill, if we get to Paris at 10 or 11 the night of the 23rd, which would be best, for us to go right through or to -- what do you think?

No. You'll have to spend the night. You'll spend the night with me. I'll make arrangements for you all to spend the night in my house.

H. M. Jr: Well, we're a pretty big family.

Well, I don't care how big you are because I've got two houses, I'm living in the country.

H. M. Jr: Yes.

If you're going to be in town, I'll simply open the house in town, and plant you all in there.

H. M. Jr: Well, now. You better be sure that you want to do that.

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B: Oh no,
And I'll look for you on that day and then you'll
go down south and then you can let me know when
you're down south about when you'll be back here.
But you won't see anybody at all until

H.M.Jr: I don't think so.

B: How's that?

H.M.Jr: I don't think so.

B: Fine.

H.M.Jr: I mean - don't you think - I mean if I saw one
person or two then, the others would say - might
hurt somebody's feelings.

B: Yes. I think that's all right. I think that's
a perfectly good idea. I'll simply say you're
going through to Antibes and not stopping at Paris
and that you said that you haven't much time.

H.M.Jr: Right.

B: You can see them all on the way back. Meanwhile
things seem to be going pretty well. This
gentleman that we're very much interested in
seeing in jail to prevent his nefarious activities,
seems to be going to get it in the neck.

H.M.Jr: Well, I sent you a cable of appreciation through
the Secretary of State.

B: Yes.

H.M.Jr: I sent it over last night.

B: What a pity. But that seems to be going pretty
well and the only point is just to keep after it.

H.M.Jr: Well, I thought you did a swell job and I asked
the Secretary of State please to inform you that
that's the way I felt.

B: This fellow Butler is very good.

H.M.Jr: He is.

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B: Henry -

H. M. Jr: Yes.

B: How - what's the news beyond that - anything special?

H. M. Jr: Well, things over here in business are just a little bit brighter.

B: Really. That's good.

H. M. Jr: And they've been better since the first of June.

B: Well, now, how many railroads are you going to crash? About ten or three.

H. M. Jr: I don't - I don't think - between now and next Fall - I don't think necessarily any will.

B: Oh bravo - that's fine.

H. M. Jr: Jones is working very hard on it.

B: That's fine.

H. M. Jr: And I'm not sure that there'll be any between now and the Fall.

B: Very good. That's bully.

H. M. Jr: And things are a little bit better.

B: Fine. I'm glad.

H. M. Jr: And I hit that gold devaluation thing very hard yesterday.

B: I know you did. That's very good.

H. M. Jr: And I thought we might as well put that to bed.

B: Yes. That has a very good effect.

H. M. Jr: All right.

B: Good bye. - Well Henry, I'll look for you then on that boat and I'll engage the rooms from the 24th of July on.

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H. M. Jr: Well, wouldn't it be - would it be the 24th or 25th?

Well, if you get to Paris the night of the 23rd, -

H. M. Jr: Yes.

You'll probably spend the day - go down - on the afternoon - late afternoon of the 23rd, and you'll arrive there noon on the 25th.

H. M. Jr: Yes.

Noon on the 25th and I'll engage them for three weeks.

H. M. Jr: Yes. The 25th on.

The 25th on.

H. M. Jr: They're kind of high priced, but I guess that they're worth it.

Yes.

H. M. Jr: Right?

As a matter of fact, it's damn cheap for those rooms.

H. M. Jr: Are they?

Yes.

H. M. Jr: Well -

Well, God bless you boy, take care of yourself.

H. M. Jr: Thank you.

Good bye.

H. M. Jr: Good bye.

Comptroller's
Regulation—

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not last one.

By virtue of the authority vested in the Comptroller of the Currency by Paragraph Seventh of Section 5136 of the Revised Statutes, the following regulation is promulgated:

SECTION I

(1) An obligation of indebtedness which may be purchased for its own account by a national bank or State member bank of the Federal Reserve System must, in order to come within the classification of "investment securities" within the meaning of the Seventh paragraph of Section 5136, be a marketable obligation, i.e., it must be salable under ordinary circumstances with reasonable promptness at a fair value; and with respect to the particular security, there must be present one or more of the following characteristics:

(a) A public distribution of the securities must have been provided for or made in a manner to protect or insure the marketability of the issue; or,

(b) Other existing securities of the obligor must have such a public distribution as to protect or insure the marketability of the issue under consideration; or,

(c) In the case of investment securities for which a public distribution as set forth in (a) or (b) above can not be so provided, or so made, and which are issued by established commercial, mercantile or manufacturing businesses that can demonstrate the ability to service such securities, - the debt evidenced thereby must mature not later than ten years after the date of issuance thereof

and must be fully and adequately secured; and such securities must, by their terms, provide for the amortization of the debt evidenced thereby so that it will be extinguished by its maturity date by substantial and periodic payments: Provided, That no amortization need be required for the period of the first year after the date of issuance of such securities. The total amount of securities held under authority of this subparagraph (c) by a national bank or by a State member bank for its own account shall not in any event exceed twenty-five percentum of the capital stock of such bank actually paid in and unimpaired and twenty-five percentum of its unimpaired surplus.

(2) Where the security is issued under a trust agreement, the agreement must provide for a trustee independent of the obligor, and such trustee must be a bank or trust company.

(3) All purchases of investment securities by national and State member banks for their own account must be of securities "in the form of bonds, notes, and/or debentures, commonly known as investment securities"; and every transaction which is in fact such a purchase must, regardless of its form, comply with this regulation.

REVISION OF "EXCEPTION"

The "EXCEPTION" on page 6 of the mimeographed revision should be amended by adding the following at the end thereof:

"or to real estate securities acquired pursuant to Section 24 of the Federal Reserve Act, as amended."

SECTION II

(1) Although the bank is permitted to purchase "investment securities" for its own account for purposes of investment under the provisions of R. S. 5136 and this regulation, the bank is not permitted otherwise to participate as a principal in the marketing of securities.

(2) The statutory limitation on the amount of the investment securities of any one obligor or maker which may be held by the bank, is to be determined on the basis of the par or face value of the securities, and not on their market value.

(3) The purchase of "investment securities" in which the investment characteristics are distinctly or predominantly speculative, or the purchase of securities which are in default, either as to principal or interest, is prohibited.

(4) Purchase of an "investment security" at a price exceeding par is prohibited, unless the bank shall:

(a) Provide for the regular amortization of the premium paid so that the premium shall be entirely extinguished at or before the maturity of the security and the security (including premium) shall at no intervening date be carried at an amount in excess of that at which the obligor may legally redeem such security; or

(b) Set up a reserve account in order to amortize the premium, said account to be credited periodically with an amount not less than the amount required for

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amortization under (a) above.

(5) Purchase of securities convertible into stock at the option of the issuer is prohibited.

(6) Purchase of securities convertible into stock at the option of the holder or with stock purchase warrants attached is prohibited if the price paid for such security is in excess of the investment value of the security itself, considered independent of the stock purchase warrants or conversion feature. If it is clearly apparent that the price paid for an otherwise eligible security fairly reflects the investment value of the security itself and does not include any speculative value based upon the presence of the stock purchase warrants or conversion feature the purchase of such a security is not prohibited.

(7) As to purchase of securities under repurchase agreement, subject to the limitations and restrictions set forth in the law and this regulation:

(a) It is permissible for the bank to purchase "Investment securities" from another under an agreement whereby the bank has an option or a right to require the seller of the securities to repurchase them from the bank at a price stated or at a price subject to determination under the terms of the agreement, but in no case less than the value at the time of repurchase.

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(b) It is permissible for the bank to purchase "investment securities" from another under an agreement whereby the seller or a third party guarantees the bank against loss on resale of the securities.

(c) It is not permissible for the bank to purchase "investment securities" from another under an agreement whereby the seller reserves the right or the option to repurchase said securities itself or through its nominee at a price stated or at a price subject to determination under the terms of the agreement, notwithstanding the fact that the bank may also, under such agreement, have the right or option to compel the seller to repurchase the securities at a price stated or at a price subject to determination under the terms of the agreement.

(8) As to repurchase agreements accompanying sales of securities,

(a) It is permissible for the bank selling securities to another to agree that the bank shall have an option or right to repurchase the securities from the buyer at a price stated or at a price subject to determination under the terms of the agreement, but in no case in excess of the market value at the time of repurchase.

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(b) It is not permissible for the bank selling securities to another to agree that the purchaser shall have the right or the option to require the bank to repurchase said securities at a price stated or at a price subject to determination under the terms of the agreement, notwithstanding the fact that the bank may also, under such agreement, have the right or option to repurchase the securities from the buyer at a price stated or at a price subject to determination under the terms of the agreement.

In view of the fact that some banks may have bought or sold securities under a form of agreement which is prohibited by this regulation, the bank should either terminate or modify same so as to conform to this regulation, where such action may lawfully be taken. Existing agreements of the prohibited type must not be renewed.

EXCEPTION

The restrictions and limitations of this regulation do not apply to securities acquired through foreclosure on collateral, or acquired in good faith by way of compromise of a doubtful claim or to avert an apprehended loss in connection with a debt previously contracted, or to real estate securities acquired pursuant to Section 24 of the Federal Reserve Act, as amended.

Those Who Insure

According to The Wall Street Journal Saturday, "Chairman Eccles evidently hopes he can win the President's approval [for the standards of bank examination proposed by the Board of Governors of the Federal Reserve System] on the ground that relaxed examination and investment rules are essential to the Administration's easy money policy."

As a matter of fact, that is precisely why the three other bank examining agencies now in agreement on the proposed unified standards should *not* accede to the Governors' point of view. It is also a reason why every step which would lead to the incorporation of the Federal Deposit Insurance Corporation as a branch or bureau of the Reserve System should be unceasingly opposed.

The point cannot be stressed too often that the Federal Reserve System, in its capacity of quasi-management of the nation's credit system, discharges duties which are quite different from those of the FDIC. More, their respective purposes may at times be antipathetic. One group represents the use of credit from the national standpoint; the other, safety of the deposits which it is insuring for the benefit of depositors. This basic consideration transcends any question of personalities which may be involved.

The present movement toward unification of standards of bank examination and investment does not yet propose to bring the FDIC into the Reserve system. But if the FDIC, the Comptroller of the Currency and the National Association of Supervisors of State Banks, now all in agreement, should knuckle under to the demand of the governors, or should be compelled to do so by the President, the Reserve System would have attained at least the substance of such domination.

The three agencies mentioned above, now in agreement, have all gone far in the direction of compromise. They should go no further, if in their judgment such acceptance of the Eccles proposals would constitute excessive "liberalism."

It is not necessary to examine here the specific points upon which the

authorities differ. The issue is not over the abstract merit of the contentions, but one simple question of principle—that insurers should always have the right to determine the risks they insure. The FDIC is compelled to insure all banks that qualify for its protection. Since this is true, its judgment of the banking practices necessary for safety cannot, in expediency or in logic, be subordinated to the exigencies of the Federal Reserve System. This is elementary.

TREASURY DEPARTMENT

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INTER OFFICE COMMUNICATION

DATE: June 20, 1938

TO Secretary Morgenthau

FROM M. A. Harris

A short review of the U. S. Government
security market during the past week

Although trading in government securities during the past week was considerably below that of last week's new financing market, turnover, nevertheless, was fairly large. Prices moved irregularly higher but interest in the market was of a selective nature, centering largely in the short notes, the new 2 3/4s and the intermediate bond issues. As a result of the high premiums on recent new issues speculation by banks and corporations in the "rights" has increased and notes maturing within the next two years are currently selling on a negative yield basis. There is evidence that a large amount of the new 2 3/4s is yet to be distributed but some progress was made during the week, particularly during the latter part.

The new 2 3/4s were quoted 101.30 bid at the close Saturday, up 5/32nds for the week, while other long bonds, which have been restrained somewhat by the new issues, were unchanged to 4/32nds higher. Short bonds were 1 and 2/32nds higher and the intermediate issues 2 to 8/32nds higher. The new 1 1/8% note advanced 4/32nds to 101.22 bid. Other notes were up 1 to 7/32nds with the 1940 and early 1941 maturities in best demand. Purchases by the System Account of short notes showing a positive yield in replacement of tax-dated bills probably accounts for a part of the strength in these issues. Guaranteed issues continued to advance, with gains ranging to 5/32nds being recorded.

Aside from the System operations, the Treasury bill market was very quiet.

Corporate Bonds

The market moved lower last week with weakness quite pronounced in the rail group, probably due largely to the disappointment over lack of Federal action to aid railroads. Many new lows for the year were made. Volume remained somewhat low and the weakness in the case of the rails was due to the lack of bids as much as to the selling pressure. Utility bonds have been relatively inactive with high grades showing little change and second grades tending toward weakness. Industrial bonds receded but declines were small and cannot be compared with those in the railroad group.

New Issue Market

There were no offerings of any size last week and there probably will be no large flotations until July. The lull in the market is not due to market conditions and several big deals are reported in the making. According to "Fitch Revisions" the Standard Oil of New Jersey filed a registration statement covering \$85,000,000 debentures last Wednesday and Crown Cork & Seal one covering \$10,000,000 debentures. New York Steam Corporation has taken the preliminary step looking to refund its first mortgage 5s and 6s. Yonkers Electric Light & Power is awaiting approval by the New York Public Service Commission of \$9,515,000 new 3 1/2s. Southwestern Bell Telephone has already taken preliminary steps to refund its 7% preferred stock with \$30,000,000 new 3% bonds.

Dealers' Portfolios

Dealers reduced their holdings of U. S. Government securities by \$33.7 millions last week. The principal changes were reductions of \$18.6 million and \$11.1 million in holdings of Treasury notes due after 1 year

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and Treasury bonds, respectively.

	<u>Holdings</u> <u>June 11</u>	<u>Holdings</u> <u>June 18</u>	<u>Net</u> <u>Changes</u>
Treasury bonds	68.6	57.5	- 11.1
Treasury notes (1 year)	39.6	41.6	+ 2.0
Treasury notes (1-5 yrs.)	62.5	44.0	- 18.5
Treasury bills	0.8	0.2	- 0.6
U. S. L. C. bonds	11.8	7.3	- 4.5
F. F. M. C. bonds	<u>2.7</u>	<u>1.7</u>	<u>- 1.0</u>
	186.0	152.3	- 33.7

System Account

The following transactions in the Federal Reserve System Account were executed in the market during the past calendar week:

(1) Exchanges of bonds for bonds in the market:

<u>Sales</u>	<u>Purchases</u>
\$8,500,000 2 1/2s of 1949/53	\$5,000,000 3 1/4s of 1943/45
1,000,000 2 1/2s of 1945	4,500,000 2 3/4s of 1948/51
<u>4,000,000 2 1/2s of 1948</u>	<u>4,000,000 2 3/4s of 1951/54</u>
\$13,500,000	\$13,500,000

(2) Replacement of weekly bill maturity:

<u>Amount maturing June 15th</u>	<u>Purchased in Replacement</u>
\$19,268,000 Treas. bills due 6/15/38	\$19,268,000 Treas. bills due 9/14/38

(3) Sales of tax-dated bills and replacement purchases:

<u>Sales</u>	<u>Purchases</u>
\$ 43,598,000 Treas. bills due 6/16/38	\$ 47,332,000 Treas. bills due 9/14/38
19,775,000 " " " 6/17/38	5,235,000 " " " 7/6/38
<u>5,694,000 " " " 6/18/38</u>	<u>5,500,000 Treas. notes due 6/15/40</u>
\$ 69,067,000	\$ 58,067,000 *

* Leaves \$11,000,000 to be replaced before end of current statement week.

Investment Accounts

The following transactions were executed in the New York market during the past week:

\$ 100,000 2 3/4% Treas. bonds 1956/59 a/c Mutual Mtgs. Insurance Fund.	<u>Sale</u>
\$ 150,000 2 3/4% Treas. bonds 1958/63 a/c Alien Property Custodian.	<u>Purchase</u>

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE June 20, 1938

TO Secretary Morgenthau

FROM Mr. Haas *HA*

Subject: The reduction in prices on galvanized steel sheets.

The reduction of \$3.00 a ton in the base price for galvanized steel sheets announced on June 14th by the Carnegie Illinois Steel Company and followed by other companies, merely gives official affirmation to price concessions which, according to trade reports, have ruled in actual transactions for a number of weeks. This follows the customary procedure in marking down steel prices. Official price reductions have usually represented tardy recognition of reduced competitive prices in the actual market. The present reduction, according to the Wall Street Journal, does not reflect the full amount by which actual prices recently have been marked down in individual transactions.

According to various reports, prices on other steel products have also been weak recently, which some believe may presage a general cut in steel prices when demand starts to improve. Reinforcing bars are reported to have been unusually weak. Two St. Louis companies, according to the Wall Street Journal, have cut prices \$5.00 a ton on this product, with some sales reported as much as \$10.00 a ton under the regular market. Price cutting on tin plate, the most important product in steel company revenues at present, was recently mentioned by the American Can Company.

A significant point about recent price reductions, official and unofficial, is that they are being made without corresponding wage reductions.

From the viewpoint of its meaning in the business picture, price cutting at this time is taken in the steel trade as evidence that some real business is beginning to come in. The previous stability of prices was due in part to a lack of orders in sufficient volume to test the price structure. In the absence of any substantial buying there would be little or no incentive for cutting prices. A sharp upturn in new orders reported by the U. S. Steel Corporation during the week ended June 9 apparently confirms trade reports that buying of steel is increasing.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE JUNE 20, 1938

TO Secretary Morgenthau
 FROM Mr. Haas
 Subject: Sales data for the Atlantic and Pacific Tea Company

The Atlantic and Pacific Tea Company is reporting its monthly sales currently to the Department of Commerce, which uses them as part of an index of chain store sales, under the grocery chain group. The seasonally adjusted index of sales for this group for recent months, in comparison with last year, is given below.

Grocery chain store sales, dollar values
 1929-31 = 100, adjusted

	1938	1937
January	96.2	97.9
February	93.6	97.4
March	94.6	99.1
April	91.5	96.8
May	93.5	96.9
June		93.9

The relative stability of chain grocery sales, in comparison with sales of certain other types of chain stores, may be seen by comparison with the following index:

Indexes of chain store sales, dollar values
 1929-31 = 100, seasonally adjusted

	Combined index, 20 chains 1/		Apparel store sales		Variety store sales	
	1938	1937	1938	1937	1938	1937
January	106.7	105.3	107.6	112.0	96.1	94.4
February	106.4	110.0	108.8	117.0	94.1	97.4
March	103.3	108.6	116.0	126.0	97.2	103.3
April	105.2	110.0	116.0	130.0	92.9	96.2
May	-	112.0	-	124.0	89.3	98.3
June	-	114.0	-	117.0	-	105.9

1/ Includes sales of J. C. Penney Co., W. T. Grant Co., and three restaurant chains in addition to grocery, apparel, and variety chains, for which detailed figures are given.

Secretary Morgenthau - 2

Sales by grocery chains are probably of relatively little value as an index of business conditions, since (1) they tend to remain stable throughout the business cycle; (2) the diversion of consumer purchases, in times of depression, to chain grocery stores from the more expensive stores may distort comparisons; (3) relatively wide fluctuations in food prices decrease the significance of changes in grocery sales.

SECRETARY MORGENTHAU SAID TODAY HE HAS "SERVED NOTICE ON ALL PARTIES CONCERNED" THAT AGREEMENT MUST BE REACHED ON A UNIFORM BANK EXAMINATION POLICY OR HE WILL SUBMIT A REPORT TO PRESIDENT ROOSEVELT WITHOUT CONCURRENCE OF FISCAL AGENCY OPINIONS.

6/20--R330P

ADD MORGENTHAU

MORGENTHAU SAID THAT IF AN AGREEMENT IS NOT REACHED BY MIDNIGHT WEDNESDAY HE WILL BEGIN PREPARING HIS REPORT AND SEND IT TO THE PRESIDENT, PROBABLY FRIDAY.

"IN DRAWING UP THIS REPORT THE FDIC, THE COMPTROLLER OF THE CURRENCY AND THE SECRETARY OF THE TREASURY HAD JUST ONE THING IN MIND -- THE INTERESTS OF THE DEPOSITORS," THE SECRETARY SAID.

ABSENT FROM HIS STATEMENT WAS MENTION OF THE FEDERAL RESERVE BOARD.

6/20--R333P
ADD MORGENTHAU

MORGENTHAU REFUSED TO COMMENT ON THE ATTITUDE OF THE FEDERAL RESERVE BOARD BUT SAID HE HAS CALLED A MEETING FOR TOMORROW AFTERNOON AT WHICH THREE MEMBERS OF THE FEDERAL RESERVE BOARD IN ADDITION TO ECCLES HAVE BEEN INVITED.

FDIC CHAIRMAN CROWLEY AND MARSHALL DIGGS, ACTING COMPTROLLER OF THE CURRENCY, WILL BE AT THE MEETING IN ADDITION TO THE THREE FEDERAL RESERVE MEMBERS, RONALD RANSOM, JOHN MCKEE, AND CHESTER DAVIS.

6/20--R338P

MORGENTHAU AGAIN DENIES DEVALUATION RUMORS -
TO REPORT ON NEW BANK EXAMINATIONS TO
ROOSEVELT FRIDAY - TREASURY BILL RATE REACHES
NEW LOW

JUN 20 1938

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 WASHN - SECRETARY MORGENTHAU AGAIN TODAY
 DENIED RUMORS OF IMPENDING DOLLAR DEVALUATION

- I DON'T KNOW HOW LONG PEOPLE WITH ANY HORSE
 SENSE ARE GOING TO

LISTEN TO THESE RUMORS - WHEN THE PRESIDENT OF
 THE UNITED STATES AND THE SECRETARY OF THE
 TREASURY SAY THERE IS NOTHING TO IT I THINK
 THEIR WORD OUGHT TO BE GOOD - THE MATTER RESTS
 BETWEEN THEM- SECRETARY MORGENTHAU ASSERTED

- SPECULATORS ALL OVER THE WORLD HAVE BOUGHT
 THESE GOLD STOCKS AND WHEN THEY HAVE SOLD OUT I
 THINK YOU WILL SEE THAT THESE RUMORS STOP -
 BUT I SUPPOSE BOYS WILL BE BOYS- SECY MORGENTHAU SAID

THE SECY AS CHAIRMAN OF THE INTERDEPART-
 MENTAL COMMITTEE ON BANK EXAMINATIONS SAID THAT
 HE HAD SERVED NOTICE THAT THE COMMITTEE MUST
 HAVE A REPORT BY WEDNESDAY MIDNIGHT AND THAT HE
 WILL PRESENT IT TO THE PRESIDENT ON FRIDAY - IN
 DRAWING UP THE REPORT -THE FEDERAL DEPOSIT
 INSURANCE CORP THE COMPTROLLER OF THE CURRENCY
 AND THE SECY OF THE TREASURY HAVE JUST ONE
 THING IN MIND AND THAT IS PROTECTION OF THE
 DEPOSITOR- MR MORGENTHAU ASSERTED

HE SAID THAT HE HAD CONSULTED FDIC CHAIRMAN CROWLEY AND ACTING COMPTROLLER DIGGS BEFORE MAKING THIS STATEMENT BUT THAT HE HAD NOT CONSULTED RESERVE BOARD CHAIRMAN ECCLES - MR ECCLES THE SECY OBSERVED HAS MADE PUBLIC HIS OPINION ON BANK EXAMINATIONS BUT THE SECY ADDED THAT HE WAS NOT SURE WHETHER THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE BOARD HAD EXPRESSED THIS OPINION

NEW YORK BANKS TODAY BID ON A 100 000 000 DLS OFFERING OF 91-DAY TREASURY BILLS AT AN AVERAGE DISCOUNT OF 0 016 PC COMPARED WITH AN AVERAGE OF 0 027 PC A WEEK AGO SECY MORGENTHAU ANNOUNCED

June 20, 1938

Secretary Morgenthau invited to his home at 8:30 p.m. Mr. Jones, Mr. Crowley, Mr. Diggs, Mr. Oliphant, Mr. Gaston, and Mr. Upham.

The suggested revision of the investment securities regulation of the Comptroller of the Currency, particularly that section dealing with securities which do not have a public distribution (probably thought of as securities of small local concerns) was under consideration for some time.

Mr. Jones urged that the maturity of such securities be a maximum of fifteen years. Mr. Diggs was not willing to go beyond ten years. Mr. Jones urged that the maximum limit of 25 per centum of capital stock and surplus which might be represented by loans of this character be eliminated. Mr. Diggs agreed to this.

Mr. Jones urged that the wording "established commercial, mercantile and manufacturing businesses" be changed for the sake of uniformity to the language employed in the Reconstruction Finance Corporation Act for industrial loans, "established commercial or industrial businesses or enterprises." Mr. Diggs agreed to that.

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It was urged that instead of requiring that the securities be "fully and adequately secured," that they be "of such sound value or so secured as reasonably to assure its payment." This was agreed to.

It was urged that complete amortization by maturity date be not required. Mr. Diggs agreed to a 75 per cent amortization.

GROUP MEETING

June 21, 1938,
9:45 A. M.

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

H.M.Jr: Good morning, gentlemen.

Gaston: Good morning.

Klotz: Oh, I didn't get a chance to ask you - Mr. Myrdal is in town today, with Harry Hopkins, and he is still willing to come back again on the twenty-ninth, if you want the Professor to.

H.M.Jr: Is that the Swede?

White: Yes. Yes, if you're pressed at all for time, I think you should prefer to have it the twenty-ninth.

H.M.Jr: Will he be here tomorrow?

White: He didn't say he would.

H.M.Jr: You tell him to stay over tonight if he wants to see me. I'm free tomorrow night.

White: I'll take care of it.

H.M.Jr: Tell him I'm free tomorrow, anyway.

White: That will be fine, if he can stay.

H.M.Jr: We had another good meeting last night. I think we got somewhere on this bank examinations. I'm surprised at all the publicity. I called up Mr. Jones at eight o'clock this morning and

asked him if he would postpone going to New York and come to the meeting this afternoon. I thought he would be helpful. I told him I thought he could handle Mr. Eccles better than I could. He said he'd try and arrange it. Now, I've got a very tight thing this morning +....

(Telephone:) Hello. No, I can't take it now. Well, just a minute, Mrs. Klotz will talk to him. (Mrs. Klotz talks to Mr. Feis.)

- H.M.Jr: Are those things going to be written up this morning? I mean, the Comptroller's own
- Upham: He's working on that now, and I asked him to have it ready. The others, of course, have been written up sometime.
- H.M.Jr: When you have those, will you let me know?
- Upham: Yes. When I have the regulations.
- H.M.Jr: When they are written, I'll see Oliphant and you.
- Klotz: (Low to H.M.Jr.)
- H.M.Jr: If it's Haiti - here, let me talk to him. (Over telephone.) Hello. Is it Haiti? What? Yeah. Well, you want to come over today? Eleven o'clock? All right. You're sure it isn't Haiti, and it isn't the Hungarian debt? All right, I'll see you then.
- Couldn't get a smile out of him.
- Gibbons: It's probably an Austrian - taking a Customs Agent out of Austria and sending him to Italy. He called me about it. I asked Feis for a report.
- H.M.Jr: Anyway, when you're ready, let me know.
- Upham: Smyth was here yesterday. Do you want him this afternoon?
- H.M.Jr: No, just want to let him know what we're doing.
- Upham: There's only one member of the Federal Reserve Board who isn't coming.

H.M.Jr: Who is that?

Upham: Szymczak.

H.M.Jr: Oh, for God's sake - let's have him. Call him up, and - let's have him in.

Upham: Call him up.

H.M.Jr: Will you do that?

Upham: Surely.

Oliphant: I hope we get that in time to have a little talk about it, because a phase of it has occurred to me since last night.

Upham: Suppose I stick a penny in it then.

H.M.Jr: Then I can see you right after Feis leaves. We want to be as near right as we can.

Mac?

McReynolds: This letter Danny asked me to bring in to you - Doc Putnam, telling me to sell some property. He didn't know anything about it.

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

McReynolds: Had a letter from Traynor, submitting his resignation.

H.M.Jr: (Over telephone.) All right. Hello. Ah, July twenty-third, between ten - well, that's close enough - between ten and eleven on the twenty-third. Thank you. How many hours on the train? O. K. Thank you. (To Mrs. Klotz - inaudible.)

