

DIARY

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 19, 1938

TO Secretary Morgenthau
FROM Mr. Haas *HAAS*
Subject: RFC Proposal in Relation to Treasury Cash Position
and Outstanding Volume of Treasury Bills

1. It is not clear to us whether the Treasury has made a definite commitment to the RFC to permit a public refinancing early in January of \$500 millions of the \$720 millions of its notes held by the Treasury, or whether the Treasury is still in a position to alter the amounts and timing of the refinancing.

If such a commitment has been made for all or the major portion of the RFC debt, we would nevertheless recommend against retiring bill issues at this time in order to avoid adding to the present swollen cash balance, for reasons detailed in (5) below.

The sale of RFC notes to the public would cause a corresponding reduction in the volume of excess reserves. This reduction would persist until the Treasury disbursed the Federal Reserve balances received from the RFC. Even if arrangements could legally be made for banks to pay for the RFC notes by war loan deposit, the probability is that the bulk of the payments would nevertheless be made in cash. However, with excess reserves at the new record high of \$3,480 millions, this factor is not of great importance. The volume of bank deposits would tend to remain unchanged until disbursements took place by the Treasury of the Federal Reserve balances received from the RFC.

2. If it is decided to retire Treasury bills in an amount roughly equal to the RFC note issue, it may be noted that this process would have to be spread over several weeks — presumably at the rate of \$50 millions or \$100 millions a week. To the extent that the Treasury retired bills, the decrease in excess reserves and the subsequent increase in deposits occasioned by the RFC financing would be offset.

3. If the Treasury's commitment to the RFC permits, it would be highly desirable to postpone the RFC's public offering until the middle of April, and to use the proceeds thereof in lieu of a March new money financing. If this can

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Secretary Morgenthau - 2

be done, we would avoid adding to the cash balance until the latter has been substantially reduced below present levels.

On the basis of Mr. Bell's latest figures, the working balance at the end of March would still approximate \$1,600 millions, if no new money is raised in March. This figure, moreover, does not fully reflect the increased revenues predicted in the revised budget estimates. April, however, is likely to be our peak cash deficit month, and \$500 millions of new money in that month would bring the month-end balance to about \$1,300 millions, plus any increase in revenue receipts not included in Mr. Bell's cash balance estimates.

4. If the Treasury's commitment to the RFC does not permit postponement of the whole operation until April, but does permit splitting it up into several parts, we would recommend that only a very small RFC issue be offered in January; a substantially larger one in April; and the balance in July or August.

5. We recommend against retiring bill issues at this time in order to reduce the amount of the working balance.

(a) If the recommendation made in (3) above is followed, the RFC money will not come into the Treasury until the middle of April, by which time the working balance will have been substantially reduced. Likewise, if the recommendation made in (4) above is followed, only a small addition would be made to the cash balance in January.

(b) The present volume of Treasury bills, whether judged by the market demand therefor, the banking uses thereof, or the negligible cost to the Treasury, is exceedingly small. Nearly half the entire volume outstanding is held in the System Open-Market Account of the Federal Reserve banks.

(c) In view of the fairly steady decrease in the aggregate volume of outstanding Treasury notes, as a result of repeated refunding operations, and the resulting diminution in the volume of Treasury obligations preeminently suitable for commercial bank investment, adverse criticism might well be engendered by a further reduction at this time in the volume of Treasury bills.

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(d) The banking authorities could well be expected to criticize the move on the ground that the present banking situation peculiarly requires a larger rather than a smaller volume of Treasury bills. With excess reserves at a new record high of \$3,480 millions, but with banking capital-deposit ratios remaining relatively small, commercial banks can safely make a full use of their excess reserves only by investments in short-term open-market paper. The commercial volume of such paper has now been reduced to very small proportions, considering the banking system as a whole. Treasury bills provide an excellent substitute.

(e) The retirement of Treasury bills, on which the interest cost is something less than one-fiftieth of one percent, coming so shortly after the Treasury has added to an already large cash balance through issues paying 1-1/8 percent and 2-3/4 percent, might well occasion unfavorable comment. As a matter of fact, the retirement of Treasury bills might easily call attention to the unusual size of the cash balance; whereas, in the absence of such bill retirement, the cash balance might occasion little notice.

6. The view that the Treasury's bill-issuing power should be reserved for strictly emergency use does not stand up well under critical examination. In this connection, we may think of two types of emergencies: A temporary emergency during which it may be impossible or too expensive to float long-term securities; and a long drawn out emergency, such as a major war.

In the case of the first type of emergency, the Treasury would find it possible to sell short-term securities, such as Treasury bills and certificates, almost regardless of the amount already outstanding, if it were willing to pay high enough rates of interest. These high rates, it may be noted, would be only for short periods. It does not appear to be a profitable policy to reserve for emergencies the power to issue short-term bills and certificates merely to reduce the rate of interest that might otherwise be necessary on such securities during an emergency.

When it comes to longer drawn out emergencies, such as a major war, the pertinent considerations lead also to the conclusion that it does not pay to reserve the power of bill and certificate issues for such periods. In such an emergency,

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the total volume of financing that may be necessary would altogether dwarf the significance of the volume of bill and certificate issues that were outstanding just prior thereto. During the single calendar year 1918, for example, the Federal Government increased its outstanding bonds from \$6.7 billions to \$16.6 billions; its War Savings certificates from \$.07 billion to \$1 billion; and its certificates of indebtedness from \$1.4 billions to \$3.3 billions. Further, in the next four months, the certificate issues approximately doubled -- from \$3.3 billions to \$6.3 billions.

It may also be pertinent to observe that a fire escape that is seldom or never used in ordinary times is apt to be too unfamiliar for safe reliance in the event of a real fire. It is well to keep the market accustomed to Treasury bills.

Treasury bills and certificates lend themselves well and economically to at least three types of uses: (a) To meet temporary cash needs due to the uneven timing of receipts and expenditures; (b) to permit borrowing to take place in convenient small installments as needed, instead of piling up unneeded cash by large single borrowing operations -- the bills and certificates to be later funded by bond or note issues of suitable size; and (c) to provide a type of security in special demand by the banking system for the quasi-permanent incorporation of a suitable amount of the public debt.

Presumably because of the low level of interest rates, the Treasury has not made a point of economizing on interest costs by reducing cash balances to a minimum. Hence, the third use cited above, coupled with inexpensiveness to the Treasury, provides the basis for the outstanding bills.

In the light of these considerations, a reduction in or the elimination of the present volume of Treasury bills would be an inferior and relatively expensive way to reduce the cash balance. Indeed, as we have argued in previous memoranda, there are important grounds for expanding the bill volume relatively to other forms of borrowing.



THE COMMANDANT OF THE UNITED STATES COAST GUARD

WASHINGTON

19 December 1938.

MEMORANDUM FOR - The Secretary of the Treasury
(via Assistant Secretary Gibbons).

Attached hereto is copy of a mimeographed circular, prepared by the Joint Maritime Legislative Committee of the Maritime Unions - the controlling organization of which is the National Maritime Union, an affiliate of the C.I.O. This circular was prepared for distribution among union seamen.

I feel you will be particularly interested in the following extracts:

*** "and as far as the rules and regulations now read, they could not be better worded, from maritime labor's point of view, if they had been written by us." ***

*** "there is every reason to believe that our active participation in the training program from this time on will result in helping to obtain for all American seamen an advancement in their standards, particularly of those men who are anxious to advance themselves to higher ratings." ***

*** "we can expect that from now on, if no further obstacle of this kind is placed in our way, the seamen's training plan will be a highly successful one, and prove to be of real benefit to the American Merchant Marine." ***

There are also inclosed herewith, clippings from the "Pilot", dated 16 December 1938, which paper is the official organ of the National Maritime Union, giving the action of the National Council on the training program for merchant seamen. The signatures on this statement are those of the officers of the National Maritime Union, which organization, as above stated, is an affiliate of the C.I.O.

R. R. WAESCHE
Rear Admiral, U.S. Coast Guard,
Commandant.

Inclosures:

JOINT MARITIME LEGISLATIVE COMMITTEE of the MARITIME UNIONS

Rooms 402-404, 1627 K Street, n.w.

Washington, D. C.

December 16, 1938.

Memorandum Regarding the Adoption of the Seamen's Training Plan
by the Maritime Unions

During the period when the last Congress was considering setting up a training plan for American merchant seamen, the Maritime Unions proposed that if any such plan was put into operation that it be supervised by a joint board consisting of members of the Maritime Commission and representatives of maritime labor.

The Maritime Unions had continued their campaign for such a plan right up to the time when the Maritime Labor Bill reached the stage where it was being considered in joint conference between the Senate Commerce Committee and the House Merchant Marine and Fisheries Committee. Sensing the difficulties that would be encountered in the practical operation of such a plan if our proposals were not accepted, we requested that in the event our proposals were rejected, all action on the training plan be deferred until the convening of the next Congress. However, a certain number of government officials and legislators, not knowing the actual situation existing in the maritime field, went ahead without consulting us thoroughly, and the result was that we were confronted with a training plan which had not been given due consideration, from maritime labor's point of view. Quite naturally, maritime labor's reaction to the plan was unfavorable, until quite recently.

Various government officials seemed puzzled by our attitude until it was explained to them that, in view of our not being consulted in regard to the administration of the plan, the rules and regulations which had been promulgated to carry out the Act were unsatisfactory, and would not meet with our approval. This resulted in a hesitancy on the part of, particularly, members of the National Maritime Union to participate as enrollees at the Hofman Island Training School in New York Harbor.

However, just recently, after several conferences between the representatives of maritime labor, the representatives of the Treasury Department, including the Coast Guard, and representatives of the Maritime Commission, we were requested to submit recommendations in the form of amendments to the rules and regulations governing the training plan which would be satisfactory to Maritime Unions. This action was carried out, and

resulted in all our recommendations being adopted, so that now the rules and regulations governing the maritime service are such that no one could possibly object to them on the grounds that they are in any way detrimental to the best interests of labor.

It appears that when the original rules and regulations were formulated, many of them were adopted from the rules and regulations governing the Coast Guard Service, and they were such that they would not be applicable to a training plan for merchant seamen, although they would have been entirely in order if they were to be applied to the armed forces of the United States or to the Coast Guard itself. We have no ground for believing that this was an intentional act on the part of any government official, but it seems it was simply the result of following a routine procedure that had been instilled in these officials' minds by long years of service in a government agency which was, of necessity, constrained to a set-up of a semi-military nature.

The points in the original rules and regulations to which we took exception were mainly those which revolved around the use of the word "desertion", and around the proposed "investigation boards", which boards would have had the power to investigate practically all matters pertaining to enrollees while on active service. After we had pointed out to the proper officials our reasons for protesting against these items, due consideration was given our proposals, with the ultimate result that the required changes were made, and as far as the rules and regulations now read, they could not be better worded, from maritime labor's point of view, if they had been written by us.

Therefore, taking all this into consideration, and the other facts enumerated as reasons for adopting the training program, which were set forth by the National Council of the National Maritime Union at its last quarterly meeting, there is every reason to believe that our active participation in the training plan from this time on will result in helping to obtain for all American seamen an advancement in their standards, particularly of those men who are anxious to advance themselves to higher ratings.

It is regrettable of course, that all these conferences and delays were necessary, but this simply goes to prove the point we raised at the last Congress, namely, that maritime labor, being the primary party interested and involved in this issue, should have been consulted then more thoroughly as to the administrative set-up of the training plan. Of course, this is now "water under the bridge", and having shown to the government agencies involved that in order to make this plan successful the representatives of maritime labor should at all times be consulted on all matters in which it is interested, we can expect that from now on, if no further obstacle of this kind is placed in our way, the seamen's training plan will be a highly successful one, and prove to be of real benefit to the American merchant marine.

Respectfully submitted,

(Signed)

Ralph Emerson,
Legislative Representative.

RE:ne
uppwa #27

The Training Program

The recommendation by the National Council that the membership of the NMU officially endorse the government training plan for seamen may come as a surprise to some. But to those who have followed the situation closely, this advice will be judged as logical and realistic, and in the long run, the wisest to adopt.

From the very beginning, the Union was put on the spot. In describing the opposition of the Union to government training of merchant marine seamen, the newspapers, the radio, and all the other media of reactionary propaganda, pictured the NMU as objecting to the *idea* of training. Naturally, we could rally little or no public and Congressional support, since practically every American would like to see the U. S. develop the finest merchant marine fleet in the world. Our policy was, of course, distorted by this propaganda.

What we were really opposed to was the *method* of training merchant seamen, and not the idea itself. We objected to the probability of seamen being instilled with an anti-labor philosophy by militaristic instructors, and of young newcomers flooding the industry after being trained as strikebreakers. Our position was perfectly valid, and has been finally recognized as such.

We therefore determined that the most expedient way to remove this probability was around the conference table, explaining our position to the proper government authorities. And the result of a long series of conferences is that the Union has received strong assurances that the training program will not be exploited to the detriment of the Union, and that only seamen with two years' actual sea service will be accepted as enrollees.

Certain hostile groups outside the NMU will assiduously spread the belief that the membership has been sold out. These groups are not affected by the training program, as the NMU is, and so they can talk as militantly as they please. Words are cheap. As one of the members of the National Council remarked about the flunk hall problem: "We . . . took a very militant stand on the matter of closing the flunk halls. Well, we had none, so it was easy to take this militant stand."

The National Council was elected by the membership to give leadership and direction. Leadership does not mean constant and unreasoning militancy; it means the intelligent application of policies that will always serve to advance the best interests of the rank and file. We believe that on the question of the training program, the National Council has adopted the correct policy.

Council Recommends Official Endorsement Of Training School Plan By Membership

The National Council, at its quarterly executive meeting last week, issued a statement recommending that the membership of the Union go on record as officially endorsing the merchant marine training school program of the Federal Government.

Heretofore, although the Union had reiterated its willingness to cooperate with the U. S. Maritime Commission in making the training program a success, it had withheld endorsement because the government failed to offer positive

assurances that the program would not be used in any manner detrimental to the best interests of the maritime unions.

Since the NMU has now received such assurances, the Council felt that it could recommend

(Continued on Page 16)

Council Recommends Official Endorsement of Training School Plan By Membership

(Continued from Page 1)

endorsement of the plan to the Union membership.

Objections of the Union to the training plan centered around the rules and regulations of the training school which were formulated without the Union having a voice; the apprehension of the Union that the Coast Guard, which is supervising the school might inject a militaristic, anti-labor philosophy into the minds of the enrollees; the lack of assurance from the Commission that newcomers would not be trained for merchant service and be used as strike-breakers, since at the present time there is heavy unemployment among experienced seamen; and the failure of the school to employ seamen from the merchant marine

Following is the Council statement:

"The National Council of the National Maritime Union, in executive session, recognizing the complex and technical nature of modern merchant service and the necessity for the practical training of seamen to meet this need, hereby goes on record as endorsing officially the present training plan for the following reasons:

"1. Due to the necessity of improving the technical knowledge of a large number of men in the industry so as to make our American Merchant Marine the finest and safest on the seas;

"2. Because of the fact that the present rules and regulations covering the present training plan are such that there can be no doubt of the sincerity of purpose of the administrators of the training plan, and we have positive assurance that under no circumstances whatsoever, shall the Federal Government use the training plan for any purpose that would be detrimental to the best interests of organized labor, i.e., labor disputes;

"3. The National Council of the National Maritime Union has received assurances that there is no intent on the part of the Maritime Commission at this time to extend this training plan to those other than seamen who already have 2 years actual sea service; keeping the thought in mind that when

unemployment ceases among the seafaring group, consideration shall be given to the question of injecting new and young blood into our Maritime Industry, through the medium of training young Americans for service on our Merchant ships.

"The National Council of the National Maritime Union of America therefore recommends to its members that they go on record as officially endorsing the present Maritime training plan.

(Signed)

—Joseph Curran, President,
Ferdinand Smith,
Vice-Pres.,
Jerome King, Sec'y-Treas.,
Frederick N. Myers, Chmn.,
Atlantic District
Frederick C. Phillips,
Sec'y., Atlantic District.
Geo. H. Hearn, Treas.,
Atlantic District,
Arthur Thomas, Chmn.,
Gulf District,
Chas. DeGress, Sec'y.,
Gulf District.

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resulted in all our recommendations being adopted, so that now the rules and regulations governing the maritime service are such that no one could possibly object to them on the grounds that they are in any way detrimental to the best interests of labor.

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The points in the original rules and regulations to which we took exception were mainly those which revolved around the use of the word "desertion", and around the proposed "investigation boards", which boards would have had the power to investigate practically all matters pertaining to enrollees while on active service. After we had pointed out to the proper officials our reasons for protesting against these items, due consideration was given our proposals, with the ultimate result that the required changes were made, and as far as the rules and regulations now read, they could not be better worded, from maritime labor's point of view, if they had been written by us.

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Respectfully submitted,

(Signed)

Ralph Emerson,
Legislative Representative.

RE:ne
uppwa #27

Show to Lochhead and H. White

13

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 19, 1938

TO Secretary Morgenthau
FROM Mr. Taylor

As you probably discovered through developments later in the day, Lochhead, Cairns and I went over the so-called Schacht proposal on financing refugees at 9:45 this morning with Moffat, Livesey and Achilles. The sense of our objections was contained in the suggested cable which I understand Sumner Welles submitted to you. The proposal was so outrageous that our feeling was there should be no connection established between any funds raised by the various outside individuals and the liquidation of the confiscated property.

Bewley called this afternoon to describe the circumstances which had surrounded the British suggestion for joint action on the establishment of stabilization
a fund to support the Chinese currency. I enclose a copy of the memorandum which he left with me. I thanked him for the information and said that whereas I had had no further discussion of this subject since I had last talked with him, my impression was that the tung oil credit arrangements
about constituted all we intended to do at this time; that we felt that we had made a pretty strong gesture and that whereas we were not discarding the possibilities of the type of cooperation which they suggest in the memorandum, I didn't think that it was a very immediate possibility. I based these comments on the conversation which I had with Sumner Welles and the one which I had with you on this subject. He then went on to explain that the Export Credit Guarantee which they contemplated amounted to approximately one-half million pounds to finance purchases of trucks on the Burma road,

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that Parliament would probably act on the legislation which had been proposed early in February. He asked me if we would like to have additional information about credits guaranteed by the Export Credit Guarantee Fund as they developed. I said that we would like very much to have this information and that we would reciprocate. He then expressed some curiosity about the remarks which you had made in your press conference on Latin American cooperation and I gave him the general background.

I talked to Sumner Welles at lunch about Jim Edwards. He thinks very highly of Edwards and thinks he would be very useful in the connection which I mentioned. The rest of the Latin American Republics Division of the State Department likewise reported in and gave him an excellent check. Edwards is leaving tomorrow afternoon for New York preparatory for sailing for Nicaragua. I would like to have you meet him if you find it possible to do so, and in any case, I would like to be able to have a pretty definite talk with Edwards before he leaves.



encl

T. V. Soong told the British Ambassador in October that Chinese Government were thinking of setting up a stabilisation fund. He said the Chinese dollar was undervalued at 8d. and that apart from temporary shocks to confidence the 8d. rate could be maintained, if a reasonably large fund were established. The Bank of China in cooperation with the Hong Kong and Shanghai Bank had been supporting the market. Since the attack on Canton there had been a considerable ^{main} ~~amount~~ of exchange and the Bank of China had had to put up substantial amount to support it. The Chinese banks were ready to put up £3 millions for a stabilisation fund, ^{but} ~~he~~ felt that without outside help the future was uncertain and that if this were not forthcoming they might have to conserve their resources for the military needs of the Chinese Government, in which case the dollar would probably collapse.

T. V. Soong asked that British Banks or authorities put up similar amount (£3 millions). If this could be increased to £5 or £10 millions the dollar would be impregnable for a long period.

Soong said the matter was urgent and the situation critical.

Soong suggested that a small committee of Chinese and British bankers should control the policy and operations of the fund. No details were suggested and none have yet been ^{discussed} ~~discussed~~. The Hong Kong and Shanghai Bank would be ready to put up and operate the fund if guaranteed against eventual loss, and if it had control over the operations of the fund. The operations would presumably be on the same lines as those conducted hitherto by the Chinese authorities working in cooperation with the Hong Kong and Shanghai

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Bank, the objective being to prevent the collapse of the currency and if possible to maintain it round its present rate.

If a similar concession from United States banks were available chances of success would of course be greatly increased.

MEETING OF FISCAL AND MONETARY
ADVISORY BOARD

December 19, 1938.
10:30 a.m.

Present: Mr. Eccles
Mr. Delano
Mr. Bell
Mr. Ruml
Mr. Hanes
Mr. Taylor
Mr. Currie
Mr. White
Mr. Haas

H.M.Jr: "The Fiscal and Monetary Advisory Board has been advised by the experts of the Treasury, Federal Reserve Board and National Resources Committee that:

"1. The 1938 national income is estimated at \$62 billion. For the calendar year 1939 it is estimated that the national income will be between \$65 and \$68 billion."

Any discussion on item one?

Item two: "A national income of around \$80 billion:

"a. would provide substantial reduction of unemployment.

"b. would provide Federal revenues sufficient to balance the current level of cash expenditures on the basis of the existing tax structure."

Bell: Might make it read a little better if you put "would provide" up after the "\$80 billion."

H.M.Jr: I think that's right. I think that's right.

(Delano comes in)

Hello, Mr. Delano.

Delano: Sorry to be late, sir.

H.M.Jr: Do you (Ruml) want to show Mr. Delano how far we've gotten? Have you got a copy for Mr. Delano?

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Taylor: Take that one.

H.M.Jr: We're just doing one and two, Mr. Delano - if you'll take a minute to read that; everybody's satisfied with one and two.

Delano: All right, sir.

H. M.Jr: Mr. Bell made the suggestion to take the words "would provide" and put them after the "\$30 billion," so it would read: "A national income of around \$80 billion would provide: a." That's an improvement.

Shall we go on with three?

"3. An income of \$90 billion or more is attainable through full utilization of our man power, plant and equipment, technology and natural resources, assuming the elimination of some important bottlenecks.

Any questions on three?

"4. Also it is important for Federal fiscal policy to take into account:

"a. changes in the volume of the outstanding debt of State and local governments and changes in the volume and character of their expenditures and receipts.

"b. changes in the volume of capital expenditures being undertaken by private enterprise.

"c. the fact that available supply of credit is so great that present and prospective Federal borrowing will not create a shortage of credit available at reasonable rates for private enterprise."

Haas: I've got a suggestion on that, Mr. Secretary.

H.M.Jr: Please.

Haas: I'd make a the last statement and make b a and c b. And on b I'd have it read this way: "changes in the volume of capital expenditures being undertaken by private enterprise and any hindrances or bottlenecks

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tending to restrict the expansion of private expenditures." I'd put that right at the top.

H.M.Jr: Now, you'd make b what, George?

Haas: I'd make b the first, a, and make c b, and a c.

Eccles: The idea being that that's the relative importance.

Haas: Yes, un-huh. And the whole document is speaking about the other aspect of it.

And then I'd make that addition that I suggested. Want me to read that again?

H.M.Jr: If you please.

Haas: Now a would read - a as modified: "changes in the volume of capital expenditures being undertaken by private enterprise and any hindrances or bottlenecks tending to restrict the expansion of private expenditures."

Eccles: I think that's good. I think it's all right. I like it.

H.M.Jr: Do you like it, Bell? Mr. Delano?

Sold. No?

Taylor: I think c isn't the same kind of a thing that a or b is, and I think if you make c part of your - say, your introductory statement that it is important for Federal - well, it looks as if then it's important for it - it is likewise important for it to take into account these other two

Ruml: In the original text that was a finding.

White: However, I think it might appropriately be there, for this reason - see whether this in any way modifies the view - that you're speaking of the fact that the fiscal policy has to take into account these changes listed under a, changes listed under b, and your fiscal policy also has to take into account the fact that there is plenty of credit so if it's necessary to borrow you are not restricting the

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amount available for capital. I mean with a little stretch I think it could go appropriately in there. And it didn't seem to be quite important enough to make an issue of it by itself.

Taylor: That's what I'm trying to avoid. The place that it now appears in - in other words, you say that while your experts and so on agree that the available supply of credit is so great, so and so, it is also important for Federal fiscal policy to take into account a and b.

Eccles: Your idea is to put it where, Wayne?

Taylor: I'd put it - a as part of your introductory statement.

Eccles: That "also it is important for Federal...."

Taylor: In other words, while the available supply of credit is so great, it is also important for ...

Eccles: I don't see any objection to that.

Ruml: It seems to me the appropriate way was the way it was before; that it is one of the things reported to us by our experts. They report the national income such, production such, and credit is such. And it seems to me that it ought to be a number four and that number five should have a and b attached to it.

White: Well, Mr. Ruml, the thought was that in order to tighten the document, in order to try to make every statement in here be a meaningful one, as though we were really giving the President something. That gave it a little too important a position for rather an obvious point. And we felt it tightened it somewhat by having it subsidiary to this, and I think it's quite appropriate there, that fiscal policy has to take ... Let's take it the other way around. Supposing we said it was important for fiscal policy to take into account the fact that the available supply of credit is not so great. You can see that this definitely would belong under c. So the fact it is so great doesn't mean it doesn't belong there.

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Ruml: It's a matter of literary form.

H.M.Jr: It isn't important?

Ruml: No.

Taylor: I think to have it grouped as it is now gives entirely the wrong meaning to the thing. I think you....

Eccles: I'd prefer to see it a part of four. I think that it is different, personally, than the other two items under a and b, and personally I agree with Wayne that if it were made a part of four it would give better understanding, or a better relationship. It's put in here now as one, two - or a, b, and c, just as though it had the same relationship in here as a and b, which I don't think it has.

Taylor: I don't think it does at all.

H.M.Jr: Will you settle it, Mr. Delano?

Delano: Well, when these literary fellows get at it, I'm lost. It means the same to me.

H.M.Jr: Bell, do you want to settle it?

Bell: I don't care. It doesn't make any difference to me. How do you want it, Eccles?

Eccles: I suggest it be made the way Wayne put it there, be a part of four. I don't care if you - I like George's change: bring b back and make it a, with the addition, and put the present a as b; get rid of c and make it part of four.

Bell: Make c four and make this other five?

Taylor: No, the other ones would be sub-heads of four. "Also it is important to"

Eccles: You assume there is this c and then it is important that you consider

Delano: Well, you'd have to change the reading, wouldn't you, a bit?

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Haas: Change the meaning.

White: Very definitely.

Haas: That would substantially change the meaning of it.

White: I'd like to make one more plea for the appropriateness of it, necessity for being where it is. The question is that there are certain things that it is important for fiscal policy to take into account. One of them is, as we stated, the volume of state debts; the other is the changes in capital expenditures, with the addition: "with the bottlenecks and restrictions on capital expenditures." And the third is the fact that there is plenty of credit available so any addition to the outstanding debt would not restrict capital investment. So the appropriateness of it is quite clear.

H.M.Jr: I like it the way it is - I mean very much - but I'm not going to fight about it. I'm all fought out. I like it the way it is. I went over it last night; it isn't a thing - as far as I'm concerned, I think this makes sense. But if somebody else doesn't, it's all right with me.

Eccles: Well, I don't think that it has enough importance. It's in here, and if you and Dan and Mr. Delano feel that that's satisfactory to you, I wouldn't - I wouldn't argue on a technicality.

H.M.Jr: Including the addition that Bell made - I mean that George made.

White: That goes under a.

H.M.Jr: How about it, Mr. Delano?

Delano: Well, that's restoring it to a, b and c, the way it was, but with that addition about hindrances and bottlenecks.

White: With the one exception that b becomes a and a

Delano: Oh, you do do that.

White: Just change the order to put the most important first.

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Delano: All right.

Eccles: You going to leave c where it is?

White: Yes.

Hanes: c becomes b.

White: b becomes a, c becomes b, and a becomes c.

Delano: That's all right with me.

H.M.Jr: Marriner?

Eccles: Yes, I think it's - I haven't seen it until just now, so I haven't had any opportunity except just this discussion; but I can't see that it's awfully important. It's in here, and you can argue either side of it, just as George - or as Wayne presents one side and White the other. I'm willing to go whichever way the rest of you decide.

H.M.Jr: How do you want it, Bell?

Bell: It's all right the way it is with me.

H.M.Jr: Mr. Delano?

Delano: All right for me the way it is, with those rearrangements.

H.M.Jr: All right, Marriner?

Eccles: O.K.

H.M.Jr: Now we go on with the next.

Hanes: Mr. Secretary, looking at this - may I interrupt and go back a little bit?

H.M.Jr: Please.

Hanes: I just want to go back to three. Looking at this from the standpoint of the person who has seen it for the first time, would there be any reason for saying "some important bottlenecks, such as ..." and explain what you - just give an indication of

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what you mean by bottlenecks? We all know here, but I'm wondering if the person reading it for the first time - say, "Such as what kind, for instance?" and so forth. Would you clarify it and say "such as"?

Bell: Well, then you get those groups worried.

Hanes: You don't want to do that.

Ruml: I think it's dangerous.

Hanes: I was thinking about the person seeing it for the first time. That doesn't mean anything as it is now.

H.M.Jr: If this was published this way, I think it would be meaningless to most people. We'll go over there - just got word the President will see Mr. Delano, Mr. Eccles, Bell and myself at two o'clock - we'll go over there and he'll say, "What does this mean?" and we interpolate as we go along; if he likes any of it and wants to use it - any of it - I take it we'd have a chance to interpolate and add for him.

Hanes: That's right. I just bring it up as a ...

H.M.Jr: I think you're quite right. I've been trying to do what he likes, keep this thing boiled down. And if the President said, "What bottlenecks do you mean?" then we could tell him. But if this was a public document, I think you're entirely right.

Hanes: That answers my question.

H.M.Jr: Any other question before I go on?

"In pursuit of the objective of attaining a higher national income we make the following recommendations with respect to fiscal policy for the next fiscal year:

"1. If taxes are to be increased, those selected should be such as interfere least with additions to the aggregate income of the American people. These, among others,..." - now, I wouldn't get that these - I don't get that these are the ones that we recommend, if they want ... Is that clear, that "these, among others, are"

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Eccles: That's the change we made Saturday.

H.M.Jr: Is that all right?

Eccles: We cut out the two taxes, capital gains and undistributed profits, left the four in, and then said that these taxes, among others, and without spelling out what the others would be

H.M.Jr: All right.

White: You'd like to repeat the word "these taxes." I think that will make it clearer, Mr. Secretary. "These taxes, among others...."

H.M.Jr: "These taxes, among others..."

"These taxes, among others, are: estate taxes, gift taxes, lowering tax exemptions as income rises, higher income tax on middle brackets."

White: George has a suggestion here for another phrase instead of "lowering tax exemptions."

H.M.Jr: What does he say?

Haas: That's ambiguous to me. I'd say something like this: "lowering personal tax exemptions in higher income brackets." That, I think, is what is meant - not as the income rises.

H.M.Jr: Well, clear it with Mr. Hanes first, before we put it up to the rest.

Haas: Just a question of stating it, John.

H.M.Jr: Say it again, George.

Haas: I'm not sure mine is an ideal statement of it: "lowering personal tax exemptions in the higher income brackets." That isn't perfect either.

Bell: That isn't what you mean.

Haas: It's as the bracket rises, the exemption becomes lower.

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Hanes: It stays the same.

Bell: Yes, it's uniform, as I understand it.

Haas: Well, there's two concepts, one where it stays the same, the other where you have a vanishing one, like Mr. Eccles is talking about; I don't know what's meant here.

Hanes: What we were talking about in the - talking about the idea of giving an exemption on the tax after it's computed, a flat exemption of a hundred dollars, which makes the same exemption for a man of \$50,000 as a man of \$2,500.

Haas: That's different from the vanishing concept.

Bell: Why not "lowering personal tax exemptions"?

White: Without specifying.

Bell: Yes. Nobody will interpret ...

Haas: That's a different concept of it.

Currie: That means going down to one thousand ...

Bell: It has about the same effect, doesn't it, Johnny, as going down?

Currie: No, this proposal doesn't bring new people under the income tax, as I understand it.

Haas: Unless you change the net - unless you change the net exemption of tax - I mean unless you make that a smaller amount, instead of a hundred dollars make it fifty dollars, then you go down into a lower income group.

H.M.Jr: I understand this, but maybe I'm wrong. "Lowering tax exemption as personal income rises." It makes sense to me.

Haas: If you put that in, it makes sense: "as personal income rises."

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Eccles: That's what somebody suggested.

H.M.Jr: Isn't that what you mean?

Haas: I think that's all right, but it wasn't in the first one.

H.M.Jr: "Lowering personal exemption - tax exemption as the personal income rises."

White: That would avoid the ambiguity that it might refer to national income, as George says: "lowering personal tax exemptions as personal income rises."

H.M.Jr: Is that all right, Bell? Mr. Eccles?

Eccles: That's the way I understand it.

H.M.Jr: All right. Are we ready to go on with two?

"We advise against new taxes which operate to reduce substantially consumer purchasing power. These, among others, are: processing taxes, sales taxes, taxes on payrolls, excise taxes."

I've got to stop a minute and tell a story. This is based on the fact that the President and the Vice President had about three hours together. I go down in the elevator with the Vice President after the Gridiron Dinner. He takes his thumb and drives it about four inches into my belly and he says, "How are you and Wallace getting along, old Money Bags?" That's what he calls me. So I said, "Pretty well." So he said, "Well, God damn you, don't give in an inch." Somebody must have been telling him something, and as I always say when somebody talks to him, it must have been the President.

Eccles: He doesn't apparently like processing taxes.

H.M.Jr: Nuts! So I said, "Well, how about a little support on the Hill?" He said, "You'll get it all right."

I felt it right in my stomach where he drove his thumb, too.

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Delano: Gridiron Club dinners do some good, don't they?

H.M.Jr: This is all right with me. I like "processing taxes" underlined.

Bell: It's first.

H.M.Jr: All right to go ahead?

Bell: Like "taxes on payrolls...."

H.M.Jr: Necessary things.

Bell: Wouldn't like to have it eliminated, but I'd like to have it explained that it's for

H.M.Jr: What, Dan?

Bell: ... current operating.

H.M.Jr: You want to change it?

Bell: No, I don't think it can be changed, but I hate to see us go on record as opposing taxes on payrolls for Social Security benefits. I'm agreeable to raising money for that. I'm opposed to raising money that way for financing the deficit. But as to an insurance scheme, I'm not opposed to it. As a matter of fact, I'm in favor of it.

Currie: It does say, Mr. Bell, new taxes.

Bell: If there are new benefits, then I'm in favor of new taxes.

White: Unless there were some other tax.

Bell: Well, I think if they were going to set up an insurance scheme, the people who benefit by it ought to pay for it. That's what it is.

White: Doesn't that raise a different issue? That is, if you decide on an insurance scheme, then it wouldn't be regarded as a tax, unless you

Bell: Well, I'm looking at the Social Security - old-age benefits under the Social Security as an insurance

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scheme.

White: Well, once the principle of insurance is accepted, then technically, or if one wanted to be, it seems to me, meticulous about it, it wouldn't be a tax; be sort of a collection.

Hans: Premium.

White: Premium.

Currie: I don't think that would really be the position there, because if new taxes were to be increased - that's the second one - then we advise against new taxes which operate to decrease

White: Is it your (Bell) thought that the increase that's coming in January might be regarded as a new tax?

Bell: Either that, or if you have increased benefits that you want to levy additional taxes. From the standpoint of regular expenditures of the Government, this is all right, if that is what we're talking about.

Eccles: You may have a scheme somewhat outside of that - I think Social Security is outside; it has an effect, of course, which is the thing that I think has got to be considered, but possibly considered separately.

H.M.Jr: Would this satisfy Bell: "We advise against new taxes to pay for the regular operating expenses of the Government."

Hans: Mr. Wallace would say his is not regular. He wants a processing tax coupled with ...

H.M.Jr: I don't think this is so bad. If the benefits are going to be increased, then we want to raise them the same way. I'm in the same boat. Now, if I'm misleading anybody - I don't want to leave anybody under a misapprehension.

Bell: I think it's - this is all right if we have an understanding among ourselves as to what this means.

H.M.Jr: Is that all right with you, Mr. Delano? I'm in

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the same boat. I don't know whether you are, but I'm in the same position that Bell is. Is that all right - I mean as we subsequently said?

Delano: Yes, I agree as to the interpretation.

H.M.Jr: That all right with you, Eccles?

Eccles: Well

H.M.Jr: Well, I mean so far as Dan's and my position.

Eccles: Of course, I'm somewhat opposed to increasing the payroll tax for any purpose at this stage. I think it tends to keep the national income from going up, the thing that we want. In principle I'm opposed to increasing payroll taxes for - as I say, for any purpose. I've understood the reference here to it, however, to mean as applying to the budget.

Delano: Balancing the budget.

Eccles: That's right.

H.M.Jr: Then I think we're all in agreement - I mean as to the purposes here.

White: Yes. I take it the question as to the desirability of additional payroll taxes in the event benefits are increased is not being raised at this point. Though there might be a difference of point of view, there is not an issue there. That insofar as the committee agrees, it agrees on the assumption that this relates to increased payroll taxes which would go toward balancing the budget.

Eccles: Well, we're agreed, but I don't want to be misunderstood so if it comes up in another way

H.M.Jr: We can each go our own way on that. All right, gentlemen.

"3. The Board notes with approval the proposed changes in the budget presentation and recommends that the principles embodied in these changes be extended as rapidly as feasible." Then I think we ought to have here a little something - reference "a" or something, so they know what we're referring to:

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that thing that the President approved. Don't you think so? "Well," he'd say, "what do you mean?" Just that thing we sent over to him - couldn't we just have that attached?

Bell: Attach a copy of it.

H.M.Jr: Just attach a copy of it.

Bell: That would be all right.

H.M.Jr: "Well," he might say, "what do you mean?" I'd just attach a copy.

Eccles: That's the memorandum that he's O.K.'d.

H.M.Jr: I think we ought to attach it.

White: "See appended copy."

H.M.Jr: "See appended copy."

"4. a. For the purpose of adding to the national income next year, and of preventing what promises to be a serious bottleneck within the next year or so, action should be taken to secure a large railroad equipment program."

Excuse me - right on that, I want to say that we are making considerable progress in studying for the President the possibilities of financing Government-owned power projects ...

Eccles: Government-owned what?

H.M.Jr: ... power projects ...

Eccles: ... outside.

H.M.Jr: I mean we're not ready to report on that, but we're making progress on it.

Eccles: You mean Bonneville, T.V.A.?

H.M.Jr: Yes. The ones that have revenue.

Eccles: Boulder?

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H.M.Jr: All of them; all of them that either have or expect to have revenue.

Reeles: That's not future, that's - that would cover the items that are now in the Treasury held as assets.

H.M.Jr: That's right.

Reeles: The idea being to take them out, refinance them separately, and refund the Treasury, thus reducing....

H.M.Jr: That's right. That's right. But I mean we're in the process of studying that and we're getting along nicely.

"4. a. For the purpose of adding to the national income next year, and of preventing what promises to be a serious bottleneck within the next year or so, action should be taken to secure a large railroad equipment program.

"b. Recovery could be further stimulated by additional government activities financed through self-financing government corporations. A special report on such activities will be later submitted."

Currie: Mr. Secretary, on that point, in case that should be misunderstood, - this gets over the extension of government activities - you could, if you wish, add some sentence like: "These activities should be in the main such as to facilitate private investment and promote expansion of private industry."

H.M.Jr: Say it again.

Currie: "These activities should in the main be such as will facilitate private investment and promote expansion of private industry."

H.M.Jr: Fine. I like that. As it reads....

Currie: As it reads now, it's just the extension of Government activities.

H.M.Jr: I think it's fine. All right with you, Bell?

Bell: Fine.

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H.M.Jr: Mr. Delano?

Delles: I don't know why we shouldn't put it in.

H.M.Jr: absolutely. I think that's a good addition. White - I've been kidding White about this for the last couple days; that's why I'm laughing.

All right for five? Anybody else in the room that doesn't like - as we go along, please shout.

"5. That a comprehensive survey be started with the view of immediately setting up machinery to obtain all necessary detailed information with respect to the current receipts and expenditures of State, local and municipal administrative bodies and to changes in the volume and make-up of their outstanding debt."

I like that one; I think that's good.

White: We have a preliminary report before us which the Tax Division has prepared over the week-end with some experts they have there. They just handed Mr. Hanes - Mr. Hanes gave it to me - a summary, a one and a half page summary; they have the large report, which can be ready at one o'clock. If you're at all interested in hearing the summary later

H.M.Jr: That's - let's run through this; if we're in agreement on this, then I'd like Hanes to read that. All right? But let's see if we can get together on these two pages.

"6. Arrangements should be made at once that would make possible engineering and legal planning of various public works which would be available for immediate prosecution when required to give increased flexibility in the timing of public expenditures and increased assurance of value and utility of the expenditure itself.

"These arrangements are much needed...." - can't you get a better word than "arrangements"? "Arrangements" would be all right at first, but to say "These arrangements are much needed..." - couldn't you say "these studies"?

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White: "These studies..."

H.M.Jr: I mean the second time....

White: It's a plan, but the word "plan" has sort of a bad odor.

Taylor: "Program" - "This program...."

Eccles: Yes, "program" is better.

Delano: "This program...." ?

H.M.Jr: "This program....." or would you say "These programs..."?

Taylor: "This program is ..."

H.M.Jr: "... is much needed..." Is that all right?

"This program is much needed not only because of the current magnitude of Federal, State and local public works and relief programs..." I wouldn't use the word "magnitude." Couldn't you use "current size"?

White: "... current volume...."

H.M.Jr: Current what?

Ruml: If you said "character," it would be better yet.

H.M.Jr: "...current character"?

Ruml: "... the character ..."

H.M.Jr: Marriner, ...

Delano: You wouldn't put "current character," would you? You'd put "character of current Federal,"

H.M.Jr: "... character of the current..." - how would you say it?

Delano: "... the character of current Federal, state and local public works..."

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- Taylor: "... and relief..." You don't need "programs" there and you don't need "program" under rearmament.
- Eccles: Got to reconstruct it quite a bit, making that change at first.
- H.W.Jr: "This program is much needed not only because of the character of the current..." - how does that
- Taylor: "... of current Federal, State and local ..."
- Lelano: "... Federal, State and local public works and relief programs..."
- Taylor: "... of relief..." You don't need "program" there and you need - don't need "program" after "rearmament" anywhere.
- Hanes: Put the word "expenditure" in there.
- H.W.Jr: "... but even more especially because of the extensive rearmament being undertaken. To make certain that the rearmament program shall not be continued as a device to reduce unemployment or to stimulate business activity, it is essential to have such plans perfected as will permit a ready transfer of employment from armament industries into needed productive public and private works projects as soon as peak activity in the armament program is passed."
- Gentlemen, I like that. Can you fix that up with a couple of words, boys? I mean change "current" and "character" and the rest?
- White: Well, we've got the changes that have been suggested already. Unless there's another
- H.W.Jr: Now, would you gentlemen like to hear Mr. Hanes give us what the men did over the week-end on this local and state thing? What you got there, John?
- Hanes: This is a summary of - and it's rather hastily gotten together, as you will understand ...
- Eccles: Could we come back to what - some one or two things I'd like to add to this. I'd like to come

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back to it. You're not assuming that ...