McReynolds: You don't know any reason why we shouldn't accept Traynor's resignation, do you?

H.M.Jr: Who is he?

McReynolds: He worked for Ros Magill. He's from the Coast.

Oliphant: University of California. He's going back - just according to the agreement.

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H.M.Jr: That's all right.

Oliphant: He's done an awfully good job, Mr. Secretary. Ought to give him a nice letter.

H.M.Jr: Give him a nice letter.

McReynolds: And have it for the Secretary's signature.

H.M.Jr: What else?

McReynolds: Frank Wilson has his supervising agents in here yesterday, today, and tomorrow. Wonder if you have time to see them? There are only about fifteen of them.

H.M.Jr: It would have to be sometime this afternoon.

McReynolds: He could bring them in any time. I suggested he ought to have them in.

H.M.Jr: Why not, say five minutes of one? Five minutes of one.

McReynolds: Twelve fifty-five. He can bring them in here.

H.M.Jr: What else?

McReynolds: Of particular importance, you asked to know how many cases they had telephone supervision on, the other day. Fifteen

H.M.Jr: Well, tell me that afterwards, alone, please.

McReynolds: That's all.

H.M.Jr: Here, put it on a piece of paper.
(Nods to Mr. Gibbons.)

Gibbons: I have nothing.

H.M.Jr: (Nods to Mr. Lochhead.)

Lochhead: The exchange market has a very steady tone today, after the gold drop from 35.02 yesterday to 34.92 today.
(Mr. Oliphant shows a letter to H.M.Jr.)

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Well, the comment - another comment we had here from London said that "Morgenthau's press statement considered very strong base."

H.M.Jr: (Laughing) Old ostrich. Ostrich Oliphant - or is it Oliphant Ostrich.

McReynolds: Well, I should think he wouldn't want to know now.

Oliphant: You, you, you, you

McReynolds: I'm a little surprised at his sending a man up there.

H.M.Jr: Is that letting nature take its course?

McReynolds: That's what I wondered.

Oliphant: Which man - what man?

McReynolds: Foley.

Oliphant: No, no.

H.M.Jr: Are you kidding, Mac?

McReynolds: No, I'm not kidding. He went up and talked to one of the Senators and got him to call Mr. Oliphant.

Klotz: Somebody said something funny.

McReynolds: I didn't

H.M.Jr: All right.

McReynolds: I didn't think it was funny.

H.M.Jr: Do you know which Senator it was?

McReynolds: Wagner.

H.M.Jr: Huh?

McReynolds: Wagner.

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H.M.Jr: As the boys say, "Interesting - if true."

McReynolds: Of course, I don't know that Mr. Oliphant knew that he was doing it.

Oliphant: Yes, he did.

H.M.Jr: Let's the three of us talk about it afterward.

Lochhead: The comments from London that came over the cable this morning were "Secretary Morgenthau's press statements considered very strong base." That is interesting Americans and foreigners came in pretty well on the foreign side also.

Haas: Especially France.

Lochhead: France, yes. France and England.

H.M.Jr: Have you some way, just for my own information, of watching the gold stocks today? I'm curious - Montreal and New York.

Lochhead: Yes. I'll do that.

H.M.Jr: Would you? Anything else?

Lochhead: That's all.

H.M.Jr: Harry.

White: Two little things. There's an Interdepartmental Committee, which you probably know about, to promote better relations among Latin American countries and the United States.

H.M.Jr: Radio?

White: No, all sorts of things, I think. And they requested, through Wayne Taylor, who is not here, that a report be made by the Public Health Department on what the United States is doing to promote those good relations, and what they are doing to help. That report is supposed to be ready Thursday. Nobody seems to know about it. Shall I - do I have your permission to take it up with Parran?

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H.M.Jr: Yeah.

White: The other matter is a meeting of the Munitions Control Board yesterday with regard to tin plate scrap - increasing the export quota. The Chairman of the Committee asked us to take it up with the respective Secretaries. We said we would, but the matter is very unimportant, and I'd like to drop it at that.

H.M.Jr: Anything else?

White: That's all.

H.M.Jr: (Nods to Mr. Upham.)

Upham: I think you agreed with Smith and Hanes, and the bankers who were here, to submit to them any agreement that was made. I wonder where we'll fit that in.

H.M.Jr: I don't think we have time now. We can let them have it after we send it to the White House. I don't think we'll have time.

Upham: Through White, you were going to get the agreements ...

H.M.Jr: Through White, yes. But we just can't - we're doing them the courtesy of letting them have it - maybe you can do it over the phone with White. White's the important fellow. You remind me of that.

Upham: Surely.

H.M.Jr: (To Mr. Haas.) I'm sending a copy of your this week's business report to the President.

Haas: Thank you. I've got a few things, Mr. Secretary - some of the things you asked for. A little more on that, this week.

H.M.Jr: Let me just see - you know I told Peoples last week Surplus Commodity bought five hundred thousand cases of grapefruit and five hundred thousand pounds of beans, but nobody would believe me. This week they bought a few beans,

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some butter, tobacco, some flour,

White: Was that chewing tobacco?

H.M.Jr: Nobody can find out. some oranges, just a teensy bit of potatoes, and one can of tomatoes.

White: No strawberries?

H.M.Jr: No strawberries. What!

Wlotz: That's what's the matter.

Haas: ~~I~~ I have a few other things. Dan Bell sent you a letter saying he would like to have your estimate of revenues for revised budgets. On the twenty-fifth, he says he has to have it. We have some figures for your consideration any time you want to go over them.

H.M.Jr: Let's fix him up between now and tomorrow.

Klotz: Ten thirty - tomorrow.

Haas: Ten thirty. Thank you.

H.M.Jr: (Telephone.) Hello. Well, I'll be in a meeting, but I can step out. I'll

What else, George?

Haas: Some time ago Walker, of Sears Roebuck sent you a letter commenting on the Forum F. H. A. used in modernization loans. As a result of that I sent it over to them and they crossed out eight of the items.

H.M.Jr: Send a letter to Walker. Gee, that's something, isn't it?

Haas: They didn't do everything, but they crossed out eight items.

H.M.Jr: Are you taking care of General Wood?

McReynolds: I've got a report, which is terrible. It isn't good at all.

H.M.Jr: Give me a letter to sign, to him. Let's -
I want a letter to him, please.

McReynolds: All right.

H.M.Jr: George.

Haas: I went over, with Dr. Parran, his report. Did
you want me in at that meeting?

H.M.Jr: Yes, very definitely. Ten forty-five; and I
want McReynolds in too.

McReynolds: He's coming to my office before he comes in
here.

H.M.Jr: How did you find out before - how do we give him
ten thousand dollars? Does that go through
Bell?

McReynolds: He'd have to get it through regular application.

H.M.Jr: Well, you mind finding out about it? Will you?
I mean, it's like - the ten thousand dollars -
he'd be as likely to get it if he was asking for
a million.

What else, George?

Haas: That's all I have.

H.M.Jr: (Nods to Mr. Gaston.)

Gaston: Wenchel expects to file a stipulation in the
Mellon case at ten o'clock.

H.M.Jr: Walter?

Gaston: Who?

H.M.Jr: Walter?

Gaston: Walmer?

H.M.Jr: Walter. Walter Winchell?

Gaston: No, not Walter - Phillip. A stipulation in the
Mellon case is going to be filed at ten o'clock,

and we're getting out a release, which is a bare statement of facts. ... resulted in the completion of assessments of foreign amounts involved in the Mellon case. I suppose Frank Hogan will probably put out some publicity about the same time, also.

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

Gaston: That's all.

H.M.Jr: (Nods to Mr. Oliphant.)

Oliphant: One of the important things going on its way through the shop now is a proposed veto message for the Railroad Unemployment Insurance System. It passed through my shop.

McReynolds: Danny Bell has it. We gave them the dope. The Security people were over yesterday, and the Labor Department was over yesterday too. We're suggesting that it's not good legislation.

H.M.Jr: Will you take the chance of telling me about it sometime today? I don't know a thing about it. Will you? I'd like to know about it.

McReynolds: Molly Dewson came over to see me last week - Friday and Saturday - and told me she had talked to the President about it before he left. On the assumption, see - as soon as the bill went through the House - since it was Pat Harrison's bill I knew it would go through the Senate - I phoned the Security Board and told them I thought they ought to be considering it. She talked to the President before he left - told him they would be inclined to recommend that it not be approved.

H.M.Jr: Still, I'd like to know a little bit about it. Anything else?

Oliphant: I have here a report on the Associated Gas and Electric.

H.M.Jr: I'd just like to be amused - to know who the latest lawyer is.

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Herman, do I do anything with that (letter)?

Oliphant: No.

H.M.Jr: Huh?

Oliphant: (Nods "No.") It's one of those requests for an opinion.

H.M.Jr: What do I do with it?

Oliphant: Let me have it. There is a brief report on the Harrison-Williams tax case if you want to look at that. No other information.

H.M.Jr: Anything else?

Oliphant: No.

H.M.Jr: Mac and Oliphant will just stay, please.

June 21, 1938

At the group meeting this morning the subject of wire-tapping by Treasury enforcement agencies was discussed and the Secretary invited Mr. McReynolds and Mr. Oliphant to remain after the meeting for further discussion of the subject. They did so and Mrs. Klotz was also present.

Mr. McReynolds said to the Secretary, "I am carrying out your orders, Mr. Secretary. You told us to 'let Nature take its course' and to do nothing as far as the pending legislation was concerned and I told my men to carry out your wishes." He added, "I understood that Mr. Oliphant was going to do the same. As a matter of fact, Mr. Oliphant told me that he had so informed Senator Wagner, but I understand that Mr. Foley went to see Senator Wagner and told him to call Mr. Oliphant."

At this point Mr. Oliphant became very angry and said, "If Foley went up to see Wagner and made the suggestion that he, Wagner, call me, I knew nothing about it."

The Secretary inquired what the Department of Justice was doing about wire tapping and when neither Mr. Oliphant nor Mr. McReynolds could give him the information, he telephoned to the Attorney General and a record of their conversation is attached.

HM, Jr. then gave Mr. McReynolds the following order: "After July 1, I want the Treasury Department enforcement officers to wind up all wire tapping cases and if they feel that there are some very extraordinary cases where wire tapping is necessary, I want to know about them myself and unless I give my personal permission I want them to stop all wire tapping."

* * *

Attached is Mr. McReynolds' memorandum to Mr. Graves incorporation the above instructions of the Secretary.

* * *

Mr. McReynolds came in to see Mrs. Klotz later

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in the day and gave her the following information.

Mr. Oliphant sent Mr. McReynolds a copy of the memorandum which he had sent to the Secretary reporting his telephone conversations with Senators Wagner and Wheeler. (Copy is attached hereto.) In the meantime, however, Hester came in to see McReynolds and told him that he was sitting in Oliphant's office when Senator Wagner called and heard Oliphant tell Senator Wagner that the Secretary wished to have the bill killed. Upon hearing this, Hester said he interrupted Mr. Oliphant to remind him that it was his (Hester's) impression that the Secretary wanted to "let Nature take its course". Mr. Oliphant then told Senator Wagner that we did not want to influence the legislation one way or the other.

Mr. McReynolds also told Mrs. Klotz that Hester had told him that Foley went to see Senator Wagner and told the Senator to call Mr. Oliphant. In other words, this was Oliphant's way of keeping faith with the Secretary and not contacting the Hill, but the Hill contacted him.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

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DATE

TO Secretary Morgenthau
FROM Herman Oliphant

June 16, 1938

For your information

At 12:17 this morning, Senator Wagner called me. He was a good deal exercised about the wire-tapping bill which had passed the House and had gone back to the Senate because of a House amendment. He referred to the dispute in New York and said he, personally, felt there should be no wire-tapping without a court order in advance of such tapping. I told him that, while the Department was convinced of the soundness of the pending bill, it was standing aside so far as this legislation was concerned in view of the great importance which the subject had assumed because of recent developments, such as those in New York. He asked if he might tell this to Senator Wheeler, and I told him he could.

Within a few minutes, Wheeler called me and I repeated to him that we were standing aside so far as this legislation was concerned. Wheeler said that he would not push the bill as he had no special interest in the matter since he had been handling it for us. I expressed to him appreciation of his helpful cooperation on this and other matters.

Tuesday
June 21, 1938
10:13 a.m.

HMJr: Hello.

Operator: The Attorney General.

HMJr: Hello.

Homer
Cummings: Hello, Henry.

HMJr: How are you?

C: Grand. How are you?

HMJr: I'm all right.

C: That's good.

HMJr: Ah - Homer - ah, in view of what happened on our so-called "wire-tapping" bill in Congress...

C: What's that?

HMJr: In view of what happened on the Hill in regard to the "wire-tapping" bill...

C: Yes.

HMJr: ...and every thing else, I wondered whether you'd care to advise us informally on wire-tapping and just what you people are going to do yourselves from now on.

C: Yes, I'll be glad to do that, Henry.

HMJr: I mean I don't want any written - just purely informal.

C: All right. Are you in any particular hurry for it?

HMJr: Ah - no, I mean - I don't....

C: The trouble is I'm going away today - up to New York and will be gone the greater part of the rest of this month. I'll be back about the first of July or the thirtieth of June.

HMJr: No, I'd like to get it cleaned up before - all I'd like you to say to me is - ah - "Henry, I'd stop it," or "I'd continue," or "We're doing it," or "We're not." That's what it amounts to.

C: Well, ah - I can tell you that now.

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HMJr: Would you, please?

C: Yes. Ah - we are cutting it out.

HMJr: You are?

C: Yes, we are. Ah - ah - we haven't done very much of it

HMJr: Yeah.

C: Ah - but - ah - I'm - of course you can continue it in certain - ah - certain places I suppose, but not in the District of Columbia apparently and not interstate and not in States that forbid it by their own law.

HMJr: I see.

C: But in States that are silent on the subject it can be done but it should be done with the utmost discretion and only in rare cases under - where you know a vicious crime has actually been committed. But generally speaking we lay off and officially are out of the game.

HMJr: Well, it's awfully hard - of course, we have been doing it - I mean and - and - ah - and I was going to tell the boys to either continue or stop it.

C: Well, ah - the only thing you can - you can tell them - I've told my people to - I've drawn their attention to the decision of the Supreme Court...

HMJr: Yeah.

C: And told them to abide by the law.

HMJr: Yeah.

C: And then I've left it that way.

HMJr: Well that might mean that Hoover might continue under that instruction.

C: No, he won't. He's been told to obey the law and he'll obey it.

HMJr: I see.

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- C: But - ah - I've always had in mind the possibility that there might be some change of attitude or some new development or some extraordinary situation develop that - ah - there - I might wink at it possibly.
- HMJr: I see. But it'd have to be an extraordinary situa.....
- C: Yeah. So officially we're out.
- HMJr: I see. Well, that - that's all I want to know and I am going to take it under serious consideration.
- C: Yeah. All right, Henry.
- HMJr: Because I think it's (laughs) going to get a hot potatoe.
- C: Yes. Yes, it is. It - in some ways it's rather too bad. Ah - for instance, take a kidnapping case. Suppose we got a - could get a message over the wire from ^{one} kidnapper to another.
- HMJr: Yeah.
- C: It's just too bad.
- HMJr: Well, it's been terrifically useful to us with counterfeiters.
- C: Oh, and - your counterfeiting and narcotic cases and all that - it's been very useful I suspect.
- HMJr: And it's been very useful to your District Attorneys to help make the cases.
- C: Yeah, but you can't use the evidence anyhow, - if you got it. The only advantage in getting it would be to get information that would lead to certain activities but you can't use the - the transcripts of testimony over the wire or anything of that kind. See the courts have ruled that out now under the direction of the Supreme Court....
- HMJr: I see.
- C: - in interstate cases.
- HMJr: Uh huh.
- C: And most of them are.

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HMJr: Well, thanks so much. It's just what I wanted.
C: All right, Henry.
HMJr: Thanks so much.
C: Goodbye.

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MEMORANDUM

June 21st, 1938.

To: Mr. Graves

From: Mr. McRaynolds

I discussed with the Secretary this morning the policy to be followed in the Treasury Department by enforcement officers in the use of telephone taps and other means of supervision of communications in the investigation of criminal cases.

The Secretary directs that after July 1st, no supervision of telephones or other communication lines be undertaken by any Treasury personnel under any circumstances except with his personal approval, which may be given only in very unusual and important cases. Leeway is to be allowed in the period between now and the 1st of July for the purpose of cleaning up cases of this character now under way.

Will you be good enough to promulgate this instruction to all Treasury personnel involved.

MR

June 21, 1938

10:45 am

Present:

Dr. Parran
Dr. Haas
Mr. McReynolds

Dr. Parran: I have a copy of the memorandum here, and have amplified it. The Washington study is already under way.

HM, Jr: What it boils down to is you need \$1,000?

Dr. Parran: Between \$1,000 and \$2,000 will be expended this year and for that purpose we have some balances that will carry.

In this further study which I have recommended to get some basic information concerning nutrition it will cost approximately \$31,000 so roughly for the next fiscal year we need \$40,000. If we are to get the real picture it will take a year to do it.

HM, Jr: You might as well ask for \$50,000 and not have to go back and ask for some more. It's a white collar project, isn't it?

Dr. Parran: Not in any substantial amounts.

HM, Jr: I told Mac to find out how we get this money. Do we get it from Hopkins?

Mr. McReynolds: The only way.

HM, Jr: Does the President have to approve it?

Mr. McReynolds: Yes.

HM, Jr: Does it go: Parran to me to Bell to the President to Hopkins?

Mr. McReynolds: No. The application will have

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to be made to Hopkins; come back to Bell, and then to the President, but what Doc wants is not a white collar project; he wants money to spend as an administrative expense; he wants to hire technical people.

Dr. Parran: On the larger budget, the last page, \$31,000 is for eight physicians.

HM, Jr: Better leave it as you said, \$41,000.

Mr. McReynolds: Of course, Doc has in that bill some money to pay for hospitalization. Only got half of what he asked for. If you can get the Comptroller, as Corry Gill says you can, to pay bills direct for hospitalization, then you have a leeway on administrative expenses that you can pay this out of.

HM, Jr: The President is only going to be here two days. I would like to get it cleaned up this week. What's the first move?

Mr. McReynolds: We had better put in an application for a request for this allocation. Two things he will do: get up a request for this allocation to take care of this project and that will expedite it, and try to get it rough. They may not be able to do it. At the same time I will take up with the Comptroller's office the question of their approving the payment of Hopkins for the hospitalization of the people who are on WPA rolls. If they can pay Public Health on the basis of cost charges out of that, then we don't have to pay out of the administrative allotment.

HM, Jr: Let's do it this way. Make it number one, and when you need a little help, call me.

Dr. Parran: All right.

HM, Jr: But let's see if we can get it through this week.

Dr. Parran: That takes care of one of the two points.

The other is, actual distribution of food. While we do not know the full extent of malnutrition, we know

-3-

there are gross inequities and I hoped we could get the machinery of the Surplus Commodities Corporation working in

HM, Jr.: Let's call up Wallace and ask him to call a meeting and I will come over to his shop.

Dr. Farran: I hope we can move on that front.

HM, Jr.: Are you ready?

Dr. Farran: Yes. And I have written on page 2 the conditions which I think need to be met if Surplus Commodities are to be of any value to relief people. It starts there at the bottom of page 1.

"Through the Surplus Commodities Corporation, purchases of foodstuffs should be made with an eye both to the acuteness of the surplus of a particular food and the nutritional needs of the population. This will require a radical reversion of the policy which has been followed up to this time.

"Of equal importance is to arrange for the orderly distribution of foods. To be of value, the following conditions need to be met:

1. Local relief agencies should know in advance the amount and kinds of food which will be available for distribution.

2. The products will need to be ⁱⁿutilizable form. For example, families cannot use dried skimmed milk supplied in bulk; there is great difficulty even in utilizing white flour because of the lack of other ingredients and of cooking facilities.

3. There should be continuity of food distribution.

4. The amounts of food to be distributed should approximate the additions to the relief diet of the particular locality which are necessary to maintain health.

5. To accomplish the above purposes, it would seem desirable that a medical officer and a person familiar with relief mechanics be attached to the Surplus

-4-

"Commodities Corporation with authority to influence policy and organize procedure in the directions indicated."

Number 5 is particularly important.

HM, Jr: Why don't I call up Wallace? He controls Surplus Commodities.

Dr. Parran: A doctor should be on the Board.

HM, Jr: I would much rather have him there in a consultant's capacity because I would not want any Treasury people on it. Frankly, I don't want to get blamed. If he is there as a consultant and they don't take our advice, it's too bad, but if he is on the Board we can get blamed. We are jointly responsible. As far as the responsibility is concerned, I will leave it there.

Dr. Parran: Do you think orders will be taken unless they are orders from the White House?

HM, Jr: No. I will put it up to them. I will say we would like to come over to your place and talk about it from the standpoint of adequate diet and if I don't get any place I will go to the White House. I thought I would do it this way first.

Dr. Parran: Miss Lonigan made a very good point that someone familiar with the mechanics of relief should be on the Board. Someone familiar with how relief is handled in a particular city should be available to advise on that score. The local relief people have no one to turn to.

(At this point, HM, Jr spoke on the telephone to Secretary Wallace and a record of their conversation is attached.)

Dr. Parran: This money that Hopkins has for direct relief may be a fund which would make this whole thing work, and without it it wouldn't work.

HM, Jr: Yes, but \$10,000,000 out of \$25,000,000 is going for clothing.

-5-

Dr. Parran: I think the most important purpose to put some of that money is to rent a store in Cleveland, put in a social worker, because the whole machinery has broken down. There is nobody in Cleveland handling relief who can get the commodities out to the people.

HM,Jr: I don't think Harry appreciates it and I know Wallace doesn't.

Mr. McReynolds: It should be one of Harry's men and not Miss Lonigan.

HM,Jr: No. No. No, Miss Lonigan should not do it.

Dr. Parran: Not in Cleveland.

Mr. McReynolds: Not any Treasury person. That belongs to Harry Hopkins. Let him take his own responsibility.

HM,Jr: I think you will find that Harry will say that is up to the city administration. He won't touch direct relief. But let's find out.

Dr. Parran: I don't think we can pursue this much further here.

oOo-oOo



IN REPLYING
ADDRESS THE SURGEON GENERAL,
U. S. PUBLIC HEALTH SERVICE
AND REFER TO

TREASURY DEPARTMENT

PUBLIC HEALTH SERVICE

WASHINGTON

June 18, 1938

Memorandum for the Secretary of the Treasury.

Subject: The Nutrition Problem.

Although scientific data are not complete in revealing the full extent of malnutrition in the United States, there is convincing evidence to show that diets of relief and low income families are grossly inadequate in amount and kind of food as compared with the diets of families above the submarginal economic group.

There is adequate evidence, also, to show that the diet of the Nation as a whole is lacking in essential nutritional elements, especially those contained in milk and milk products, green vegetables and wheat germ.

In view of the fact that there is a large surplus of certain foodstuffs in the United States, particularly wheat and other cereals, it should be possible to make these surpluses available to those in need, both directly and through conversion of surplus cereals into milk products and meat. Such a policy certainly is desirable from the standpoint of national health. There are two courses of procedure which in my opinion should be pursued simultaneously:

I. Distribution of Food.

Through the Surplus Commodities Corporation, purchases of foodstuffs should be made with an eye both to the acuteness of the

-2-

surplus of a particular food and the nutritional needs of the population. This will require a radical reversion of the policy which has been followed up to this time.

Of equal importance is to arrange for the orderly distribution of foods. To be of value, the following conditions need to be met:

1. Local relief agencies should know in advance the amount and kinds of food which will be available for distribution.
2. The products will need to be in utilisable form. For example, families cannot use dried skimmed milk supplied in bulk; there is great difficulty even in utilizing white flour because of the lack of other ingredients and of cooking facilities.
3. There should be continuity of food distribution.
4. The amounts of food to be distributed should approximate the additions to the relief diet of the particular locality which are necessary to maintain health.
5. To accomplish the above purposes, it would seem desirable that a medical officer and a person familiar with relief mechanics be attached to the Surplus Commodities Corporation with authority to influence policy and organize procedure in the directions indicated.

II. Further Studies of Nutritional Status and Needs.

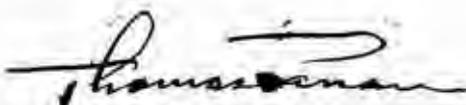
There are three studies which should be made to gain essential knowledge of the nutrition problem.

1. In a separate memorandum I have recommended that a spot study be made in the City of Washington, and in three other cities, of the actual food status among relief and low income families. (Copy attached.)
2. Similar spot studies should be made in several rural areas. Data are now available as an incident to a study of tuberculosis which the Public Health Service is making in one Alabama county and one Tennessee county. These data will be summarized as soon as possible.

-3-

3. A more comprehensive study of the relation of nutrition and physical health should be carried out. (A detailed statement concerning the proposed studies is attached.)

Will you not please indicate whether the above outline of a program of action and a study program meets with your general approval? If so, please indicate the ways in which I can be of assistance in initiating the program of action, and suggest ways of financing the study program.



Thomas Parran
Surgeon General

June 16, 1938

Memorandum for the Secretary of the Treasury.

Subject: Proposed study of diets among low income and relief families.

Following your suggestion, I have considered with my own staff and with representatives of the Bureau of Home Economics and the Milbank Memorial Fund the study of diets among low income and relief families in Washington. It is recommended that this study be extended also to three additional cities -- Detroit, Atlanta, and Omaha.

It is planned to make a spot study of family income, amount spent for food, and actual food consumption in approximately 600 families in each city. About two months will be needed to complete the investigation and prepare a report. Preliminary results from Washington, however, should be available within four or five weeks.

The cost of this study will be \$10,000 and a budget is attached.

It is recommended also that spot studies such as are planned in four cities later be extended to a number of rural areas.

In addition to the studies which are recommended, the nutritional experts point out that the cumulative effects of a poor diet on growth, mental and physical development, resistance to disease, and general health are poorly understood. Recent evidence indicates that there are subclinical and not easily recognized cases of malnutrition which are a result of long continued inadequacies in diet. A detailed statement concerning these more complex and urgently needed studies will be submitted within a few days.

Even before these studies are completed, I hope you and I can continue to press for prompt modification in the policies of the Surplus Commodities Corporation so that the distribution of food can be geared to the obvious relief and nutritional needs in those cities where local relief machinery has broken down.

(Sgd) Thomas Farran
Surgeon General

TP:AMM

BUDGET.

Estimated cost of the collection of 600 schedules in each of the 4 cities — Washington, D.C., Detroit, Mich., Atlanta, Ga., and Omaha, Nebr.

10 enumerators for 2 weeks at \$30 per week -	\$600.00
1 supervisor for 1 month at \$200 per mo. - -	200.00
Incidentals - - - - -	<u>200.00</u>
Total for 1 city - - - - -	\$1000.00
Total for 4 cities - - - - -	\$4,000.00

Estimated cost of the supervision of the field and processing work, and the preparation of a report on the 2,400 schedules to be secured in the four cities:

20 statistical clerks for 5 weeks at \$30 per week - - - - -	\$3000.00
1 supervisor for 2 months at \$300 mo. -	600.00
1 asst. supervisor for 1 mo. at \$200. - -	200.00
Space - - - - -	300.00
Travel- - - - -	1500.00
Equipment and supplies- - - - -	300.00
Incidentals - - - - -	<u>100.00</u>
Total - - - - -	\$6,000.00
Total cost of the study - - -	\$10,000.00

PROPOSED STUDY OF PHYSICAL HEALTH AND NUTRITION

Evidence is not available which shows whether or not, or to what extent, growth and health of the general population is being affected by inadequate diets. It becomes necessary, therefore, to determine precisely what physical and mental impairments might be corrected by the improvement of diets. Immediately useful knowledge on these questions probably can be obtained from studies which include, broadly, the simultaneous investigation of foods consumed and the state of health. The effects of subnormal diets, however, are complex, and probably cumulative. Moreover, these effects can be measured accurately only by very complete individual health and dietary studies, made at intervals over an extended period of time. In addition, it may be assumed that the most pronounced forms of malnutrition appear in children since growth and development impose added dietary requirements.

Satisfactory studies of this character should include the following:

1. Records of food consumption, made either continuously or at frequent intervals during the course of one year. Such records would permit an evaluation of important seasonal fluctuations in dietaries and would reveal the extent to which deficient dietaries are consumed for prolonged periods of time.

-2-

2. Complete physical examinations, including those special measurements and tests which detect the onset of deficiency disease before they have reached their manifest or severe stages.

3. Continuous or repeatedly collected records of physical and mental efficiency during periods of one year. Such data may be expected to reveal the lowered vitality and loss of productivity which may constitute an important manifestation of inadequate diets.

The approach to the general problem of nutrition has two fundamental objectives:

1. To obtain specific information on the actual impairments of health which result from the consumption of subnormal diets.
2. To develop a practical routine methodology for use in appraising nutritional status.

A study, from the perspective outlined above, is proposed as a cooperative undertaking with the Departments of Pediatrics and Preventive Medicine of the Cornell Medical School, The Milbank Memorial Fund, and the Public Health Service. Observations would be collected from students in the Seward Park High School in New York City. This group is selected because the children to be studied are predominately from relief and low income families and because it is known that the school health services can be adapted readily to such a study. Records for the following would be collected:

-3-

1. Dietary histories
2. Records of illness and of school progress
3. Medical histories and physical and dental examinations
4. Special physiological examinations
 - a. Dark adaptation test for vitamin-A
 - b. Galvanic reflex test for calcium
 - c. Anthropometric measurements; height, weight
 - d. Roentgenographs of wrist and hand
5. Special blood examination
 - a. Hemoglobin
 - b. Red blood count
 - c. White
 - d. Differential count
 - e. Ascorbic acid
 - f. Blood vitamin-A
 - g. Blood phosphatase
 - h. Serum calcium

As a preliminary to this investigation, it is proposed to include in the dietary surveys of relief families in Washington, Detroit, Atlanta and Omaha, a physical examination by competent physicians of a sample of the population canvassed. Two physicians in each city would examine approximately one-fifth of the individuals covered by the survey. These physicians would conduct careful physical examinations, together with measurements of height and weight and estimates

-4-

of nutritional status. The results of this supplementary investigation would show only the severe effects of dietary deprivation and will point the way for the immediate corrective measures that may be most urgently needed.

BUDGET.

Salaries	\$25,120.00
8 Physicians (2 months) . . .	\$3,800.00
1 Director	5,000.00
3 Technicians	7,200.00
1 Nutritionist	3,800.00
3 Clerks	4,320.00
Material and supplies	\$ 4,800.00
Travel and per diem	\$ 1,500.00
	<hr/>
Total	\$31,420.00



DEPARTMENT OF THE INTERIOR
BUREAU OF THE BUREAU OF MINES
U. S. PUBLIC HEALTH SERVICE
AND BUREAU OF MINES

TREASURY DEPARTMENT
PUBLIC HEALTH SERVICE
WASHINGTON

June 16, 1938

Memorandum for the Secretary of the Treasury.

Subject: Proposed study of diets among low income and relief families.

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Thomas M. ...
Surgeon General

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Total cost of the study - - -	\$10,000.00

Tuesday
June 21, 1938
11:03 a.m.

HMJr: Hello.

Operator: Secretary Wallace.

HMJr: Hello.

Henry
Wallace: Hello, Henry.

HMJr: How are you?

W: Fine.

HMJr: Ah - I have Doctor Parran here in my office and we would like to suggest that if you would call a little meeting together on the question of adequate diet why Doctor Parran and I'd like to come over.

W: Why, you mean you want to have some of our leaders in, or what?

HMJr: Well, I mean, the

W: You mean several of your bureau chiefs or

HMJr: Well, whoever - I mean it's in connection with the Surplus Commodity Corporation.

W: Oh, it centers around that?

HMJr: It centers around that. And - ah

W: You mean looking into the?

HMJr: Well, the point....

W: ... the quantity of different products?

HMJr: Well, ah - to get - ah - what we'd like to present is Doctor Parran's viewpoint which is a question of adequate diet - ah - and if that could be worked in.

W: Now, we should have some one from Harry Hopkins' outfit 'too?

HMJr: Very much.

W: And who should we have from there would you think? - Aubrey or Harry or?

- 2 -

HWJr: Well, I'd try Harry.

V: You'd try Harry. Yeah.

HWJr: I'd try Harry.

V: All right. And Harry and I suppose Jesse Tapp and - Jesse Tapp and Wilcox?

HWJr: And - ah - I don't know whether - Dr. Stanley I suppose.

V: Oh yes, Dr. Stanley.

HWJr: Yeah.

V: Ah - is Parran with you now?

HWJr: Pardon me? Parran's right here now.

V: Yeah. Now would he - would you ask him if he thinks of anybody who ought to be there?

HWJr: Just a minute. (Short pause)
Dr. Parran says he thinks it's important to have Hopkins but if not whoever is acting for Hopkins.

V: All right.

HWJr: See? Because, now, here's the point which we've got right up here in the Treasury which is - which is - I'd like to discuss at this meeting - bring it up. We do the buying as you know, for Hopkins. He's got twenty-five million for relief and he expects to take now - to take ten million out of that twenty-five for clothing.

V: Yeah.

HWJr: But that would only leave fifteen. Hello.

V: Yeah.

HWJr: So - ah - I mean they're moving awfully fast and if they move in that direction that throws all the more burden on you, you see?

V: Yeah. Well now, we'll try for this some time tomorrow morning and call you back.

HMJr: Well, you want to ?

W: - How are you fixed on tomorrow morning?

HMJr: Well, ah - I could come any time between ten-thirty and eleven-thirty.

W: Ten-thirty - all right. I'll see if Harry can come some time between then and call you back as to what time suits best.

HMJr: And you let us know and I'll....

W: I guess you'd have to be out of here by eleven-thirty, is that it?

HMJr: Well, I - I - well, I could stretch it a little bit. No, I mean, I'll keep - I mean, I'd like to get out from your place not later than twelve.

W: Not later than twelve?

HMJr: Yes.

W: All right.

HMJr: Goodbye.

W: I'll check with Harry and let you know.

HMJr: Thank you.

W: Goodbye.

R+S. 142

June 21, 1938.

My dear Mr. President:

I thought this report on business conditions by George Haas was particularly interesting and quite cheerful.

Yours sincerely,

(His name)

The President,
Hyde Park, New York.

Cc in WA. JHR Hlder

143

Copd - memo

5 sheets

MRS. FORBUSH
ROOM 470

at 4-13

PT

Confidential

June 20, 1938

Secretary Morgenthau

Mr. Haas

Subject: The Business Situation, week ending June 18

Conclusions

The continued rise in commodity prices over nearly three weeks has been accompanied by an upturn in new orders for steel and other products, and by other evidences of an improvement in business sentiment. The almost universal feeling a few weeks ago that business would continue to decline until late summer has been modified by developments which have some appearance of indicating a turn. Among them are the following:

(1) Automobile sales recently have been better than previously expected, and production has been increased for the second successive week.

(2) The rate of steel operations has risen slightly at a season when output would normally be contracting, and a further increase is suggested by an upturn in new orders.

(3) Construction contract awards have recently shown a sharp improvement.

(4) Cotton mill activity showed an increase during May, when seasonal influences would call for a decline, and has improved further during early June.

(5) Freight car loadings continue to rise, especially in the more significant miscellaneous classification, after reaching a low the latter part of April.

(6) Some tendency toward improvement has appeared in certain areas.

(7) The price structure is improving. Sensitive commodity prices are rising, with improvements in the statistical positions of a number of commodities, while steel prices are weakening.

Secretary Morgenthau - 2

New orders improve

Probably influenced by the strong upturn in commodity prices over the past two weeks, new orders during the second week in June turned upward, according to our weighted index, to the highest level since the last week of April. (See Chart 1.) Orders for steel, textiles, and electrical equipment showed substantial increases.

Steel activity higher

A 1-point improvement in the rate of steel operations over the past two weeks, while relatively small (3.8 percent) appears significant since (1) steel operations are usually contracting at this season. (2) The upturn was apparently unexpected in many quarters, since as recently as Monday of this week the Journal of Commerce mentioned that "Youngstown is barely holding to its rate of 25 percent of capacity. The industry is evidently working down to its proverbial low of the year around Independence Day when a pace as low as 15 percent would not be surprising." (3) A further increase seems in prospect, judging from the upturn in new steel orders last week to an equivalent of 37 percent of capacity. The Youngstown district is scheduled to raise operations to 29 percent next week, with a further upturn possible before the end of the week. Steel scrap prices have improved.

A reduction of \$3.00 a ton on galvanized steel sheets, giving official recognition to price shading that had been prevalent for some weeks, is taken in the trade as evidence that buying is beginning to appear in sufficient volume to test the price structure. A further test of prices is expected to come when the automobile companies begin seeking quotations on steel for their fall requirements.

Some improvement beginning to appear

While certain factors in the present business situation continue unfavorable, these are, for the most part, factors which are well known, which have been well advertised, and probably pretty well discounted. Some evidence that they are becoming well discounted appears in the stability of industrial production over the past several months. We have, therefore, thought it advisable in this statement to list the factors which may indicate a coming upturn.

Such indications have recently become more numerous. The increase in new orders in various lines during the second week in June, a tendency toward improvement in the commodity price structure, and a contra-seasonal rise in steel operations, have

already been mentioned. Other favorable factors, of greater or less importance, include the following:

(1) Automobile production this week increased to 41,500 units, the second successive increase from the low output of 27,000 units during the Memorial Day week, as sales in this country and abroad have been maintained at a higher level than previously expected. Production in July is now expected to be not much lower than in June.

(2) Construction contract awards have recently shown a marked upturn, particularly for public works, nonresidential and public utility projects, with residential contracts rising to approximately last year's level.

(3) Reports to the National Association of Real Estate Boards indicate that sales of home sites ready for building have been increasing throughout the country during the past two months, and are now equal to, or greater than, those of last year in the majority of cities.

(4) Production in various consumer goods industries has already turned upward.

(a) Cotton mill activity, which often rises in advance of the general business trend, showed a contra-seasonal increase during May, the FRB adjusted index rising to 81 as compared with 77 in April. The New York Times weekly index shows a further increase in cotton mill activity in early June.

(b) Rising trends in boot and shoe production, and in production of wool and silk goods, have been under way for several months.

(c) Activity in the paper industry expanded during May, and has been maintained to date, apparently marking a turn in the trend. Sales have held up well, and the inventory position has improved.

(5) Carloadings have continued to rise (after seasonal adjustment) from their low reached near the end of April. Loadings of miscellaneous freight, which is believed more significant as an index of business, has shown most noticeable improvement.

Secretary Worgenthau - 4

(6) As a composite measure of recent trends in several business series, the New York Times Index for the week ended June 11 rose 1.5 points from its low for the year reached during the previous week. Continuous seasonal improvement in steel and automobile output suggests a further upturn during the current week.

(7) An upturn in replacement buying of automobile tires has recently been reported, coincident with improved buying of steel and other products. Inventories of tires at the end of April were 20 percent smaller than a year previous.

(8) Increased prices for gasoline indicate that drastic production curtailment is proving effective in remedying weakness in the crude oil and gasoline supply situations.

(9) Industrial production has continued for many months below the level of demand, indicating that inventories have been steadily reduced. A rise of about 10 points in the PNB Index would be necessary to adjust production to the current level of demand.

(10) On the financial side, recent successful flotation of large corporate security issues, a part of which has represented new capital, provide a strong influence toward a revival of business confidence and an increase in industrial buying.

Some regional improvement noted

Business recovery may start, as in 1953, from some important strengthening influence in one section of the country and extend from there to other sections. Some evidence of regional improvement has appeared, though not extensive enough so far to be conclusive.

In residential construction (Chart 2) a marked upturn, in residential awards, as compared with last year, has occurred in the South Atlantic and Middle Atlantic States. In the Pacific district (for which total building permits are shown, since purely residential data are not available) improvement has been under way since December. A well-maintained trend is shown in the East South Central district.

Secretary Morgenthau - 5

Evidence of well-maintained or improving business in these same regions is shown by department store sales. (Chart 3.) While the Federal Reserve districts for which these sales are reported do not coincide with the census districts shown in the previous chart, it will be noted that in the districts covering the South and the Pacific Coast, department store sales have been maintained above the national average. In the Dallas and Atlanta districts an improvement in sales has occurred during May, while the national average was declining.

The improved trends in the South appear to be due partly to well-maintained levels of farm income in the East South Central and West South Central districts, as compared with the previous year. (See Chart 4.)

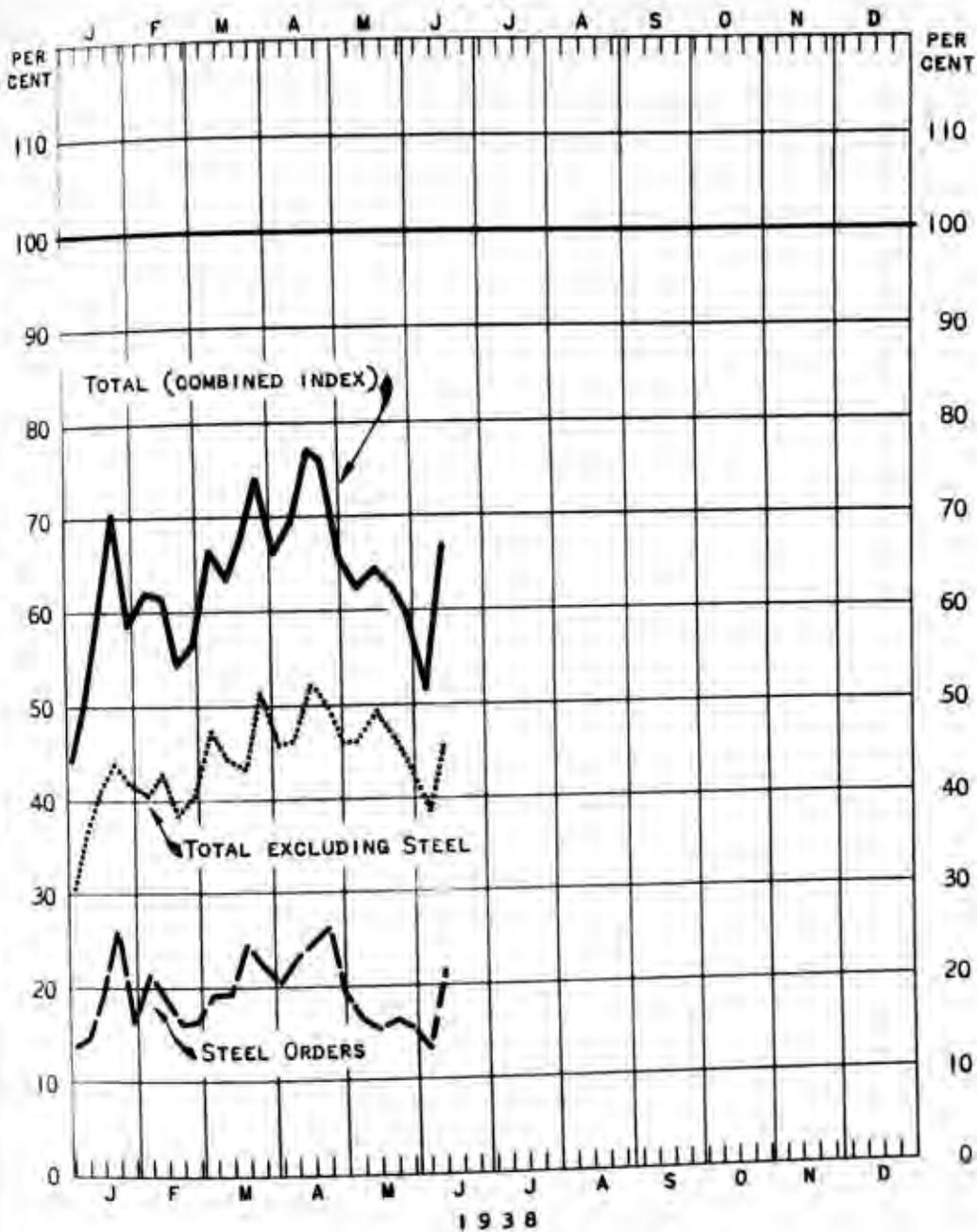
Sales by Sears Roebuck and Company, divided as between metropolitan and rural areas, provide some basis for judging whether an upturn in sales in a given district has arisen chiefly from industrial and commercial or from agricultural sources. (Chart 5.) It will be noted that in District 6, which includes States from Texas north to Nebraska, sales have been best maintained in the metropolitan areas, while in District 8 (lower Pacific and Western States) the sales have been best in rural areas.

INDICES OF NEW ORDERS

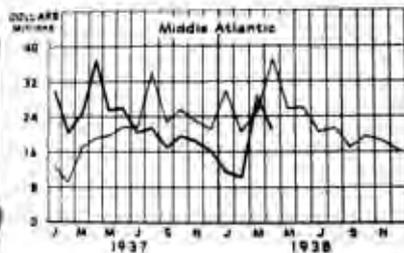
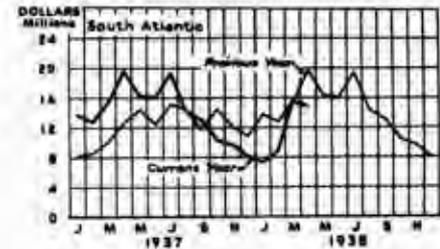
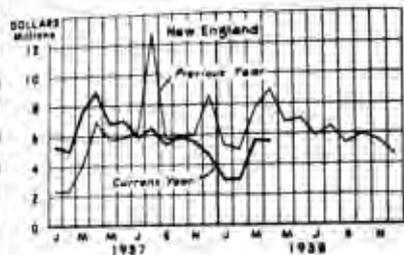
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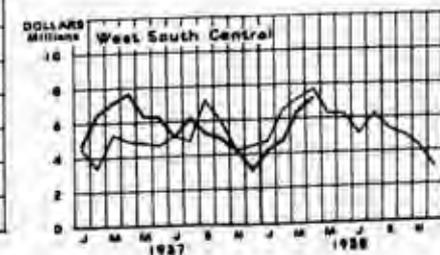
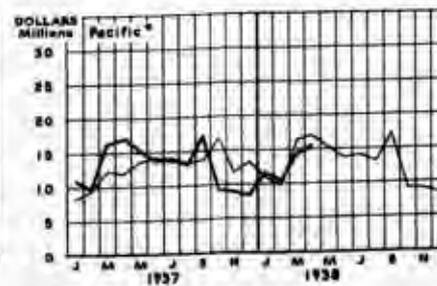
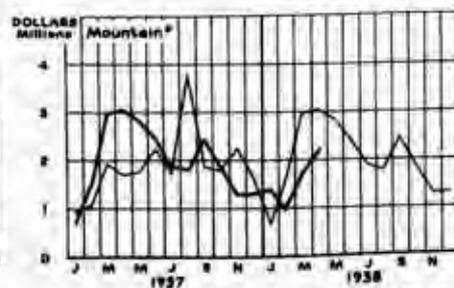
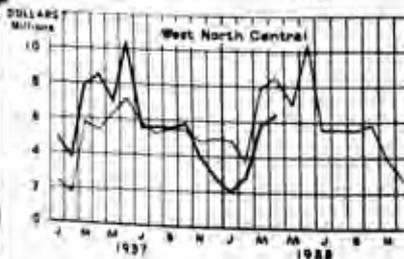
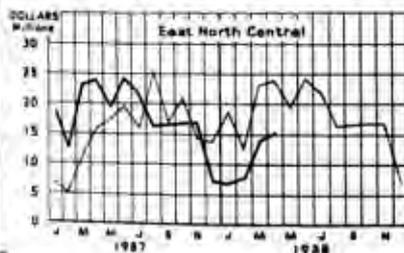
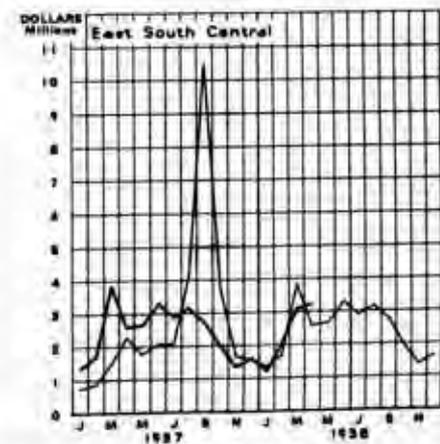
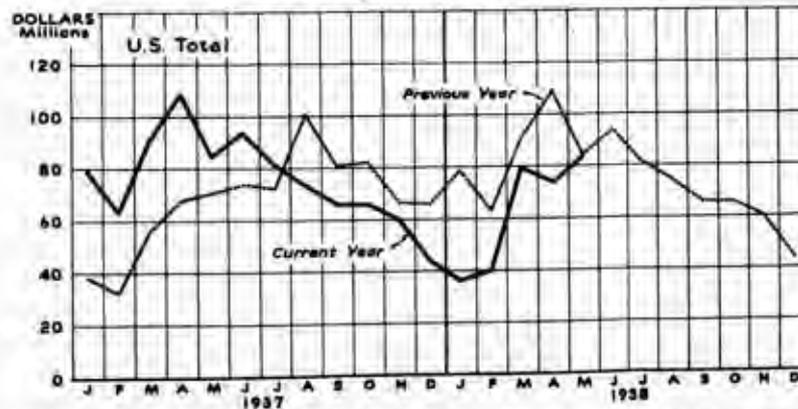
1938



RESIDENTIAL CONSTRUCTION By Census Districts



TOTAL MONTHLY CONTRACTS AWARDED F.W. Dodge, 37 Eastern States

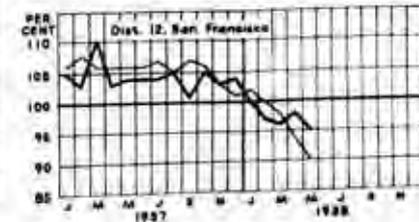
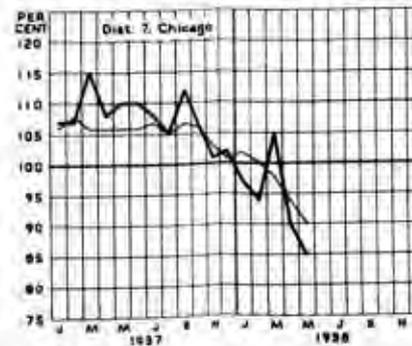
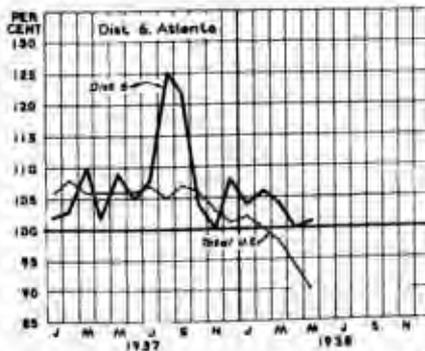
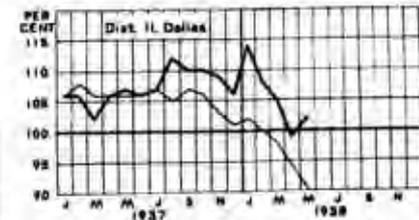
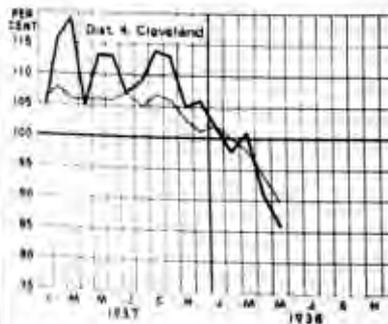
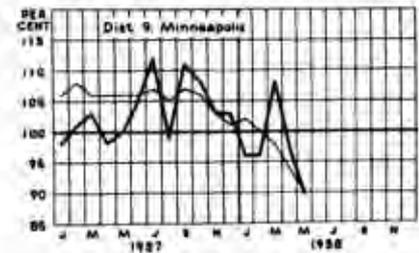
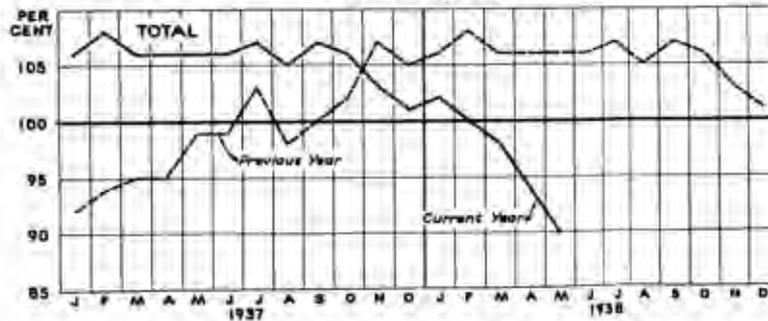
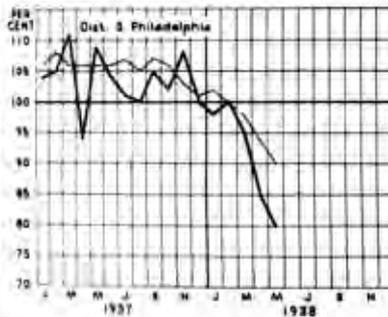
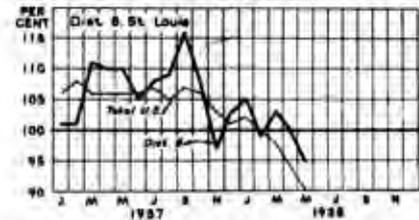
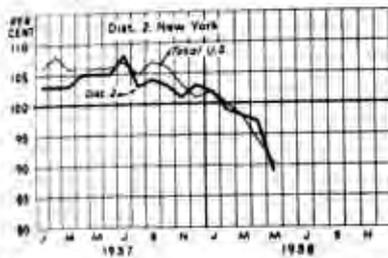


*Total Building Permits

DEPARTMENT STORE SALES By Federal Reserve Districts



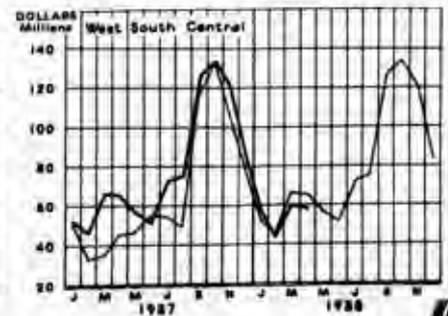
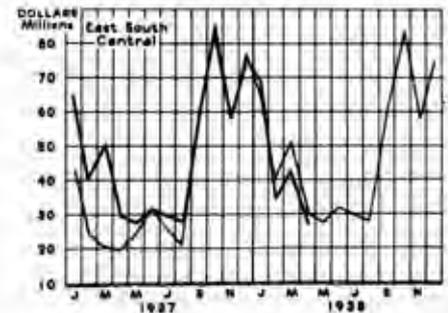
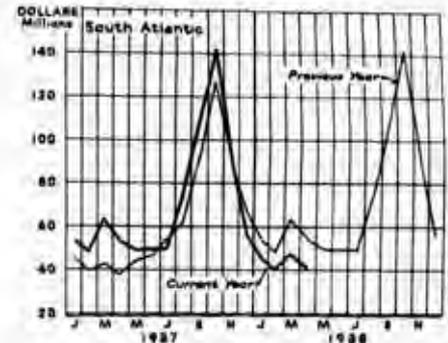
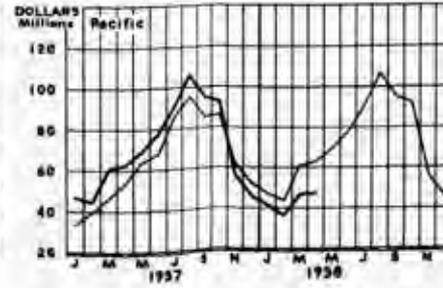
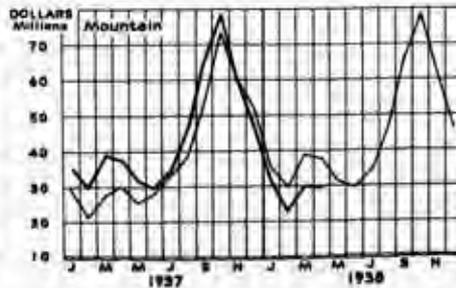
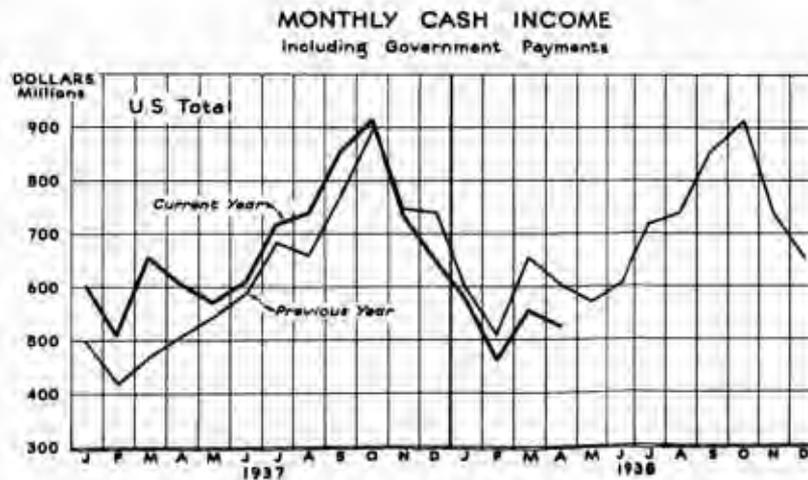
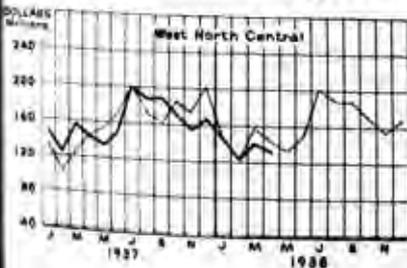
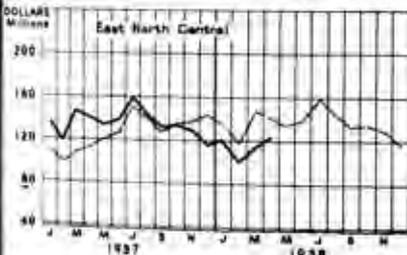
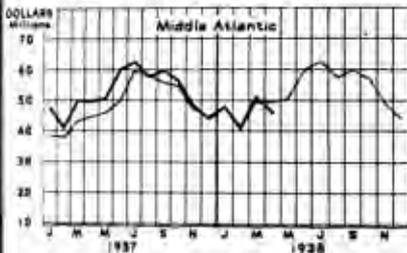
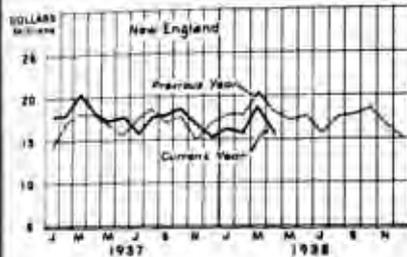
MONTHLY INDEX OF SALES
1936=100, Adjusted



Note: All latest figures are preliminary.