H.M.Jr: No. I was, but I'll come back to it.

Eccles: All right.

Hanes: "1. The analysis of published data for the past years can be analyzed by the Division for Tax research." And so forth.

"Either consultants such as those from....." - that tells what they need on the technical thing. This thing is not something you want to take over there this afternoon.

H.M.Jr: Let's let it go, John.

Hanes: It just in summary is an outline of a plan to do what you contemplate doing to get this state and local and subdivision data available to this committee. That's what it is.

White: There is a question raised there. I don't know whether you want to raise it now. That might require some additional consultants, and they give an estimate of the amount ...

Hanes: They give an estimate of the cost of this thing to the Treasury, doing this kind of work: about \$450,000 a year. That's a guess; nobody knows what it is.

H.M.Jr: well, I don't think we ought to

Hanes: I don't think it's something that you want to discuss. Say you're studying the possibility of getting this coordination between local and state governments with the Federal tax authorities. That covers it, in my opinion.

H.M.Jr: All right, Mr. Eccles.

Eccles: I think this is very good as far as it goes. It does seem to me, however, that it isn't - it isn't quite complete. Just what is it that we're aiming at? As I understand it, it is to attempt, in looking forward to 1940, the 1941 budget, to avoid, so

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far as fiscal and monetary policy is able to do so, a bogging down.

Now, that can well happen. If, in other words, the Federal expenditures are not what the budget - this is all based on an assumed - budget expenditures based upon an assumed cash contribution by the Federal Government - if taxes are substantially increased and the Federal revenue, what they collect, is substantially more than is anticipated, and the Federal expenditures should be less, you could very well get a budget, so far as the cash is concerned, which is the thing that affects the economy, that could bring down in 1940 - that could bring about a deflationary period again. I think that's - and it doesn't seem to me that we've covered that possibility here.

You make an estimate, Dan, that there will be expenditures, we'll say of eight billion - what, eight billion four, for '40 - for '41?

Bell: On the basis you're talking about, yes - eight billion four.

Eccles: Eight billion four.

Bell: About eight billion nine is the total.

Eccles: Yes. That's with armament.

Bell: No, that's with Social Security investment in it. That's cash

Eccles: That's cash.

Bell: Somewhere between eight billion and eight billion four, I should say, would be the cash outlay.

Eccles: And then you estimate the revenue, without any new taxes at all, at a certain figure, don't you? Now, that would then give the cash deficit of so much.

Now, assume then that taxes are very substantially increased, on the one hand, and the expenditures just don't go out, you don't get the expenditure of

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the eight nine, so that you actually have your cash deficit during the first half of '40, the calendar year '40, which is the last half of the fiscal year, actually come together very rapidly, on this size of a national income, the proposed - we estimate a national income of, say, at the end of the year, 70 billion. Now, if you begin to get a cash balanced budget on that basis, you'll get the same condition I think you got in 1937.

Now, I mean I just wanted to - I think that that after all is the thing we're aiming at here. And we have stated some general principles, which I concur in, but it just doesn't seem to me that the report can be complete unless - and I have this thought in mind here: that if we favor any new or any additional taxes to apply to this fiscal year, 1940, that we should only favor them if there is a corresponding increase in the aggregate cash expenditures in that year. Now, that - that doesn't mean that we don't favor an increase in taxes of, say, 500 million if you're going to spend 500 million more than we are now spending. But if we believe in the principle that the budget is going to be balanced out of an increased national income, then to balance it by an increase in taxes before you get the increased national income can well prevent us from getting the increased income.

You said the other day, Mr. Secretary, that you favored increasing the taxes and the income together - I mean the taxes and the expenditures; that if they were going to increase the expenditures, you were favorable to increasing the taxes along with them. Well, I'm favorable to that, and not necessarily increasing the expenditures first and then the taxes after. But unless we - if they're going to increase taxes here for armament and then decrease expenditures for other purposes, so that the aggregate expenditures are not increased but the taxes are increased, you can very well, it seems to me, stop the increase in the national income by increasing taxes too soon.

S.M.Jr: Mr. Delano, is this the way you feel?

Delano: Yes, I have - I had prepared a statement with Dr. Suml here about this matter. I may say that our

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Resources Committee, the four - Dennison, Merriam, Ruml, and I, were together on Saturday. In fairness to the others, I think I ought to say that I think Dennison is in complete agreement with Ruml and me; that Merriam, who has been a student of politics all his life, raises a bugaboo which a good many practical men would raise, and that's the expediency of certain action; the political expediency has got to be considered. Well, of course, we know that you and the President will take those things into consideration.

But I do say this: I believe that the projected report on possible fiscal and monetary situation in 1940 is of particular interest, since I am impressed by the facts presented to us by the experts; that real danger of another sharp depression in 1940 exists, particularly in view of the disappointing present estimates on national income for the year '39. I cannot but believe that the Federal budget has an important influence on national income and that some expenditures have more influence on national income than other expenditures, and that some receipts have more influence than other receipts. Accordingly, it seems to me that it is part of public fiscal wisdom to consider what we are able to do in the present state of our knowledge to protect our nation against the demoralization of another economic crisis, and if possible to assist towards the higher national production, income, employment and standard of living and well-being, which we are convinced our national resources are able abundantly to provide.

Of course, that's been shown in a good many ways, if you wanted me to argue it. For instance, a Boston architect pointed out that in public works the nation dropped from something like 13 or 14 billion down to about three billion; and a good deal of it was speculative building: bank buildings, apartment buildings, hotels. All sorts of things were built all over the country - speculative building - and the states and the cities were going wild on building. Then, all of a sudden, they all quit and left the Government holding the bag.

E.W.Jr:

True.

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- Delano: Now, either Government has got to continue to hold the bag or else it's got to convince these other people that they've got to do their share.
- H.W.Jr: The trouble is we've never given business a chance.
- Delano: That may be true.
- H.W.Jr: That's the trouble. We get up to a point where business is about ready to step in with new investments and then we crack down on them in this place and that place. We never give business a chance, and we take it for granted that business won't come through. As long as Government is doing this thing, as long as Government is the chief borrower, business won't. And this assumption that we've got to keep these big deficits - as long as we keep these big deficits, there isn't much reason or encouragement for business to go in. I mean the question of either business or the Government - I agree with you one or the other has to do it or this country
- Delano: Well, of course, these big deficits you speak of - when you look at it from the standpoint of national deficit, some of these figures that are being made show that the national deficit is nowhere near as big as the Government deficit.
- H.W.Jr: I don't know what you mean by national deficit.
- Delano: I mean in the same sense that we use the words "national income." We're speaking of the aggregate income of all the citizens of the country.
- H.W.Jr: But you see, Mr. Delano, if I understand - if I could read that again - I don't think that you and I are very far apart, but I don't think we ought to do any more shadow-boxing. I mean
- Delano: No, I don't want to do that either.
- H.W.Jr: And I don't want to. And I'm not going to try to ask you to try to conform, but I think that there is an honest difference of opinion between Mr. Eccles and myself, and I don't think that we can get those two opinions together, that's all. I mean - I'd like to read this if I may - I just don't

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think you can get us together. But that's no reason why Mr. Eccles shouldn't present his own views this afternoon.

Do you want to look at this (a short written statement used by Mr. Delano as basis for his oral statement on page 23), Dan, with me?

Bell: Go ahead; I'll (Looks over H.M.Jr's shoulder)

Is this proposed to be incorporated in this?

Delano: No, it was - Ruml and I thought that perhaps you ought not to, in talking to the President, stop here without warning him; in other words, it's awfully easy to have convinced the country that we're out of the woods and that we see a way of getting out of the woods and - without foreseeing what may happen in 1940.

H.M.Jr: Well, I don't know what's going to happen in '40. I don't pretend to be smart enough. And I want to be very, very frank with you. I think the only contribution that I can make is - going over this afternoon, the only thing I can do personally is to try to get the President - I mean I'm just repeating myself - to think in terms of an income of 80 to 90 billion dollars, and that in the various things which he has which he is going to propose, that he will give careful consideration whether - not only the budget but all the various legislation which he may or may not have in mind - whether it's going to help us attain this 80 to 90 billion dollars or whether it's going to retard it; the budget is only one thing. Now, all I can do is to do that. I heartily believe in it. I go along thoroughly with the idea of planning future public works so we should be ready in case - particularly if and when we get out of this armament program. I mean I believe in these various taxes.

I cannot go along, as I understand what Mr. Eccles says - I mean this thing that it is - this is what I may refer to as a school of thought - that it is something to worry about if in the second half of '40 our deficit is smaller. I mean I just can't get myself to subscribe to that, you see.

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Ruml: Mind if I say ...

H.M.Jr: I just can't get myself But what I'd like to say is, please feel free, both you (Delano) and Mr. Eccles, to hand him in a supplementary report on anything you want to. Can I be any fairer, Mr. Delano? I mean I'll go along as to this. Will you (Bell) go along so far?

Bell: Yes, sir.

Delano: I'd like to have Mr. Ruml ...

H.M.Jr: But beyond that I just can't go. That doesn't mean that Mr. Delano can't hand in a supplementary report and Mr. Eccles hand in a supplementary report. And I can't go beyond what's on this paper now. And it's an honest difference of opinion. It's an approach. I'm more than willing to continue to study this thing.

but I can't help but think if in the second half of '40 our income is up and the nation's income is up and the expenditures are down - I think it's good news; and you people think it's bad news.

Eccles: No, you're wrong on that.

H.M.Jr: I can't help but think it's good news. What?

Bell: Stand up and cheer.

Eccles: Let me clarify my position here. We've said here ...

H.M.Jr: "ayne, are you - do you agree, do you want to say something?

Taylor: I don't think you're very far apart. I don't think you say it the same way; that's about all it amounts to.

H.M.Jr: It's pretty fundamental with me.

Bell: The Secretary of the Treasury certainly can't say in a report that because we fear the deficit is going to be smaller in the second half of this year 1940, that we're going to have a depression.

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Eccles: Well, nobody's saying that.

Bell: Coming close to it.

Eccles: You say right here - here's what you say in number two: "A national income of around \$80 billion would provide Federal revenues sufficient to balance the current level of cash expenditures on the basis of the existing tax structure.

Now, we say further that next year we're going to have a national income of not more than 68 billion. We're 12 billion from 80 billion dollars - 12 billion from it. Now, all I'm saying is, let's let the 80 billion of national income that we want to reach - let's let that balance the budget on the basis of what we say is existing Federal revenue sufficient to take care of the current level of cash expenditures. Now all I'm arguing for here is for the maintenance of the current level of cash expenditures and the current level, generally speaking, of cash - of receipts from present taxes.

Bell: Even though the national income goes up from other causes.

Eccles: The national income going up will increase the revenue and will decrease the need of expenditures. Now, the only difference - and I don't think there is a difference - I'm merely arguing for letting national income, which will give you an increased tax revenue and will make possible a reduction through relief of expenditures - I want to let the budget be balanced out of that increased national income and not increased taxes and decreased expenditures in a manner that would tend to avoid getting that 80 billion dollar national income.

Now, that's - ... and I think we can well do it. I think we can just do that. I think we can increase taxes and not increase expenditures, accordingly force a decreased deficit on a national income of 68 billion and you'll never get the 80 billion.

Sumit: Mr. Secretary, I was at the meeting Saturday; Mr. Delano was not here. After the meeting I again

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went back to the Resources Committee, I again communicated with Mr. Delano on the subject. It was my thought some statement of this character, in addition to the concrete proposals, should be made to the President at this time. But in view of our discussion on Monday, I think it was - or on Thursday, when both you and Mr. Bell expressed some reservations at the present time about going along in a statement that the national budget has an influence on income, that some expenditures have more influence than others, some income more than others, it seemed to me that at the time our minds as a group were not sufficiently clear to warrant that statement being made by the group.

On the other hand, after talking with Mr. Delano and with the Committee, we felt that the President should at least have that expression from one member of the committee, and accordingly this was prepared as a statement which Mr. Delano could make personally, if you wish.

H.M.Jr: Perfectly proper.

Auml: I think this question of policy we're discussing is extremely fundamental to the whole economy. I think up to the present time the attitudes have been misunderstood. I think they can be made clear. I think the English language is perfectly able to transmit the ideas necessary. But I don't think the time now has come to make any statement that would involve the group.

H.M.Jr: Mr. Bell can talk for himself, but if I understand him correctly, he's agreeable to the statement as we've cleared it up through that. Isn't that right?

Bell: That's right.

H.M.Jr: It's agreeable to me. Now, if Mr. Delano, representing the National Resources Committee, wants to make a supplementary statement, and Mr. Eccles, as Chairman of the Federal Reserve Board, wants to make a supplementary statement, it is perfectly proper.

Auml: One place it does not tie in - in the meeting on Saturday there was one item referring to the fact

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that a study would be made referring to the situation in 1940. This starts out by saying, "I believe the projected report is of particular interest" If that paragraph is not going to be included here, this statement should read: "I believe a projected report should be made."

White: The reason that was dropped out, Mr. Ruml - it was thought that there's a good deal in this memorandum; that the committee is young yet and has lots of time, and the time would be quite appropriate and propitious any time later, after possibly a more careful study of the budget, which will have been ready by that time, is made, for a further memorandum to go forward to the President taking up that specific fact; that there was no need to further complicate this important first report by snooting all the works at once; so that there was nothing to be lost at this time by leaving out that reference, and possibly something to be gained, when there will have been fuller time for discussion, fuller time for examination of the budget, and ample time to give in an additional report. I take it this committee doesn't intend to give just one report a year.

Ruml: This first sentence can be modified. But it was principally from the point of view of indicating our knowledge of the existence of the problem, that at the meeting Saturday such a paragraph was in.

H.M.Jc: I asked that it be left out because I wasn't ready for it personally yet, and I felt that that particular paragraph would not help the President one way or the other in writing his budget message. Everything in here would. I think this is as far as I can agree to it. But that doesn't mean that as the year goes on and other things come up - there will be plenty other things come up. But I just think it is always better to call a spade a spade; I'm just not ready for that yet, personally. Now, again, I'd say that any gentleman here of this group can hand it in if they wanted to. I want you people to feel that when we go over there the President is yours, and I'll take a back seat.

Wyles: Which was it you cut out? I'm not just entirely clear on this discussion here. What was cut out, Harry?

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White: The statement that the budget for the first half of 1940 - that the deficit in the budget of 1940 would result in a decrease in Government contribution to the national income in the second half of 1940, and that that fact justified the preparation of a special report to be made on the possible effects.

Tell: It was number four on page two. Discussed a great deal on Saturday. "In view of the fact that the anticipated deficit will be greatly less in the second half of the coming fiscal year, and in view of the consequent decline in additions to buying power...." - then we went on and said that we would make - we recognize this problem and will make a special study and report later on it. Do you remember?

Reebs: Yes; I still don't see why.... It seems to me that that's the heart of the whole issue. The rest of this is more or less just sneer verbiage. We talk about what the income is going to be next year and that the national income around 80 billion will do certain things, and we can get an income of 90 billion. We do all that, but then we don't get down to really the heart of the whole thing. We get right up to the point and then

White: Not wholly. That's being a little less than fair to this. I think there are a lot of very important things being said.

Reebs: Yes, but they lead up - lead right up to the ...

White: Do you feel there would be anything lost, realistically and practically, in the way of helping to clarify the President's mind with respect to a formulation of budget policy if this particular point were postponed, let's say, within a reasonable period, so you would have ample time, if you so felt subsequently and if there wasn't agreement, to submit a special report on it - do you think there would be anything realistically lost?

Reebs: I don't think we're ready, of course, with the report now, but it doesn't seem to me that this report to the President is complete at all without advising him that there is this very important

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problem that we expect to make a later report on; that otherwise we give him this and no reference is made at all to what seems to me may be a very vital issue, a very vital question, the question of timing this whole thing.

Bell: And on which you have a whole year to report.

Acles: Six months.

White: I'm not quite sure that the Secretary and Mr. Bell understand the position which you stated. In fact, I feel with Wayne Taylor that there is some lack of understanding of the expression and not of the real idea. In other words, I think if they interpreted what you say as I interpret it, there would be no disagreement. But I don't think you would possibly be able to clear it up sufficiently at this time. I don't know, I'm not sure; there might be something a little worth while waiting for.

Acles: I wish you and Wayne would undertake to do that job, because I agree with you. I don't think - if there is any fundamental difference, I'd like to know where it is.

Currie: Do you think, Harry, it might be acceptable to just put in here that a problem of timing of the Federal budget with the development of private business in the more distant future than the year 1940 would be under study and a report will be made, just to indicate we have thought about the problem of timing and of gearing the two things in with each other?

White: I think there would be less opposition to it.

Taylor: I think you would be better off if you mention that in conversation rather than trying to get that particular statement or a similar statement included in the thing that you have here.

Acles: Well, that's all right. I think that this part that was taken out - what we have agreed to in the statement seems to me to be somewhat incomplete. It takes us step by step up to a very important point, and that's the timing, the question of timing. And then, we're not prepared now to make a report on this question, but it does seem to me that either in this

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report we should say to the President that a later report should be made covering this question, which is so vital, of timing Government receipts and expenditures with that of private, and we're trying to forecast the thing into 1940.

H.M.Jr: well, you can say that when you get over. But I'd like to personally see some of the forecast before I even put my name to it. See?

Currie: Sure.

H.M.Jr: I'm not saying that if later on the people can come in here and we see something - but, in other words, I'm not yet convinced that 1940 isn't going to be a good year; I'm not convinced it's going to be a bad year. But before I begin to put my name down and say that I'm going to worry that 1940 for business is going to be bad, I want to be awfully convinced.

Eccles: well, I think what we're speaking of here is the first half - it's the last half of the fiscal year and the first half of the calendar year '40 that we're considering in connection with this 1940 budget. Now, I'm not convinced either that the first half will be good or bad, but I do think that whether it is good or bad will depend very, very greatly upon what the fiscal program is, and I should like to - I think it is absolutely essential that it be made good. We can't - we can't possibly, it seems to me, let things turn down again in '40 because of an improper timing of fiscal policy. That's the

H.M.Jr: well, why don't you, when you get over there, either say it verbally or hand him a memo on it? But I'm not ready yet to cross that bridge.

Eccles: Well, I'm only crossing it as a problem that we must consider. I'm not crossing as to a question of any detail.

Taylor: well, what you're really saying is, isn't it, Harriner, that a billion dollar new tax program is too heavy and a half billion is probably all right. Isn't that about it?

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H.M.Jr: No.

Eccles: No. What I'm saying ...

Taylor: I mean for additional taxes for this period.

Eccles: What I'm saying is that if we're going to put on additional taxes, then we should have additional expenditures, or if we're going to have additional expenditures then we should have additional taxes.

Taylor: You know you're going to have the additional expenditures in the form of this armament program, so, going back through that thing, why,

Eccles: I mean additional aggregate expenditures. Now, if you're going to have additional aggregate expenditures, then you should put on additional taxes. If you're not, I think it is a very serious question - I don't say you shouldn't, but I think it's a matter - that it's a very serious question as to whether or not additional taxes should be levied; if you don't have additional aggregate expenditures, it cannot but be deflationary. And there are certain types of taxes such as we mention that would be very much more deflationary than other kinds. And it is that question that I think is so terribly important now: whether, if we put on additional taxes, which I think Johnny reported was being considered - if we're going to put those taxes on and not have an aggregate increase in expenditures, that you can't help but get a deflationary development.

Sumi: Harriner, you would take this into account: that if you had extreme activity outside the budget in these aggregate amounts ...

Eccles: I'm speaking of the whole thing, yes.

Sumi: That's what I mean. You have to take the whole picture into account.

Eccles: Well, I don't want to be misunderstood on that. That is, this - if we get this railroad equipment thing and - or if you get a building activity outside the budget, as a result of Government activity outside the budget, that's just as good so far as its effect on the community buying power as if it were in the budget, and you may well get a reduced deficit

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of a billion dollars if we can get a billion dollars of activity outside of the budget. So what I'm thinking of is not merely the technical budget; I'm thinking of the over-all picture of items which the Government can stimulate outside of the budget as well as within the budget.

H.S.Jr: You people lay so much stress on what the budget will do. Give us 15 million bales of cotton that the Government owns and a five cent price of cotton, having nothing to do with the budget at all, and look at the effect it has on one-third of the population of the United States. And we're talking as if the budget was the last answer to this year. I'm just not convinced.

Waml: I agree with you.

H.S.Jr: I think it's a piece of the picture.

Waml: It is a piece.

H.S.Jr: But to put this down and not, for instance, talk about agricultural commodities and our world market and all the rest of it - and our exports and our imports, all the other things, our balance of payments, the gold question - everything else which goes into it, makes up this national prosperity, and hang this whole thing on just this one thing and not mention the others - I'm just not going to do it. But that doesn't mean

Wodles: I wouldn't do it either.

H.S.Jr: That doesn't mean - I mean I am, for instance, very much convinced that if the South isn't prosperous, the rest of the country can't be prosperous, and with ten million bales of cotton, more or less, owned by the Government, you can't do anything about cotton prices. Now we don't say anything about it, but it's a very important thing, and one seventh of the total revenue goes to this agricultural program. And so I mean before you go to that, I'd want to say a lot about agriculture; well, I don't think we've got room for it, but it has a very important effect on the whole question of national wealth.

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So what I again say is that I will do the least talking when we go over there. If it's agreeable to you people, I'll read this memorandum, let the President read it; then I'll say that Mr. Delano has a supplementary statement and that Mr. Eccles has a supplementary statement, and you people are at liberty, of course, to say whatever you have on your mind.

Delano: Perhaps Mr. Eccles ought to come first on that.

Eccles: Well, I don't - I won't argue that. It doesn't make any difference to me. And I - I don't want you to get the impression, Mr. Secretary, that I think that the whole solution either is within merely the budget. I think we've done a lot of things in the past that have retarded private activity that aren't within the budget. I go just as far as you do in that regard.

H.A.Wr: I think there are so many things. I mean this question of this whole economic fabric - I mean there are so many things which I think are wrong, and I - this is - I'm more than willing, after the first of the year, to sit down with you people and continue these studies. I've found them very profitable, I've found them very useful; I'd like to continue them. But I think if the President will give us the time and thought and go over those things, then listen to your supplementary statement, that, I think, is about all we can hope to go over.

But, as I say, I'm raring to go and talk about what is happening to the farmer in this country. I think it's a terrible situation, think it's getting very much worse. But I'm not going to ask you people to join me in a statement today.

White: Could I say something?

H.W.Jr: Excuse me - can you hold your thought?

White: Yes.

H.W.Jr: I think what's happening in the agricultural picture is very dangerous; you don't have to wait until '40, it's right on us now, and it's getting worse every

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day. But I didn't say - I don't think that - maybe later on we may want to say something about the purchasing power of the farmer and what's happening to him, and the effect of the purchasing power on the purchasing in the cities, and all that. But there's so many things, and I don't have to wait until '40, I can show you fellows right as of today what is happening in agriculture and the whole commodity picture. Go ahead, Harry.

White:

afraid I'll have to step a little out of my role. But I'd like to say this very brief statement: that I should myself feel badly if a supplementary statement of any kind went in with the original statement at this time, for this reason: this is the first report made by this committee. I think its - the value of its advice is greatly enhanced if there is no indication that there is any difference of opinion. In view of the Secretary's repeated statement that he is glad to continue and to study these problems where there is a probability of some common meeting ground, as I very definitely feel there is, I think there is something very substantially to be gained by postponing any supplementary views until an adequate time has been had to reexamine both positions and see whether there isn't some common ground; so that when it does come to the President it will be the opinion of this committee and not the opinion of certain individual members; because to come forward, say, with supplementary opinions will merely be to repeat what the President has heard from different quarters at different times, and he again will have the feeling that "oh hell, they disagree too; there's disagreement among the experts and the advisers; well, maybe I better go slow on this."

So that I should feel much happier if some postponement of the supplementary statements could take place until the near future, though I can quite agree with both Mr. Eccles and Mr. Delano that if they continue to feel that way, they would be remiss in their duty to not bring it to the attention of the President in sufficient time to affect present policy; but I don't think that time need be today.

Eccles:

You don't mean, Harry, that verbally we - you think it would be inadvisable to say that - for instance,

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that we feel that this report wouldn't be complete unless it is followed up a little later on by a supplementary report after studies are made with reference to this particular situation.

Willie:

No, I don't think that would fall in the category of the kind of formal supplementary statement that I had reference to. If you say that orally, I think it's fine, but if there's any appearance of formal disagreement which has to take the form of a minority report or supplementary statement to which all the members do not agree - I think there is something to be gained by not raising that at this time.

Currie:

Could we get this agreement? The last point there indicates that further study is going to be made of the state and local thing. Further study is going to be made in this question of armaments. Can't we put in a colorless phrase there that a further study - without raising the issue - that when a clear view is gotten of how much the budget is shaping up, the tax revenues, and we get a clearer view of the prospects for 1940, another report will be made on the problem of timing.

I'm afraid I was guilty of drafting that, talking about the sharp reduction in buying power. I'm sorry. But just put down that a problem will arise there.

Eccles:

You mean in addition to the last paragraph.

H.M.Jr:

Currie, you see - what are we going to say about the agricultural situation right now? I mean we're facing that right today. What are you going to say about that? That's what - what you going to say about ten million bales of cotton, what you going to say about the wheat?

Bell:

One hundred million bushels of wheat.

Walter:

I take it in this report from the Fiscal and Monetary Advisory Board - I question whether you'd want to bring in all the troubles under this tent.

H.M.Jr:

They all have an effect on the national income. They're right here with us.

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- Eccles: You could bring in endless problems in that field.
- Carrier: I didn't mean to exclude that. I think we can phrase it so that the problem of gearing in timing with the whole fiscal picture - with what's happening in agriculture, business, housing, construction, everything else; I mean tie the two together.
- H.V.Jr: If you want to put in a sentence of timing, I don't have any objection. I have no objection to timing - that the question of timing should be considered - both private and public expenditures.
- Eccles: Sure, that's right.
- White: Could you dictate a sentence of that kind right now, Lauch?
- Eccles: If your national income goes up, your budget is balanced; that takes care of the timing.
- White: If you could get some sentence of that kind - if it's agreeable to the others, the report could
- H.V.Jr: I don't know whether we have time.
- Belmont: Mr. Secretary, I want to assure you that on behalf of the Resources Committee I don't want to - certainly, to muddy up the water, and although I read the statement to be sure I got it across correctly, I think I didn't have in mind anything more than an informal statement that we had - this wasn't - this wasn't the complete answer to the whole problem, that we had to do some more studying on it, there were dangers, rocks ahead, and all that, without considering even those serious ones that you have in mind. But that's all I had in mind: that we wanted to play fair with the President to the extent of not letting him get the notion that this was the complete answer and everything was lovely until 1940.
- H.V.Jr: Well, I think you ought to say it. I still think you should say it. I think you should make that statement, Mr. Eccles should say what he has in mind.

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Delano: I think we have made splendid progress in a better understanding.

H.M.Jr: I think so, and I think that - that this is the best that we can do for people who approach the thing from different angles. Now, if there are certain things unsaid and undone, I think by all means you should say what you have on your mind, and Mr. Eccles should say it. And the President after all has the benefit of what these people can collect and bring to him to help him.

Rumi: Mr. Secretary, isn't the answer that there is a third thing that Harry doesn't mention? There is agreement, disagreement, and unwillingness to make a commitment at the present time. And it seems to me perfectly reasonable that among four people some people have ideas, other people don't want to commit themselves at the present time.

H.M.Jr: Which is me.

Rumi: Doesn't imply disagreement.

H.M.Jr: Which is me.

Bell: Three minutes late now.

H.M.Jr: Haas and Currie and White have this thing retyped and get us over one fresh copy, ribbon copy, for every person at five minutes of two, please - the White House.

White: With or without the statement of timing?

H.M.Jr: Don't know what that statement is.

Currie: I very hastily - I've just scratched this out. "When a clear picture is obtained of (a) the whole budget picture for the next fiscal year; and (b) the prospects of developments in business and agriculture, a further report will be presented on the problem of timing Government expenditures and receipts with private expenditures in the next fiscal year."

Haas: Put the foreign situation

-40-

H.M.Jr: I don't like these things on the run.

Haas: I'd be inclined to leave it out.

H.M.Jr: I'd rather let Mr. Eccles or Mr. Delano make a verbal statement or written statement.

The Fiscal and Monetary Advisory Board has been advised by the experts of the Treasury, Federal Reserve Board and National Resources Committee that:

1. The 1938 national income is estimated at \$62 billion. For the calendar year 1939 it is estimated that the national income will be between \$65 and \$68 billion.
2. A national income of around \$80 billion:
 - a. would provide substantial reduction of unemployment.
 - b. would provide Federal revenues sufficient to balance the current level of cash expenditures on the basis of the existing tax structure.
3. An income of \$90 billion or more is attainable through full utilization of our man power, plant and equipment, technology and natural resources, assuming the elimination of some important bottlenecks.
4. Also it is important for Federal fiscal policy to take into account:
 - a. changes in the volume of the outstanding debt of State and local governments and changes in the volume and character of their expenditures and receipts.
 - b. changes in the volume of capital expenditures being undertaken by private enterprise.
 - c. the fact that available supply of credit is so great that present and prospective Federal borrowing will not create a shortage of credit available at reasonable rates for private enterprise.

In pursuit of the objective of attaining a higher national income we make the following recommendations with respect to fiscal policy for the next fiscal year:

1. If taxes are to be increased, those selected should be such as interfere least with additions to the aggregate income of the American people. These, among others, are: estate taxes, gift taxes, lowering tax exemptions as income rises, higher income tax on middle brackets.
2. We advise against new taxes which operate to reduce substantially consumer purchasing power. These, among others, are: processing taxes, sales taxes, taxes on payrolls, excise taxes.

- 2 -

3. The Board notes with approval the proposed changes in the budget presentation and recommends that the principles embodied in these changes be extended as rapidly as feasible.

4. a. For the purpose of adding to the national income next year, and of preventing what promises to be a serious bottleneck within the next year or so, action should be taken to secure a large railroad equipment program.

b. Recovery could be further stimulated by additional government activities financed through self-financing government corporations. A special report on such activities will be later submitted.

5. That a comprehensive survey be started with the view of immediately setting up machinery to obtain all necessary detailed information with respect to the current receipts and expenditures of State, local and municipal administrative bodies and to changes in the volume and make-up of their outstanding debt.

6. Arrangements should be made at once that would make possible engineering and legal planning of various public works which could be available for immediate prosecution when required to give increased flexibility in the timing of public expenditures and increased assurance of value and utility of the expenditure itself.

These arrangements are much needed not only because of the current magnitude of Federal, State and local public works and relief programs, but even more especially because of the extensive rearmament program being undertaken. To make certain that the rearmament program shall not be continued as a device to reduce unemployment or to stimulate business activity, it is essential to have such plans perfected as will permit a ready transfer of employment from armament industries into needed productive public and private works projects as soon as peak activity in the armament program is passed.

Treasury Department
Division of Monetary Research

Date Dec. 21 1938

To: Secretary Morgenthau

Mr. Taylor has read and agrees
with this memo.

MR. WHITE
Branch 2058 - Room 200

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 19, 1938

TO Secretary Morgenthau
FROM Mr. White

Subject: Price of Domestic Silver for 1939

1. A decision must be reached before January 1, 1939 with respect to the price that the Treasury shall pay for newly mined domestic silver. A decision with respect to the price paid for domestic silver can be made at this time without committing the Treasury or the Administration with respect to any subsequent decisions which may be taken on the whole silver purchase program.
2. The economic aspects of the problem, whether to maintain the present price or to reduce the price, are of secondary importance. The amounts involved are small and the net economic effect is of almost negligible importance to our national economy.
3. In view of the relatively minor importance of the economic considerations involved, we feel that the decisive considerations should be political.
4. The immediate and economic considerations - though only of minor importance - favor, on balance, the continuance of the 64½ cent price for the following reasons.
 - a. Any reduction in the price from present levels would increase the unemployment in the mining industry. Were the price reduced even to 50 cents an ounce, the loss of employment in the mining industry would be a maximum of 2,000 workers, and probably half that number. (The statements made by the silver interests as to the expected increase in unemployment consequent upon a drop in price give figures which are preposterously high and quite inaccurate.)
 - b. The present price paid for domestic silver does have the effect of increasing the purchasing power in the hands of the people at this time when there is a large volume of unused labor and plant capacity. A

Secretary Morgenthau - 2

10 cent drop in the price paid for domestic silver will, we estimate, have the effect of reducing the national income by something like \$15 million, over half of which represents wages, direct and indirect. Though the increase in buying power is quantitatively very unimportant for the country as a whole, it is important for certain mining communities in the Western States.

g. The purchase of domestic silver does not add to the government debt. A difference in the price paid merely changes the amount of the seigniorage profit which the Treasury might use at some time in the future to reduce the outstanding debt.

h. It is claimed by numerous economists that there are other and better ways of increasing buying power than granting a subsidy to silver producers. Unquestionably this claim is sound. Unfortunately, it is quite irrelevant. The other methods are not politically available. Even if they were available they could not be available in sufficient volume to render purchases of domestic silver uneconomic under present conditions. With much fuller employment a subsidy to domestic silver producers would be economically quite indefensible.

5. The objections to the policy of subsidizing domestic silver production are:

a. The chief objection to the continuation of paying a higher price for domestic silver than the world market price of 43 cents is that such a policy constitutes an unearned and unmerited income for the owners of mining stocks. The value of such a subsidy amounts to \$12 to \$15 million per year (assuming an alternative price of 43 cents), a large part of which goes to the stockholders of a few mining corporations. Nor must it be overlooked that even the 43 cent world market price is in fact a subsidized price.

b. By paying a higher price for silver, we are increasing the amount of silver production and adding to our huge stock of silver. In view of the fact that there seems to be no prospect that the bulk of this monetary silver will ever have any monetary use, the additions to our monetary stock would seem to be wasteful. (However, as stated above, our silver purchases do not represent

Secretary Morgenthau - 3

waste so long as the silver is being purchased at a time when we have a large volume of unemployed labor and capital goods.)

c. By maintaining a high price for silver, we render impossible the large scale industrial use of the metal which would take place if the world price fell to (say) 30 cents.

6. Realistically, the balance of economic considerations is, for the present, on the side of continuing to pay the subsidy to domestic silver producers. However, we must bear in mind that this is perhaps the least justified of our "public-works expenditures". It should therefore be one of the first to be curtailed as we approach full employment.

December 19, 1938.
4:01 p.m.

HMJr: Hello.

Operator: Senator Glass.

HMJr: Hello.

Carter
Glass: Hello.

HMJr: Hello, Senator.

G: How are you, Mr. Secretary?

HMJr: Fine. I talked to the President at lunch today about what I came to see you about Yesterday.

G: Yes?

HMJr: About postponing anything until after the first of February.

G: Yes?

HMJr: And he said he would be glad to go along with you on that basis.

G: All right, if he'll just stick . You might consider, however --

HMJr: Yes.

G: You might consider the feasibility of introducing the bill --

HMJr: Yes.

G: And making such changes in it as hearings may suggest, because that would give it the prior status to any other bill, --

HMJr: I see.

G: On the calendar.

HMJr: May I think that over?

G: Just think it over. I thought of it after you left yesterday, but I didn't want to call you back about it. You think it over.

HMJr: Thank you very much. I'll do that.

G: Because I want to cooperate with you as fully as I can.

HMLJr: Fine. Well, the President said he would be glad to go along with you on that basis, but I -- I -- give me a chance to think it over.

G: All right.

HMLJr: Thank you.

REB

GRAY

London

Dated December 19, 1938

Rec'd 3:03 p. m.

Secretary of State,
Washington.

1448, December 19, 6 p. m.

FOR TREASURY.

After a fairly active foreign exchange market on Saturday when the dollar opened bid but closed fairly heavily offered at 4.67-3/8, the market has been quiet today. The dollar opened this morning at 4.67-1/4 but went to 13/16 at fixing time. 78 bars of gold were dealt in, 67 being married and the remainder being supplied by the market. The price was 148 shillings 8 pence which gave one penny premium. There were practically no after fixing gold dealings. This afternoon the dollar has been bid with the British authorities selling a few dollars at 4.67-1/8. The close was around 1/2.

The French authorities acquired a fair amount of sterling on Saturday and permitted a slight improvement in the spot rate and today they have purchased a small further amount of
sterling

REB

2-#1448, From London, Dec.19,6p.m.

sterling around 177.55 after which the rate remained around
.52 with lesser amounts of sterling acquired by the French
fund.

JOHNSON

HTM

HPD

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 19, 1938, 5 p.m.

NO.: 2129

FOR TREASURY.

The market was quiet with the franc again in active demand. It is estimated that during the day the fund obtained about 1,000,000 pounds. At opening the fund entered the market offering francs at 177.60. It gradually lowered the peg to the official closing rate of 177.52. 5 centimes is the forward rate for one month; for three months, 72 centimes.

Very strong and active security market; gain of from 3 to 4 francs in rentes.

In the Chamber the discussion of the 1938 budget is progressing smoothly and rapidly. That body will probably vote on this before Christmas. It is expected that on December 26 or 27 the discussion in the Senate will begin. In financial circles it is felt that while the discussion of the finance law for 1939 will bring up criticism of the decree laws, there are not likely to be any political complications because of the more favorable atmosphere created by signs of improvement in the financial situation, the recent reassuring declarations by Bonnet, and the amelioration of the labor situation.

For the month of October budgetary revenue was around 180,000,000 francs less than the revised estimates, but it was about 1,176,000,000 francs more than for the same

- 2 -

period of last year.

Today's French financial press carries detailed accounts of the reported results of the visit to London by Schacht. However, so far there is very little comment on these reported results. Schacht failed entirely in his mission, according to reports telegraphed from London. The AGENCE ECONOMIQUE representative in London understands that Schacht told his friends in London that the financial outlook for his country was preoccupying; this correspondent adds that it was made clear to Schacht that so long as the present policy of pressure abroad and oppression at home is continued by Germany, the City was not disposed to envisage any sort of collaboration with that country.

END MESSAGE.

WILSON.

EA:LWW

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TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 19, 1938.

TO Secretary Morgenthau
FROM Mr. White
Subject: Digest of Governor Eccles' Speech of December 1, 1938
to the New York Chapter of the American Institute of
Banking

In order to preserve our present system, it is essential to understand the nature of a capitalistic democracy and the operation of the profit motive. The role of the Government should be that of an impartial coordinator. The basic objective of national policy should be the maximum encouragement to private enterprise so that it may furnish the greatest possible employment and production and distribution of goods and services. The Government should not discourage, displace or undertake to compete with private enterprise.

But there are purely economic reasons why the Government should maintain a volume of expenditure necessary to sustain consumer buying power. As private enterprise diminishes, the Government can partly compensate for it by increasing expenditure.

Functionally, the Government, through monetary and fiscal policy, can do much to make economic progress smoother and steadier.

The primary purpose of the banking system is to create and maintain an adequate supply of money -- that is, of bank deposits -- by its lending and investment operations. In the process of deflation, after 1929, forty percent of our volume of bank money was extinguished. The Government did nothing to "destroy confidence", but there was no confidence to destroy. What was required was collective action on a scale which only the Government could undertake. It ought to be clear from this experience that neither the individual bank nor technical rules can provide liquidity. Liquidity should be provided collectively by the Reserve Banks being in a position to lend on all sound assets.

Bankers are now worried about the relative scarcity of opportunity to make loans or investments outside the Government and municipal securities. If the banks do not meet

Secretary Morgenthau - 2

present credit needs, there will be a demand for Congress to enact legislation setting up Government agencies that will meet the needs.

It is not realistic to complain that interest rates are low. The solution of the individual bank's problem lies in expanding the market so that the returns, even at low rates, will exceed the returns on a restricted high price product.

With respect to taxation, what we are really concerned about is not the tax rates by themselves, but how much we have left over after we pay the taxes. A high rate of tax does not necessarily impoverish a nation. The real point is not the rate of taxation but how much is left over after paying taxes. Our major objective must be a maximum of production and employment. That is the only way to achieve balanced budgets. To attempt to cut down expenditure, whether private or public, before we have reached a reasonably adequate national income would be a very short-sighted repetition of a mistake which has been made before.

The problems facing us are essentially economic and not political. No central banking policy can provide an adequate productive use of creative funds. When national income declines rapidly, a democratic government must try to arrest the cumulative deflationary forces. Private capital cannot employ people profitably when there is no demand for their products or when excess capacity is developing. Positive action by the Government is essential to increase consumer purchasing power and to provide employment. To this end the Government, through its borrowing power, must temporarily take over and put into action the otherwise idle funds of its investors and when there is a vast shrinkage in the volume of bank money, must create new money by the sale of securities to the banking system and put this newly created money to productive use.

With the arresting of deflation we must try to sustain an orderly recovery, avoiding such pitfalls as excessive inventory accumulation and excessive extension of consumer credit, of inadequate capital expenditures in the basic industries and of wrong timing of public with private expenditures as in 1936 and the Government's too sharp withdrawal of funds from the spending streams as in 1937. We must better understand the bad effects of unbalanced price conditions.

We must recognize that taxation policy should be closely integrated with monetary and fiscal policy. The type, timing and effect of taxation upon the stimulation of private enterprise, or restraint if a speculative boom threatens, must be considered, as well as the raising of revenue. Taxation should not be increased in a depression and decreased in a boom. We must recognize that the principle of a flexible budget is a necessary safeguard of private capitalism.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE: December 19, 1938

TO: Secretary Morgenthau

FROM: W. H. Hadley

A short review of the U. S. Government security
market for the week ending December 17, 1938

Except for Monday, when the market was strong and active, the government security market was reported to be relatively quiet last week. However, turnover by government security dealers indicated a rather sizeable daily volume, which may be accounted for in switching operations and secondary distribution of the new issues. Inactivity is typical of this period just prior to the year-end. Insurance company and savings bank buying appeared in the market for limited amounts, but what trading there was appeared to be mainly switching operations. The market showed a firm tone throughout and any evidence of demand tended to force prices upward because of limited offerings.

Prices of Treasury bonds were generally better with intermediates and long issues up an average of 3/32nds. The two new bond issues showed the greatest gains. The 2s of 1947 closed the week up 7/32nds at 102.6/32nds bid, and the 2-3/4s of 1960/65 were up 10/32nds, closing at 102.11/32nds bid. The six shortest bonds eased off somewhat and were down an average of 3/32nds, which change may be attributed in part to the fact that the Treasury note maturities have been fairly well extended into the years during which these bonds are callable. Prices of Treasury notes were about unchanged on average. The new 1-1/8s of December, 1943 closed the week unchanged at 101.7/32nds bid. Guaranteed obligations were unchanged on

average. The net result of the week's price changes was that the average prices of all Treasury bonds, the longest Treasury bonds and the longest Treasury notes regained the record high levels attained in October.