FARM INCOME

By Census Districts



U.S. DEPARTMENT OF THE TREASURY
BUREAU OF ECONOMIC ANALYSIS

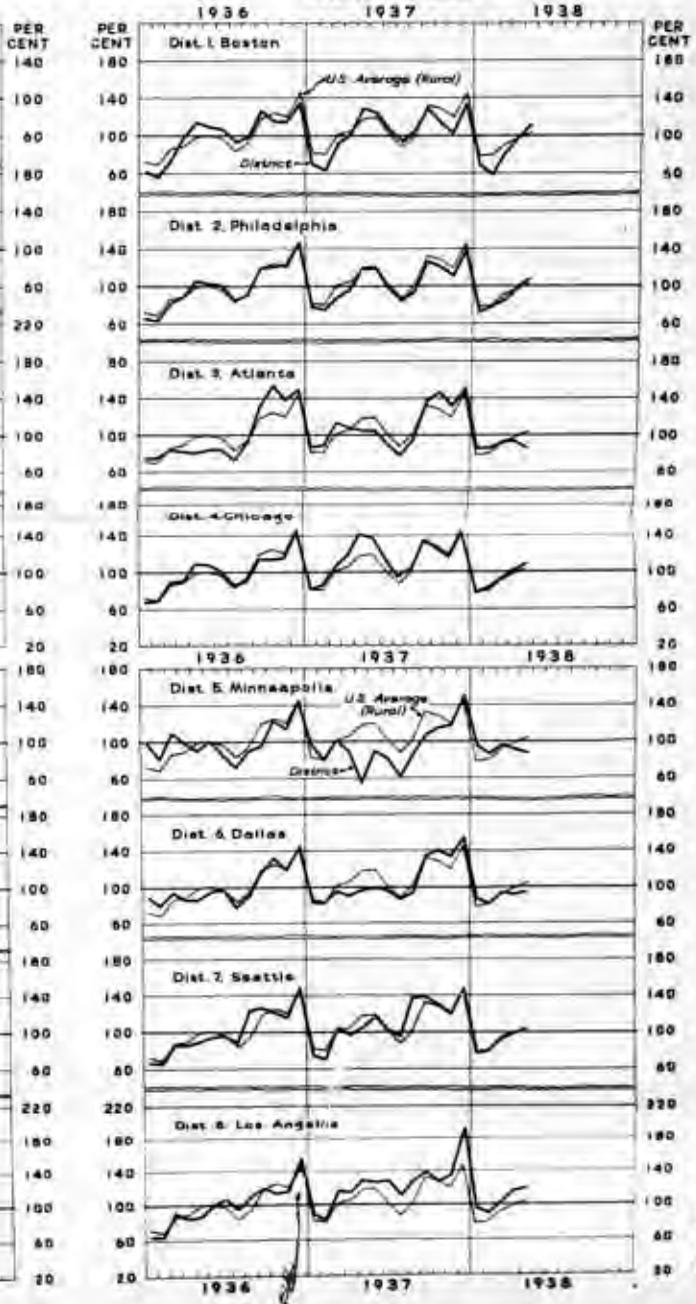
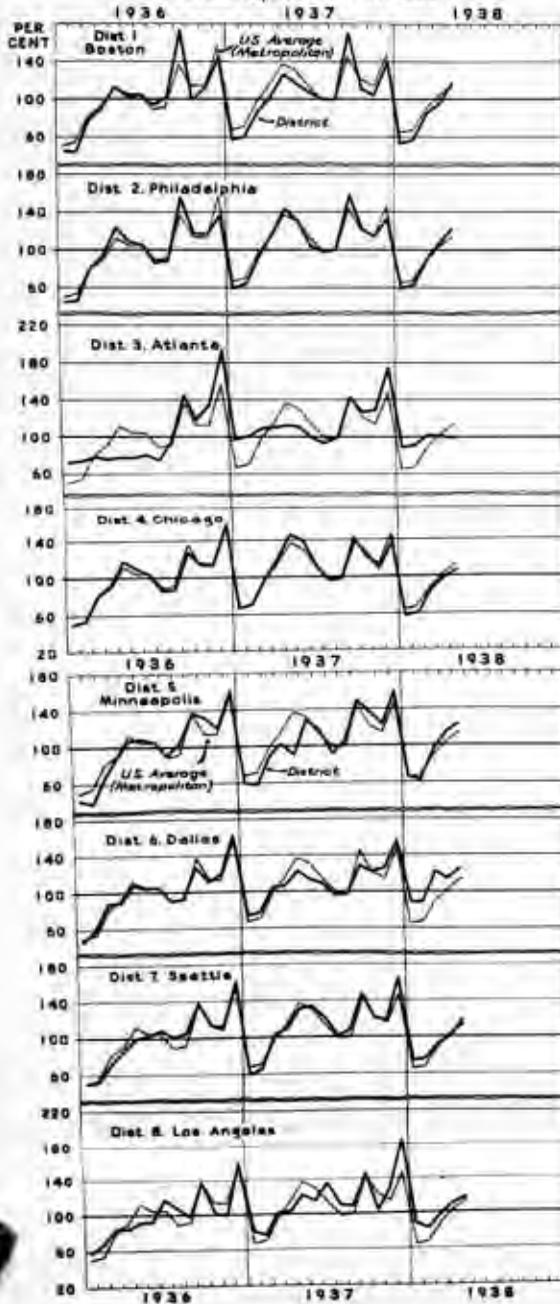
SEARS, ROEBUCK & CO.
 FOUR-WEEK SALES BY DISTRICTS
 Four-Week Average 1936 For Each District = 100

Confidential



Metropolitan Areas

Rural Areas



June 21, 1938.

Dear Mr. Roberts:

I appreciate your giving me the summary of the regular weekly business report to Mr. Bentschler. The information you compressed into a paragraph is most interesting, and I am glad to have it.

Sincerely,

Henry Morgenthau, Jr.

Mr. George E. Roberts,
Vice-President, The National City
Bank of New York,
New York, New York.

GEF/dbs

The National City Bank
of New York

ESTABLISHED 1812

New York June 17, 1938

MAIL ADDRESS CITIBANK

IN REPLYING PLEASE QUOTE INITIALS

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

My dear Secretary Morgenthau:

I take pleasure in giving you the following summary of our regular weekly "high-spot" business report to Mr. Rentschler:

General inventory position making slow but steady improvement. Commodity prices firmer. Steel mill operations steady at 26-27 per cent; other indexes sideways to slightly downward trend. Department stores averaging 17 per cent off; expect further decline during Summer, turn for better about September. General view regarding industrial activity is not much ahead for summer, but moderate improvement consumer goods industries in the Fall with heavy industries continuing sluggish. May building figures encouraging, total contracts ahead of last year due to public works; residential even with last year. Crop prospects pasture conditions favorable on the whole but wheat estimates considerably reduced due to low threshing outturn and crop damage. Bonds firm except rails weaker on failure relief legislation.

Respectfully,



Geo. B. Roberts
 Vice-President

June 21, 1938

10:35 a. m.

Mr. Helvering, Mr. McReynolds, Mr. Schoeneman and Mr. Graves met with the Secretary.

Mr. Helvering called to the Secretary's attention the fact that the Bureau had discovered, on a review of the production in the various Collector's offices, that some adjustment would be necessary as they were overmanned, particularly with clerical employees and deputy collectors, due to the fact that Social Security returns are now being made quarterly instead of monthly. Helvering said that it was necessary, therefore, to revise the allocation of funds to the collectors who have been put on notice that they would have to come down to that level and instructed, in reducing their personnel, to drop the people least competent. Helvering also said they had received compliance from 34 offices out of 64.

The Secretary said he was receiving some complaints and was fully aware of the fact that there was going to be "a little rough going", but he told Mr. Schoeneman "Go to it; you have the Commissioner and me behind you."

Mr. Schoeneman left the Secretary's office.

Mr. Helvering gave the Secretary, for his information, a copy of the attached memorandum on Mellon's case. He said he had also given a carbon to Oliphant.

The Secretary reminded Mr. Helvering that the Treasury was giving out a statement on this matter at ten o'clock. McReynolds reported that Mr. Helvering was entirely familiar with the contents of the statement.



TREASURY DEPARTMENT

WASHINGTON

June 16, 1938.

Memorandum to the Secretary:

There were two major issues involved in the Richard B. Mellon Estate; (1) whether certain transfers of property by the decedent were made in contemplation of death, and (2) the value of the common stock of the Aloxite Corporation (a holding company) which was involved in those transfers.

The Bureau took the position, to which it adhered in the final settlement, that certain transfers, particularly those including the stock of the Aloxite Corporation, were made in contemplation of death and that the value of the stock thus transferred was greatly in excess of the value placed thereon by the executors. The executors had the assets of the Aloxite Corporation valued by the Standard Statistics Company which, after an extended investigation lasting 22 months, arrived at a valuation for the Aloxite Corporation stock of \$54,000,000.00. In the final settlement effected with the executors, this stock was given a valuation of \$75,499,053.11.

The tax shown by the executors' return was \$1,743,343.89. The tax determined by the Bureau before allowance for credit on account of payment of State inheritance taxes, amounted to \$37,567,802.59. The deficiency in tax thus determined after allowance for inheritance tax credit amounted to \$22,500,000.00. The additional tax collected as a result of this deficiency, with interest thereon, amounted to \$25,437,959.12.

In my opinion the settlement effected in this case would not have been so favorable to the Government had it not been for the wide publicity given to the income tax case of Andrew W. Mellon. The moving consideration which, in my opinion, prompted the representatives of the R. B. Mellon Estate to accept the Government's determination was a very distinct understanding I had with a representative of Richard Mellon, Jr., that there would be absolutely no publicity given to the case.


Commissioner.

TREASURY DEPARTMENT

Washington

FOR IMMEDIATE RELEASE,
Tuesday, June 21, 1938.

Press Service,
No. 13-69

Commissioner of Internal Revenue Guy T. Helvering announced today that, by agreement with representatives of the taxpayer, a stipulation has been filed with the Board of Tax Appeals accepting settlement in the amount of \$485,809.49, plus interest of approximately \$182,220, or a total payment of approximately \$668,000, on account of deficiencies in tax payment by the late Andrew W. Mellon for the calendar year 1931. The stipulation involves agreement that no appeal in this case will be taken either by the Government or by the taxpayer. Action on the same basis has been taken in the cases of the estate of R. B. Mellon, C. D. Marshall and H. H. McClintic.

Under decision of the Board of Tax Appeals a deficiency of \$403,053.85 was found in the case of Andrew W. Mellon involving tax liability for the year 1931. While the Government had under consideration the appeal of this decision representatives of the estate of the taxpayer conceded the principal question of law that would have been involved in such an appeal.

Deficiency in Andrew W. Mellon's tax payment for the calendar year 1931 was asserted by the Bureau of Internal Revenue in March, 1934. Hearing of the case by the Board of Tax Appeals began in Pittsburgh on February 18, 1935, and was concluded at Washington on February 12, 1936. The Board's opinion was promulgated December 7, 1937, and the final order was entered on March 24, 1938.

The facts elicited and the precedents set in the Mellon case have been of great importance to the Bureau in the determination of other cases. As a result, deficiencies have been asserted and collections made in amounts much larger than those involved in this case.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

100

DATE June 21, 1938

TO Secretary Morgenthau
FROM Herman Oliphant

For your information -

Under the pending Work Relief Bill two opportunities for a grade-crossing elimination program present themselves:

(a) Under Title I of the bill, \$484,500,000 (which may be increased by not to exceed 15%, i. e., \$72,675,000 through the transfer of amounts from other classes of projects) is made available to WPA for "highways, roads and streets." These projects will be constructed with WPA labor - the rights-of-way and materials to be provided by local public sponsors. Assuming the Comptroller General holds this language to be broad enough to include grade-crossing eliminations, it would appear that a considerable grade-crossing elimination program could be developed in the rural areas where the rights-of-way costs would not be substantial. However, it is doubtful if much of a program of this character could be put under way in the metropolitan areas where the rights-of-way costs are considerable and the delay incident to the acquisition of the land considerable.

(b) Under Title II of the bill, \$965,000,000 is made available to PWA to be used, among other things, for loans and grants to States and public agencies. The projects to be financed in this way are limited to useful public works of the kind and character heretofore financed by PWA. This language is broad enough to include grade-crossing elimination projects. However, the extent of the program would be limited to the number of applications for loans and grants for such projects received by PWA from eligible borrowers and grantees. An additional deterrent is a provision in the laws of some of the states providing for a substantial proportion of the cost to be borne by the railroad whose right-of-way would be improved (the New York Constitution requires 50% of the cost to be borne by the railroad, and the remaining 50% to be apportioned between the State and the county or city in which the grade-crossing to be eliminated is located). In the present state of railroad finances there would appear to be little likelihood of very many roads being able or willing to add to their already overburdening debts for this purpose even though the money may be borrowed by the roads from the RFC. In the

- 2 -

metropolitan areas it is possible that there may be a few large grade-crossing elimination projects which the cities and counties can finance with the help of the railroads. However, only a relatively small proportion of the PWA money has gone for grade-crossing elimination in the past and there appears to be little likelihood of a very sizeable program of this character under the pending bill.

As of June 1, 1938, the Bureau of Public Roads had \$78,000,000 available for grade-crossing work and an additional \$20,000,000 becomes available from the regular appropriation on January 1, 1939. This agency contemplates a program of approximately \$98,000,000 for grade-crossing elimination during the next twelve months. According to Captain Curtis of the Bureau of Public Roads a grade crossing elimination program of approximately \$57,000,000 was carried on by that agency during the twelve months previous to June 1, 1938.

Per Foley

HO
✓

June 21, 1938.
11:05 A.M.

H. M. Jr: Hello. Hello. Hello.
Put it on this line.

Operator: Go ahead.

H. M. Jr: Hello.

Jesse
Jones: Good morning, Henry.

H. M. Jr: Hello, Jesse.

J: I wonder if you wouldn't tell Marshal and Upham
to get those things ready. I'll call you about
ten and ask you to send me copies --

H. M. Jr: Yes.

J: He said that Kelly hadn't come down and he'd
written Kelly to redraw them.

H. M. Jr: Yes. I haven't got one yet either and I've been
waiting.

J: So he said he thought he'd actually redraw them,
and I suggested that he go ahead and do it.

H. M. Jr: Who's going to - who's doing the work?

J: Marshal.

H. M. Jr: Oh.

J: His lawyer, Kelly, was going to do it, he said,
but Kelly hadn't come down, so Marshal volunteered
that he would come down and do it.

H. M. Jr: I see.

J: And so he - I thought that you'd jog him up a little
maybe that - you needn't tell him that I told you -

H. M. Jr: I know. Now, what are your plans for us today?

J: Well, I'm coming over whenever you say.

H. M. Jr: Well, are you coming over at 2:30?

J: Yes.

H. M. Jr: What?

J: That's when you asked me.

H. M. Jr: Yes.

J: All right.

H. M. Jr: And, I'll - I'll do this at once.

J: Yes.

H. M. Jr: And I'll call Diggs at once, and say that you and I are waiting for a copy.

J: That's right because I need to study them a little before we get over there, you see.

H. M. Jr: All right.

J: And then -

H. M. Jr: Do you think we should get together before that?

J: Well, I might come a little earlier.

H. M. Jr: Why not come, say, two o'clock?

J: Well, I'll try to do that. What - have you got a luncheon engagement?

H. M. Jr: Well, I- I kept it open for you.

J: You did, eh?

H. M. Jr: Yes.

J: Well, why don't I come about 1:30? For lunch - Would that be too bad for you?

H. M. Jr: I'll split the difference with you - 1:15.

J: Well, I'll try to make it 1:15 then.

H. M. Jr: All right.

- 3 -

J: And we'll have lunch and just go right on in to the meeting.

H. M. Jr: Right.

J: All right - thanks.

H. M. Jr: All right.

J: Good bye.

June 21, 1938.
11:07 A. M.

- H. M. Jr: Jesse just called and he said he's sitting there waiting for the revised report of the Comptroller's Office. He can't get a copy. He doesn't want Marshal Diggs to know that he called me, but he's sitting there waiting.
- Cy Upham: Yes. I don't even have one yet myself. I sent him the - the
- H. M. Jr: Well, put the --
- U: The material on banking examination.
- H. M. Jr: Well, put the heat on, will you?
- U: Yes.
- H. M. Jr: Just see that Jesse gets one.
- U: O. K.
- H. M. Jr: And Jesse is coming to our meeting at 2:30
- U: Yes.
- H. M. Jr: What about -
- U: I'm afraid Jesse's going to be sympathetic in some particular with Harriner.
- H. M. Jr: Well -
- U: But maybe not.
- H. M. Jr: Better have them ^{all} here - they're/appointed by the President.
- U: Sure, sure, O. K.
- H. M. Jr: And, what about this fellow from Chicago? Is he coming?
- U: Who? -- I don't know anything about anybody from Chicago.
- H. M. Jr: Oh, the fellow with the Polish name.

U: Szymczak?

H. M. Jr: Yes.

Oh, Ronald said he would ask him.

H. M. Jr: Oh.

I couldn't get Marriner.

H. M. Jr: Well, I can't -

Ronald said they'd include him.

H. M. Jr: Well, we'd better ask Jesse here and then he's on
the inside --

Yes, O. K.

H. M. Jr: And I'd rather have him on the inside than on the
outside.

OK. O.K.

H. M. Jr: And when you get that thing, let me know.

All right.

H. M. Jr: Thanks.

June 21, 1938.
1:15 P. M.

H. M. Jr: Hello.

Operator: Mr. Ransom.

H. M. Jr: Hello.

Operator: Go ahead.

R: Good morning.

H. M. Jr: Hello, Ronald.

R: Yes.

H. M. Jr: Henry Morgenthau.

R: Yes.

H. M. Jr: Two things: I've got the new revised regulations for Comptroller.

R: Yes.

H. M. Jr: I just got them a few minutes ago.

R: Yes.

H. M. Jr: I want to get them over to you fellows so you can have a look at them before.

R: Yes.

H. M. Jr: And as near as I can tell, they've gone a long way --

R: Yes.

H. M. Jr: Towards meeting what you fellows have in mind.

R: Yes.

H. M. Jr: In fact, I think that as far as I can tell, with one small exception they've almost got everything, see?

R: I see.

- 2 -

- H. H. Jr: Now, we had a meeting last night and I think they've gone a long, long way.
- R: Yes.
- H. H. Jr: I wanted to give this thought, /I think you and I see ^{because} eye-to-eye on this thing, -- I mean, trying to work this thing out. Supposing this - supposing this is 75% of what you fellows want.
- R: Yes.
- H. H. Jr: 75% of what Jones wants, see?
- R: Yes.
- H. H. Jr: Why couldn't we go along and then say we'd meet after Labor Day and take another look at them again?
- R: At the regulations?
- H. H. Jr: At the whole business.
- R: At the whole thing?
- H. H. Jr: Yes.
- R: Not a bad idea.
- H. H. Jr: I mean, just let's say that this is - I think what my boys tell me that this was 75% of what you fellows wanted, maybe 90%.
- R: Yes.
- H. H. Jr: Now, we're not God Almighty. We can't sit down and write a - hand out the last word on anything.
- R: Not yet.
- H. H. Jr: And what I say is take a look at the thing, is this 75% agreeable? We're all supposed to be working for Mr. Roosevelt. And then, we can say, well, we'll take another look at it after Labor Day.
- R: Yes.

- 3 -

H. M. Jr: That -- I -- In that sp^{irit} I'm going to approach the meeting this afternoon.

R: Yes.

H. M. Jr: And I wanted to give you that thought before you came over.

R: All right. Now you're going to send your re-draft of regulations right away?

H. M. Jr: I'll have it there - where - could you tell me where - a messenger will leave here in ten minutes.

R: All right. If he'll bring it to my office it'll be brought to me at once.

H. M. Jr: Well, let me ask Cy, he's sitting here --

R: Yes.

H. M. Jr: He'll send a messenger. It will leave at once.

R: I'll send the messenger to Cy's office or to yours?

H. M. Jr: No, he'll come to your office.

R: The messenger will come to my office.

H. M. Jr: At the Federal Reserve.

R: All right then, I'll submit it to the Board immediately.

H. M. Jr: Thank you.

R: All right.

C
O
P
Y

June 21, 1938

Dear Henry:

I hope the finer sensibilities of your nature were not offended by the picturesque language to which you refer.

It may be possible to revise the record when I see a transcript of the proceedings.

Sincerely yours,
(Signed) Jesse H. Jones

The Honorable Henry A. Wallace
Secretary of Agriculture
Washington, D. C.

PERSONALHankow, China.
June 21, 1938.

Dear Mr. Morgenthau:

Since returning to China, I have often thought of you and recalled with appreciation the hospitality which you were good enough to extend to me during my visit in America last summer. Often I think of writing to send you my greetings and remembrance, but unfortunately my multifarious duties leave me hardly any time to myself. As Mr. J. Lossing Buck is soon returning to the States, I take great pleasure in sending you this message which I hope will find you in the best of health and spirit.

I need hardly reassure you that I appreciate the ready co-operation which your Government has, through you, extended to us during the past years towards the realization of our monetary reform. Especially thankful I am for your efforts in making possible further progress in our co-operation through the new arrangements which you and I had the satisfaction to make personally last summer. Your sympathetic interest and friendly assistance towards our financial problems, further evidenced by your continued purchases of silver, have been of considerable help to us at this difficult time, and I want you to know that I remember them.

Japan's invasion came when our progress in economic and financial reconstruction had acquired a momentum that was remaking the country and making it a stronger factor in the world situation. For one thing, the success of our currency reform had brought great benefits not only to our own people but also to others who traded with us. Undoubtedly, the interruption of our progress in self-development by Japan's undeclared war must be considered a great tragedy in history.

Nevertheless, China's finances have stood up well under the strain imposed by the hostilities and we are courageously and resolutely facing the urgent problems that confront us. In spite of the hostilities, we had been able to hold our currency at a stable level for months until recently the Japanese attempted to sabotage our credit structure. By instigating the puppet regime in helping to establish the so-called "Federated Reserve Bank", issuing notes with a nebulous reserve and not freely convertible into foreign currency, Japan's financial strategists sought to force their yen notes and the worthless puppet notes on the Chinese people in the occupied areas and to take advantage of our source of foreign exchange by exchanging the Chinese legal tender notes for foreign currency. At the same time, they created rumors to disturb our money market and shake our credit. Shanghai, which is infamous for rumor-mongers and speculators, easily fell prey to this sinister Japanese scheme. However, with new measures adopted by the Government to prevent speculation and combat the Japanese plot of sabotage, I believe the recent decline of our currency will soon prove a passing phase.

The Hon. Morgenthau, Jr.--page two

At the same time, we are forging ahead with our reconstruction program, notably the relief of agriculture, the development of industries in the interior, the promotion of export trade, and the building of highways and railways. In this connection, I remember you have asked Mr. Buck to inquire whether the Burma road is being built. I am glad to inform you that we are not only building the highway to Burma but are also proceeding with our plans to construct a railway connecting that territory with our Southwest.

While we cannot minimize the urgent problems we have to face in the successful prosecution of this protracted war, we are fully aware of the still greater ones that will arise at the end of the present hostilities. We are accordingly planning ahead, and when that day comes, China's need for foreign capital and technical assistance will yet be greater than ever before.

I am glad to note that the American Government and people have gradually come to appreciate the real menace of Japanese aggression, not only to China's integrity and existence but also to America's vital interests and security in the Pacific and even on the American Continent. Rightly they have become more positive in their condemnation of Japan's lawlessness and militarism and in their faith in China's cause. To-day the victim of Japanese aggression is the Chinese people; to-morrow it will be Japan's next nearest neighbours if her mania for war and destruction is not checked in time. I cannot overemphasize that close co-operation among peace-loving and democratic nations is the only means to preserve world peace and collective security. To enjoy peace we must have the foresight and courage to defend peace. To-day China is taking a courageous stand against the onward march of brutal force and ruthless barbarism. Can the isolationist policy or the Neutrality Law protect America from this common menace? My American friends tell me that 70% of America's people are in sympathy with China's cause. If that is the case, it should give your Government a strong backing with which to strengthen its policy towards the Japanese aggression. China does not ask any nation to fight this war for her. But if sympathetic nations will only take a firmer line of action, I believe even Japan's mad militarists will have to pull in their horns.

May I close by requesting you to convey to your illustrious President my kindest personal greetings and heartfelt gratitude for the many expressions of his sympathy and assistance in our national cause? The same I extend to you together with my best wishes for your continued success and health.

Sincerely yours,

W. L. KUNG

The Honourable Henry Morgenthau, Jr.
Secretary of Treasury
Washington, D. C.
U. S. A.

MEMORANDUM

June 21, 1938.

TO: Secretary Morgenthau
FROM: Mr. Gaston



SUBJECT: A Comparison of the Volume of Business of the Federal Reserve Banks and the Farm Credit Administration.

While the Farm Credit Administration has sometimes been described as "A Federal Reserve System for the Farmer," the character of the business of the two institutions is so different that comparison is difficult.

The Federal Reserve banks at present operate as (1) Banks of issue, (2) Depositories for member bank reserves, and (3) Fiscal agents of the Treasury. Their lending function under present conditions is unimportant.

As of May 25 all Federal Reserve banks had on deposit reserve accounts of member banks in the amount of \$7,716,352,000. "Total Reserve bank credit outstanding" as of that date was given as \$2,583,138,000. But this included United States Government securities owned by the banks in the amount of \$2,564,015,000, so that credit actually extended to the member banks and through them to the business of the country amounted to only \$19,123,000.