Dealers' Portfolios

The principal change in dealers' holdings was an \$18 million reduction in Treasury notes maturing from 1 - 5 years, which appears to be the result of distributing part of their holdings of the new 1-1/8% notes of December, 1943 received on allotment. Total holdings were reduced about \$25 million which, in effect, reverses the gain of that amount during the previous week.

(in millions of dollars)

	Holdings Dec. 10	Holdings Dec. 17	Net Change
Treasury bonds	39.2	34.2	- 5.0
Treasury notes (1 year)	46.6	43.7	- 2.9
" " (1-5 yrs.)	36.6	18.7	-17.9
Treasury bills	5.4	0	- 5.4
H. O. L. C. bonds	-1.2	-1.5	- 0.3
F. F. M. C. bonds	2.3	8.4	+ 6.1
	128.9	103.5	-25.4

Dealers' turnover (purchases plus sales) continued in considerable volume during the week although somewhat reduced from the week before. The daily average was about \$200 million a day, of which about \$100 million was in Treasury bonds.

New Security Issues

Corporate security financing during the week totaled \$57.4 million of which only \$6 million was for new capital. The three most recent new corporate issues, two of which were mentioned in last week's report (the Central Illinois Public Service and the Chesapeake & Ohio bond issues) were sluggish and sticky all week. The third issue was a \$7,750,000 offering of Green Mountain Power Corporation 3-3/4% first and refunding

-3-

mortgage bonds of 1963. The cool reception given these issues in the market may be attributed in part to the pricing which was considered a bit too close to the market and in part to the fact that they were offered at a time when banks and other investors were directing their attention mainly toward the new Treasury issues.

Corporate Bond Market

The main feature of the corporate bond market during the week was the strengthening of second grade bonds which had declined about 1-1/2 points during the previous four weeks. Moody's BAA bond price average advanced about 1/4 point. Railroad issues were the strongest section of this group throwing additional weight into the advance. Utilities were up about 1/8th point as a rise in utility stocks brought about a sympathetic upswing in the lower grade utility bonds. High grade bonds maintained the high levels reached during the second week in November. In the foreign list, European issues continued sluggish with a tendency toward further softening.

Federal Reserve System Account

The only transaction by the Reserve System was the replacement of \$40,100,000 maturing December 14, 1938 Treasury bills with \$29,000,000 new Treasury bills maturing March 15, 1939, \$8,100,000 other Treasury bills, and \$3,000,000 1-1/2% Treasury notes of March, 1941.

Treasury Investment Accounts

There were no purchases made on the New York market for investment account during the period December 12 through December 17, 1938.

JR

~~Confidential~~

Tokyo

Dated December 19, 1938

Rec'd 8 a.m.

Secretary of State,
Washington.

795, December 19, 6 p.m.

Department's 419, December 15, 7 p.m.

The following statement, as furnished to us by
Hugh Byas, was made this afternoon by the Foreign
Minister in reply to questions at a press conference
with the foreign correspondents:

"Mr. Arita: An early cessation of hostilities
in China is earnestly desired not only from the standpoint
of peace in East Asia but for the sake of the nationals
of third powers in China as well as of the 300,000,000
Chinese. Reported foreign loans to the Chiang Kai Shek
regime though they may be purely trade propositions will
necessarily lead to the prolongation of hostilities
and the consequent embarrassment and inconvenience of
foreign nationals. The report of an American loan is
therefore an opportunity to say what we cannot but say:
it is a regrettable act on the part of the United States
which has hitherto acted with discretion and understanding

in

-2- #793, December 19, 6 p.m., from Tokyo.

in Chinese affairs; and if as the United States papers say, it is a political gesture of the United States towards Japan, I think there will be nothing more dangerous.

The Japanese people may regard that the present loan is really intended as economic pressure but with powerful economic unit, and its results will prove quite contrary to what is expected by America. At least the Japanese people will undoubtedly find new grounds for strengthening the proposed new order in East Asia.

Personally, I am surely not inclined to regard the loan as a political gesture towards the activities of Japan.

Asked if those remarks would apply to a loan by Great Britain and how he would regard the prospect of common economic pressure by the United States and Great Britain the Minister replied: 'I say exactly the same thing; this applies to a British loan. But personally I am inclined not to regard that kind of loan as a political gesture.'

GREW

RR:DDM

EDA

Confidential

PEIPING VIA N.R.

Dated December 19, 1938

Received 12:51 a.m. 20th

Secretary of State

Washington

731, December 19, 5 p.m.

Department's 650, December 15, 7 p.m., concerning credits to Universal Trading Corporation.

One. To date there has been no direct reference to the American and British loans financing exports to China in the Peiping vernacular press. This initial lack of publicity is possibly inspired by a desire to minimize the importance and implications thereof. A Tientsin Chinese newspaper of today's date published a Domei report from Japan of a statement by the Minister at Large to China, Tani, to the effect that the credits extended the National Government will have no effect upon the outcome of the present situation and that the foolishness in nations will soon disappear.

Two. An indirect reference to the financial assistance thus rendered is found in a Domei report from Nanking dated December 17, stating that certain provincial and municipal delegates

EDA - 2 - #731, December 19, 3 p.m. from Peiping

delegates are to telegraphically circularize foreign embassies and legations in China and the American and certain European nations requesting that the supply of money and munitions to the National Government be stopped. The Foreign press in Peiping has thus far published news items regarding the loan without comment.

Three. The announcement of these loans has had as yet no appreciable effect on the currency market in North China which was unchanged. The banking report of today's financial market in Tientsin mentions only unimportant transactions at $17\frac{1}{4}$ and $17\frac{5}{16}$ and otherwise reports a dull period.

Repeated to Chungking and Shanghai. By mail to Tokyo.

LOCKHART

WWC:PEG

EDA

Confidential

CHUNGKING (VIA N.R.)

Dated December 19, 1938

Received 12:15 a.m. 20th

Secretary of State

Washington

607, December 19, noon.

Department's 6, December 15, 7 p.m.

News of the granting of credits to be used in financing the exportation of American products to China which reached Chungking almost simultaneously with reports from London of the imminent granting of British credits to China was greeted in Chinese official and private circles with marked elation. The Minister of Finance is reported in the press as having expressed gratification "at this further evidence of America's friendly interest in China's progress and development, which China will not forget". "This credit," Dr. Kung is quoted as saying, "will further the development of China's economic potentialities and will enlarge American trade in China".

The local press has given much prominence to the matter of which the motive of the TA KUNG PAO on December 17 is representative. This Journal emphasizes that the credit is purely commercial, that it constitutes a fresh testimonial

EDA - 2 - #607, December 19, noon from Chungking

testimonial of Sino-American friendship, that China despite financial difficulties will continue to fulfill its financial obligations, and that though purely a commercial transaction it will have the political effect of dealing a blow to Japanese aggression. This paper expresses the hope that the granting of these credits will cause Great Britain to follow suit. The CHINA TIMES comments that the significance of the granting of credits lies not in their amount but in their implications which in its view amount to the first step on the part of Great Britain and the United States in making a "concrete reply" to Japan's wish to set up a new order in East Asia and that they constitute a warning that "Chinese cooperation with the European powers and the United States cannot be destroyed." The fact that the credits came after the fall of Wuhan is noted and the conclusion drawn that Anglo-American recognition of the National Government has not been affected by military or political developments. The extension of Anglo-American credits to China is held not only to manifest the traditional friendship existing between China and these Anglo-Saxon powers but to reflect the commencement by Great Britain and the United States of steps to implement

EDA - 3 - #607, December 19, noon from Chungking

implement the League resolutions to assist China.

Repeated to Peiping for mailing to Tokyo.

PECK

RGC:WWC

(Above reference (Department's 6, December 17, 7 p.m.)
evidently refers to Department 650, December 15, 7 p.m. to
Shanghai.

REB



Shanghai via N. R.

Dated December 19, 1938

Rec'd 3:30 p. m.

Secretary of State,
Washington.

1485, December 19, 4 p. m.

One. General reaction in local foreign and Chinese circles to the extension of credits to China appears to be that continuous Japanese disregard of American and British rights has at last resulted in a definite stiffening of the American and British attitude and that the extension of those credits is a symbol of this change. Local press reaction is summarized below as of possible interest to the Department.

Two. The NORTH CHINA DAILY NEWS welcomes the extension of British credits and an American "loan" to China as indicative of a stiffening attitude; points out that the size of the extension of British credits is political rather than commercial; expresses the belief that the action of the British and American Governments will undoubtedly annoy the Japanese but that Japanese disregard of foreign rights and interests in China tends to invite no strong consideration for that nation; asserts that in any event this action constitutes no infringement of international law; and concludes that

REB

2-#1485, From Shanghai, Dec.19,4p.m.

that should Tokyo decide upon retaliatory measures, Great Britain and the United States are in a position to retaliate more effectively.

Three. The SHANGHAI EVENING POST AND MERCURY refers to this development as the "biggest piece of news out of Washington in many months", and points out that both the American and British credits will be used to develop communications which are a primary need in the industrialization of the far hinterland. The EVENING POST concludes: "Most of all, perhaps, it is cause for rejoicing that the full facts of the China situation are at last being realized abroad and that we have probably passed an important turning point."

Four. The CHINA PRESS characterizes the action of the American and British Governments as encouraging and stresses the fact that if China can be given credits for the purchase of machinery for productive industry, her natural resources will produce sufficient exports to finance the war.

Five. The local Chinese press enthusiastically welcomes this assistance to China and describes it as an "epoch making" event of great political significance. This action of the American and British Governments is also believed by local Chinese

REB

3-#1485, From Shanghai, Dec.19,4p.m.

Chinese papers to mark the beginning of close cooperation between these two governments in dealing with the situation in the Far East.

Six. The local Japanese papers have not yet editorially referred to the extension of these credits to China, nor have local Japanese officials or business men thus far been heard to comment upon these developments. There are no indications yet that the Japanese contemplate any retaliatory measures in this area.

Repeated to Chungking and Peiping. To Tokyo by mail.

GAUSS

ROW

EMB

TREASURY DEPARTMENT

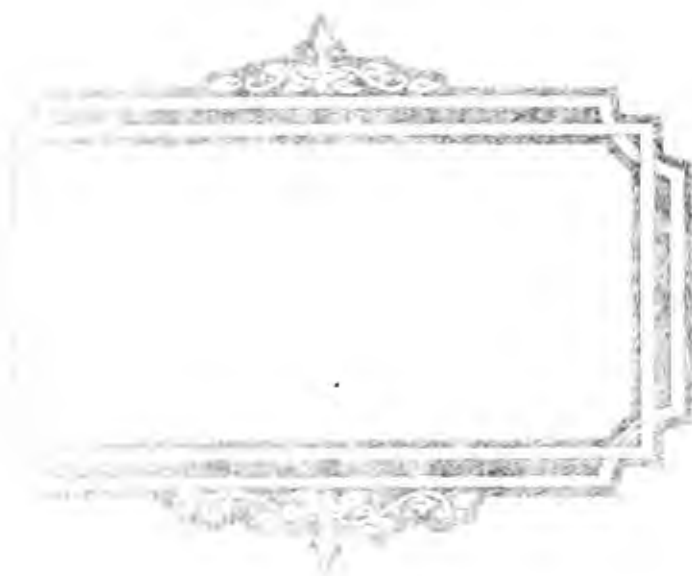
INTER OFFICE COMMUNICATION

DATE December 19, 1938.

TO Secretary Morgenthau
FROM Mr. Haas *HA*

As I mentioned to you sometime ago, Mr. Bell asked if we would give him some assistance in preparing the President's budget message. Attached is our No. 1 preliminary draft. We have incorporated in the draft some of the material which we worked up at your request last summer, when you expressed the possibility of making a speech this fall concerning the fiscal position of the government.

The draft as it now stands is, of course, very preliminary and needs a careful rechecking, which we shall be glad to do if it is decided to utilize the material in the message.



BUDGET MESSAGE OF THE PRESIDENT

To the Congress of the United States: Pursuant to provisions of law, I transmit herewith the budget of the United States Government for the fiscal year ending June 30, 1940, together with this message, which is a part thereof.

Economic Recovery

In my budget message of last January, I was obliged to call your attention to the then-current recession in the level of business activity. Today, in contrast, it is gratifying to be able to call your attention to the vigorous business recovery that has been under way since early summer.

The recession which began in the fall of 1937, and which has been so happily reversed during the past seven months, altogether lacked the earmarks of a major economic depression. The rapidly rising level of business activity in 1936 and the first eight months of 1937 had been accompanied, it is true, by a repetition on a small scale of some of the ill-advised business and speculative practices of 1928 and 1929. But the sounder economic framework established by Congress in recent years, among other factors, helped to prevent a development of those deep and grave maladjustments that bring on a major economic crisis.

This time there was no crisis. Our banking system marched through unruffled. Wholesale forced liquidation

was absent. We avoided the shocks, the disorganization, and the despair of late 1929 and the early Thirties.

Nevertheless, large inventories of many kinds of goods had been built up; and when demand slackened, a great many businessmen took fright, mistakenly fearing a repetition of that long and disastrous economic decline which lasted from 1929 to 1933. Employment fell off with great rapidity. There is always the danger that any business recession, however mild at the outset, may become greatly accentuated by unreasoning fear -- may feed upon itself to produce a downward spiral.

When, after six months of declining production and declining employment, business still gave no sign of imminent revival, I decided that it was time for the Government to act. On April 14, 1938, in fulfillment of the pledge made by this Administration that it would not stand idly by when the course of events threatened the economic well-being and security of our population, I sent a special message to Congress proposing immediate action to start an upward spiral of fuller employment and fuller utilization of our material resources.

I proposed three groups of measures: In the first group, additional appropriations for the Works Progress Administration, the Farm Security Administration, the

National Youth Administration, and the Civilian Conservation Corps. These appropriations were made by the Congress.

In the second group, I placed the Administration's plans to make additional bank resources available for the credit needs of the country through the desterilization of approximately one billion four hundred millions of Treasury gold, accompanied by action on the part of the Federal Reserve Board to reduce reserve requirements by about three-quarters of a Billion dollars. These proposals, which did not require legislation, were made effective in short order.

My third set of proposals was designed to provide definite additions to the purchasing power of the Nation through the creation of thousands of new jobs on public works, including the following: Enlarged authority for the low-cost housing program of the United States Housing Authority; the renewal of Federal aid for public works projects of State and local governments; flood control and reclamation works; additional highway construction; and additional Federal buildings. The necessary legislation for these proposals was likewise enacted by the Congress.

What have been the results? It is, of course, impossible to isolate the results of this many-sided program, which is still in progress, from the natural forces of recovery that

have been increasingly operative. After all, the business recession of the latter part of 1937 and the early part of 1938 was largely an inventory recession, springing from temporary overproduction of manufactured goods, and not the product of deep-seated maladjustments. Nevertheless, as I have said, it was essential to insure that this recession not get out of hand. And this was precisely the result of our program.

The downward spiral in business and employment was checked within a few weeks of the mere announcement of the program; and the upward movement, which began in June, has been proceeding with great vigor ever since. The level of output of our factories and mines, as measured by the Federal Reserve Board index, was 76 in May; it rose to 77 in June, to 83 in July, to 88 in August, to 91 in September, to 96 in October, to 101 in November, and a preliminary estimate gives the figure of 103 in December.

We know, further, that the additional funds made available by the Congress for the Works Progress and Public Works Administrations have enabled us to relieve want and to strengthen purchasing power during the months of slack though increasing employment; and that these will continue to contribute to employment and to the vitality of industry for many months to come.

It is reassuring to all of us who believe in the fundamental soundness of the system of private enterprise to see our country vigorously resuming its march toward higher levels of economic prosperity after so brief an interruption. It is also conducive to confidence to note that the average annual volume of industrial production in the United States, as measured by the Federal Reserve Board index, has shown a gain in every year since 1932, with the single exception of the year just ended; and that the present calendar year has opened with the Nation facing and already experiencing a broad-gauged economic recovery.

The General Budgetary Outlook

The budgetary outlook of the Federal Government is inseparably bound up with the economic outlook for the Nation as a whole.

Without any change in the tax structure, the Government's revenues automatically rise when business turns up and automatically fall when business turns down. The reverse situation obtains with respect to several important classes of Government expenditures. As you all know, the aggregate net deficits of the past six years have been due primarily to

extraordinary outlays -- extraordinary outlays designed to provide work for the unemployed, loans for needy farmers and home owners, and financial aid also to banks, railroads, and other important elements of our economic structure. The demands upon the Government for expenditures of this character naturally increase in bad times and diminish when times get better.

Times are getting better. And, for this reason, we may look forward to substantial reductions in certain important classes of expenditures. For the same reason, we may look forward to increases in the revenues from our present tax structure. In a word, assuming that adequate revenue provision will be made for all new expenditures, we may look forward with confidence to an improving budgetary situation.

Some improvement is already manifest. Since the Budget Summation estimates of last July, the Treasury Department has raised its estimate of total revenue receipts for the current fiscal year 1939 by something more than half a billion dollars; and the present estimate for the fiscal year 1940 shows a further increase of approximately \$152 millions.

Nevertheless, the full effects of improving business upon the budget will be delayed. In the payment of most Federal taxes, a delay of from one to fifteen months is

allowed the taxpayer. Hence, the Treasury's receipts do not promptly and fully reflect changes in the underlying economic situation. Thus, the income taxes to be received by the Treasury during the first half of the fiscal year 1940 will mainly represent the tax liability incurred on the incomes of the calendar year 1938. The lag is much smaller in the case of excise taxes, but even here there is some delay.

On the expenditures side, we cannot escape the fact that the greater part of the total Federal budget is not open to significant reduction without curtailing or eliminating essential governmental services.

The more flexible part of our total Federal expenditures consists of the emergency outlays, principally those for public works and work relief. I believe that a substantial reduction in the total of these items will gradually be possible.

In my opinion, however, it would be a very serious mistake if Congress and the Administration were to undertake at this time an arbitrary and violent curtailment of these outlays without reference to the immediate economic and employment situation.

A private enterprise may lay off a thousand men for reasons of economy and profit thereby. For the Nation as a

whole, a man laid off is no economy unless he finds another job. Every man laid off is a dead loss. To the Nation, a day's labor lost can never be recovered. It is lost to all eternity.

I think the businessmen of this country, no less than the needy unemployed, are entitled to speedy reassurance on this point. The Government is going to reduce its work relief expenditures and its public works expenditures just as fast as other jobs can be found for the workers on these rolls. But, in my opinion, the Government should not curtail these expenditures any faster.

To undertake violent contraction before the natural expansion of private industry is ready to take up the slack would mean several things, all of them bad: It would mean throwing back upon the inadequate treasuries of our State and local governments the entire burden of unemployment relief. It would mean great suffering and want, and loss of self-respect for many of the unemployed. And it would mean a disruptive withdrawal from American industry of a volume of purchasing power that business needs right now.

Redirection to National Defense of Part of
Work Relief and Public Works Expenditures

On the other hand, I believe the time has now come to transform the character of part of our work relief and public

works expenditures. A substantial proportion of these outlays should now be redirected to service national defense needs.

We are all aware of the grave and unsettling developments in the field of international relations during the past few years, and particularly during the past year. International agreements have been violated repeatedly. Great new armament programs are being prosecuted by a number of the leading countries of Europe. With modern weapons of warfare, the nations of this hemisphere are no longer as safe from attack as was formerly the case. And under the conditions of modern war, adequate preparedness means doing many things in advance that formerly could be postponed until the actual outbreak of war. In consequence, the whole problem of the national defense of the United States has been transformed.

I expect in the very near future to send to the Congress a special message bearing upon our new requirements for national defense, making specific and detailed recommendations. I want to say at this time, however, that the Nation during the next few years will be able to find very useful, and even vital, employment for thousands of workers now on the relief rolls.

In this, as in other connections, it is important to realize that the problems of unemployment and reemployment have been accentuated by the virtual disappearance during the depression of the apprentice and employee training practices of private industry. Formerly these training practices converted thousands of grammar school and high school graduates into skilled workers.

Taking into account the numbers arriving at working age each year, and the number of workers eliminated by death or retirement, it appears that the number of available workers in the United States has been increasing at the rate of some 600,000 a year during the past few years of diminished training opportunities. This means that more than three and a half million workers have joined the available labor force since the beginning of 1933.

I believe that our new program should include provision for training large numbers of relief workers in the industrial processes related to our national defense needs. This will not only relieve the national shortage of skilled workers that exists in these fields, which are as necessary to our peace time prosperity as to our national defense, but will also prove a blessing to the individuals involved.

Budgetary Aspects of Capital Outlays
Made by Federal Government

I believe that the present is an appropriate time to call your attention to the importance and significance of capital expenditures in the budgetary outlays of the Federal Government during the past few years. A true and widespread understanding of the Federal finances during this period is the more desirable because of the frequent misconceptions and misstatements in this connection.

Some of the misunderstanding is traceable to the special character of our Government's bookkeeping and accounting practices.

In our Treasury's accounts, no distinction is made between capital investments and ordinary operating expenses. When the Government buys land and erects a new post office building on it, thereby, perhaps, eliminating a previous rent expense; or when it lends money to a municipality for the construction of a new sewage system, the outlays are entered on the Treasury's books as current expenses, no different from those for paper and pencils.