In their function as banks of issue, the Federal Reserve banks had outstanding on that date Federal Reserve notes in the amount of \$4,116,875,000. While the law permits the pledge of commercial paper and United States Government securities behind Federal Reserve notes and requires only 40 percent backing in gold certificates, the fact is that at the present time the amount of Federal Reserve notes outstanding is more than 100 percent secured by gold certificates and the banks hold gold certificates and gold certificate credits in an amount more than double the outstanding Federal Reserve notes.

The total loans and investments of all reporting member banks of the Federal Reserve System as of April 30 were \$20,819,000,000. The relation of member institutions of the Farm Credit System to the Farm Credit Administration is quite different from that of the member banks to the Federal Reserve banks. In the case of the land banks, their capital is in part subscribed by the Government and their source of loanable funds is principally the sale of obligations through the central offices of the Farm Credit Administration. In part, these

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obligations are guaranteed by the Government and those not guaranteed are in practical effect Government obligations. Commissioner loans are made from public funds. Quite similar relations exist as to other organizations in the System, so that all loans of the various organizations in the System may be considered as Farm Credit Administration loans. The total of these loans to farmers and farmers organizations as of December 31, 1937, was \$3,538,000,000, as compared to the outstanding credit of the Federal Reserve banks of approximately \$19,000,000.

The itemization of loans of the Farm Credit Administration as of December 31, 1937, is as follows:

Land banks	2,035	millions
Commr. loans	813	"
Prodn. Credit Assns.	138	"
Banks for Coops.	88	"
*Int. Credit Banks	177	"
Crop and Feed	115	"
Drought relief	57	"
R. A. C. C.	16	"
Revolving Fd. Ag. Mkt. Acct.	99	3,538 millions

*Exclusive of Production Credit rediscounts.

June 21, 1938.
2:19 P. M.

H.M.Jr: Hello, George Haas?

George
Haas:

Yes, sir.

H.M.Jr: You know, George, this thing of having a meeting and the finding of what the revenue is going to be was just in the middle of what may be an improvement in business.

H: Yes.

H.M.Jr: I think it's silly.

H: Yes, it's very difficult.

H.M.Jr: And - I don't - who the hell wants this anyway?

H: Well, Bell wrote you a letter as Director of the Budget asking that he have the estimates by the 25th of the month.

H.M.Jr: Well, he can't have them until after the first of July.

H: Uh huh.

H.M.Jr: And I'm not going to give them to him.

H: Uh huh.

H.M.Jr: And I - I'll meet with you fellows after the Fourth of July and we'll take a look at it.

H: O. K.

H.M.Jr: And this means that we're right in between.

H: O. K. But you're right - it's very difficult.

H.M.Jr: Oh, it's silly, George.

H: Yes, I know, But I'll just - I'll

H.M.Jr: You can tell Dan I say it's a silly thing, and after the Fourth of July we can take a look at it.

- 2 -

H: Yes.

H. M. Jr: We'll take a look at it and by that time, I mean, if this thing should out of the speed it's going now, but if it should keep this upward trend -

H: Uh huh.

H. M. Jr: Between now and the Fourth of July well, then we'll know something of where we're at because then it would be a month old.

H: That's right.

H. M. Jr: Is that right?

H: That's right. That's right. You're ^{absolutely}right. I think that will work out probably as well for his purpose too.

H. M. Jr: I agree with you 100%, George.

H: All right.

H. M. Jr: Thanks.

RE BANK EXAMINATIONS

June 21, 1938.
2:30 p.m.

Present: Mr. Gaston
Mr. Upham
Mr. Eccles
Mr. Ransom
Mr. Szymczak
Mr. McKee
Mr. Draper
Mr. Diggs
Mr. Crowley
Mr. Jones
Mr. Oliphant

H.M.Jr: Well, here we are. I think the easiest way to start would be maybe to let the Acting Comptroller read the latest revision of his rules and regulations. How would that be?

Ransom: May I have one of your pencils?

H.L.Jr: You may have two.

Eccles: We got this digest already.

H.M.Jr: For those who haven't read it.

Diggs: I think everyone has seen it, Mr. Secretary. I just gave them copies here.

H.M.Jr: Well, why don't you read - well, how would you like to do it?

Diggs: The only change that has been made at all is in Section C - that is, C under Section I. "In case of investment securities for which a public distribution as set forth in (a) or (b) above can not be so provided, or so made, and which are issued by established commercial or industrial businesses or enterprises that can demonstrate the ability to service such securities, the debt evidenced thereby must mature not later than ten years after the date of issuance of the security and must be of such sound value or so secured as reasonably to assure its payment; and such securities just, by their terms, provide for the amortization of the debt evidenced thereby so that at least 75% of the principal will be extinguished by the maturity date by substantial periodic payments: Provided That no amortization need be required for the period of the first year after the date of issuance of such securities." That's the only change.

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- McKee: Is this an open forum, Mr. Secretary?
- H.M.Jr: Completely.
- McKee: May I ask the question why that last "provided" is necessary, just to get your thinking?
- Diggs: That is, not for the first year?
- McKee: Yes.
- Diggs: Well, it was thought by the staff and those who worked on it that paying for the first year might work a hardship on the company borrowing the money or issuing the securities, and we'd make it as easy as we could. It was even suggested there not be any paid for two or three years, but we thought that one year was sufficient.
- McKee: The only thought I had was that you get away from the ordinary form of debenture that is amortized from the date of issue. That's
- Jones: John, I think a great many borrowers, particularly for planning improvement and things of that kind - they figure that they wouldn't get into production during the first year; have to have a year to get started, to get prepared, and then a year to get in production.
- McKee: But isn't that figured in the loan?
- Jones: It doesn't need to be. It can be. It's
- Eccles: It's optional.
- Jones: This is merely an optional
- Diggs: It need not be required.
- Jones: I thought give as much latitude as you can.
- Szymczak: In other words, they may make a payment the first year.
- Diggs: Oh yes, may pay it out in five years.

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- Eccles: Well, this 75 percent in effect means a 12½ - about a 12½-, 13-year - that's what in effect it does.
- Jones: -hat's about the equivalent of that. I think it's good enough.
- Eccles: Yes, I do. I think it's all right.
- Jones: It's a good starter. I'd like to have had it a hundred years, but couldn't get it.
- McKee: You and Morris Cooke.
- Eccles: On the ten years, it was based on somewhat - Congress has already acted on mortgages; they have said that up to - can't be made longer than ten years, but in that period they must be paid down to at least 40 percent. But I think that's all right.
- Jones: Having stock, Mr. Secretary, in more banks than anybody else - I own several thousand banks - I think it's all right.
- Szymczak: Jesse, are you speaking of the whole regulation or just this section?
- Jones: Well, I think the whole thing, as far as I can see. I've read it over two or three times, and I don't know how I could arrive at any better, and I haven't written this.
- Szymczak: You say that with a smile.
- H.M.Jr: But he helped.
- Szymczak: He smiled when he said that.
- Jones: I think it's a pretty nice - pretty nice affair.
- H.M.Jr: Let's go around the room and see. Leo?
- Crowley: I join Jesse. Jesse, as the insurer of these banks, I'll go with you.
- Jones: You're behind more of them than we are.
- Crowley: I think it's all right.

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H.M.Jr: You're satisfied?

Crowley: Entirely satisfied.

Eccles: We

H.M.Jr: Ronald?

Eccles: Excuse me.

H.M.Jr: No, go ahead. Would you rather

Ransom: I'd rather defer to the Chairman, Mr. Secretary.

H.M.Jr: All right.

Eccles: Well, I was just going to say that

H.M.Jr: I'm just going around, but if

Eccles: It's all right. We had about a half, three-quarters of an hour, and we got the digest of it, and we all agreed that this met the thing very satisfactorily.

Jones: I think it's very helpful.

H.M.Jr: Now, is that - anybody from the Federal Reserve Board want

Jones: John McKee, do you think it's all right?

McKee: Yes. I'd like to see

Jones: When John agrees, everything's all right.

McKee: I'd like to see it in fewer words, but you can't do it, I guess.

H.M.Jr: Well, then, you were saying

Eccles: It's a question of lawyers - the words.

H.M.Jr: Well, the lawyers have been over it, at least my counsel.

Oliphant: We had them all together. I called George in, and Marriner direct.

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- Eccles: I'd say the question of verbiage has been left up to the lawyers anyway.
- H.M.Jr: Well, then ...
- Jones: Mr. Reed's out of town, so I couldn't call our counsel.
- H.M.Jr: Well, Mr. Hughes is in Europe, so I couldn't call
- Jones: Call yours.
- H.M.Jr: No, I called mine, but I couldn't ask for a ruling. So I'll take mine as I have always.
- Well then - this leaves me sort of breathless.
- Szymczak: Takes you off your feet.
- H.M.Jr: I don't like it.
- (Hearty laughter)
- Szymczak: Must be something wrong.
- Jones: Kind of framed up on you, Henry.
- H.M.Jr: All I want to say - I congratulate Cy Upham.
- All right. Well then, we can send one piece of paper over that's unanimous. I think we ought to call in the President right away.
- Now, what's the next piece, Professor Upham?
- Upham: Well, I This is the ...
- H.M.Jr: I'm still kind of breathless, but it's all right.
- Upham: This is the statement of the agreement that the Comptroller and the F.D.I.C. reached.
- H.M.Jr: Well, bring us up to date. How long since this has been gone over? I mean how long has it been in this form?
- McKee: The reason you don't put dates on it.

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- Upham: No, there isn't any date on it. It's been in this form for a week, I should say.
- Crowley: Wonder if I might suggest, Mr. Secretary, that Mr. Upham read a statement that was prepared at the Comptroller's office and that the Federal Deposit concur in.
- Jones: Is this it?
- Szymczak: No, before this. A statement as a preamble to this. Is that right, Leo?
- Crowley: That's right.
- Jones: That's the second; that's just a
- H.M.Jr: No.
- Szymczak: Yes.
- Oliphant: Yes.
- Szymczak: Yes, it has to be filed.
- H.M.Jr: I thought this was it. Here, this is it, I guess. Is this what you're going to read?
- Upham: No. I don't have copies.
- Jones: Suppose you speak extemporaneously.
- Oliphant: Or read it in your best elocutionary manner, with gestures.
- Upham: That's the statement of the issues that are involved.

"Bank Examination Program.

"The Comptroller of the Currency and the Federal Deposit Insurance Corporation, together with the Executive Committee of the National Association of Supervisors of State Banks, have agreed on a program of uniform standards in connection with the appraisal and classification of loans and securities in bank examinations. These standards have been adopted

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with a view to promoting a wholesome recovery and providing permanent high standards in bank examinations and bank supervision.

"This program, which is the result of careful study and of conferences extending over a period of several months, is a substantial step forward toward attaining a high degree of uniformity in future examinations of banks of all classes. A better coordination of bank supervision and a greater degree of protection to the millions of depositors in the nation's banks are thereby assured.

"An important aspect of the program is the proposed abandonment of the term 'Slow' in connection with the classification of loans in bank examinations. The confusing nature of the term 'Slow' is evidenced by the present requirement of the Federal agencies that a loan should not be so classified if its ultimate repayment is reasonably assured, even though the loan is slow in a literal sense. The adoption of numerical captions for the loan classification units, with each classification uniformly and clearly defined, should do much to eliminate this confusion.

"It has long been recognized that the lending of funds to sound and solvent borrowers, small and large, for reasonable periods, is a legitimate function of a commercial bank, provided there is proper provision for the orderly or ultimate payment of such loans. Bankers should be willing to assume reasonable risks and should not be criticized for so doing. No loan should be classified in a bank examination if the loan is sound in view of the valuable net worth of the maker or endorser, his earning capacity and character, or the protection of collateral of sound intrinsic value. All of these steps add up to more reliable and trustworthy bank examinations.

"The abandonment of emphasis upon quoted market prices as a basis for valuing investment securities"

Jones: Would you mind - you say "the abandonment..."

Upham: "The abandonment of emphasis upon quoted market prices as a basis for valuing investment securities is another constructive aspect of the program."

Jones: That's all right.

Upham: "Both appreciation and depreciation in securities of this quality are to be disregarded. The use of market values has not proved satisfactory as a method of appraising high grade bonds. Approximately 85% of the securities presently held by banks are of investment quality, and appraisal at cost will give recognition to the principle that such securities are investments and are not intended to be continually turned over in the market.

"Securities of speculative quality, although not defaulted, represent about 10% of bank holdings. Consideration of net depreciation in these securities in determining a bank's net position is necessary if the risks involved in speculative securities are to be appropriately reflected. Defaulted bonds and stocks are approximately 5% of total bank holdings and net depreciation in these securities is an estimated loss which should be charged off. The present practice will be continued under which premiums on securities purchased must be amortized.

"Another important part of the program relates to the treatment of profits from the sale of securities. Until losses have been written off and adequate reserves established, the use of profits from the sale of securities for any other purposes will not be approved. The present practice will be continued under which the establishment and maintenance of adequate reserves, including reserves against the securities account, are to be encouraged.

"This treatment of profits is a sound procedure which many well-run banks have been following for some time past. It will tend in some measure to discourage speculative in-and-out trading in the bond market which is a practice to be criticized and penalized. Too many bankers have viewed their bond holdings not as investments but with a view to obtaining speculative profits from turnover and this condition has contributed to the instability of the bond market. Furthermore, the so-called profits from security sales are in many instances not actual profits but merely write-ups in book value. This results from the fact that a banker, in disposing of securities at a profit, frequently reinvests at approximately the same price levels.

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"In connection with the Regulation of the Comptroller of the Currency governing purchases of securities by member banks of the Federal Reserve System, purchases of local issues of high credit quality will be permitted, provided there are sound provisions for the regular amortization of such debt by the obligor, and provided further that such issues are not held in excessive amounts. The Federal Deposit Insurance Corporation will continue its present practice which is in line with the above.

"This program, viewed as a whole, is believed sound and workable. The nation's banking system is a strong factor in the present situation and the merited confidence of the depositing public in this system must be preserved. This merited confidence cannot be preserved unless bank supervision is courageous and realistic."

That's a statement supporting the agreement on that mimeographed sheet, as I understand it.

H.M.Jr: What's your pleasure, gentlemen?

Eccles: I don't see how anyone can disagree with the statement; that is, stating the general objective that is to be followed. The question gets down to the question as to whether or not the proposed procedure of the majority report here really meets or carries out these objectives. That's where we disagree in certain

Jones: You mean whether this fits that.

Eccles: That's right. That's the whole question.

Upham: This.

Jones: In what way doesn't it?

Eccles: I was going to say, there are certain points where there is some disagreement.

Jones: What, for instance?

Eccles: I want to say this, that the Board, even before the Committee was appointed, gave a good deal of

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consideration to the whole question of examinations, as well as the question of regulations with reference to the purchase of securities. We spent considerable time on it, and we brought down some people from New York who had experience in both the market and also the examination, and the program that we worked out we were unanimous on - with reference to it.

Now, as I say, that was really prior to the appointment of the committee. It was done because of the fact that we were asked to participate in the President's recovery program, and in decreasing the reserve requirements it was done with the expectation that there would be some modification to meet what we felt was some of the conditions that seemed to exist.

There had been a very substantial deflation in loans during the last six months throughout the country, and it seemed to us necessary to try to stop that. There had also been some liquidation in securities, and as the market in certain bonds continued to go down, pressure was increased on banks with reference to it. And in reviewing a lot of reports from New York - I have a whole sheave of them - the comments of examiners were deflationary as the dickens; that they were putting pressure upon the banks to get rid of their sub-standard bonds and constantly calling their attention to slow and doubtful paper. And it was the opinion of those from New York that the action was very deflationary.

Now, we recognize the need, the desirability, certainly, of coordination. We also recognize the difficulty of three bodies being able to agree entirely on every detail, and that some compromise or some modification is necessary. We felt, however, in this instance, that outside now of the Comptroller's regulation, which has gone a long way, that in all the rest of it there wasn't a single point in the thing that we had made that was accepted - I mean that we

Jones: You mean in this?

Eccles: Yes. Now, with reference to the question of loans, this is possibly an improvement over the present proposal. We have all been anxious to get rid of the classification of "Slow." It was a misnomer, and

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there was a lot of paper that during periods of this sort got into "Slow" and as that column built up in total, pressure was brought on the banks and there was always an effort to try to reduce that total.

This does get rid of "Slow" but it does do - bring in two elements, two classes of "Doubtful." We might say "Very Doubtful" or "Tinged with Doubt." You've still got your three columns of "Tinged with Doubt" and "Very Doubtful" and "Loss," and that's what these numerals really mean; in effect, that's the definition. We had felt that "Loss" and "Doubtful" were sufficient, that a loan or a portion of a loan could be a loss or a doubtful loan, and that those columns - that definition spoke for itself without the use of any numerals or without writing out a definition.

Jones: Well, he doesn't classify this Number One.

Eccles: Number One is "Good." But it's Two, Three, and Four, Jesse. It's Number Two takes the place of "Slow." Two takes the place of "Slow."

Jones: Well now, let's see - "Loans or portions thereof which appear to involve a substantial and unreasonable degree of risk to the bank by reason of certain unfavorable trends and other unsatisfactory characteristics noted in the examiner's comments." That's Number Two. "There exists in such loans the possibility of future loss to the bank unless they receive the careful and continued attention of the bank's management. No loan is so classified if ultimate repayment seems reasonably assured in view of the sound net worth of the maker or endorser, his earning capacity and character, or the protection of collateral or other security of sound intrinsic value." Now, that you don't - that's your slow loan.

Eccles: That's right, but if

Ransom: Now, is it? That's the very question that I'd like to ask, Mr. Secretary, if I may, right there at this point. As I understand this Roman numeral I, it would be the position of the examining authorities that they would not commit themselves to the fact that there was

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a single sound loan in any bank that they examined.

Crowley: I don't think so at all.

Ransom: Because you say "appears reasonably assured."

Crowley: We understand that this is our One. If you're going to give any regard to the good securities, you have to classify them. Now, you don't classify your Number One loans, your A-grade loans, at all. You don't mention them.

Ransom: Oh. That is, clearing your thoughts, that's the A-grade loan. Why not say that they're good loans, without saying they "appear reasonably assured"? Of all the qualifying words I ever heard put together, that seems to me to head the list. Aren't we willing to say that a bank has a class of loans that are good?

Crowley: Yes, they're good.

Ransom: Why not say that Class One are good loans?

Crowley: You don't list Class One loans at all.

Ransom: No, but this thing reads so that the impression on the bank is that the examining authorities do not really believe there is a single good loan in the bank.

Crowley: If I was a bank examiner, I wouldn't examine any bank and say that the loans were good.

Ransom: Then what you ought to do is to say what's bad.

Crowley: All you do is take the definition of that type of loan as having a reasonable chance of payment. Now, you won't make the loan ...

McKee: If it's a collaterally secured loan of \$7,000 with \$15,000 worth of Governments, does your answer still remain good?

Crowley: Well, I think you're going to an extreme.

McKee: I don't mean to embarrass the Secretary, because his name is on the notes.

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- H.M.Jr: You can't embarrass me when you talk about Governments - not today. I don't know about tomorrow. But you can't embarrass me. We sold an all-summer bond, don't forget that.
- McKee: It better stay sold.
- H.M.Jr: All summer.
- Eccles: Ronald, wouldn't this be - got a lot of stuff to cover - ...
- Ransom: I know, but we can cover it very quickly if we will just determine whether or not the examining authorities must think it necessary to throw a shadow of doubt on all the loans in every bank.
- Crowley: I think you're just raising a straw man to knock down there, Ronald. I think every security you have in a bank has a reasonable doubt as to it.
- Eccles: But you don't want to state that in the report.
- Szymczak: Isn't it a fact that you wouldn't want to call your Class Two loan as Number One?
- Crowley: You don't want your Class Two loan - that's a different loan.
- Szymczak: In other words, you wouldn't want to call it a Class One loan, an A-One loan; that's the whole thing. It's the numerical order that we
- H.M.Jr: Gentlemen, Mr. McKee makes the suggestion that we do the thing next which it would seem we might get together on first. That's the approach on the question of securities. And let the one on the loans go to the last.
- Crowley: Well now, wait a minute.
- Ransom: I think we're awfully close to an agreement on this.
- Crowley: Let's go right down the line.
- Ransom: Awful close to an agreement.
- Jones: Go ahead, Ronald.

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- Ransom: I just think that there are two or three thoughts - if we'll get them clear in our own minds, there won't be very much issue. First, whether or not, if we think it necessary to substitute the Roman numerals, we do intend that Roman numeral I to mean loans that are not specifically criticized or commented upon.
- Crowley: That's right.
- Ransom: Now, I would much prefer language that was definite rather than by implication throw a doubt on all existing loans.
- McKee: ~~Loans~~ Subject to no criticism.
- Ransom: Loans subject to no criticism.
- Now, there are two or three - I would like to ask this question. Mr. Jones raises a very important point. He said he understood Number Two to be really slow. I don't so understand it.
- Crowley: We say - if you read your definition there ...
- Ransom: I don't think it means slow.
- Crowley: If you read our statement, we said that a loan, Ronald, even though it may be slow, if it was being amortized and the payment was not in question, that it would not be listed at all. Now, the only loan you list
- Szymczak: That would go in Number One.
- Crowley: That goes in Number One. Now, the only loan you list in Number Two is your
- Szymczak: In other words, you really have two
- Crowley: The ones that ought to be further collateralized and put in better shape.
- Ransom: Need comment or criticism.
- Szymczak: You really have two doubtful classes, Two and Three.
- Crowley: That's right. Your Three are more doubtful than Number Two.

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- Ransom: But Two is doubtful. That's all right. I personally like the words "Doubtful" and "Loss," but if we're going to abandon those, let us abandon them with an understanding amongst ourselves that Two and Three are "Doubtful" and Four is "Loss" and that the definitions are simply refinements of those two simple words.
- Crowley: I think, Ronald, that "doubtful" and "very doubtful" is what they mean in our own minds.
- Ransom: All right. Mr. Secretary, I'm through, sir.
- H.M.Jr: You're through. You mean you take Number One as is?
- Ransom: I'm through clearing up the point that I thought was raised by Mr. Jones' asking if Two wasn't slow paper. Mr. Crowley and Mr. Diggs I understand to have answered that they do not intend that to be slow paper, but doubtful paper of a somewhat less doubtful class than Three.
- Diggs: It's the same kind that has always been in the "Doubtful" column since 1934.
- Szymczak: In other words, your Number One loans are not subject to criticism. Period.
- Draper: I think that's the way to describe it.
- Szymczak: It doesn't make any difference, that's the essence.
- H.M.Jr: Gentlemen, where are we now? You're taking Number Two.
- Crowley: We're taking - we're through with Number One and Two.
- Szymczak: Can't do anything else about it. In substance, Number One means "loans not subject to criticism."
- Ransom: I understood both Mr. Diggs and Mr. Crowley that they would accept "loans not subject to criticism" as the definition of One.
- Crowley: Wait a minute, Ronald. We agree with that thing you say, that you think the word "reasonably" in there - and now let's go through this thing and see what else we've got.

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- Ransom: Oh, all right, I'm perfectly willing.
- H.M.Jr: Now wait a minute. Do I understand in Number One that Ronald Ransom will take it or he's changing the language?
- Eccles: He'd like the word "reasonably" cut out. "Loans or portions thereof the repayment of which appears assured."
- H.M.Jr: Wants to leave out the word "reasonably."
- Szymczak: Makes it just slightly doubtful.
- Ransom: I just don't like that
- Szymczak: It's "after midnight."
- Ransom: Let's have it either a virgin or
- Draper: Could you say "Chaste"?
- Crowley: When we're going back and throwing back these so-called "slow" loans into Class One that have been in the bank a hell of a long time, although we think they're good, there is a little bit of a reasonable doubt as to whether they're quite as good as some other loans.
- Szymczak: In One? Wait a second.
- Crowley: We're just disregarding them, throwing them back as good, but there is a reasonable question in your mind whether you'd like to see a bank have too many of them. If you have a bank that has 50 or 60 percent of their Grade One loans in ten-year loans or five-year loans, now you can't say that that bank is an A grade bank; there is some doubt, because you're getting a freezing process going on there that ultimately may get you into some difficulty. That's what I mean, Ronald.
- Eccles: Well, Leo, now you're getting to the question of liquidity instead of soundness.
- Szymczak: That is, in your own mind.
- Crowley: We're only talking here - I think in your mind there is a question too. Now, it's just a question as to

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the balance of the bank's portfolio, isn't it?

- Ransom: Yes, in the total bank portfolio, not in Two or Three or Four; and lots of times they're going to be very bad in course of time, but are not bad now. And words seem immaterial to me so long as the language doesn't cast a doubt on the entire portfolio.
- Crowley: Well, you don't disagree on the Two, do you?
- Ransom: No.
- Jones: I want Marshall to hear this on Number One. I just suggested for consideration "Loans or portions thereof the repayment of which appears assured are regarded good and are not classified in the examiner's report."
- Szymczak: Right. That's all right.
- Jones: Now, I like the word "reasonably."
- Szymczak: Well, better take it out.
- Jones: You fellows are so contentious that I'm willing to take it out to get along.
- Crowley: Wait a minute, let's go through this thing.
- McKee: Maybe you need another classification, five instead of four.
- Szymczak: No, he doesn't.
- McKee: Help it a lot.
- Crowley: Might need that all right, John.
- Ransom: Go into five classes.
- Upham: I like Mr. Ransom's "loans not subject to criticism." I think this says the same thing.
- Ransom: It says it a little more specifically. I like what Mr. Jones suggests more than I do my own.

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Diggs: I think "comment" is better than "criticism."

Crowley: Let's go ahead with this thing. Let's not

H.M.Jr: I think we can do one at a time.

Upham: He wants to trade, see?

Crowley: No, we've worked six, seven or eight weeks on this thing; you bring it in here and in 15 minutes kick it all to hell.

H.M.Jr: No, Leo. Now

Szymczak: No, Leo.

H.M.Jr: Up to this minute

Szymczak: Going along lovely now, Leo. Don't let your Swedish get the best of you.

Jones: I belong here with you and I'll vote with you in the final analysis, but

Crowley: Now, Jesse, you know any time you get yourself a little bit

Jones: "Loans or portions thereof the repayment of which appears assured are regarded good and are not classified in the examiner's report."

Crowley: Now wait a minute, we've got a hell of a lot of things more important than this one.

McKee: I'd like you to hear the Comptroller of the Currency's suggestion. It's simple and I think it covers everything you're talking about.

Diggs: I don't like the word "good" if you're going to change it: to say they're good. I'd rather say that "loans or portions thereof are not subject to comment."

McKee: That's right.

Diggs: "Loans not subject to comment. These loans are not classified in the examiner's report." If we're going to change it at all, I'd rather not say anything about "good."

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- Szymczak: You wouldn't use the word "criticism" instead?
- Jones: I'd rather have it the way you've got it written than that. I think it would ...
- Diggs: I'm willing to take it as it is, don't misunderstand me.
- Jones: I am, but I was just trying to get along with these contentious fellows over here.
- Eccles: It's a damn small matter.
- Ransom: Not being contentious; I'm simply suggesting to you that you've got language in there that's going to come back and give you a certain amount of trouble.
- Diggs: Since it's minor, I think we might pass on. If we agree on this
- Crowley: There isn't any argument in Two.
- Jones: Who's got any question to raise about Two?
- H.M.Jr: Who wants to raise anything on Two? Gentlemen, anything on Number Two?
- McKee: I think it's too damn long.
- H.M.Jr: But beside that, Mr. McKee?
How about Number Two?
- Szymczak: When you speak of unfavorable trends, do you speak of unfavorable trends in the bank or in the country, or both?
- Crowley: Unfavorable trends is unfavorable trends of the assets of the business, of these loans.
- Szymczak: Of that particular business.
- McKee: How about the condition at the time - the economic condition of the country?
- Crowley: We got not a damn thing to do with that monetary or credit thing.

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- McKee: I'm not talking about monetary. Now, you know me well enough to know I'm not talking about that subject.
- Szymczak: Never heard the word.
- Crowley: If you go in and examine the point whether they're losing money, whether their inventory is made up of a type of assets that is depreciating at the time, that's your trend of a financial statement.
- McKee: That's the trend of banks as well; and yet you've seen them come back.
- Crowley: - All right, but I don't think you can write a bank examination report for 90 days or six months.
- McKee: I don't think we can either.
- Crowley: We're trying to work out something here for bank examinations in season and out of season. If a lot of banks are in difficulty and the condition of the country is such that their banks are in trouble, then I think you've got to determine your policy after that.
- Szymczak: Well, you don't - Leo, you don't want the examiner to be deflationary-minded during a deflation period, and you don't want him to be inflationary-minded during an inflationary period. I mean that unfavorable trend - you don't want him to be ...
- Crowley: I don't think we're - we're agreeing here to these so-called slow loans that are not, not being criticized; we're going a long ways against deflationary trends too.
- Szymczak: You mean on Number Two.
- Crowley: The only thing that's going in Two is a really criticized asset. If they put it in that column and then get some payments on it, it goes out of Column Two.
- McKee: Let's be frank. That's what you think is going in there. What's going in there is what the examiner is going to have time to put in there.

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- Crowley: But you've got examiners. What are they going to do?
- McKee: The same things your examiners do.
- Crowley: We've all got to take this thing in the spirit in which it's written.
- McKee: But you're not going to be the fellow that examines the bank. It's the other fellow who's going to interpret what you say about this thing.
- Crowley: All right, I'm willing to have them examined on that basis, John. So are you.
- Szymczak: See, that "certain unfavorable trends" is the general term, that may be taken any way by any examiner.
- Jones: That's like the trade winds.
- Szymczak: Exactly.
- Draper: You can change the wording.
- Jones: Who wants to change it? I don't.
- H.M.Jr: Who wants to change Two?
- Eccles: I think that if you're going to have Two and Three and Four, that they're about all right as they are. What we - our position has been that you'd want "Doubtful" and "Loss" - that either a loan is doubtful at all or in part, and record that fact; and loans then that require - may not be the best loans, but they haven't reached a stage of doubt; that they would merely be loans for comment, and you'd list them in the report and they would be loans that would be subject to requiring close attention, but they haven't reached the doubtful stage. Now, that was our position. However, if we're going to accept the three classifications, two classifications of "Doubtful," one of "Loss," it seems to me this is all right.
- H.M.Jr: Well, as I understand it - do I understand it you're talking now for your group and you go along on Two, Three, and Four as it's written?

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Szymczak: In substance.

Eccles: Yes, if we're going to have the three classifications. Our preference has been that we have "Doubtful" and "Loss" and that's all we put on that sheet.

H.M.Jr: Then it gets down to changing Number One in some way and then we'd all be together, is that right?

Eccles: Well, we'd

H.M.Jr: Say we've reached a compromise.

McKee: I don't think that's quite the right interpretation, Mr. Secretary. I speak for myself - that I haven't seen anything produced in these conferences that has in my opinion met a different approach to the examination problem, one that gets away from putting the responsibility on a man - now this is particularly effective against smaller banks - a man who has to do a job in a limited time, to go in there and throw notes promiscuously from one column to the other, mindful all the time that he's going to probably be followed up by another examiner and his record is going to be criticized if and when that examiner shows a different report of that bank's condition within the next six months. Now, that - you can't help that; that's organization, and it's been in organization for 35 years.

Now, the whole approach to this examination problem - and we've followed and studied this thing since 1932 with one thought in mind, that some day we could make people conscious of the effect of the examination. I don't think you got that, because none of you seemed to have grasped it, because maybe you haven't seen what we have seen - now I'm speaking of myself - that sooner or later you're going to find out that this approach to examination is not a question of loaning the bank funds; that the banker is still responsible to his stockholders for his capital, and that that banker is going to consider first the protection of his capital in advancing funds; you can't make him make loans, no matter how you regulate him.

H.M.Jr: You and I agree.

McKee: Now, the approach to this examination has always been,

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accelerate it on a downward trend of general conditions; first, by what? - market; second, by the complex of examiners influenced by market on their approach to the classification of loans; and thirdly, because they themselves had a record to maintain with the office of the supervisor in Washington so that they may be able to keep their job. They go out into a little bank; they go in at three o'clock in the afternoon; they've got to get the 7:30 train to get to the next town. They've got to examine that bank.

Now, I'm not worried about the big bankers. Now, here's another thing that I don't know whether you're conscious of. The big bankers are not interested in this. You talked to them and we talked to them, but we know they weren't interested. Why? The big banker - when the examiner goes into his bank, he doesn't look at any loans under \$50,000. The little fellow isn't penalized in the big bank if he loans him any money, but it's the little fellow with a million dollars of assets that they look at every nickel and dime he's got on his books.

And it's that little examiner, far removed from Washington, who goes in to examine these little banks, that dries up your credit in these small communities. Now, that's where it started in 1929, and it went - it's gone on from one depression to the other.

Now, unless you're going to look - and maybe this isn't the time, but unless you're all ready to sit down and think of this thing seriously - now, don't misunderstand me, I'm not for liberalization in any kind of times or contraction in other times, but I'm for a fair and just approach to this situation, and I don't think it has ever been done by the form of examination we had heretofore.

H.M.Jr: May I answer you briefly?

McKee: Yes.

H.M.Jr: There's no disagreement, see? But don't lose sight of this, that what we're trying to do here isn't the

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last word that's going to be done on bank examinations. All that we're attempting to do is to make a start to move - all of us to move in the same direction, just as a start, that's all.

Szymczak: And then take inventory later.

McKee: Now let me answer that question.

H.M.Jr: Just a second. Now, as I was saying before, there is no reason in the world that if after - let's say we come to an agreement by give and take - that after Labor Day, if necessary, there's no reason why we shouldn't take another look at this thing; no reason we shouldn't take a look at this thing four times a year, or as often as necessary. And I don't think anybody, no matter what their experience is, whether they come from a small or a large community - to turn out a group of regulations which is going to be the last thing in bank regulations - anybody that thinks he can do it, I think, is just dumb.

But I do think that the importance of the thing is that out of Washington all of us here appointed by the President should try to make a start.

Szymczak: Be uniform and cooperative.

H.M.Jr: As I said facetiously, if we only agreed that we're going to use pink paper and blue ink, at least all of us - that we all have the same kind of stationery; if we simply agree we're all going to use the same color stationery and the same type of ink - if we just did that, I'd say it was a step forward.

But I say here and now, in answer to John McKee, that I would be more than delighted if you people want to sit down after Labor Day and take a look. Now, that's my approach. And where we've never done this thing before, I think we've all got to give and take and, as I say, turn out something so that in the minds of the depositors of the country and the bank management, they feel that at least Washington knows which way it's going.

Szymczak: Mr. Secretary, at that point, after Labor Day, let's say, using that just as a sort of tentative date,

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who would call the agencies together to take a look at this thing?

H.M.Jr: If the President wanted me to, I would.

Szymczak: In other words, somebody will initiate this, so we just don't ...

Jones: If anybody felt ...

Szymczak: No, I think it's important to do the actual

H.M.Jr: All I've done at any point here - haven't tried to put my ideas down on paper; I've just acted as chairman. And I'm more than willing, if the President wants me to, to do it again. But none of these ideas are mine. I've kept

McKee: May I ask the Secretary one question, one thing?

H.M.Jr: Does that answer you?

Szymczak: Yes.

McKee: One thing that has impressed me is that you want to be fair with your customers.

H.M.Jr: Yes.

McKee: Now, these banks are what - the customers we're talking about. Do we want to have one approach - a different approach every 90 days?

H.M.Jr: No, not a different one, but

McKee: All right. Why shouldn't we be sure before we go ahead?

H.M.Jr: Listen, you're the head of a hundred thousand dollar business or a ten million dollar business, and in these times can you plan your sales campaign, your advertising campaign, and your credit campaign for more than 90 days?

McKee: No.

H.M.Jr: No.

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- McKee: Do you want to break down all the good in the change that you're going to do by creating uncertainties in the minds of bankers that we got one type of examination now and one again in September?
- Boymozak: You wouldn't want that to go out to the public, the statement you've just made.
- H.M.Jr: No.
- McKee: You want to keep that in your mind.
- H.M.Jr: No, but I'm saying that what's happened here - I mean during the last two months, the uncertainty that's gone out is the delay in trying to get you fellows together. When I say you fellows, I mean everybody. That's the uncertainty.
- Boyles: Let me make this suggestion, that in accepting, say, this proposal, in answering the question that - the problem that John makes, which is an important one; unless from time to time the examination agencies send out letters of instructions, because after all there is the question of examination, which should possibly record the facts, and then there is the question of the supervision - you don't want the examiners to go into the bank and attempt to manage them, tell them what to do and what not to do. Let them record what they see to be the facts. Then the supervisors can use discretion as to what ought to be done with a given situation at a given time. That gives you elasticity.
- Crowley: That's what goes on anyway.
- Boyles: I was just going to say, with that understanding, now, I'm very much impressed with a letter that the Comptroller sent out October 26, 1933, with reference - and I want to just read this section of it, because it goes right to the root, it seems to me, of the way these things should be approached. For instance, it says, "After the bank holiday, National Bank examiners were largely engaged in the examination of banks which did not receive a license for the purpose of reorganization. It appears that some examiners, in making examinations of the licensed banks, have become what might be termed reorganization-minded and have lost sight of the President's recovery program and its relations to licensed banks."

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It is the Administration's desire that credit channels be opened through licensed banks, and this policy cannot be accomplished if examiners follow a deflationary policy in examinations. We are all concerned with insolvent banks, but there is a wide distinction between the potential and intrinsic values of assets of a going concern, and liquidating values. Examiners, in appraising and classifying assets of banks, will not apply liquidating values, but will appraise on the basis of fair values on a recovery basis."

Now, that seems to me to state the approach, for instance, if it is deflationary, and you can't write all that out in instructions or in a thing of this sort now.

Now, he came along later, March 13, 1934, and he said, "Reports of examinations received by this office recently clearly indicate that some of the examiners throughout the country have not fully grasped the meaning of the instructions communicated to the Chief Examiners under date of October 26, 1933, and are making more drastic classifications of assets of the banks examined by them than is necessary under the circumstances, and more severe than is contemplated by the instructions contained in office letter referred to above. If there are in the Federal Reserve district any examiners who in your opinion are making unnecessarily drastic classifications of assets, please confer with them promptly looking toward having their classifications as lenient as circumstances in each case will permit, and in order that they will be in accord with the policies of this office. While you are familiar with the character of the examinations made by your examiners, it is suggested, in determining whether or not any of them are too severe in their classification, you give particular attention to their appraisals of banking house, furniture and fixtures, and loans secured by real estate."

Now, the bad loans and the bad investments are made in good to boom times, when there is a lot of optimism. They are seldom made in the depression times. And it seems to me that you can necessarily shift and change a thing of this sort, the form of examination report as such, but you can, by instructions that may be sent out by all of the agencies

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combined to the chiefs, see, in their districts, keep them in accord with what may be the President's or any recovery program.

H.M.Jr: There's no argument about that.

Eccles: That does give the thing a degree of flexibility without saying so to the public, without talking about laxity. We're not for laxity. We're for approaching the thing in a perfectly realistic manner and trying to stop the pressure of examiners when - you don't improve assets very much in times of this sort by bringing pressure; you don't protect depositors. If such had been the case, we wouldn't have had the banking collapse. We got the banking collapse largely through the effort to get liquidity, through the effort to protect depositors. And it destroyed depositors.

Crowley: Let me ask you a question. But you can't make banks stop paying dividends and build reserves and things like that unless you get a true classification of their picture.

Eccles: Of course, I'm for stopping paying dividends.

Crowley: You've got to get your picture first.

Eccles: Well, I just wanted to say that

H.M.Jr: Well, I think that's a very good point.

Now look, as I understand it, nobody is entirely satisfied, but if every person could be 75 percent satisfied, I would say it was a good day. Now, they seem to be satisfied with the Two, Three, and Four. They want a slight change in One. Now, Diggs, how did you have it over there in Number One?

Diggs: "Loans not subject to comment. These loans are not classified in the examination report."

H.M.Jr: Say it again, please.

Diggs: "Loans not subject to comment. These loans are not classified in the examination report."

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- H.M.Jr: Why not just say "Loans not subject to comment"?
- McKee: Plus the last sentence.
- Ransom: That doesn't permit the examiner to debate whether they're good or bad - just classify them. He may not know.
- Diggs: Is that all right with you, Leo?
- Jones: I think you're wrong on that. The way you got it is much better.
- Szymczak: Why?
- Jones: I know the difficulty the bank examiner will have. He'll get a little consolation out of this thing the way you got it written, but if he's got to say whether John McKee's note is good - he doesn't know whether it's good.
- Ransom: But he doesn't say "good."
- Jones: If he doesn't put him there, he'll put it down here.
- Eccles: What objection is there to Jesse's language? That's perfectly acceptable to me.
- Crowley: There was no disagreement on One, as I understand, with any of the three Chief Examiners. They all agreed.
- Diggs: I'm agreeable like it is. Don't misunderstand me.
- Jones: Why don't you accept it?
- Crowley: It binds - these fellows made a study of this here, they worked for six or seven weeks; if we're going to have to kick the thing apart for some little bit of a thing - there's more important things on the next page.
- Jones: You can use better language or use what I have, but I think the substance of it is all right.
- Szymczak: In other words, there are loans in a bank's portfolio that are not in Number One.

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- Crowley: Oh no.
- Szymczak: Well, everything you don't classify is in Number One - everything.
- Crowley: That's right.
- Szymczak: Well, why can't you accept that definition?
- Crowley: You don't want to assure - you want to guarantee, don't you?
- Szymczak: No, of course you don't want to guarantee anything that's in the bank.
- H.W.Jr: Well now, let's see if we can't get on this once, so we can get off this page, Leo.
- Ransom: Mr. Secretary, I'm sorry I brought up that point. It's perfectly clear to me that it's inevitable that the examiner is going to grade all loans as bad until somebody proves they're good by paying them, and maybe after all that's the real test, so we might as well leave it on that basis.
- McKee: Then we have three "Doubtful" and one "Loss."
- Ransom: That's all right.
- Szymczak: In other words, you start with this: that every loan in a bank is doubtful.
- Jones: I think in view of what John says about these Chief Examiners and these fellows - I think leave it like it is.
- Ransom: Leave it like it is as far as I'm concerned. By God, there are more important things in life than that. I just want to be sure that it is the examiner's point of view that all loans are bad until they are paid.
- Eccles: Say "Loans or portions thereof the payment of which is assured." It is assured at this time.
- Crowley: You can't say that they're assured.
- Szymczak: That's going too far.

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Oliphant: Marriner, it says "appears," that's what it says.

Szymczak: "Appears assured." Strike out "reasonably."

Oliphant: Strike out "reasonably."

Szymczak: Agree to that, Leo?

Crowley: All right. Well, hell, don't mean a damn thing.

Szymczak: Everything that "appears" is "reasonably."

Gaston: That's a think word - "We think."

Diggs: Too long a word.

McKee: Boys, keep your guns in your pocket, because I'm afraid we're being traded.

H.M.Jr: You let me know how we're being traded.

Eccles: I'd like to say, though, this whole thing as far as I'm - we're concerned, is a compromise. We accept it, but we ...

Jones: You can come back next spring and look at it again. I think Labor Day's too early.

Crowley: One, Two, Three and Four are cleaned up. No doubt about losses.

Szymczak: No, there never was.

Jones: Now, where are you?

H.M.Jr: Aren't we through with this page?

Szymczak: Two paragraphs ...

Ransom: One more point.

H.M.Jr: God, we've been one hour on one word.

Oliphant: And we struck it out.

Ransom: The word "trend" appears in Classification Two, and I suggested to Mr. Crowley that it be "certain

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unfavorable developments in connection with the particular loan."

- Gaston: Why not say "an unfavorable record or other unsatisfactory characteristics"?
- H.M.Jr: Say it again. Jesse didn't hear it.
- Gaston: "By reason of an unfavorable record or other unsatisfactory characteristics."
- Jones: Check.
- Crowley: Very good.
- H.M.Jr: God, Ronald, you're doing swell. Anything else, Ronald?
- Ransom: No, I'm satisfied.
- Szymczak: Or other what?
- Gaston: The same as it is - "or other unsatisfactory characteristics noted in the examiner's report."
- Diggs: Would "factors" be better than "characteristics"? That's a long word.
- Szymczak: What's the word?
- Diggs: "Factors."
- Szymczak: I don't like "factors."
- Diggs: All right, I'm agreeable.
- H.M.Jr: All through on this first page? Good. Going. Going. Sold!
- Diggs: Where's the hammer?
- H.M.Jr: All right, next page. What's your pleasure, gentlemen?
- Jones: I move that
- Eccles: Now wait a minute.

(Hearty laughter)

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- Szymczak: Who said this was a Democratic convention?
- Draper: You (Jones) have my vote for President.
- Eccles: I want to say this, that on the first page I want to leave the last part for consideration when we get over to the question of sound capital. You've got at the bottom of the page "Present practice will be continued under which the totals of III and IV above" - which are the doubtful, see - "are deducted in computing the net sound capital of the bank."
- Crowley: I was afraid you were going to miss that for a minute.
- Szymczak: Let Marriner make a statement on that, Leo. That's very important.
- Eccles: I'd like to come back to it when we get through with the bonds, because that's the last part of the statement.
- H.M.Jr: Fair enough. What's your pleasure, gentlemen, on page 2?
- Jones: The motion's brought out.
- McKee: And I disagree with it.
- H.M.Jr: The whole page. All right, we'll leave page 2 out. We'll skip page 2.
- Well, who doesn't like a word in page 2?
- Eccles: I'd like to make a statement on this whole bond question here.
- H.M.Jr: All right, go ahead. Don't mind if I take it standing.
- Jones: Now, don't make it too long, Marriner.
- McKee: Goddamit, you don't recognize he used to be a preacher.
- Eccles: Hell yes, give me a little credit.
- Jones: He ought to know that souls are saved in the first five minutes.

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- Jones: Let's read it before you make a statement.
- Eccles: All right, read it. Go ahead and read it, Cy.
- Upham: He (Jones) wants to read it to himself.
- Crowley: In other words, gentlemen, on your Group A bonds you show neither appreciation or depreciation, just simply
- Jones: All right. Now, Number Two. Depreciation in the securities in Group Two - don't show that either.
- Crowley: You show that and you deduct it.
- Eccles: Take that plus part of Group One.
- Upham: The fourth grade of general market obligations is in Group One.
- McKee: Now, in substance this is a tightening up of the approach of examination. Now, nobody can deny that in this room.
- Upham: Yes, if Folger were here he'd deny it, and I suppose I'll have to for him.
- McKee: But how can you justify it?
- Upham: You said couldn't deny it. I'll stop.
- McKee: All right.
- Eccles: What you have - you have two groups of securities. You have Group One, which are satisfactory or eligible for purchase and are looked upon as sound investment securities. Now, in Group One are the first four classes of rated bonds. Those are all of the A's and the first class of the B's.
- Jones: Does that mean fourth grade?
- Eccles: No, you see, you have your ratings, you have a lot of classes. You have your three - AAA, your AA, and A; B, BB, and BBB.
- Crowley: Cy, come over here a minute, will you?

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- Eccles: So that what you have in Group One are considered sound investments for banks, and they do include the first four classes, and according to the four rating bureaus all of those classes are considered good.
- Jones: How would you change this thing, then? The application?
- Eccles: What I would do - I would eliminate the "except the fourth grade of general market obligations."
- Jones: From Paragraph One?
- Eccles: That's right.
- Jones: What else would you do?
- Eccles: Well, I - what I would like to do is when you get to the next group I'd like to list them at book and get away from following a ticker tape.
- Jones: You mean Number Two.
- McKee: Can I give you an answer in a few words? You see, this "neither appreciation nor depreciation in Group One" and so forth - now, you have always given credit for appreciation when you consider depreciation.
- In this statement, right here in Paragraph Five or Four, you say, "The abandonment of emphasis upon quoted market prices as a basis for valuing investment securities is another constructive aspect of the program. Both appreciation and depreciation in securities of this quality are to be disregarded." You don't do that.
- Crowley: Yes, we do.
- McKee: Excuse me, Leo, we don't do that. We disregard the appreciation and we only offset it by the depreciation in a group where, by God, there isn't any depreciation, do you understand? But then, you're going to penalize the sound capital structure by not giving credit for the appreciation but deducting the depreciation in the lower grade. See what I mean?

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Now, nobody is - we're all of one mind on the Group Three and Four, which is defaulted bonds and stocks to be charged to market and considered loss. But the point at issue is that, Leo, and the Comptroller's office wants to disregard appreciation in your Government bonds and everything else, but charge depreciation in your second group of bonds.

Eccles: On the basis of a ticker tape.

McKee: Now, if this paragraph in this memorandum means anything, you're inconsistent in this program.

Jones: What about that, Leo?

Crowley: All right.

Draper: Do you agree?

Crowley: Let me say this. What you want now is One and Two treated alike. Right, Marriner?

Eccles: Yes.

Crowley: Now, you don't object ...

Eccles: But we

Crowley: Wait a minute. You don't object to Three and Four, do you?

Eccles: No.

Crowley: And "Present practice will be continued under which premiums on securities purchased at a premium must be amortized." You don't object.

Eccles: No.

Crowley: And you don't object to the listing of the bonds as long as

Eccles: But not at the market. Don't want to follow it. Don't want to get to a day-to-day quotation.

Upham: What's this, you agree with him?

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- Crowley: Wait a minute.
- Draper: Yes, he agrees. Sold.
- Crowley: So we understand one other. What he wants is to disregard depreciation in the B-AA bonds and treat them the same as you do your Group Ones.
- McKee: In the second group of bonds.
- H.M.Jr: Well, in your Group Two; in other words, the bonds that your Comptroller's regulation recognizes. Is that right?
- McKee: No, no, you're not going - your second group is B-A, C-AA and C-A. That's your second group of bonds.
- Upham: I'm lost.
- McKee: No, you're not lost. Now, wait a minute, he's talking about one thing and I'm talking about something else.
- Diggs: Let's talk on the same subject.
- Gaston: You're (Eccles) talking about combining One and Two and treating them alike.
- Eccles: That's right.
- Gaston: And Leo wants to take one issue out of Group Two and include it.
- Crowley: Why, let me ask you this. As I understand it, in the B-AA bonds and up - it represents about 93 percent of the securities of our banks.
- Upham: Well, I believe that's your figure.
- Crowley: That's what they said.
- Upham: That's what I understood.
- Crowley: Now, the balance of them is 7 percent. Now, what we originally talked about, John, was disregarding the depreciation in the B-AA.

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McKee: What was your percentage?

Crowley: 93.

McKee: No, you're including Governments in that. We're not talking about Government bonds.

Crowley: But it's on their security portfolio. You've got to talk about that in order to get your percentage.

McKee: Aren't we talking about corporate bonds subject to the Comptroller's regulations? Has he ever ruled on Government bonds?

Crowley: He's ruled on B-AA's.

McKee: Yes, they're corporate bonds.

Crowley: We're willing to go along with any bonds that are bought under the Comptroller's regulation of B-AA, but if you're ever going to make these fellows conscious of the fact that they're buying bad securities, you can't let them go in and buy this stuff and then as soon as the market goes out from under them let them sit in the same favorable position as the man who has bought good securities and been satisfied with a lesser yield.

McKee: Aren't you going to try to police your reserves to protect your defaults?

Crowley: We'll agree on all AA bonds for to treat them without showing any depreciation on the market. On anything lower than that - that we'll treat as a doubtful, and the Threes and Fours be treated as a loss.

McKee: What's the difference in your net sound capital picture?

Crowley: We have never gone on the theory that "Doubtful" impaired a bank's capital.

McKee: You show it.

Crowley: But legally we don't. We don't serve a notice of impairment.

McKee: You scare hell out of the management.

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Ransom: Examination report doesn't deduct "Doubtful" in determining net sound.

Crowley: Wait a minute. Marshall, are you sure of that?

Diggs: Wait, it does for net sound.

Crowley: But it does not for impairment of capital.

Diggs: It does for net sound.

Eccles: Net sound is impairment for all practical purposes. You can't send that out to a Board of Directors and have any other effect.

Crowley: Well, the way we

Eccles: Listen here, what you want - what you have done, you have said that the first four grades of bonds are sound investments, and that's what the four rating bureaus say. They get down to the fourth grade and they say they're good, see? Now, when you get below that, you get into what may be termed speculative or unsatisfactory securities. I would say that you list your bonds with the four classifications - bonds and stocks - defaulted bonds - stocks in one classification, defaulted bonds, two; and what we term inferior - I think that's a good word to use - inferior securities or bonds; and then the other, the higher grade bonds. You would charge off the depreciation in your stocks and in your defaulted bonds in the second group and the third group - I mean the second group and the first group.

What I'd like to see done - and I'm willing to compromise it - but I'd like to see it done, and I think it's a good thing to do it, and that is get away from listing the market, because the market today in one bank is not the market tomorrow or next week in another bank, and you tie your banks to the market. Now, it seems to me that it should be enough to list those as inferior bonds, see, and in the recap to show the total of inferior bonds just like you show the total of doubtful paper. But why on earth follow

Crowley: Well, aren't you going to show - make them set up

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reserves to take care of that depreciation?

- Eccles: I'd make them set up a reserve based on total amounts they've got invested in that classification, just like the total amount of doubtful. I'd make them set up a reserve, but I wouldn't say that - here's a market here today hard to justify on these securities; next day or next month, it's an entirely different market. And I think it's time that we're getting away from that, having banks operating on a cash basis. And when you tie it to a market, you're tying the banks to Wall Street, you're tying them - their valuation of their assets to Wall Street. And it does seem to me that - and you know just as well as I do that that market does not mean a market in which you can sell any substantial number of bonds without the bottom going out of that market. There's a great amount of these bonds
- H.M.Jr: Excuse me. How would you price them, Marriner?
- Eccles: Book value. And then I would show the total, just like you take a loan at the book value, class it as doubtful or loss. I would take your bonds
- H.M.Jr: Now look, old man, a stock might - lots of stocks, say, have a book value of 20, but they might be selling at 30.
- Eccles: I'm not talking of stocks. I'm speaking of bonds that have a fixed maturity. Stocks - I'd put them right down to the market. Banks are not
- McKee: Wait a minute, will you? This seems to be a day of compromise. Would you boys be willing to forget these first and second groups that you have had heretofore in your report of examination and go down to C, including B, and forget bond depreciation and take everything else and charge it off?
- Crowley: No.
- McKee: Why wouldn't you?

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Crowley: God no!

McKee: Now listen, don't forget you're passing up that depreciation, Leo.

Crowley: but the first thing you do here - you just pass a Comptroller's regulation recognizing that banks should buy a B-AA bond or better; now we're willing to compromise ourselves and say that anything that is bought under the Comptroller's regulation - that we'll disregard the market, and that takes in a large percentage of all bonds.

McKee: Yes, but you haven't got any yardstick any longer if the Comptroller amends his regulation.

Crowley: Listen, when it's all said and done, the fellow in the bank is responsible for the condition of that bank. Now, if he's gone out and tried to buy when they were trading in and out of these industrial securities, and he's finally sold and paid out his profits to the stockholders, and now he's got a list of bad bonds, why in the hell should the depositors or the F.D.I.C. pay that loss?

McKee: If you've got an adequate reserve on the total bond - corporate bond portfolio

Crowley: It'll take these fellows 20 years to build an adequate reserve.

McKee: Have it transferred so it can't be used for something else.

Now, I haven't asked you much on that, if you'll look at that, but you're just closing your mind to it, see? You forget your first and second group of bonds and consider it all as one group of bonds.

Crowley: What good is the Comptroller's regulation, then?

McKee: You're changing the Comptroller's regulation. The Comptroller's regulation isn't going to refer, as I understand it - correct me if I'm wrong - to any group of bonds or any grade of bonds.

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Szymczak: Just in the background, to be kept in the background.

Crowley: Let me tell you something, that the Banking Commissioners of states like New York, Ohio, Pennsylvania, and Illinois, those large states, will laugh at the Federal agencies if they say that that type of a bond is a bond that ought to be in our institutions. Now, the only reason that they are there is because the fellow bought them and he can't get rid of them, and you're willing to tolerate it as long as necessary, but you mustn't encourage him to buy any more.