And, if the Treasury during a given year takes in less money in taxes and similar receipts than the sum of what it pays out in operating expenses, capital investments, and

loans, together, the formal result on the Treasury's books is a deficit, even though the net result of all these operations has been a real and large increase in the assets of the Federal Government, or in the income-producing assets of the Nation.

In private business, deficits of this kind are not called deficits at all. They are called capital investments.

The ordinary business enterprise excludes capital outlays from its operating expense accounts. It treats them as additions to its capital account and it is often glad of the opportunity to sell bonds to investors to obtain the money to make such outlays. The same is true of many foreign governments. Further, many of our own State and local governments distinguish between capital and current expenditure in their annual governmental budgets.

Because our Federal Government does not do so, and because, in consequence, distorted notions of the character and significance of the formal Federal deficit frequently find wide acceptance, I am submitting below two very interesting tables covering the five and one-third years between July 1, 1933 and October 31, 1938:

Comparison of Federal Outlays for Durable Improvements and Recoverable Loans and Investments
with the Net Deficit for the Period July 1, 1933 to October 31, 1938, inclusive ^{1/}
(In millions of dollars)

	July 1, 1933 to June 30, 1934	July 1, 1934 to June 30, 1935	July 1, 1935 to June 30, 1936	July 1, 1936 to June 30, 1937	July 1, 1937 to June 30, 1938	July 1, 1938 to Oct. 31, 1938	Total July 1, 1933 to Oct. 31, 1938
Net deficit (gross deficit less debt retirement)	2,895	3,209	4,550	3,149	1,384	1,124	16,311
Less: Prepayment of soldiers' bonus	-	-	1,673	557	-	-	2,230
Net deficit excluding bonus	2,895	3,209	2,877	2,592	1,384	1,124	14,081
Federal outlays for durable improvements and recoverable loans and investments:							
Direct Federal public works	326	396	435	456	446	154	2,213
Recoverable loans and investments	893	463	95	192	141	45	1,829
Public roads	268	317	244	351	237	91	1,508
Conservation work through Civilian Conservation Corps	332	436	486	386	326	105	2,071
New construction projects of WPA ^{2/}	-	-	406	595	464	244	1,709
PWA grants to States and local governments for public works (including administration)	19	49	234	273	190	70	835
Total outlays	1,838	1,661	1,900	2,253	1,804	709	10,165
Deficit (-) or surplus (+) on current account, excluding bonus ^{3/}	- 1,057	- 1,548	- 977	- 339	+ 420	- 415	- 3,916

^{1/} On the basis of daily Treasury statements as revised on July 1, 1938, to reflect more accurately the financial transactions of the Reconstruction Finance Corporation, Commodity Credit Corporation, Rural Electrification Administration, and Export-Import Bank of Washington.

^{2/} Excludes outlays for maintenance and repairs of roads, buildings and other previously constructed public works.

^{3/} Exclusive of suitable provision for debt reduction.

Table B

Comparison of the Net Increase in the Public Debt with Federal Outlays for Durable Improvements and Recoverable Loans and Investments for the Period July 1, 1933 to October 31, 1935, inclusive 1/ (In millions of dollars)

Increase in gross public debt	15,884
Less: Increase in General Fund balance	<u>1,707</u>
Net increase in public debt	14,177
Less: Prepayment of soldiers' bonus, not previously included in formal public debt	<u>2,230</u>
Net increase in public debt excluding bonus	<u>11,947</u>
Federal outlays for durable improvements and recoverable loans and investments:	
Direct Federal public works	2,213
Recoverable loans and investments	1,829
Public roads	1,508
Conservation work through Civilian Conservation Corps	2,071
New construction projects of WPA 2/	1,709
FWA grants to States and local governments for public works (including administrative expenses)	<u>835</u>
Total outlays	10,165
Stabilization Fund	<u>2,000</u>
Total	<u>12,165</u>

- 1/ On the basis of daily Treasury statements as revised on July 1, 1938, to reflect more accurately the financial transactions of the Reconstruction Finance Corporation, Commodity Credit Corporation, Rural Electrification Administration, and Export-Import Bank of Washington.
- 2/ Excludes outlays for maintenance and repairs of roads, buildings, and other previously constructed public works.

Note: The net increase in the public debt is less than the cumulated deficit, exclusive of public debt retirements, because certain funds which were not accounted for as budgetary receipts nevertheless increased the General Fund balance of the Treasury, and thereby reduced the need for borrowing. Some \$517 millions of funds used in the first instance to increase the General Fund balance, as well as the \$2 billions appropriation for the Stabilization Fund, arose out of the increment resulting from the reduction in the weight of the gold dollar. The General Fund balance was also increased by seigniorage on silver acquired under the Silver Purchase Act of 1934 and under the President's Proclamation dated August 9, 1934, amounting to \$467 millions; and in other ways, including net transactions in governmental checking accounts (\$689 millions) and excess of receipts over expenditures in trust accounts (\$190 millions). Partly offsetting these increases were expenditures for melting losses (\$2 millions) and payments to the Federal Reserve banks for loans to business (\$27 millions). Transactions respecting national bank note retirements are excluded from the foregoing figures because they are essentially public debt transactions.

The first of these tables, called Table A, shows that much the greater part of the formal Treasury deficit between July 1, 1933 and October 31, 1934, exclusive of outlays for debt retirement and the prepayment of the soldiers' bonus, is accounted for by what a businessman would call "capital investments".

Thus, during these five and one-third years, your Government invested four billion dollars in such things as improvements in rivers and harbors, the Tennessee Valley Authority, reclamation projects, public buildings, additional quarters to house army and navy units, and recoverable loans and investments.

Some of these capital outlays will be directly self-liquidating in large part or in whole. Thus the conservation and utilization of part of the Nation's great water power resources, through the Norris Dam in the Tennessee Valley, the Boulder Dam in the Southwest, and the Grand Coulee Dam in the Northwest, are not only adding immeasurably to the Nation's basic wealth, but through their electric power output, they will directly return to the Treasury a large part or all of the moneys advanced for their construction. Other outlays, in the form of loans, will also be returned directly to the Treasury as these loans are repaid.

Besides capital outlays of this character, more than six billion dollars additional of Federal money was invested during this period in other types of public improvements. Some of this was in the form of grants to State and local governments for public highways, schools, hospitals, libraries, water and sewage systems, and so on. Most of this group of capital outlays will not be directly recouped by the Federal Government. They have added, nonetheless, to the tangible and useful wealth of the Nation, and will add to the real national income for many years to come.

The total of these two groups of Federal investments during the past five and one-third years exceeds ten billion dollars, and constitutes more than 72 percent of the total formal deficit, exclusive of debt retirement and the soldiers' bonus.

In other words, the whole of the remaining deficit over this five and one-third year period amounts to less than four billion dollars. This sum covered all of the emergency expenditures for direct relief, the great bulk of the outlays for work relief, as well as substantial additions to the durable equipment of the Army and Navy, such as ships, tanks, planes, and the like, which are not accounted as capital outlays. For the fiscal years 1937 and 1938 taken together, the budget was altogether balanced on current account, exclusive of suitable provision for debt reduction.

Increase in Public Debt Entirely Offset
by Increased Treasury Assets
and Capital Outlays

The situation appears even more favorable when approached from the standpoint of the public debt, as is done in Table B. The increase in the gross public debt in the five and one-third years ended October 31, 1938 was roughly sixteen billion dollars. More than two point two billions of this represents only the substitution of formal debt obligations for the soldiers' bonus certificates which were not previously included in the public debt, leaving fourteen billions to be accounted for. A little more than ten billions is accounted for by the expenditures for durable improvements and recoverable loans and investments that I have previously cited. Another seventeen hundred millions is offset by a corresponding increase in the amount of cash in the Treasury's General Fund. Finally, even the remaining two billion dollars of the increase in the gross public debt is offset by another item -- the Stabilization Fund --, the proceeds of which will eventually be available for debt retirement.

In other words, the whole of the increase in the gross public debt is equaled by the increase in cash and other

assets on the books of the Treasury or by expenditures for durable improvements -- capital expenditures; with the exception of the payment of the soldiers' bonus.

Federal Aid to State and Local
Public Works Projects

It is, of course, quite possible that some of our public works projects of recent years could have been completed at somewhat lesser cost if we had disregarded the objective of absorbing the unemployed so far as possible. Likewise, there are doubtless a few blind individuals who would object to giving any pecuniary value to the conservation work of the CCC camps, and who would perhaps cavil at other items. Personally, I am convinced that we got good economic value for the money we spent.

Further, there are some persons who may complain that nothing was added to the assets of the Federal Government as such to offset the Federal grants of money to State and local governments to help them finance the schools, hospitals, public roads, bridges, recreational facilities, and other durable public works completed under Federal programs during the past few years, because the legal title to all these improvements remains in the State and local governments.

I believe that nearly all will agree that this is an extremely narrow view of the case. Nevertheless, let us follow it up a little.

As many of you know, the total interest-bearing debt of State and local governments had been increasing without interruption during the two decades ended in 1933. That year found many State and local governments in a precarious position. The demands upon them for the relief of the unemployed were enormous. But falling tax collections had cut seriously into their resources. To cap the situation, their credit status and their ability to borrow had been greatly impaired.

In this situation, what happened? The Federal Government took over a large part of the burden of unemployment relief. Further, its grants of money in connection with new local government construction projects made it possible for needed improvements to be financed. Then as the force of the Government's many sided attack upon the depression became increasingly effective and the level of business activity rose, the problem of delinquent taxes began to recede and the financial stability and credit position of State and local governments were restored.

I am sure that every member of Congress has seen examples of the thousands of local public works erected with Federal

aid. Every single county in the United States contains one or more of them. Yet, how many of us realize that, instead of increasing at the rate of nine hundred million dollars a year, as had been the case during the previous decade, the total net debt of State and local governments actually declined by one hundred million dollars between 1932 and 1937.

Without the Federal spending-and-lending programs, taxpayers as a whole would now be paying added State and local taxes to cover relief expenditures and interest on borrowed funds. Further, a very large fraction of the Federal Government's non-capital work relief outlays has consisted of expenditures for the maintenance and repairs of the public works of State and local governments.

This is one country; and it is the duty of the Federal and State and local governments alike to minister to the needs of the people. There are some purposes and some occasions in connection with which the Federal Government is in a better position to raise and distribute funds than are the State and local governments. In the end if, because of such emergency spending of Federal funds, Federal revenue requirements should rise, it is clear that this has made it possible for State and local government revenue needs to remain lower than they would otherwise be.

Federal Expenditure Program Increased
the National Income

It is clear, then, that even when we confine ourselves to the cold figures and the limited objectives of private bookkeeping, much the greater part of the budgetary deficit and of the increase in the public debt during the past five and one-third years have been offset by increases in the material assets of Federal, State and local governments.

This fact will doubtless come as a surprise -- and a pleasant surprise -- to many persons. But I do not want to exaggerate its importance. Even if immediate tangible public improvements and recoverable investments had accounted for a much smaller proportion of the total, our deficit expenditures would nevertheless have been thoroughly justified as essential parts of any sound program of economic statesmanship.

I think you will all agree with me that the active use of an adequate volume of purchasing power is essential for national prosperity. In the last analysis, we all give employment to one another through our spending and our investing. When some of us become frightened and stop spending or investing our incomes, we force other people out of jobs and compel these other people to reduce their spending. This is the way in which a vicious spiral of deflation and unemployment progresses.

When this process began on a huge scale late in 1929, the failure of the Hoover Administration to come quickly to the rescue reinforced the fears that were freezing up private spending. Since 1933, the Federal Government has been making up, in part, for the defaults of private spending, thereby directly creating jobs, and, in addition, helping to thaw out the fears restraining private spending.

Many persons have failed to understand that Federal deficits, Federal borrowing, and Federal spending and investing during periods of subnormal business activity and subnormal employment create real additions to the national income. When our Government borrowed money to finance its great work relief, public works, and lending programs, it did not create debts to foreigners; it borrowed money from its own people. In effect, the Government said to them:

"There is a great deal of unemployment and want and financial distress in this country, because you are afraid to spend or invest your money. Unless someone spends that money, men and women who have been thrown out of work by your failure to spend it will be kept out of work. If you are afraid to spend your money at this time or to invest it, we will borrow it from you and spend and invest it in your stead."

So the Federal Government stepped in, borrowed that idle money, spent and invested it, and in that way gave useful employment to millions of idle workers.

We took millions of idle dollars, millions of idle workers, and thousands of idle or half-idle factories and gave them all work to do. And the value of the goods produced by these millions of workers and thousands of factories, plus the value of other goods and services whose production was stimulated by the first wave of reemployment, was added to the national income.

And, since labor constitutes, directly and indirectly, the major cost of production, I can tell you that, regardless of bookkeeping, there is a very real sense in which this country got for virtually nothing, all those bridges and highways and dams and schools and hospitals that we built with deficit expenditures. Why? Because directly or indirectly, they were built with labor that would otherwise have remained idle.

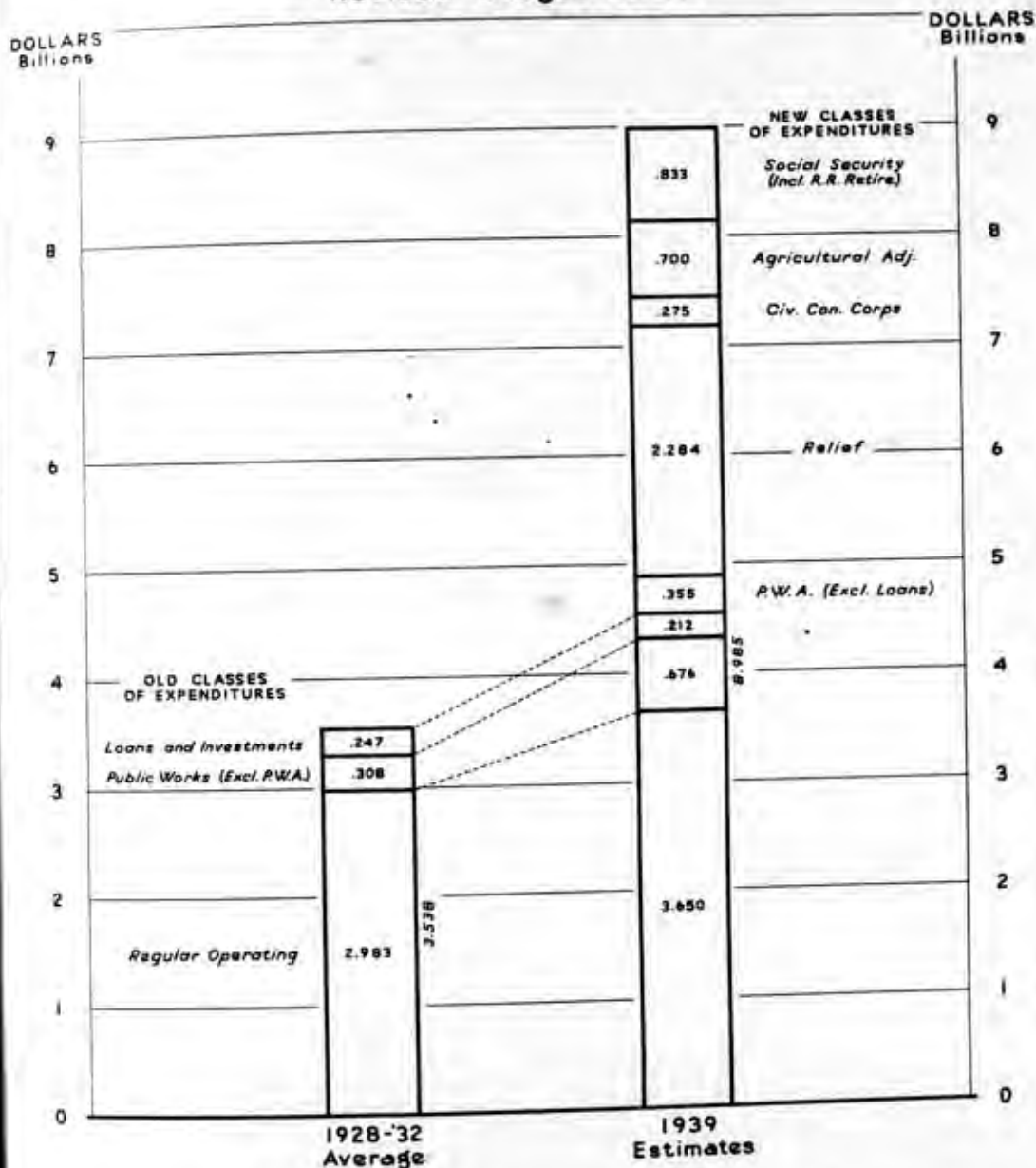
When analyzed in the fashion that I have just outlined, the Government's formal budgetary deficits of the past few years take on a new character, and one that is wholly different from the operating deficits that might be reported by a private business enterprise.

The Level of Federal Expenditures

An analysis of the character that I have just made is essential to a clear understanding of the fiscal history of the past few years. But what of the future? To what extent may we reasonably look forward to a reduction in the level of Federal expenditures? And how adequate is our present tax structure to meet our revenue requirements under normal conditions?

To anyone who has followed in detail the annual budgets of recent years, it is clear that, although added responsibilities have increased the Government's regular operating expenditures, the large excess of the present level of expenditures over the pre-depression level is due primarily to new classes of outlays that were altogether missing from former budgets. This is clearly portrayed in Chart 1 and Table C, which present a comparison, by classes of outlays, of the average expenditures of the fiscal years 1928-1932, inclusive, with those estimated for the fiscal year 1939.

COMPARISON OF 1939 EXPENDITURES WITH 1928-'32 AVERAGE* Revised Budget Basis†



*Excluding debt retirement.

†Excludes expenditures resulting from the operation of the Reconstruction Finance Corporation, Commodity Credit Corporation, and Export-Import Bank.

Table C

Classified Expenditures*

Average of fiscal years 1928-32, inclusive, compared
with Budget Summation estimates for 1939
(In millions of dollars)

	: 1928-32 : : average :	1939 : estimates :	: Increase
Total - old activities	3,538	4,538	1,000
Total - new activities	-	4,447	4,447
Grand total (exclusive of public debt retirement)	3,538	8,985	5,447
Old activities:			
1. Regular operating expenditures:			
Legislative, judicial, and civil establishments	832	1,113	281
Veterans' pensions and benefits	829	539	-290
Interest on the public debt	656	976	320
National defense	666	1,022	356
Total	2,983	3,650	667
2. Public works (excluding PWA):			
Public buildings	47	65	18
Public highways	132	235	103
Rivers and harbors	82	175	93
Other	47	201	154
Total	308	676	368
3. Loans and investments			
	247	212	- 35
Subtotal - old activities	3,538	4,538	1,000
New activities:			
1. Agricultural adjustment program	-	700	700
2. Civilian Conservation Corps	-	275	275
3. PWA (grants and administrative expenses)	-	355	355
4. Direct and work relief	-	2,284	2,284
5. Social security (expenditures not met from payroll taxes)	-	277	277
6. Social security and Railroad Retirement (expenditures met from payroll taxes -- self-financing)	-	556	556
Subtotal - new activities	-	4,447	4,447

On the basis of daily Treasury statements as revised on July 1, 1938, to
reflect more accurately the financial transactions of the Reconstruction
Finance Corporation, Commodity Credit Corporation, Rural Electrification
Administration, and Export-Import Bank of Washington.

Several useful observations may be made from the data in Table C:

(1) About half the total budget for 1939 consists of classes of outlays that were altogether missing from the budgets of the years 1928-1932, inclusive.

(2) More than one-half of the gross increase and nearly three-fourths of the net increase in the outlays for the older classes of expenditures is accounted for by national defense and public works. The decline in the outlays for veterans' pensions and benefits, resulting from the prepayment of the bonus, is roughly offset by the increase in the cost of our legislative, judicial, and civil establishments. Much of the latter increase is attributable to the administrative costs of the new executive and independent agencies established in recent years.

(3) The total of the older classes of outlays for the fiscal year 1939, \$4,538 millions, is substantially less than the actual receipts, exclusive of payroll taxes, of \$5,041 millions and \$5,487 millions, respectively, in the fiscal years 1937 and 1938, and the estimated total of such receipts of \$4,790 millions for the fiscal year 1939.

Although the older classes of expenditures will be about \$1,000 millions greater in 1939 than the average of the years

1928-1932, inclusive, the possibilities of drastic reductions therein appear to be limited. The past few years have witnessed a considerable growth in the responsibilities imposed upon the Federal Government and a necessary growth in the machinery by which those responsibilities must be discharged. Further, the outlay for national defense is far more likely to increase than to decrease in the years immediately ahead. The chief opportunity for savings in the older classes of expenditures appears to lie in the field of public works, where the 1939 outlays, exclusive of the Public Works Administration, are scheduled at some \$676 millions, as compared with an average of \$308 millions in the five years 1928-1932, inclusive.

It is among the newer classes of expenditures that substantial reductions should be possible as the national income increases. Direct relief, work relief, and the Public Works Administration account for \$2,639 millions in the 1939 budget. If, as a result of economic prosperity, these expenditures could be eliminated, and our other public works outlays reduced to normal proportions, the level of Federal expenditures would be reduced by three billion dollars. A well-balanced prosperity would also permit us to reduce the cost of the Agricultural adjustment program and of the Civilian Conservation Corps.

Moreover, the very forces that would make possible a substantial reduction in all these outlays could be expected

to produce a large increase in tax revenues. Our primary budgetary problem, in other words, is one of restoring and maintaining national prosperity.