McKee: Are you thinking of yourself or are you thinking of the bank, Leo?

Crowley: I'm thinking of both.

McKee: All right, I'm trying to think of the public in general that's got - if you're going to continue a profit system in this country and a capital market, you've got to have a capital market.

Crowley: Now, Marriner, you're going farther than you were going Friday afternoon on these securities.

Eccles: No, not at all.

McKee: I'm making that suggestion. I'm not binding anybody.

Eccles: Just brought it up. We haven't discussed anything.

Szymczak: What do you (Crowley) want, thinking out loud?

Crowley: Take the B-AA group bonds and ignore the bond depreciation. That's a compromise on all those bonds below the - you might say, the Group One.

McKee: It isn't as far as the Comptroller's office are concerned. They never did consider that before, and - unless you're doing it now, are you?

Diggs: B-AA's?

McKee: Yes.

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Crowley: You're putting them in and deducting for net sound capital.

Szymczak: Are you doing it now? How long have you been doing it? Since '35?

Diggs: '36 - I think '36.

Jones: Don't you agree with that, John?

McKee: That far, but he's not off the page yet.

Crowley: We agree with the balance.

Jones: We got one page.

H.M.Jr: Listen, Comptroller, you better get in on this.

Diggs: I better look.

Crowley: We'll agree on the other bonds to take - except the threes and Fours - take the market and deduct that from your net sound capital, make them set up reserves to take care of it.

Jones: How does that strike you? Say it again.

McKee: Going to give them any credit on appreciation?

Crowley: No, don't give them a damn cent credit. You wouldn't either, John.

McKee: Well, if you're going to take something away from these fellows

Crowley: We're not taking it away. They bought these bum bonds themselves, John.

Eccles: Wait a minute.

Jones: Wait a minute.

Eccles: I want to see how far apart we are.

Crowley: There's about 7 percent of the bonds here that are in these bonds that are of a low-grade status,

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and we say that we want some reserve set up to take care of that. In order to make them take care of it, we want to deduct that from the net sound capital, but after we deduct our loss, hike it and make them build reserves to take care of that depreciation in order that they will not tie those kinds of securities together.

Jones: That's sort of punitive.

Crowley: Yes. That's right.

Eccles: This is a fine time to do it.

Crowley: We've always done that to them.

Eccles: We've never done it. We've never done that. The Comptroller didn't do it until '36.

Jones: I don't think it makes a great deal of difference.

Crowley: Let me say this to you fellows. Marriner, your banks that you supervise - New York was here, and they agreed to it; Ohio was here, and they agreed to it.

Szymczak: You're speaking of the supervisors.

Crowley: Yes, but they're your banks.

Eccles: Yes, but the New York banks didn't agree to it.

McKee: But Leo, you didn't get them drunk first?

Crowley: We should have had a bottle here.

Jones: How far - you're not very far apart, are you, John?

McKee: If he can get himself down to B there and just forget these two classifications - you've got some mighty good bonds down at that level that I have full confidence that the public is going to get a hundred cents on the dollar; either that, or your country is ...

Crowley: Would you fellows pass a resolution that for the next ten years you will discount those bonds at par?

Eccles: We'll make advances against them.

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- Crowley: At par?
- Szymczak: Not at par. Use them as collateral.
- Crowley: What the hell - what do you mean by collateral?
- Eccles: Listen, we can't
- Szymczak: Get money for four months - collateral, or anything else.
- Crowley: You want us as an insurance corporation to insure the depositors of these banks on these bonds at par or cost, but you won't loan the Federal Reserve money on that same basis.
- McKee: We haven't got any authority to loan money, Leo.
- Crowley: I don't think we have any authority to let those banks operate that way.
- Eccles: What we've got, as far as the Federal Reserve Bank is concerned - God, it's opened so we can take anything. We got Regulation A, in which we put a
- Szymczak: They haven't been using that.
- McKee: (To Jones) I'm talking about 18 percent plus 24 percent of the portfolio. Now, Leo wants to include 46 percent of it; I want to include this other 18 and 24 in there. If you're going to take away their depreciation from them, see, I say that depreciation you're going to take away will wash itself out in this credit he's going to give them. Now, I'm just - I know I'm sound as hell on that.
- Szymczak: Sounder than hell.
- Ransom: John, they're caucusing on you there. Better look out.
- Jones: Get some dice. Settle it with the dice.
- Crowley: How you going to arrive at a value, Marriner?
- Eccles: The value changes every day.

- Crowley: But you're going to make changes.
- Jones: Now, what Leo is talking about is a little bit more conservative, isn't it, Marriner?
- Eccles: It's more conservative than the way you're doing now. It's deflationary. I've got a bank here. The real difficulty here
- Crowley: No, this is a big liberalization of what we're doing now.
- Ransom: Tell me how, will you? I'm interested in that.
- Crowley: You take your bonds today in your various states. They're making these fellows put up - these stockholders put up to take care of depreciation in anything below your A grade bonds.
- Draper: Allow them appreciation on it?
- Crowley: No, they don't. No one has ever allowed it.
- Ransom: You're talking about state bank supervisors.
- Crowley: We would never have got these banks in any kind of shape at all, as Jesse will tell you, unless we went in and made them rebuild their bond portfolio. They had a terrible mess with them. There's not very many of that kind of securities in your large state members, Marriner. It's mostly in your smaller banks.
- Eccles: That's why you don't want the deflation.
- Crowley: Let me tell you about deflation. Do you realize
- Eccles: You agreed with me the other day that on this bond approach, Leo, you don't like them at the market.
- Crowley: I don't want to list the market on these AA bonds.
- Eccles: Any bonds.
- Crowley: I'm perfectly willing to go with you on what you were talking the other day, if we can agree on reserves.
- H.M.Jr: Well, gentlemen, where do we differ?

- Eccles: The Comptroller and Leo here want to take only the A - the three upper grades of bonds and ignore the market, including Governments. Now, those are the group of bonds where there is appreciation.
- H.M.Jr: Appreciation?
- Eccles: appreciation. They don't want to allow the taking of the appreciation at all in that group. Now, you get down to all bonds that come below that group, including the BBB's, which are the first grade bonds below it, which the Comptroller says are eligible for investment, see, but yet they're expected to take the depreciation in bonds which they say are acceptable, and the depreciation in all other bonds in that group. That depreciation doesn't mean anything, because it's based upon a market, and that market changes; therefore, the amount of the depreciation changes from day to day. That total depreciation - they want to deduct that in the recap in showing what is left of the capital, see?
- Now, what we want to do is to take and put in the first group of bonds all bonds in the three A classes and the BB, put that all in.
- Jones: Now, you agree on that, don't you?
- Crowley: We agree on that.
- Eccles: And we don't want to take market on those at all, just list them at cost, see? The bonds in the next group would be listed separately and would be termed inferior bonds, see?
- Ransom: Sub-standard.
- Eccles: Well, we - that you don't take the market on those either. See, I want to get away
- Jones: Wait a minute. You don't agree with them on that; that's where you differ.
- Eccles: That's right.

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- H.M.Jr: May I make a suggestion, possibly, on this third group. As I get it, you're getting down to two groups, because on the first two - you're going to lump them. Now, on the inferior, where you seem to be apart, let me make a suggestion. What Governor Roosevelt did in New York, the way he saved the insurance companies - as I remember, he took the average quarterly price of their investments - I think it was either the previous 18 or 24 months, and averaged them.
- Eccles: Something like that.
- H.M.Jr: See? As I understand it - I think that White, the superintendent of New York banks, when he was here made that suggestion.
- Eccles: Sensible.
- H.M.Jr: That's what Governor Roosevelt did in New York, and if he hadn't every insurance company would have been closed up. Now, I'm just offering that as a suggestion. And White, the superintendent of banks, I think, made that suggestion when he was here.
- Crowley: Except this, that Governor Roosevelt took it on all of your bonds and then he had the benefit of the Ones and the Twos. Now, we're allowing them the depreciation on the B-AA's, and if you take your average on your so-called BB's and on down, you're going to get a false picture of your bank at the time. Now, I'm perfectly willing to
- Upnam: Excuse me a minute.
- H.M.Jr: Let him finish.
- Crowley: We're down here, Marriner, to a group of bonds that represent a very small percentage in the total, but it represents a hell of a large percentage in a lot of small banks of five hundred thousand and a million dollars in this country.
- Eccles: Well, you don't want to put the pressure on now.
- Crowley: Now wait a minute. Here's what those fellows do. They went out in 1934 and they bought in and out and

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in and out, and they wanted to pay back their debentures and their preferred stock out of their bonds profits, and we wouldn't let them. They paid dividends and raised salaries and everything else on the profit that they made. Now they find - they've given up guaranties that the directors had in the bank to help take care of impaired capital - now we find they've got a large percentage of these damn bad bonds, and just as soon as they get in a little trouble they hold up their hands and we say, "Now, fellows, you shouldn't have done it, but we're going to go along with you."

The only way you can make these cashiers of these small banks realize they can't buy those securities is to penalize them for it. The small banks really shouldn't buy any industrial corporate securities at all.

- McKee: May I ask you one simple question? Now, listen to this.
- Crowley: The way Marriner
- Eccles: I was just going to say ...
- McKee: May I ask you one simple question? If and when you classify securities as you suggest, what's going to be the final answer of the new classification on today's market as compared with the old classification?
- Crowley: I think if we get to that point, the Secretary or someone can call us together and we can sit down and discuss it.
- McKee: That isn't the answer to my question. Penalizing them for appreciation and classifying as is suggested in the second page of that memorandum, what will be the total answer of your portfolio?
- Crowley: You've given up every damn thing you've ever stood for in getting these banks to buy bonds of investment quality.
- McKee: You don't come out dollars and cents with me yet. I'll give you the answer: that it's going to be worse than it is now.

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Crowley: That's just a statement, John, that's not a fact, because you take - in your own examination it won't be a fact.

Booles: Leo, what happens - they make investments in the bonds the Comptroller's regulation permits, first four upper grades, during good times. Those bonds will get into bad times and will be dropped by these rating bureaus, and they will rate an A bond down into the BB, and an AA to a BBB. We say, "It's perfectly all right for you to buy these bonds when they're 100, yielding $3\frac{1}{2}$ percent, but if they drop down to 50, when they may be a buy, then we say that you've got to take your loss on those bonds." Now, if you hold those bonds and those bonds go back again, just as has happened - those bonds that are rated up here in A, they'll drop down when earnings drop down, and they come back up with an improvement, and what you want to do is to let them take them when they can buy them high, when they're selling at par or at $3\frac{1}{2}$ yield; the minute they drop down, because of the Comptroller's regulation/the yield is from $3\frac{1}{2}$ percent on the upper group to 7 percent in the lower - there is just a demarcation just that quick.

We favor the big business, we give them easy credit, we give them the high rating, and

Crowley: Marriner, two thirds

W.A.Jr: Go ahead, I can wait. Go on, Jesse.

Jones: As I understand, Leo, the only thing you're talking about is these low-grade bonds in your little banks.

Crowley: That's right, below the B-AA's.

Jones: All right, suppose we agreed with you; then what, in your opinion, would be the result?

McKee: It would be a penalty on sound capital.

Jones: All right, then what happens? The bank examiner goes in and examines this little bank and he says, "You've got to knock off two thousand dollars here off your sound capital because of this bond depreciation." Then what you going to do to him?

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- McKee: Then he's going to say, "I can't pay interest dividends on my debentures to Jesse Jones." Going to raise the rate from $3\frac{1}{2}$ to 4 percent on them.
- Jones: I don't believe that that works that way. I'm talking about now
- McKee: So am I. When that fellow can't keep his articles of association current with you, he's penalized in interest rate. Now, this is going to penalize him more, because he's going to have to take his earnings and charge that stuff off.
- Jones: How much - how many dollars involved?
- Crowley: Oh, in the little banks, Jesse, there would be from four to five hundred million dollars.
- Szymczak: What percentage is that of ...
- McKee: In their bond accounts, no, Leo.
- Crowley: I'm talking about the entire United States.
- McKee: Then you're still high.
- Crowley: Then if I'm high it doesn't make any difference.
- McKee: You're talking about something that doesn't cost me any money.
- Crowley: I'm not saying
- Jones: Only got about a hundred million dollars involved.
- Crowley: You mean of bonds of that type?
- Jones: Well, let's say two hundred million dollars. I don't think it's going to affect anybody much.
- Crowley: But Jesse, you can't hold - if you go out with this statement to the public that you're going to disregard bond depreciation on all securities, you're going to have an effect on bank supervision and confidence of banks, and any fellow that knows anything about investments is going to laugh his head off.

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- McKee: But at the same time you're not going to give them any credit.
- H.M.Jr: Look, what we're talking about now is lower grade A bonds. What's the matter with that suggestion I raised, that you take these lowest-grade - I don't know what the practice is in New York State - and you average them over 18 or 24 months, the average price. What's the matter with that?
- Crowley: All right, we'll do this with you.
- Draper: That sounds very good and feasible.
- Crowley: Wait a minute. Where's Marshall?
- Szymczak: "Where are my glasses?"
- H.M.Jr: Under the table.
- Crowley: Supposing we do this. We agree on the depreciation in B-AA and better bonds. We'll agree on the other bonds, except defaulted and the stocks, that we'll take an 18-months average of the market and put that in, deduct that from their net sound capital after we charge off the losses.
- Eccles: That's on the second ...
- Crowley: That's right.
- Jones: On Group
- H.M.Jr: On Group One, we just ignore the market.
- Jones: I move it.
- Eccles: I think that's all right, because you have an 18-months
- Jones: That sounds reasonable to the public.
- Eccles: You're giving them an average on it.
- Jones: I could understand that.
- Diggs: They're not legal investments for National Banks.

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- McKee: But you can treat what is already there in that fashion.
- Eccles: When you say legal
- Diggs: Can't buy now under our regulation; even with the change, still can't buy them.
- Eccles: That's true, they can't buy them; they acquire them when they're A and when they're BB they drop
- H.M.Jr: Now, gentlemen, you all right on this?
- Crowley: O.K.
- Jones: O.K.
- Eccles: Leo, I want to figure just a minute now - we'll take that - let's see about this net sound capital both on loans and investments, whether or not that should be actually
- H.M.Jr: Excuse me one second. How are you going to take it? Take what they do in New York, or are you going to take 18 months, or are you going to take in quarterly dates?
- Crowley: No, we're going to take it in 18 months.
- McKee: That's fair.
- H.M.Jr: Just wanted to know.
- Crowley: That won't hurt us any, Marshall.
- Upham: Month's-end averages.
- H.M.Jr: Well, they'll work it out.
- McKee: Give me that sheet here.
- Eccles: This next thing is, we get down to the question of what's sound capital.
- Szymczak: And what relation it has to unimpaired capital.
- H.M.Jr: This is the last thing.
- Eccles: This is the last one. Four subjects, and you've

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covered three of them.

The last page. Now, let's read the last page here.

"Until losses have been written off and adequate reserves established, the use of profits from the sale of securities for any purpose other than those, will not be approved." That's O.K. Agree on that one.

"Present practice will be continued under which estimated losses must be charged off." Agreeable - both loans and investments and stocks - agreeable.

"Present practice will be continued under which the establishment and maintenance of adequate reserves, including reserves against the securities account, are encouraged." Well, that's more or less a repetition of the first one. There's no objection.

"Present practice will be continued under which speculation in securities is criticized and penalized." No objection to that.

McKee: Why leave this third in here? Don't see that it means anything.

Eccles: Let me get back to the reservation I made on page one at the bottom of the page, as applying on both loans and securities.

"Present practice will be continued under which the totals of III and IV above are deducted in computing the net sound capital."

Now, I don't know, you've overlooked one thing and that is, the present practice would be continued of deducting the market depreciation on the inferior securities; they do both, ~~we~~, that is, both the doubtful bonds and the doubtful loans. And right there is the point where we disagree.

Crowley: Now, where do we disagree on this?

Szymczak: No.

Eccles: Yes, we do disagree. Leo wants to deduct that in determining the sound capital.

Crowley: Deduct what, Marriner?

Eccles: The doubtful paper.

Crowley: Here's what they agreed to, Marriner. Here's a bank's capital. They deduct their loss. Then they make a footnote showing the amount of this so-called note; Item Two is not deducted, you understand. This here is not deducted. It's only - it's in Three, that's deducted.

Eccles: That's doubtful.

Upham: Doubtful and loss.

Eccles: But you deduct all the doubtful and ...

Szymczak: Well, that's the extremely doubtful, not the slightly doubtful.

Eccles: Just a minute. You deduct that doubtful and then you also want to deduct the depreciation on this second grade of securities.

Crowley: That's right, because that's a doubtful item.

Eccles: My point is, why deduct it? Here's the form of statement. Look here, Jesse; it's in the recap; there's no objection to listing, we've agreed to all the listing. Now, when you bring up the recap, here's what you have. You have your surpluses put in here, undivided profits, and your reserves, and so forth. There's the total capital structure as shown by the books of the bank when the examiner goes in there. See? Now, deduct here your losses, see, both on your loans and also on your defaults and your stocks; and then put down here capital structure after the deduction of losses.

But what they do - and we don't, and never have done it; it was never done by them until 1934 or '35.

Crowley: We didn't start until '34.

Eccles: He didn't - the Comptroller didn't do it.

Jones: He says he's never done it.

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Eccles: They've done it since then. Now, they come in here and they enter in here the depreciation on these securities, that is, the market depreciation on this sub-standard group of securities. They put that in here and then they take the doubtful items in the loans - they're not loss, they're doubtful, and these securities are not loss yet; they're depreciated and they're sub-standard, it's true. But they want to deduct those two items as well, and then they don't make them charge them off, but so far as the recap is concerned, they come and they say, "Then this is the sound capital."

Now, it seems to me

Jones: What you're talking about is this doubtful item.

Eccles: I'm talking about the doubtful loans, because there is always a lot of recovery. And instead of deducting them and showing the sound capital, let them do that on their work sheet. Let them write a letter to the banks if they want. I would list that in a memorandum right here, for instance. I'd put "total depreciation on securities of sub-standard value, so much money; total doubtful loans, so much" - call those to the special attention of the examiners. But don't take and deduct them here.

Jones: What you got to say to that, Leo?

Crowley: You can't do that.

Jones: That's out. You made a good speech.

Eccles: Well, but I'm just saying that it's something that we didn't follow.

Szymczak: What relation has your net solvent capital to your unimpaired capital?

Crowley: Not at all.

Szymczak: That's important. That's all right.

Crowley: Are we through?

McKee: No, it's penalizing them.

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- Crowley: John, you've got to penalize these fellows some place.
- Eccles: You've giving them notice, Leo, that what this amounts to is their - the law provides that whenever a bank ...
- Jones: Well, we can come back and have another meeting.
- H.M.Jr: Don't want another meeting. Let's finish it.
- Jones: Six months or a year from now - if they holler about that.
- H.M.Jr: I thought you meant now.
- McKee: Let me ask the Secretary, has there been hollering? The answer is, yes, some of it.
- H.M.Jr: Yes.
- McKee: I say when you come out today you haven't made one inch of progress.
- Eccles: Well, I think you've made some.
- Oliphant: Do I understand your suggestion, Marriner, that instead of putting that at the bottom of that form you'd put it on a separate sheet of paper that went to the back?
- Eccles: I would put it as a memorandum. I'd advise the directors. But here's what it does. Our lawyers say that that's a serious question if that isn't equivalent to a legal notice, Herman; that when you write it in like this and you've served notice on them in the report, you've served notice in the report here that they've got an impairment, whereas as a matter of fact ...
- Oliphant: Your suggestion is that you look at the report and if you decide to make a comment on the report, then you put it in a separate letter instead of putting it in the recap. I just wanted to see what the question was.
- Eccles: That's right. But this is not doubtful, it's recovery.

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- H.V. Jr: Can't you get those fellows ...
- Jones: Do you deduct all your doubtful?
- Crowley: We do this, Jesse. We take and deduct for the purpose of determining bank capital all of its lost paper and all of its defaulted bonds and all of its stock down to the market. Then we take their doubtful paper and we total it up and we deduct that in determining what portion of their capital is left as a cushion to the depositors, assuming that you've got enough recovery in your doubtful stuff to help take care of some of this stuff that's in Group Two; because there's more losses in Group Two, you're not setting up any doubtful in that at all.
- Jones: You couldn't take half your doubtful?
- McKee: That's what we did here to capitalize banks. Remember?
- Crowley: This isn't - the fellows have all agreed; we've gone with you on bond depreciation.
- McKee: What do you mean you've gone with us?
- Crowley: Marriner and you fellows are all satisfied on that.
- McKee: Who said we were satisfied?
- Crowley: That's what your chairman said.
- Eccles: We accepted it, that's all.
- Crowley: We can't go with you on the doubtful, it's out of the question.
- Eccles: How can they do it?
- Crowley: Marriner, my dear sir, most of your banks are doing it right now. Most of your banks are doing it right now, and it hasn't caused any hell of a ... You can't stop these
- Eccles: Our examiners are not doing it.
- Szymczak: Some of them are.
- Eccles: They're doing it one place, and they're doing it down in Dallas. New York object to it very strenuously.

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- Crowley: Just the last two months New York hasn't done it.
- Eccles: Because they never did it before.
- McKee: You mean the doubtful.
- Crowley: No, no.
- McKee: Now listen, Leo, before you came to town nobody did it.
- Crowley: Well, by God, it was a good thing we came to town.
- McKee: Maybe so, but before you came to town - maybe you did it.
- Crowley: You fellows are just. . . .
- McKee: Half of it, in order to arrive at a point as to the ratio of capital to deposits
- Eccles: Here's what happens.
- Crowley: I'm with you, but I'm not with you on that doubtful business.
- Eccles: As the depression proceeds, the amount they have thrown in the doubtful increases.
- Jones: As the depression recedes.
- H.M.Jr: Listen, fellow, have you seen the stock market the last two days?
- Eccles: I've been too damn busy. I've been too busy. I've seen it do that before.
- McKee: Because Leo Crowley is getting liberal.
- Eccles: The amount in the doubtful increases, Leo; the amount in the second grade bonds drops down, and as it does it temporarily impairs the capital structure. To put directors on notice that the bank can't accept deposits - now, that's just the same as a legal notice, and I say, why not give them a legal notice and call it a loss while you're at it? Now, I'm perfectly willing to put it as a memorandum item,

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but why you should go so far as to say that your sound capital is thus and so, and deduct the doubtful and deduct the depreciation on these securities, which is a market matter, just doesn't seem to me to make sense.

- Jones: Well, you want to take the doubtful out entirely, huh?
- Eccles: I'd like to take the doubtful and the depreciation out as a deduction. I'd just like to take the capital structure of so and so, as shown by the books, and then deduct your loss and then list the other as a memorandum item. But don't serve notice that the sound capital is so and so, which might show an impairment.
- Jones: I got a suggestion to make. Suppose you said that instead of deducting the doubtful items - say that the sound capital is X dollars, with the footnote that "this includes X dollars of doubtful items."
- Crowley: You mean on your front.
- Jones: Right along - included
- Crowley: Aren't you going to show your directors the condition of their bank?
- Eccles: But you don't make a figure of sound capital.
- Jones: Put it in there right along the side.
- Crowley: What's the use of trying to hide it?
- Eccles: "hat you do, Leo, is deduct it and write in here your sound capital. It says only so much.
- Crowley: That's all it is.
- McKee: May I say one word, please?
- H.M.Jr: I'd like to see anybody stop you.
- Jones: Boys, it's exactly an hour and - 4:22.
- McKee: If you have any loss - nobody is penalizing your examiner and putting it in the loss column. Now, the reason he's got it in the doubtful column is

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because he's not so goddam sure whether he's right or not. Isn't that right? That's the reason it's in the doubtful. If he thought it was a loss, it would be in the loss column.

Crowley: I'll tell you the reason. A hell of a lot of it ought to be over in the loss, but by God, with this idea of monkey business with examinations, you throw it back in doubtful so you don't show an impairment. A hell of a lot of it ought to be loss.

McKee: I'm not in favor of monkey business. If it's loss, put it in the loss. But when it's determined on a man's opinion as to whether it's collectible or not, then it's doubtful. Now, if he can't assure himself that some part of it is loss, then he can't afford to put it in there. Then it shouldn't be penalized as far as the capital is concerned. Now, is there anything unsound about that argument? The thing that you're not sure of is that your bank examiners will operate that way.

Crowley: I'm not so sure as - of my own as of the other fellows, too.

Eccles: Let's do this - let's compromise this.

Jones: You mean let's compromise by agreeing with Leo?

Eccles: Instead of deducting all the doubtful - see, when you deduct it all, that means that it's all loss - let's compromise by deducting half the doubtful and deducting half the market depreciation. Now, you deduct it all; we go 50-50.

Crowley: Wait a minute, you're going to get us both ways here. We took the Secretary's 18 months.

Eccles: That's all right. We're talking now about whether you're going to deduct that depreciation and this doubtful paper in arriving at sound capital. Now, you want to deduct it all, we don't want to deduct any. I say let's compromise it and deduct half of the depreciation.

Crowley: Let me ask you a question.

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Jones: Wait a minute.

Draper: He agrees.

Crowley: Let me ask you a question. You said that your lawyers said that the doubtful would have to be an impairment of capital if it was deducted.

Eccles: Our lawyer said - I didn't get a written opinion of this - he said that putting that in, in his opinion, see - offhand opinion was that that was equivalent to serving notice to the directors that that was their sound capital, and if it showed an impairment and they accepted deposits after that period, they were liable.

Crowley: Then in your mind that's something that impairs their - that would impair their capital.

Eccles: Well, I don't know.

Szymczak: Not in his mind - I don't want to speak for Marriner - I mean in the minds of the directors.

Crowley: One time he tells us they don't want to do it because it's a notice of impairment.

Eccles: You don't

Crowley: All right, then he says 50 percent. When I get ready to say I'll agree to the 50 percent, providing he'll consider that as notice of impairment and make them improve their capital, he runs away.

Eccles: No, I'm willing to do - that's perfectly all right.

McKee: All right, Leo.

H.M.Jr: Come on. Sold!

Crowley: All right. Sold.

Szymczak: I move it.

Crowley: You pulled me back to ...

H.M.Jr: Now restate it, so that you see where you are.

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- Crowley: That we take the total of the doubtful assets, we split it in two, and we carry 50 percent of the doubtful paper over.
- Eccles: That's Number Three doubtful.
- Crowley: No, not Number Three doubtful.
- McKee: My God, you're not going to take Number Two and Three.
- Gaston: Number Three classification.
- H.M.Jr: Start over again, Leo.
- Jones: If you let him repeat it
- Crowley: That we take the so-called doubtful paper and we total it; we take 50 percent of the total, we deduct it in the net sound capital.
- Eccles: Same as you do losses.
- Crowley: And if that deduction shows an impairment of capital, we shall consider it an impairment of capital.
- Eccles: That's O.K. And the same with the depreciation; 50 percent of the depreciation.
- Crowley: That - no, now we're taking the Secretary's provision on the depreciation - 18 months.
- Eccles: We're not going to deduct that at all.
- Crowley: That goes in as a loss. You agreed to that.
- Diggs: That's a loss.
- Eccles: You mean the whole amount of that - are you going to deduct that in showing - arriving at sound capital, or showing impairment?
- Crowley: Arriving at sound capital.
- Eccles: I don't want any misunderstanding. I'm not sure that I thoroughly understand that. Now, here's the statement. Let's just see how we're going to put that in there.

- Jones: You get down there and show him.
- Crowley: Where's Marshall? Get around here, Marshall.
- Eccles: Now, you're going to continue this. All right, you've got - there's your capital structure. Now, this in here - what you've put - see this doubtful item? Now, that, your doubtful item, is on loans - one-half of Number Three classification would be put in there.
- Crowley: That's right.
- Eccles: All estimated loss on bonds be put in there.
- Crowley: Less this depreciation arrived at
- Eccles: What I'm contending is that all of this should also be put in there. Then this should be figured on a basis of impairment. Not fool ourselves a damn bit. Let's actually figure it.
- Crowley: Well, all right, what you want to propose to do is to take half of doubtful and half of estimated losses and figure sound capital.
- Eccles: I mean all of loss and half of the
- Crowley: Let's do this, Marriner. Let's wait - let's do it - all right, let's agree on that in principle, but let's wait until we get our technical men to work it out. But we don't disagree on the principle.
- Eccles: Take the doubtful item and the loss item and you could say, "Capital structure shown by both"; then you could say, "Less one-half of the doubtful, less estimated loss," here, and in which you would then show, "This is the sound capital." Then you could write, "In addition to this, there is a depreciation on these securities which should be taken into account in considering the condition of the bank," or something of that effect.
- Crowley: Let me say this to you.
- Eccles: And you've got your actual sound capital.
- Crowley: Let me make a prediction. I bet it won't be 48 hours after you get your technical fellows on this that you'll be back and want it our way.