There are some persons who do not see the problem in this light. They would choose what seems to them the "easy" and "obvious" way to balance the budget. They say "Let us turn this whole problem of relief back to the States, counties, cities, and villages. Let us eliminate completely from the Federal budget all outlays for direct relief, for work relief, and for public works grants to State and local governments."

To me, a balanced budget achieved in this fashion would be spurious, if, indeed, it turned out to be balanced at all. I see no advantage whatever to the country as a whole in achieving a formal balancing of the Federal budget at the cost of unbalancing the budgets of our State and local governments.

For, in one way or another, the unemployed should and must be provided for. I believe that State and local governments may rightly be asked, as they are being asked today, to assume the primary responsibility for their unemployables -- the physically and mentally disabled. I believe, further, that State and local governments can properly be asked to assume a large share of the repair and maintenance work that is being done for them today by WPA labor at Federal expense. Federal work relief expenditures should be supplements to, rather than substitutes for, the regular public works maintenance outlays of State and local governments.

But the general problem of large-scale involuntary unemployment is a national one and is best handled on a national scale. To force the whole financial cost of meeting this problem upon the State and local governments, with their greatly varying resources and burdens, would be, in my opinion, an unwise and even shameful step backward.

I believe, then, that outlays for direct relief, work relief, public works, and the Civilian Conservation Corps should constitute flexible elements in our annual budgets, rising when the need increases and falling off rapidly as unemployment diminishes. During the next fiscal year, as is indicated by the budget estimates contained herein, I expect some of these expenditures to be notably diminished.

In the case of one important type of outlay -- social security --, we must look forward to substantial increases for some years to come. The largest part of the present social security expenditures -- for the Old-Age Reserve and Railroad Retirement Accounts -- is being separately financed by current and scheduled increases in special taxes on employers and employees.

In addition to these specially-financed expenditures, however, the Federal Government is committed under the Social Security Act to large outlays for grants to the States for old-age assistance, child welfare, dependent children, aid to the blind, vocational rehabilitation, and the like. It is

not sufficiently recognized that, unlike the scheduled increases in other social security expenditures, these grants are not covered by any special statutory provisions for increased revenues. These uncovered social security expenditures, which amounted to about \$230 millions in the fiscal year 1938*, and are estimated at \$277 millions for the fiscal year 1939, and \$ millions for the fiscal year 1940, are expected to continue to rise for some time to come.

It is clear that the new duties and responsibilities assumed by the Federal Government during the last few years will make impossible a return to the previous levels of Federal expenditures. Quite in the other direction are certain new demands for Federal assistance that are now receiving and deserving increasing attention in the fields of medical care and education. Nevertheless, the high level already reached by total Federal expenditures, and the additional commitments already established by acts of Congress, should exert a very powerful restraining influence upon both Congress and the Executive in connection with all proposals for additional Federal outlays.

* For the fiscal year 1938, however, receipts from the payroll taxes levied for old-age benefits were in excess of the expenditures therefor, including transfers to the Old-Age Reserve Account and the Railroad Retirement Account; and, for this reason, the net total budgetary outlay for social security in excess of payroll tax receipts was only \$73 millions, exclusive of refunds. For the same reason, the net total budgetary outlay on account of social security for the fiscal year 1939, after deducting payroll tax receipts, is estimated at \$241 millions instead of \$277 millions.

The Revenue Side of the Picture

The enlarged responsibilities and obligations now resting upon the Federal Government can be effectively discharged, in the long run, only if adequately financed by the Federal revenues.

I do not mean that every dollar of expenditure, regardless of its character, must necessarily be met by tax collections in the precise year in which it is paid out. The cost of emergency outlays, for example, may sometimes be spread over several years. Likewise, the cost of capital improvements, particularly those of a self-liquidating nature, may properly be spread over a number of years. But we must be sure that over a reasonable period of time the aggregate receipts of the Treasury are more than the aggregate expenditures, leaving a margin for debt retirement.

We have not yet had an opportunity to witness the full revenue-yielding power of the present tax structure under conditions of sustained prosperity. Estimates of the total revenues that would be produced by the tax system under varying economic conditions cannot be made with any great measure of accuracy. The Treasury Department, after careful study, has found that the revenues are influenced not only by the

volume of business activity, the level of prices, and the size of the national income, but also by many other factors.

Among these are: The distribution of the national income among the various income classes; the pattern as well as the level of business activity; and the rapidity and direction of changes in incomes and prices. Hence, we must be content with rough estimates.

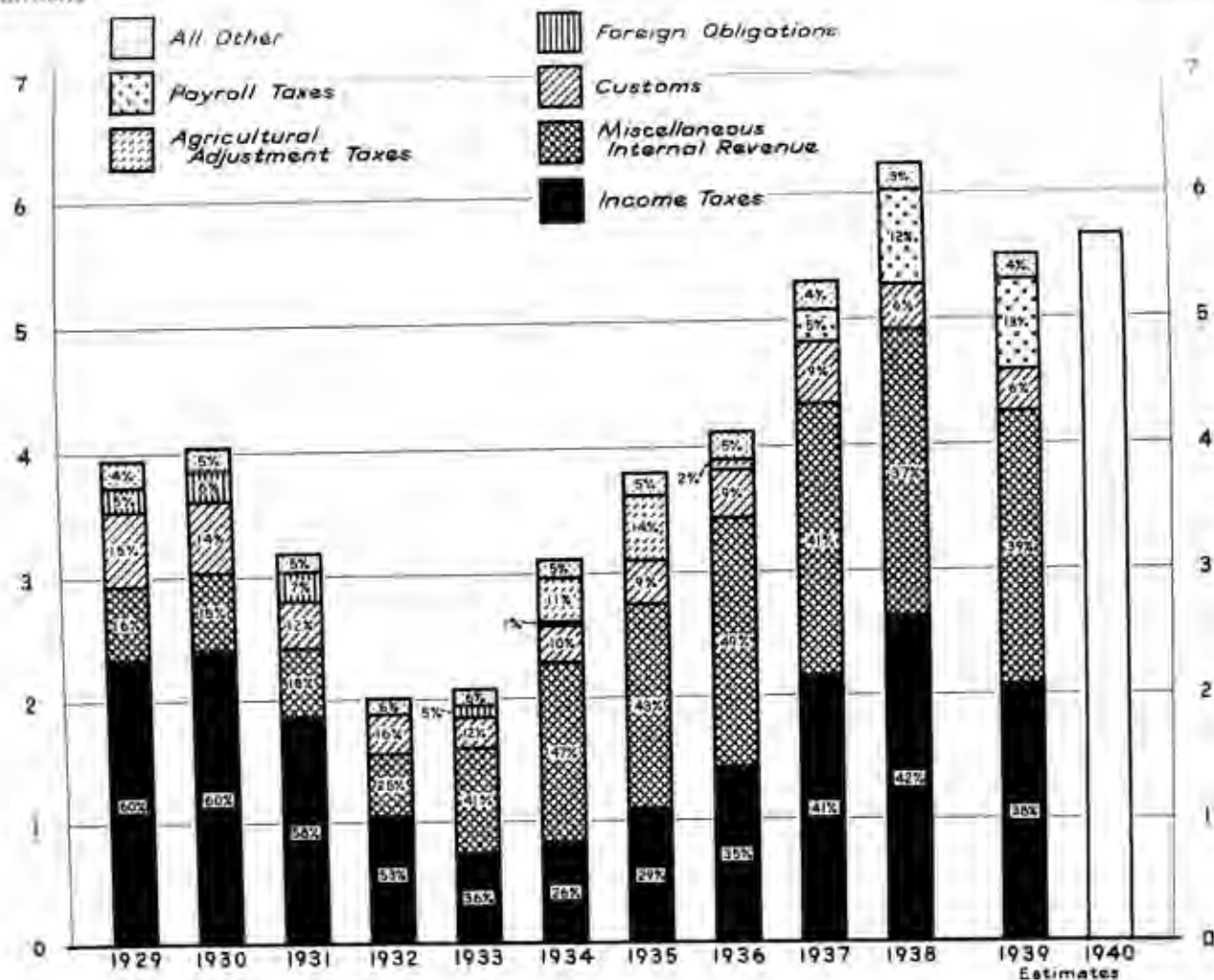
Nevertheless, we have excellent grounds for believing that the revenue structure of the Federal Government has been greatly strengthened during the last five years. The very considerable expansion in the volume of actual receipts since 1932 is shown in Chart 2 and in Table D. The great improvements in business activity, employment, prices, wages, and profits have been important factors in this growth of actual revenue; but changes in the underlying tax structure have likewise been of very considerable importance.

With full knowledge of the limitations attaching to the most skilful estimates in this field, I asked the Treasury Department to make the best estimate it could of the increase in the revenue-yielding power of the tax system since 1932, assuming a level of national income of \$70 billions -- approximating that of the calendar year 1937. That estimate, outlined in Table E, shows that the aggregate yield of our present tax structure under the general condition named is

Fiscal Years 1929 to 1940

DOLLARS
Billions

DOLLARS
Billions



*Excluding Trust Accounts

Table D

Receipts ^{1/}. Fiscal Years 1929 to 1940 by Principal Sources

(In millions of dollars)

	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938	1939 estimated	1940 estimated
Income and excess profits taxes	2,330.7	2,411.0	1,860.4	1,057.3	746.2	820.6	1,105.7	1,426.6	2,157.5	2,634.6	2,086.0	
Miscellaneous internal revenues .	607.3	628.3	569.4	503.7	858.2	1,467.0	1,650.6	2,009.6	2,181.2	2,279.5	2,173.0	
Duties	600.3	585.0	376.6	327.7	250.8	313.4	343.4	386.8	486.4	359.2	335.0	
Foreign obligations.	199.1	239.6	236.1	-	98.8	20.4	.7	.5	.6	.6	.6	
Agricultural adjust- ment taxes	-	-	-	-	-	353.1	521.4	76.6	-	-	-	
Payroll taxes	-	-	-	-	-	-	-	-	252.5	754.6	719.8	
All other	165.7	184.7	147.1	117.0	125.7	141.1	178.7	215.8	215.6	213.2	195.7	
Total receipts	3,903.1	4,048.6	3,189.6	2,005.7	2,079.7	3,115.6	3,800.5	4,115.9	5,293.8	6,241.7	5,510.1	5,661.7

^{1/} Excluding trust accounts.

Table E

Estimated increase in Federal receipts, 1938 tax structure
compared with 1932 tax structure, at an assumed
national income level of \$70 billions

(In millions of dollars)

Income taxes	480
Miscellaneous internal revenue	
Capital stock tax	140
Estate tax	170
Gift tax	20
Tobacco taxes	-
Stamp taxes	- 10
Manufacturers' excise taxes	- 60
Miscellaneous taxes	20
Alcoholic beverage taxes	590
Customs	
Spirits, wines and other beverages	50
All other	- 50
Payroll taxes ^{1/}	790
	<hr/>
Total	<u>2,140</u>

^{1/} The estimated revenue from payroll taxes under the
1938 tax structure is based upon the rates applicable
in 1938.

more than \$2 billions greater than that of the tax structure as it existed in 1932. If the payroll taxes levied under the Social Security Act and the Carriers Taxing Act of 1937 are excluded, the total increase is estimated at \$1,350 millions, of which some \$640 millions may be attributed to the repeal of prohibition.

I also asked the Treasury Department to make similar estimates, rough though they must necessarily be, of the aggregate receipts that might be expected from the existing tax structure at various levels of national income. These estimates, which are intended to indicate only general orders of magnitude, are presented in Chart 3 and Table F.

These exhibits indicate what I mean when I say that the problem of balancing the budget is primarily a problem of economic recovery. At a level of \$80 billions in the national income, not only would receipts approximate \$7-3/4 billions, but our emergency relief problem will have disappeared. With the unexcelled natural resources with which our country is blessed, with its wealth of skilled workers and able industrial leaders, our national income is clearly capable of rising not only to \$80 billions a year, but to \$90 billions, and \$100 billions.

Table F

Estimated Federal Receipts* by Principal Sources,
at Various Assumed Levels of National Income

Based on December 1938 Tax Rates

	National income paid out				
	\$60	\$70	\$80	\$90	\$100
	billions	billions	billions	billions	billions
(In millions of dollars)					
Income taxes	1,780	2,573	3,329	4,268	5,350
Miscellaneous internal revenue	1,983	2,385	2,761	3,153	3,559
Duties	309	400	496	602	712
Miscellaneous receipts	200	200	200	200	200
Payroll taxes	720	824	938	1,058	1,173
Total	4,992	6,382	7,724	9,281	10,994

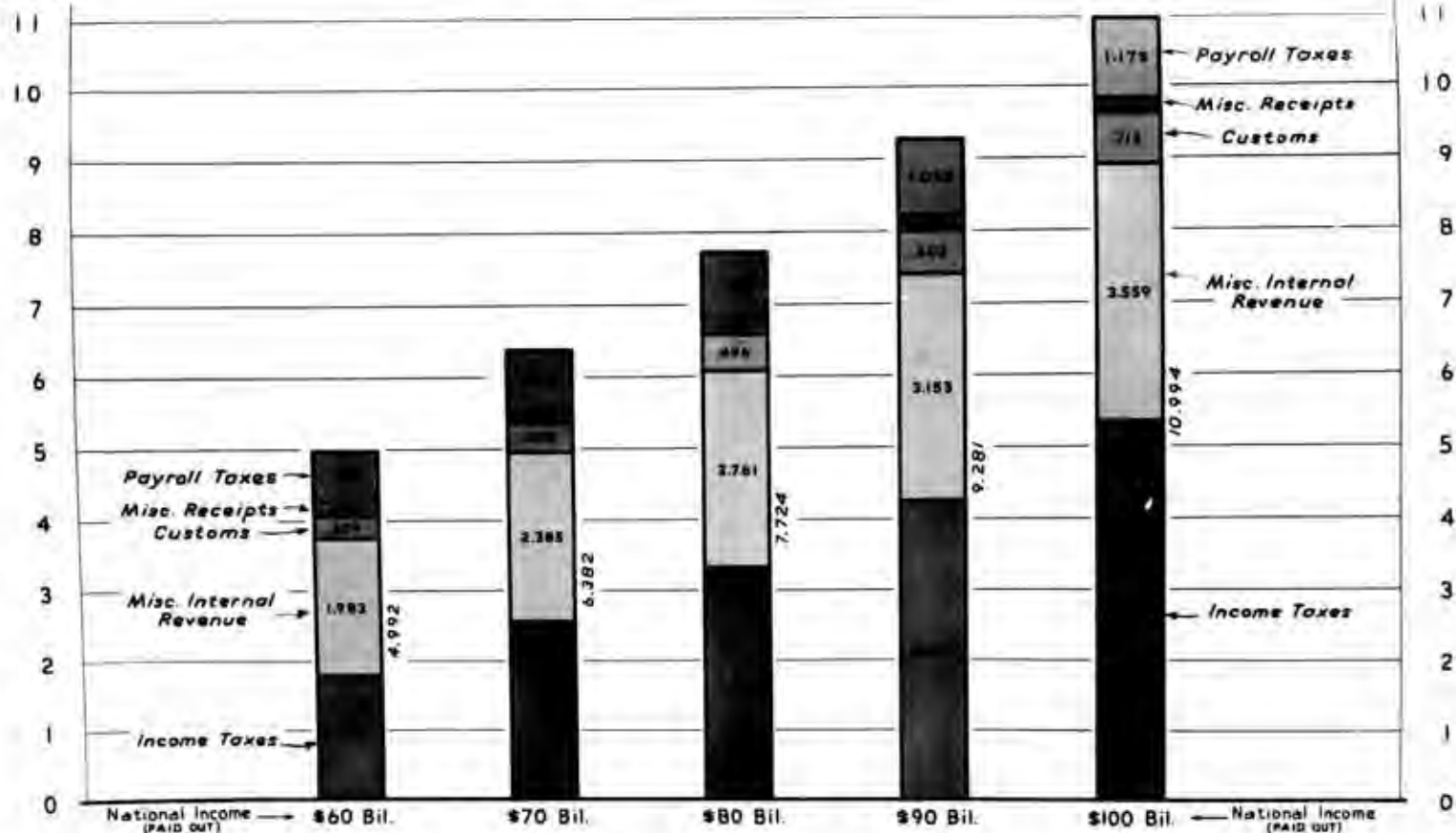
* Excludes trust accounts. Payroll taxes at 1938 rates.

ESTIMATED FEDERAL RECEIPTS BY PRINCIPAL SOURCES AT VARIOUS ASSUMED LEVELS OF NATIONAL INCOME

Based on December 1938 Tax Rates

RECEIPTS
DOLLARS
Billions

RECEIPTS
DOLLARS
Billions



*Excludes Trust Accounts. Payroll Taxes at 1938 Rates

Nevertheless, I strongly believe that our tax structure requires further strengthening. This strengthening is needed to insure that its underlying power keep pace with the growth in the obligations and responsibilities of the Federal Government.

During the past five years, partly in cooperation with the States, the Federal Government has established a comprehensive system of social security for our citizens. The great majority of our workers are now members of the contributory old-age benefit system, under which they will be entitled to regular payments as a matter of right when they have grown too old to work. For the dependent aged who do not qualify for benefit payments under this system, the Government, in cooperation with the States, has provided for old-age assistance payments. Federal-State cooperation has also brought about the establishment of unemployment compensation systems in every State in the Union. In addition, the Federal Government under the Social Security Act provides grants to the States for child welfare, public health work, vocational rehabilitation, and aid to the blind.

This comprehensive system of social security, as I have previously pointed out, is by no means wholly self-supporting. Outlays from the general revenues will be required for parts of the system from year to year. Further, as you all know,

we have established in recent years a soil conservation program and related agricultural adjustment activities that are now costing about \$700 millions annually; and, as I have previously pointed out, there have been other increases in the regular requirements of the Federal Government. Chief among these for the immediate future are the requirements for national defense.

One thing we must all appreciate: In the long run, the new social responsibilities that have been assumed by the Federal Government will be supported by tax revenues, or they will inevitably be abandoned. The only certain protection that we can make for the preservation of our reforms is to see to it that the strength of our revenue system keeps pace with the demands which it is called upon to bear.

Recommendations

I therefore recommend that the Congress devise and impose additional taxes that will provide \$500 millions or more of annual revenues. I further recommend and strongly urge that any and all new outlays beyond those provided for in this Budget be financed by further additional revenues. I also recommend that all of the temporary manufacturers' excise taxes be renewed and that the corporation income taxes that expire this year be reenacted in such form as will, at the minimum, yield no less revenue than they are estimated to yield at present.

GROUP MEETING

December 19, 1938.
9:30 a.m.

Present: Mr. Banes
Mr. Taylor
Mr. Oliphant
Mr. White
Mr. McReynolds
Mr. Baas
Mr. Lochhead
Mr. Gibbons
Mr. Gaston
Miss Chauncey

H.A.Jr: I just - so everybody will know, Mrs. Morgenthau and I are planning to leave here on the night of January 2, get back here most likely on the morning of the 10th, unless something comes up. I've cleared it with the President.

Mac?

Mac: I haven't anything.

Lochhead: I spoke to you on Saturday about the Chinese request to renew the gold loan - the privilege for another year. I've taken it up with the legal department, found out it would be better to make it just six months.

Oliphant: That's because the statute has expired, and so forth. You know about it.

H.A.Jr: He told me about it.

Lochhead: Mr. Bernstein spoke to me about it.

H.A.Jr: Herbert,...

Gaston: Yes, sir.

H.A.Jr: ... would you prepare for my signature a letter sending the tear sheets of the stabilization article in Fortune - I'd like to send it to every member of the Committee in the House that passes on the stabilization bill, and every member in the Senate that will pass on it. You see?

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Gaston: Yes, sir.

H.M.Jr: Plus the leaders in the Senate and the House.

Gaston: Yes.

H.M.Jr: What?

Gaston: Yes.

H.M.Jr: And if - you might consider the possibility in the case of, let's say, the Vice President and the Speaker, of maybe actually sending them a copy of Fortune. We have them.

Gaston: Have they arrived?

H.M.Jr: I think so.

Gaston: Yes, twenty-five copies.

H.M.Jr: See? See, you might in the case of two or three But that's what I've got in mind. Want to get a little propaganda in. Will you fix it up for me?

Gaston: Yes.

H.M.Jr: To the Vice President and Barkley and the Speaker. I'd send it so they get it right after Christmas, so it won't come in with their Christmas mail. But everybody on the House and everybody on the Senate who will have to pass on the stabilization fund.

Oliphant: In the Senate you have both the Appropriations Committee headed by Glass and the Banking Committee headed by Wagner.

Gaston: You want both committees.

H.M.Jr: Yes. Then you might think of taking up with Colonel .. thingumabob... - the Secretary of the Senate ..

Gaston: Halsey - yes ...

H.M.Jr: Halsey - and get him to put it in the first issue of the Congressional Record.

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Gaston: fortune will appreciate ...

H.M.Jr: so will I. Also do it for me. If you want me, I'll call Halsey myself.

Gaston: Might be better.

H.M.Jr: Think not?

Wright: You (Gaston) can do it.

Gaston: All right.

H.M.Jr: Tell him that if he wants to speak to me ... - what? Do you know Halsey?

Gaston: I've met him, yes.

Gibbins: I know him quite well. I think it would be a nice thing for you (H.M.Jr) to call him. Just a question of time, that's all.

Wright: It isn't necessary. I know Halsey very well.

H.M.Jr: Well, will you do it?

Wright: I'll be glad to do it.

H.M.Jr: You do it in the name ...

Wright: Do it what?

H.M.Jr: He'll get it in in somebody's name. I think it would be nice.

Gaston: I think it would be a good idea.