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- Eccles: You mean half of your depreciation.
- Crowley: You'll come right back to our proposition.
- Eccles: What you're talking about is half the doubtful. That is, in Number Three.
- Ransom: Why do you say that?
- Crowley: Because you're going to impair a hell of a lot of your banks that we never intended to impair.
- Szymczak: That may be true in some cases.
- Eccles: But the point is, you impair it this way. That's the point I'm making.
- H.M.Jr: Gentlemen, will you - Jesse, McKee, just listen a minute, please. What I would suggest, so there be no misunderstanding - the press has been out there for two hours; if it's agreeable to you, I'd like to ask them in now, see, right in here.
- Eccles: Let's wait a minute. Why not - why not
- H.M.Jr: Just take our time.
- Eccles: I was just going to say, why not say that we've reached a compromise on this thing?
- Jones: Agreement, not compromise.
- Eccles: We've reached an agreement. We've reached a unanimous agreement on this and that. As to what it is, we'll be able to say later. And then we'll get together for the purpose of writing up the announcement of what it is. Now - I mean it's a lot of stuff; they're going to be interested in a lot of detail, and I don't think we should discuss it. Merely say - let the Secretary say to them - we don't need to be here - ...
- H.M.Jr: I want you here. I want you all here.
- Eccles: .. we've reached an agreement. As to the detail of it, I don't think we ought to get into a discussion of that now; that the three agencies should get together and agree upon the

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- Jones: Well, we've already agreed.
- Eccles: I know, but what I mean - as to what
- Jones: We've reached an agreement, and the Secretary will make a statement.
- Oliphant: Marriner, is this what you mean: "We've reached an agreement and turned it over to the technical men"?
- H.M.Jr: No, no. What I'd like to say is this. Going to say, "We've reached an agreement - a number of changes - and we're going to have this thing written up, and it's going to be - we're going to take a look at it tomorrow afternoon, and then Thursday we'll send it to the President."
- Eccles: After it's submitted to the President, we can release it. We can't do it before. And nothing should be said about the details.
- H.M.Jr: Now, may I say this, looking at the light - I'm not looking at anybody in particular - that there's more leaks on this thing than anything I've ever had. I don't know where they come from, but there have been a hell of a lot of leaks. Now, this time I don't - hope that everybody will impress it on his subordinates that until the President gets this - now, we do him the courtesy of not letting it leak; it becomes a White House document, and when it becomes a White House document
- Eccles: He might have something to say about it.
- H.M.Jr: You bet your sweet life.
- Eccles: So I don't see why we should
- Oliphant: Say you have reached an agreement on your recommendation to the President.
- Szymozak: We no longer speak of a minority and majority; that's out.
- Oliphant: That's out.
- Gaston: Reached unanimous agreement on recommendation to the President.

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- Szymczak: No such thing as a minority.
- Crowley: Mr. Secretary, may I say something to you? I don't like to leave here with the thought that we're going to leave any impression with the press that you're going to after Labor Day start this ...
- H.M.Jr: I'm not saying anything about that.
- Crowley: Now, couldn't we have the Secretary say this, that we've reached an agreement, that we're in accord on loans, we're in accord on bonds of investment quality?
- Eccles: Don't get into any detail.
- H.M.Jr: No, no, I think the important thing, if you don't mind, is to say that after consultation the various agencies involved have come to a unanimous agreement on a report to be submitted to the President.
- Oliphant: Just exactly.
- H.M.Jr: * unanimous report.
- Eccles: The staffs have come to an agreement.
- H.M.Jr: The people in the room here.
- Crowley: Now let's have it understood, though, we're not going to have any backing in on this loan business.
- Szymczak: What do you mean?
- Crowley: On this business of ...
- Eccles: We're not going to go back; we'll stick with you on that.
- McKee: You want to see them alone?
- H.M.Jr: No, no, I want - very much want you people here.
(On phone) Tell Miss Chauncey and Mrs. Klotz to come right in, please.

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May I say to you all, I appreciate - I'm very serious now - the spirit of give and take, and I'm delighted that you all ...

Szymczak: We feel the same way about it, Mr. Secretary.

Eccles: I want to say this, Mr. Secretary, that this is a great relief to me, because, damn it, I've been put on a hell of a spot.

Szymczak: You're off it now.

Eccles: And I felt quite embarrassed, and I'm appreciative to you for the way this matter has been handled, and the results. I speak for myself as one member of the Board; I'm very well satisfied with the entire outcome and the spirit in which this whole matter has been handled.

Szymczak: And no more speeches and no more statements.

Jones: I want to make a statement. I want to congratulate Leo; I want to congratulate Leo for being so amenable and so agreeable to everything.

(Mrs Klotz and Miss Chauncey come in)

Szymczak: You say being so mean?

H.W.Jr: I think this - I really was terribly worried, because I've said right straight along I think that the thing that would be most harmful to the Administration would be to have a real break between any of these agencies, and I was terribly worried that we were going to have one, and now I find that we're not. And I think the reason is, we're all more interested in the success of the Administration than we are in ourselves as individuals, and I think as long as that's true, why, the country will have confidence in us. But they can't have a great deal of confidence in us if we can't get together ourselves.

Hansom: Mr. Secretary, doesn't it mean too that these agencies can continue their study with a better understanding of one another's points of view from this point on?

H.W.Jr: I think so.

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Ransom: Isn't that really the most important achievement that has been attained?

H.M.Jr: I think we all owe a debt of gratitude to Mr. Upham.

Szymczak: Cheer, cheer.

Eccles: He's very patient.

H.M.Jr: All right, now, Mr. Gaston.

Gaston: I summon the press.

(Gaston goes out)

H.M.Jr: The place looks so neat and so quiet all of a sudden. All the scars of battle removed.

(Gaston returns with newspapermen)

Well, gentlemen, in behalf of the men present, they have asked me to make a very brief statement, and I am pleased to announce that the four agencies - five agencies represented here have all come to an agreement and we are now drafting a unanimous report which will be ready for the President when he returns to Washington. I think that it's a very constructive move.

Q: Give us any details?

A: No, it now becomes a White House document, and I think you'll have to wait until the President releases it.

Q: Can you say, Mr. Secretary, whether it pertains to anything more than standards of - unification of methods, particularly as to liberalization of loan policies?

A: No, I think, if you don't mind, now that we've come to an agreement, it becomes a White House document, and that it's up to the White House to decide whether it's acceptable and what disposition they will want to make of it.

Q: If the President approves it, why, then you'll put it into effect automatically?

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- A: Yes.
- Q: Requires no legislation?
- A: No legislation.
- Q: Can you say, Mr. Secretary, whether the unanimous report differs in any important respect from the one that was tentatively agreed to by the three agencies?
- A: Well, we arrived at a unanimous report through the democratic form of give and take.
- Q: What does that mean, sir?
- A: Just what I say.
- Q: Mr. Secretary, might I ask Governor Eccles one question?
- A: You can ask him three, or anybody else.
- Q: Governor, does it take care of the situation that you mentioned in your letter to Senator Vandenberg when you said that one of the reasons that credit was not flowing into credit channels was the severe restrictions?
- Eccles: I don't think it advisable for me to make any statement at this time. I would prefer that the report, after it has been acted upon by the White House, speak for itself.
- Q: Any idea about the state people on this thing?
- H.M.Jr: No.
- Q: Well, they weren't consulted about this meeting, were they, sir?
- Q: No, we haven't had time, but we will send them a - I think we will send them a copy of this report. We just haven't had time to think the thing through, but we most likely will send them a draft, in confidence, because they have been very helpful during the last two months in advising and consulting with us.

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- Q: Mr. Secretary, when you said five agencies, were you counting the Treasury and the Comptroller separately?
- A: Well, there is really - as chairman - it's really four agencies.
- Q: Thank you.
- A: It's four agencies. It's the Comptroller of the Currency, F.D.I.C., Federal Reserve Board, and R.F.C. - four agencies.
- Q: How does the R.F.C. come into this particular picture, Mr. Secretary?
- A: Mr. Jones is Chairman of the R.F.C. I think he's about the largest holder of bank stocks in the United States, and as that, plus the fact that he's had a lot of experience, why, I felt that his counsel would be helpful, and it was, and I invited him to join the group.
- Q: No further meeting is necessary, then?
- A: Well, we're going to meet again tomorrow afternoon after we've got this thing down formally, just to take another look at it. But as to the principles - we're all in agreement as to the principles.
- Q: When will it be submitted to Mr. Roosevelt?
- A: It will go to Mr. Roosevelt at once.
- Q: At once?
- A: I mean it ought to go to him tomorrow night or Thursday morning.
- Q: The changes would be made effective, Mr. Secretary, at what time? Any particular time?
- A: I don't know how those things are done.
- Eccles: That's a matter that wasn't discussed - as to the details and the mechanics of putting it into effect.
- H.M.Jr: Say within a reasonable time.

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- Q: There is some discussion of July 1.
- Crowley: Take at least 30 days before it takes effect.
- Eccles: Say just as soon as we can take care of the practical mechanics of the thing.
- Q: Mr. Secretary, does this unanimous report include the possibility of supplemental or concurring reports from any particular agencies?
- A: Well, it's sufficient unto the day.
- Q: Beg your pardon?
- A: Sufficient unto the day.
- Q: Well, Mr. Eccles, will you report anything to the President beyond what will be in this report?
- Eccles: This report will speak for itself. The Secretary has reported that it meets the unanimous approval of all those present, including the Board, so there is nothing further to report.
- Q: I see.
- H.M.Jr: All right, gentlemen?
- All: Thank you very much.

June 10, 1936

MEMORANDUM:

Subject: Bank Examination Program

The Comptroller of the Currency and the Federal Deposit Insurance Corporation, together with the Executive Committee of the National Association of Supervisors of State Banks, have agreed on a program of uniform standards in connection with the appraisal and classification of loans and securities in bank examinations. These standards have been adopted with a view to promoting a wholesome recovery and providing permanent high standards in bank examinations and bank supervision.

This program, which is the result of careful study and of conferences extending over a period of several months, is a substantial step forward toward attaining a high degree of uniformity in future examinations of banks of all classes. A better coordination of bank supervision and a greater degree of protection to the millions of depositors in the nation's banks are thereby assured.

An important aspect of the program is the proposed abandonment of the term "Slow" in connection with the classification of loans in bank examinations. The confusing nature of the term "Slow" is evidenced by the present requirement of the Federal Agencies that a loan should not be so classified if its ultimate repayment is reasonably assured, even though the loan is slow in a literal sense. The adoption of numerical captions for the loan classification units, with each classification uniformly and clearly defined, should do much to eliminate this confusion.

It has long been recognized that the lending of funds to sound and solvent borrowers, small and large, for reasonable periods, is a legitimate function of a commercial bank, provided there is proper provision for the orderly or ultimate payment of such loans. Bankers should be willing to assume reasonable risks and should not be criticized for so doing. No loan should be classified in a bank examination if the loan is sound in view of the valuable net worth of the maker or endorser, his earning capacity and character, or the protection of collateral of sound intrinsic value. All of these steps add up to more reliable and trustworthy bank examinations.

The abandonment of emphasis upon quoted market prices as a basis for valuing investment securities is another constructive aspect of the program. Both appreciation and depreciation in securities of this quality are to be disregarded. The use of market values has not proved satisfactory as a method of appraising high grade bonds. Approximately 85% of the securities presently held by banks are of investment quality, and appraisal at cost will give recognition to the principle that such securities are investments and are not intended to be continually turned over in the market.

Securities of speculative quality, although not defaulted, represent about 10% of bank holdings. Consideration of net depreciation in these securities in determining a bank's net position is necessary if the risks involved in speculative securities are to be appropriately reflected. Defaulted bonds and stocks are approximately 5% of total bank holdings and net depreciation in these securities is an estimated loss which should be charged off. The present practice will be continued under which premiums on securities purchased must be amortized.

Another important part of the program relates to the treatment of profits from the sale of securities. Until losses have been written off and adequate reserves established, the use of profits from the sale of securities for any other purposes will not be approved. The present practice will be continued under which the establishment and maintenance of adequate reserves, including reserves against the securities account, are to be encouraged.

This treatment of profits is a sound procedure which many well-run banks have been following for some time past. It will tend in some measure to discourage speculative in-and-out trading in the bond market which is a practice to be criticized and penalized. Too many bankers have viewed their bond holdings not as investments but with a view to obtaining speculative profits from turnover and this condition has contributed to the instability of the bond market. Furthermore, the so-called profits from security sales are in many instances not actual profits but merely write-ups in book value. This results from the fact that a banker, in disposing of securities at a profit, frequently reinvests at approximately the same price levels.

In connection with the Regulation of the Comptroller of the Currency governing purchases of securities by member banks of the Federal Reserve System, purchases of local issues of high credit quality will be permitted, provided there are sound provisions for the regular amortization of such debt by the obligor, and provided further that such issues are not held in excessive amounts. The Federal Deposit Insurance Corporation will continue its present practice which is in line with the above.

This program, viewed as a whole, is believed sound and workable. The nation's banking system is a strong factor in the present situation and the merited confidence of the depositing public in this system must be preserved. This merited confidence cannot be preserved unless bank supervision is courageous and realistic.

The Classification of Loans in Bank Examinations

The present captions of the classification units, namely, "Slow," "Doubtful," and "Loss" are to be abandoned;

The classification units hereafter will be designated numerically and the following definitions thereof will be printed in examination reports:

I. Loans or portions thereof the repayment of which appears reasonably assured. These loans are not classified in the examination report.

II. Loans or portions thereof which appear to involve a substantial and unreasonable degree of risk to the bank by reason of certain unfavorable trends and other unsatisfactory characteristics noted in the examiner's comments. There exists in such loans the possibility of future loss to the bank unless they receive the careful and continued attention of the bank's management. No loan is so classified if ultimate repayment seems reasonably assured in view of the sound net worth of the maker or endorser, his earning capacity and character, or the protection of collateral or other security of sound intrinsic value.

III. Loans or portions thereof the ultimate collection of which is doubtful and in which a substantial loss is probable but not yet definitely ascertainable in amount. Loans so classified should receive the vigorous attention of the management with a view to salvaging whatever value may remain.

IV. Loans or portions thereof regarded by the examiner for reasons set forth in his comments as uncollectible and as estimated losses. Amounts so classified should be promptly charged off.

Present practice will be continued under which the totals of II, III, and IV above are included in the recapitulation or summary of examiners' classifications.

Present practice will be continued under which the totals of III and IV above are deducted in computing the net sound capital of the bank.

The Appraisal of Bonds in Bank Examinations

Neither appreciation nor depreciation in Group I securities (except the fourth grade of general market obligations) will be shown in the report. Neither will be taken into account in figuring net sound capital of the bank.

Net depreciation in the securities in Group II and in the fourth grade of general market obligations will be deducted in computing the net sound capital of the bank.

Present practice will be continued under which depreciation in the securities in Group III and Group IV — defaulted issues and stocks — are classified as loss.

Present practice will be continued under which premiums on securities purchased at a premium must be amortized.

Present practice of listing and pricing all securities will be continued.

The Treatment of Securities Profits in Bank Examinations

Until losses have been written off and adequate reserves established, the use of profits from the sale of securities for any purpose other than those, will not be approved.

Present practice will be continued under which estimated losses must be charged off.

Present practice will be continued under which the establishment and maintenance of adequate reserves, including reserves against the securities account, are encouraged.

Present practice will be continued under which speculation in securities is criticised and penalized.

Classification of Loans

Majority

Refine but not name four classes of loans. Designate them by numerical symbols. List classes II, III and IV (which would include the same loans as are now included as Slow, Doubtful and Loss). The three classes listed will be totaled in the summary of examiners' classifications, and the totals of III and IV will be deducted in figuring the net sound capital of the bank.

Minority

Eliminate the slow column from the pages where it now appears. List elsewhere in the report under some such heading as "Loans listed for information or comment" loans fitting that description. (These would probably not be those now called Slow, some of which would be thrown over into Doubtful, and some not criticized at all.) This class of loans would not be totaled in any recapitulation. Eliminate computation of net sound capital from report.

Issues: The change in name; including (by reference) uncriticized loans; three columns or two with a separate list; recapitulating "Slow" loans; figuring net sound capital in the report. Undoubtedly also there is a difference of opinion as to what loans are criticizable.

Appraisal of BondsMajority

That appreciation and depreciation in Group I securities (except the fourth grade of general market obligations) be neither shown in the report nor taken into account in figuring net sound capital. That the net depreciation in Group II securities (including the fourth grade of general market obligations in Group I) be deducted in computing net sound capital. That all securities be listed and priced.

Minority

Do not list or price securities in Group I in the report.
Do not list or price securities in Group II in the report.
Do not compute net sound capital.
Attach to the report for transmission to the supervisory authorities a complete list of securities.

Issues: Listing and pricing securities in the report; computing net sound capital in the report; if computed, deducting net depreciation in Group II securities (plus that in the fourth grade of general market obligations.)

Treatment of Bond Profits

I think we have a unanimous agreement 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) Until losses have been written off and adequate reserves established, bond profits should be unavailable for any other purpose; and (4) Speculation should be criticized and penalized.

The main issue here was whether bond profits should be required to be actually impounded in a special reserve account and no other use of them permitted.

June 21, 1938.
5:09 P. M.

H. M. Jr: Hello.

Operator: Upham. Go ahead.

U: Hello.

H. M. Jr: Cy.

U: Yes.

H. M. Jr: In the excitement, I want to make it plain I expect this group to be back at 2:30 tomorrow.

U: All right.

H. M. Jr: And then I expect you to have certain documents for them.

U: All right.

H. M. Jr: If that isn't pushing you too hard.

U: No, I'll do that.

H. M. Jr: And then after that, you'd better take a holiday.

U: Mr. Crowley suggested that I come over to his office and we'd both of us go over the work together so that White would know that he was in agreement.

H. M. Jr: Fine.

U: So I thought I'd humor him that way.

H. M. Jr: Well, you know, that's all right with me.

U: All right.

H. M. Jr: What?

U: All right.

H. M. Jr: And - that's all right, anyway they want it.

U: Sure.

- 2 -

H. M. Jr: And - are you in Crowley's office?

U: Yes.

H. M. Jr: He's satisfied, isn't he?

U: I think so.

H. M. Jr: I think he should be.

U: I think so.

H. M. Jr: I think everybody is. There was a fine spirit all around.

U: Yes.

H. M. Jr: Right.

U: I'm very well pleased.

H. M. Jr: I am too.

H. M. Jr: Good night.

U: All right. Good night.

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: June 21, 1938, 5 p.m.

NO.: 973 FROM COCHRAN.

In late trading after filing of my 966, June 20, 5 p.m., franc yesterday evening strengthened to 177.94. At 177.92 this morning French control acquired considerable amount of sterling but yielded some this afternoon at .95. By half past three Guaranty had purchased \$1,680,000 for the control at from 35.8525 to .875. National Bank of Belgium acquired some gold in London. French rentes and shares better; market again taking Treasury bills and National Defense bonds.

Bank of Italy representative, Pennachio, thinks that announcement of French closing of Spanish border and prospect of more favorable Franco-Italian negotiations has been a help in improvement of atmosphere here. The complete and formal denial of dollar devaluation intentions by Secretary Morgenthau delighted Jay of Morgans and other Paris-American bankers. They believe that this has relieved the franc from fears of upsets in currencies. I had a telephone conversation this morning with Jacobson of the BIS. He is still convinced that June is to witness the upturn in world economic trends, and the latest rise in American wheat and cotton delighted him.

END SECTION ONE.

BULLITT.

PARTIAL PARAPHRASE OF SECTION TWO, TELEGRAM NO. 973
OF JUNE 21, 1938, FROM PARIS.

Local observers note increased pressure on reichsmark as clearings are threatened because of German attitude on Austrian debts and particularly upon tourist mark with unfavorable prospect for tourists in Germany including Austria. At the last meeting of the BIS directors, one German banker regretfully admitted that it would be expensive for Germany to incorporate Austria. He said that Austria at the same time would no longer draw in so much foreign exchange from tourists or from loans as when it was an independent country.

European press not surprised at Ambassador Kennedy's denial of stabilization plan since financial writers generally recognize this as premature in present circumstances. Some French circles are disappointed since they thought they saw an opening for possible favorable settlement of war debts and/or abrogation of Johnson law.

END OF MESSAGE.

BULLITT.

EA:LWW

JR

GRAY

Berlin (part air)

Dated June 21, 1938

Rec'd 8:20 a.m., 22nd.

Secretary of State,
Washington.

319, June 21, 5 p.m.

Embassy's 313, June 18, 1 p.m., paragraph number two.
FOR TREASURY FROM HEATH.

Although as far as the British Embassy here knows the Germans have not submitted a definite new proposition with regard to the Austrian and German debts following the British refusal of their last offers the Anglo-German trade and negotiations will be resumed this week. It is surmised here that Leith-Ross conferred with the German Ambassador in London and the conclusion reached was that both sides were near enough to agreement to justify meeting in final negotiations. As a result a German trade and financial delegation understood to consist of some 14 experts including Wisl, Director of the Commercial Policy Division of the Foreign Office, and Bergemann, Brinckmann's right hand man in the Economics Ministry are leaving for London. Leith-Ross told me here two weeks ago that there was no real difference between the two delegations as regards the trade

-2- #318, June 21, 5 p.m., from Berlin.

trade side of the payments agreement: the Germans have practically agreed to take somewhat larger proportions of partly and completely manufactured goods than they have in the past.

The British regard their payments agreement as the most generous arrangement for Germany that that country has been able to conclude and that view is practically admitted in the Reichsbank and Economics Ministry.

During the negotiations the Germans admitted that the agreement provided them during 1937 with 40,000,000 reichsmarks of free foreign exchange. The British delegation believes that the figure was considerably higher. The surplus on trade account in favor of Germany was 123,000,000 reichsmarks. This surplus was reduced by debt payments of 52,000,000 reichsmarks representing (approximate figures) payments on the Dawes loan 10,000,000; Young loan 8,000,000; potash loan 8,000,000; standstill agreement 16,000,000 and funding bonds 9,000,000 reichsmarks. The Germans claim that they also paid for freight royalties, licenses and miscellaneous items 30,000,000 reichsmarks more to the British than they received for corresponding services. This estimate is contested by the British delegation.

It

-3- #318, June 21, 5 p.m., from Berlin.

It was learned today that the German-Swiss negotiations respecting the inclusion of Austria have been suspended. I understand that negotiations broke down over the question of the amount of free exchange to be made available to the Reichsbank. The Swiss are understood to be awaiting the outcome of the Anglo-German negotiations before resuming discussions. The Swiss continue to refuse to change their present clearing arrangement with Germany into a payments arrangement along the lines of the present Anglo-German arrangement.

WILSON

KLP:CSE

PARTIAL PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: June 21, 1938, 11 a.m.

NO.: 989

Reference is made to telegram No. 377 of June 17 from the Department. When it was received Cochran telephoned to Jacobsson in the BIS. By a personal and confidential letter dated June 20, he sent the following reply:

"In response to the question which you put to me over the telephone I am now able to give you the following personal answer.

"In the annual report of the Reichsbank for 1937 published on 11th March 1938 the following sentence appears.

"German commercial debts arising out of clearing agreements and out of special accounts with foreign countries for domestic payments (aski) were redeemed by approximately 150,000,000 reichsmarks at the end of the past year to 313,000,000 reichsmarks for the most part through deliveries of German goods to foreign countries.

"We believe that the indebtedness of 313,000,000 reichsmarks is a gross figure i.e. that such surpluses on certain clearing accounts as are held by Germany have (begin underlining) not (end underlining) been deducted. A friend of mine at the Reichsbank told me at the beginning of this year that the net indebtedness would be about 200,000,000 reichsmarks but I quote this figure from memory and therefore with due reservation.

END SECTION ONE.

BULLITT.

WA:LWW

REB

SPECIAL GRAY

Paris

Dated June 21, 1938

Rec'd 1 p. m.

Secretary of State,
Washington.

969, June 21, 11 a. m. (SECTION TWO)

The 313,000,000 represents the indebtedness in respect of commodity transactions only. This figure does not include for instance the indebtedness of the German state railways to Poland in respect of transit traffic. It should moreover be noted that the clearing accounts only show such payments as are due and that commercial credits may have been given which are more important than the clearing debts. It was found at one time that the German clearing debts to the Netherlands were more than covered by German credits granted to Dutch importers of German goods. We have no estimate of the total of German commercial credits granted in recent years but it is known that many German commercial and industrial firms have given credits to their foreign exporters for three, six and twelve months. I should personally not be astonished to hear that the total of these credits

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REB

2-#969, From Paris, June 21, 11a.m.
(Sec. Two)

is above 1,000,000,000 reichsmarks. Such credits are almost indispensable for German exports are of a nature that they can only be bought if the customer is given a certain amount of credit (as for instance in the case of sales of machinery to Balkan countries).

BULLITT

KLP

COPY FOR SECRETARY

JR

SPECIAL GRAY

Paris

Dated June 21, 1938

Rec'd 1:25 p.m.

Secretary of State,
Washington.

969, June 21, 11 a.m. (SECTION THREE)

I am not able to give you any detailed information with regard to the debts to different countries exclusively, if one goes through the information of the position of the clearing accounts in Italy, Czechoslovakia and other countries one may be able to make up very roughly the German total. Mr. Conolly who as you know deals with these problems will be back at the beginning of July and he may give ^{you} some further information at the time of the next board meeting. The German clearing debt to Austria was of the magnitude of about 60,000,000 schilling and that have all been repaid presumably at the old rate.

In relation to Italy, Germany has a credit item which about a month ago amounted to 83,000,000 lire. In the Austrian Italian clearing Italy was also indebted to Austria to the extent of about 300,000,000

lire

LMS 2-No. 969, June 21, 11 a. m., Sec. 3, from Paris.

lire i.e., about 90,000,000 schillings. It has been reported that an agreement has been concluded with regard to the Italian indebtedness but I am not able to furnish you with any details of the settlement. In some cases arrangements have been made for repayments over a prolonged period as for instance between Germany and Denmark but it is then difficult to tell to what extent the amounts due are still booked as clearing debts.

BULLITT

CSB

PARTIAL PARAPHRASE OF SECTION FOUR OF TELEGRAM NO. 989
OF JUNE 21, 1938, FROM PARIS.

"In relation to those countries with which payment agreements have been concluded no clearing debts are arising and that is of course one of the advantages of the payment agreements.

"I am often asked whether the existence of clearing debts has not helped Germany in recent years to sell her products to, for instance, Balkan countries as these countries are almost compelled to buy German goods in order to make themselves paid. That is probably so but it must not be forgotten that many countries are trying to divert their trade from Germany to other countries in order to get 'edel valuten'. If Germany had a sound currency and would be able to pay cash I personally believe that she would obtain a still greater part of the trade of the countries in Southeastern Europe.

"I am afraid that is all I can give you for the moment."

Last December the Department received a copy of a memorandum of October 25 by Conolly which gave certain data in this regard. At present Conolly is visiting several European monetary centers. On June 23 when Cochran saw him at Basel, he said that about June 30 he would call at the Paris Embassy. At that time he will be asked to get together by the time of the July meeting such further data as he may be able to collect. Right now Beyen is in Rumania, Auboin is in Paris and Conolly is traveling, and very shortly Jacobson is due to be absent from Basel; therefore with

Hechler

- 2 -

Reehler in charge of the BIS, nothing can be immediately
sought there.

END MESSAGE.

BULLITT.

EA: LWW

RECEIVED
JUN 23 1938
TREASURY DEPARTMENT
OFFICE OF THE ASSISTANT
SECRETARY IN CHARGE OF THE BUREAU