Gibbins: I think if you get time some time and would talk to him, Halsey would feel nice.

H.M.Jr: Oh, I talk to him all the time.

Lockwood: I'll speak to Mr. Gaston about whether or not - they had a release - whether or not the Chinese should announce this had been renewed, and let it go that way,

H.M.Jr: Any way.

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Lochhead: ... or whether we should just put out that this had been renewed for a further period. I'll speak to Mr. Gaston.

Gaston: What's that, silver?

Lochhead: No, this is to make available the exchange. Came out originally in '37. Simply say it had been renewed, I think, keep it very simple.

H.M.Jr: All right?

Lochhead: That's all.

H.M.Jr: Steve?

Gibbons: I've been after Anslinger on this Coster thing. He assures me that their record is such that there couldn't be any mix-up there.

H.M.Jr: I told you, didn't I, about Tommy Corcoran - keeps calling up about these jobs for new Congressman Fay.

Gibbons: Yes.

H.M.Jr: And I turned it over to Helvering - Commissioner Helvering; that I didn't want to get into ward politics.

McR: He cleared it that afternoon.

Gibbons: He spoke to me Thursday or Friday about it.

H.M.Jr: I just wanted to make sure you knew about it.

Harry?

White: The capital flow has been reversed again; it's inward now.

H.M.Jr: Yesterday at twelve o'clock I called on Senator Glass and had, I think, a most profitable conversation, and I went into the whole history of what's happened here in connection with the Comptroller's office and everything else since the first of September down to date, the whole business; and then I told him that the purpose of my visit was to

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recommend that they do not consider any banking legislation until after the first of February, so the public might be informed of what the S.E.C. would bring out in their hearings on Transamerica. It then developed that he had a commitment to Leo Crowley; and he asked Leo to come in and sit down, and Leo agreed that that was the thing to do. But the Senator was very much worried about what Marriner Eccles would or wouldn't do; that he was so close to the President, so forth and so on. So I told him I couldn't vouch for Marriner Eccles, but Mr. Crowley was there and I could vouch for the Treasury and I could vouch for the Comptroller of the Currency.

So I'm going to speak to the President about it at lunch. But I'm quite sure that it's all right. And I told him I thought that the public would write the bill after they had heard these hearings for two weeks. Because the way they have it now, it would just freeze the situation.

But the Senator made a lot of statements about the Chairman of the Federal Reserve. He keeps saying, "Isn't this right?" I said, "I can't tell you, Senator; I don't know. I just don't know." Because I don't know.

Suffield: Did he say anything about the gold plaque they're going to unveil to him down there?

H.C.Jr: Yes, very embarrassing, very unfortunate; placed him in a very embarrassing position. Didn't like it at all.

W.C.: Is he still full of pep?

A.C.Jr: Wonderful. Wonderful.

White: There's a bill prepared for Philippine independence which has been sent by the interdepartmental Philippine committee here. Their legal staff worked a great deal on the bill. It is now before the Treasury for approval. It will be sent through the legal staff. Is there anybody else who's interested?

H.C.Jr: I don't know. Who else is interested in the Philippines?

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Oliphant: I think Taylor might look it over from the general department standpoint, Mr. Secretary.

H.M.Jr: All right. And then me. O.K.

Hanes?

Hanes: Can you see for five minutes the new officers of the American Bankers Association? They're here for two days. They want to stop here. Going to stop at the Comptroller's office between 9:30 and 10; want to stop for five minutes.

H.M.Jr: Not today. I can do it tomorrow.

Hanes: Tomorrow? Be here today and tomorrow. They're going to see the President tomorrow.

H.M.Jr: 10:15 tomorrow?

Hanes: 10:15.

H.M.Jr: 10:15, if they'll be up by that time.

Hanes: I hope so.

H.M.Jr: Banking - A.B.A.?

Hanes: A.B.A., yes, sir.

H.M.Jr: And if you and Oliphant would stay after this meeting, I'd like to talk to both of you.

Anything else?

Hanes: Nothing else, no.

Duffield: If you'd like to put the power group down for tomorrow morning, we'll be ready - or any time tomorrow.

H.M.Jr: Power - 11:15 tomorrow.

Oliphant: 11:15.

H.M.Jr: 11:15. And would you get - well, I'll tell Bell myself. I want - I'll tell him myself; he'll get it for me - something I want on this.

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Duffield: That's all I have.

H.M.Jr: Yes. Did you clear that thing about that attorney? You asked me about some attorney. You wanted to go outside ...

Duffield: Never mind. Never mind.

H.M.Jr: All right.

Duffield: Never mind.

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

Wayne?

Taylor: (Moes nothing)

H.M.Jr: George?

Moes: White ...

Mos: Black.

H.M.Jr: Listen, George, you mumbled a couple remarks to me the other day while we were having these meetings with the up-and-down-hill committee that you weren't entirely satisfied, so if you're not

Moes: I did some talking after you left.

H.M.Jr: Did you? Because if you're not ...

Moes: There is one other part of it, you see, which is not the experts' report - if I were a member of the committee I wouldn't write it just that way. But I felt that was the committee itself.

H.M.Jr: Well, you better get in touch with Harry before 10:30 and see if there's anything in it you don't like; we're meeting again at 10:30 - Mac.

-GK: Yes, I've already notified them.

H.M.Jr: And give me a little memorandum if there's something you don't like - if you'll do it for me.

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Hess: All right.

H.M.Jr: I changed a little bit yesterday. The point that I'm making, in the room here: if Mr. Eccles wants to go out on this compensatory budget, I'm going to let him do it over his own signature - watch Harry - because I can't go along with him that we need bigger deficits in order to get more prosperity.

White: If you put the word "yet" on there, it will be all right.

H.M.Jr: Why? Where does the word come in?

Gaston: Just add it.

H.M.Jr: "Yet more prosperity."

(Hearty laughter)

G.M.Jr: That came close.

H.M.Jr: Now, if anybody - if Mr. Hanes or Mr. Taylor wish to overrule me on that, have very strong feelings on a compensatory budget, why, ...

Hanes: I haven't collaborated with you on it at all, and I told Harry White I wouldn't go along with it.

H.M.Jr: On which?

Hanes: On that line that says you've got to spend every dollar you collect in taxes.

White: Oh, that was out after you and the Secretary stated that - we decided to take it out.

H.M.Jr: He put it a little bit differently. He said in order - before we raise more taxes we have to have bigger deficits.

Hanes: That's what it means: you've got to spend every time you get it, and go into debt.

H.M.Jr: And I've also crossed out the part where they're worrying about a smaller deficit the second half of the fiscal year '40. I told them that they could take that up as a separate worry. I mean Eccles

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can write anything that he wants to, but I'm not going to write that kind of stuff.

Hess: Well, my qualification on - I have nothing to say.

H.E.Jr: Pardon?

Hess: I have nothing to say, if that's your stand.

H.E.Jr: I'm not going to worry about a - I mean those are the kind of worries that I enjoy; if the deficit is going to be smaller the second half of '40, I'm going to say, "Three cheers."

and one of these days when I get a little breathing spell, I'm going to take the cash deficit position, which struck a low in November '37, and then show what the Federal Reserve did after that; how they increased the marginal requirements on the Stock Exchange, how they increased the reserve requirements. And this idea that everything was done here is just the bunk, and one of these days I'm going to just let go.

Hess: My comment was ...

H.E.Jr: I think I'm correct that after November 30 - I know I'm correct - that the cash - we practically were in balance in November '37, then from then on the deficit steadily increased before they passed another law or did a thing, just began to rapidly mount. Our inventory position changed, but never mind that. But along comes the Federal Reserve after that, and they increased reserve requirements, and they increased up to 50 percent.

And I learned something last night that I didn't know: that the first time that the S.E.C. learned about the increase in marginal requirements was when they read it in the newspapers. I learned that last night for the first time from the Chairman of S.E.C. So I says, "Well, you weren't treated any worse than I was."

But that's just this Monday morning bile.

Taylor: I think you're wrong on your calendar there.

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H.M.Jr: You think the thing on the Stock Exchange was before November.

Taylor: And the reserves.

H.M.Jr: Oh no, the reserves came along in March....

Hess: No, it was '37.

Oliphant: Fall of '36.

H.M.Jr: You're right.

Gaston: May '37.

Oliphant: And raised them once more after it all started down; to be sure it kept on going down, raised it again.

Taylor: Did it in two - remember this long split in between there; and the last half of it did take effect as of May first, I guess it was, or March - March something ...

Gaston: March and May.

H.M.Jr: I'm going to leave bygones be bygones, unless somebody starts something, because I'm hoping we're all working for this 80 billion dollar national income. But if somebody starts something, I'm not going to take it.

White: You don't feel, Mr. Secretary, that bygones ought to interfere with a proper valuation of the issues at stake: to reach 80 billion dollars. You just said that, and I'm merely interpreting it and re-emphasizing it.

H.M.Jr: Yes, if these fellows don't quit throwing at me and trying to get me to sign things which I don't believe are so ... Incidentally, I found out where Ruml got this stuff, and I think the Treasury - there's a fellow by the name of Kahn - K-a-h-n - at Oxford or one of those places, who wrote this stuff. And then Mr. Maynard Keynes took it and didn't accept it entirely and wrote some stuff about it, and then it comes over here.

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White: That's not quite the story, Mr. Secretary, but - I mean you may have got it that way, but I don't think that's quite the technical history.

H.C.Jr: Have you ever seen the stuff?

White: Kahn is one of the brilliant young economists. It came out about two years ago, a year and a half ago - development of a theory of that kind. I think he possibly was the first one to use the term "compensatory," but the idea wasn't completely novel in any way.

H.C.Jr: Well, I never heard about it.

White: He's a very able young man.

H.C.Jr: Mrs. Holland had to bring it to my attention.

White: He's a very brilliant man. And Keynes and Miss Holland and that school - the school that Miss Holland represents and the school that Keynes represents - neither one should be trusted as to what they think of the other. They represent diametrically opposed views. But Kahn is an extremely able fellow, and he's one of the brilliant economists; he was an assistant of Keynes and gave Keynes a lot of his ideas.

H.C.Jr: Well, it's nice to have some of these Englishmen come over here and tell us

White: Well, anyhow - I mean there's more to it than just that, Mr. Secretary. That's all.

H.C.Jr: Well, to correct any doubts that you have, I've spent five half-days now of very valuable time, trying to adjust myself to the rest of these people on this committee, leaving Mr. Bell out. But I think it makes, as far as - the only thing that I hope for is the possibility, and that's a very slight possibility, that maybe after they put their name to this thing they won't go out and make some more statements which will hurt the country. Inasmuch as I don't make statements, it doesn't make any difference... But they've got to go a long way before I'm convinced. But I again repeat, if they start a public attack

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on me or on the Treasury on this stuff, believe me, they're going to get it with both guns. I'm looking for a fight.

Taylor: Thought you had one.

H.M.Jr: Well, I've been so polite, Wayne, it hurts. I haven't been so polite for so long - I don't know when. I sort of - it sort of gripes me.

Oliphant: There were speeches made during the second half of '36 that ought to be recalled in that connection.

H.M.Jr: Well, I'm willing to be a good boy just as long as they don't put the red hot poker into me.

White: I think you're unduly - I don't think they're looking for a fight in that direction.

H.M.Jr: Well, I am.

White: Don't think there's any intent....

H.M.Jr: Well, I am.

White: I'm afraid you are.

McR: He says he's sorry

Haas: I wanted to introduce the term, Mr. Secretary - the "compensatory" for private spending taken in conjunction with this other thing - more recognition being given to that. If I was a member of the committee, I'd insist on it. I don't think you can throw it all out the door. The whole thing - there's some question whether officially the Treasury or the President should take up the theory wholly as an explanation at this time, when it is in such a controversial

H.M.Jr: ... stage. Well, I still believe in private spending.

White: Anybody that doesn't?

H.M.Jr: Yes. Oh sure. Now, Harry, don't think these fellows when they come in here talk to me the way

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they do privately. Now listen ...

White: Well, Mr. Secretary, I grant that just - may I make just one statement, because I think it's being presented - the other position is being presented in somewhat an unfair light. I merely say unquestionably there is room for difference of opinion, but I don't think that that theory, that approach, is quite as bad or quite as baseless as one might gather from the rather facetious remarks, that's all. As I'll let it pass, but I just wanted to register my ...

H.M.Jr: Yes, but the statements that Eccles and - that Eccles and some of them close to him are making just scare people to death - just scare people to death. And he makes statements in private conversation that he doesn't make in front of me, and the statements he makes just scare people to death.

Herbert?

Gaston: I suppose you noticed that the Anglo California Bank made a public announcement yesterday of the plan to refinance through the R.F.C. They stated it all quite frankly.

H.M.Jr: I didn't see it.

Gaston: That they were to sell eight billion - eight million par value of their stock.

H.M.Jr: It's a private bank, Herbert.

Gaston: What?

H.M.Jr: You said "billion." I say it's a private bank.

Gaston: Yes, eight million; and they stated the amount they were to receive was 20 million and that they would pay interest on the 20 million.

H.M.Jr: Really?

Gaston: Yes, they stated the whole thing accurately.

Duffield: That was all drawn up in the Comptroller's office.

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H.M.Jr: Well, that's a victory, isn't it?

Gaston: It's a very good statement.

H.M.Jr: That's a victory, isn't it?

Gaston: You'll find it in the Herald-Tribune.

H.M.Jr: That's a real victory for ...

Oliphant: Had your Herald-Tribune this morning already.

H.M.Jr: Well, didn't you see General Johnson on that?

Oliphant: No, I didn't see him.

H.M.Jr: Get your office to get you Wednesday or Thursday night - General Johnson on that, will you? He comes right out openly and says so.

And then on this letter from Kintner, Herman asked me whether he wants a chance to correct it. He asked me. I think that Herman should correct all inaccuracies.

Oliphant: Should or should not?

H.M.Jr: Should, definitely.

Gaston: All right, I'll get hold of Bob today. I suggested he talk to Herman.

H.M.Jr: You know, he's giving us a chance to see the financial and foreign affairs, plus the anecdotes.

Gaston: Yes.

H.M.Jr: So you might ask him when he's ready, will you, please?

Gaston: Yes, I will.

H.M.Jr: Because that's a real victory, if they've done that. Anything else?

Gaston: I noticed this Social Security plan is out - the Advisory Council.

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H.M.Jr: Are you free tonight (to Hanes)?

Hanes: Yes, sir.

H.M.Jr: Can you find out?

Hanes: I'm to put my children and family on the train at 10:30.

H.M.Jr: Tonight?

Hanes: Yes.

H.M.Jr: Would you rather - you want to help them pack?

Hanes: Oh no, they're ready. I'd just like to go to the train with them at 10:30.

H.M.Jr: Well, we'll be through. Be quite frank.

Hanes: No, that's fine with me. All I've got on my mind....

H.M.Jr: Well, maybe you'd rather spend the last evening with them.

Hanes: I'm hoping to see them the latter part of the week. This isn't new to you. You've known about that before. We've both got something on our minds.

H.M.Jr: I told your Mrs. that you - didn't you say you could ask him - you'd know after you saw the President of the United States this afternoon where you're at. Did she tell you?

Hanes: She told me, yes.

H.M.Jr: What was getting at - I'd like to do Social Security tonight. If you say let's do it Tuesday night, something else might come up.

Hanes: No, this is all right with me.

H.M.Jr: 7:30.

Hanes: Sir?

H.M.Jr: 7:30. Not for dinner. Don't want to have dinner ...

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Hanes: After dinner.

H.A.Jr: No - say, come at 7:30 for dinner; then you can leave by 9:30.

Hanes: Fine.

H.A.Jr: How's that?

Hanes: All right.

H.A.Jr: What?

Hanes: O.K. with me.

H.A.Jr: Because I've got to learn something about Social Security. Is that all right?

Hanes: Yes, sir, fine.

H.A.Jr: You (Chauncey) tell the house Mr. Hanes will be there at 7:30.

Chauncey: Oh-huh.

H.A.Jr: Herman?

Oliphant: Eddie told me about his talk with Bob and Joe (Kintner and Alsop). He probably told you.

H.A.Jr: All right, gentlemen. If I could see Mr. Hanes and Mr. Oliphant ...

TREASURY DEPARTMENT

102

INTER OFFICE COMMUNICATION

TO Secretary Morgenthau

DATE December 19, 1936

FROM W. H. Hadley

TREASURY BILL OFFERING
(In New York)

	<u>Aver. on 1st 100 million</u>	<u>Aver. in N.Y. last week</u>	<u>Aver. for country last week</u>	<u>Amt. of tenders recd. in N.Y.</u>
91-day bills	0.007	0.013	0.013	\$383,242,000

Note: This average rate of 0.007 is an all-time low. The previous low was 0.011 June 29 of this year.

TREASURY DEPARTMENT

203

INTER OFFICE COMMUNICATION

CONFIDENTIAL

DATE December 19, 1938

TO Secretary Morgenthau
FROM Mr. Haas
Subject: The Business Situation,
Week ending December 17, 1938.

HH

Conclusions

(1)

December will probably mark a temporary turning point in industrial production, following the continuous rise in the FRI index from 76 in May to 102 (preliminary) in November. New orders in November made only a moderate gain. During early December they have declined to below the November level, while production has apparently increased somewhat further. This and other evidence tends to substantiate the general expectation of a temporary setback during the early part of 1939.

(2)

The unfavorable commodity price situation shows no indications of improvement, and together with its principal causal factor -- the unsettled foreign situation -- constitutes the chief uncertainty in the business outlook for 1939. The BIS all-commodities index has reached the lowest figure since December 1934.

(3)

Strengthening factors in the underlying business trend include: (a) a relatively high level of consumer purchasing power, as measured by national income payments, which at present is not being fully reflected in actual consumer buying except in certain lines, as in the buying of automobiles; (b) comparatively low levels of inventories in most lines of trade and industry; (c) the prospect of increasing stimulus to business from FVA expenditures, a growing volume of residential construction, and some amount of utility expansion.

The short-term outlook

A decline in the FRB index to a low of 95 to 99 sometime during the first quarter of 1939 is expected by a number of business analysts who were interviewed recently by members of the research staff of the Federal Reserve Board, according to the Board's confidential "Current Comments" of December 13. All agreed in the belief that any decline would be moderate, and that a further advance to above the December peak would occur later in the year. Expectations were that the average FRB index for 1939 would be around 104 or higher. There was general agreement among the analysts consulted that in most lines, except steel and automobiles, inventories are not increasing, and in some lines are still being reduced.

The possibility of some recession in business during early 1939 is substantiated by several lines of reasoning: (1) On a seasonal basis, a decline of 9 per cent during January would be registered in the FRB adjusted indexes for both the steel and the textile groups, which have a combined weight of nearly one-half in the total index, if the actual production in these industries during January is at the same rate as during December.

(2) The volume of new orders appears to have reached a turning point for the time being. Orders during November (See Chart 1) showed only a moderate increase, almost entirely due to the expansion of automobile buying. Weekly data for the first half of December (See Chart 2) show a drop in total orders to below the November average. Steel and textile orders have declined rather sharply, while building material orders have shown some increase. A general belief is held in the steel industry that orders will increase after New Year's day. It would seem that any urgent desire to buy steel after that date should be foreshadowed by some return in orders during December.

(3) On the basis of past experience, an uninterrupted business upturn lasting as long as 6 months has almost invariably been followed by a more or less extensive reaction, hence a temporary setback at this time would be a normal expectation. The fact that industrial production has recovered to the levels of new orders and consumer buying suggests that any further healthy recovery must await an improvement in new orders and an increase in consumer buying.

The longer-term outlook

In the business outlook for the year 1939 as a whole, the commodity price outlook assumes a position of major importance. Apart from the influence of production and stocks on prices of individual commodities, the commodity price trend during 1939 will, of course, represent the resultant of world and domestic forces. During the early part of 1938 (See Chart 3) world and domestic influences, broadly speaking, followed similar trends, and commodity prices accordingly moved in the same direction.

Since midsummer, however, foreign and domestic influences have been widely diverging. Commodity prices, which would normally have responded sharply to the marked rise in industrial activity, have been unable to make upward progress since the effect of improving industrial demand has been nullified by the effect of the weakening foreign situation. No evidence of improvement in the foreign outlook, so far as it relates to commodity prices, is yet definitely discernible, with the exception of an upturn in foreign industrial production during September. Political uncertainty clouds the horizon, and sterling exchange has continued to follow a general downward trend.

The BLS all-commodities price index during the week ended December 10 reached the lowest figure since December 1934, with farm products showing the largest decline. (See Chart 4). During recent months, as shown in the lower section of the chart, prices of finished products have tended downward; raw material prices have remained generally stable, with some weakness apparent during the past week; while prices of semi-finished products, after strengthening in response to increased industrial demand during the fall, have declined sharply in the past two weeks.

The effect of an unsatisfactory price outlook on business during 1939 will be minimized by the hand-to-mouth buying policies that manufacturers and industrial buyers generally seem to be following. While farmers' purchasing power would be directly affected by declining prices, the experience of the years 1925 through 1929 suggests that a declining price trend is not necessarily an insurmountable handicap to business recovery. In those years business improved in spite of a gradual decline in prices.

Secretary Morgenthau - 4

Positive factors that appear likely to support business in 1939 include: (1) An extension of recovery in the construction industry, both through PWA expenditures and through an extension of the rising trend in residential construction. The S. W. Dodge Corporation forecasts an increase of 32 per cent in the total value of residential building next year. Some extension of the utility group and some volume of industrial building may be expected to contribute to further recovery in the construction industry. (2) The relatively high level of national income payments has not yet been fully reflected in consumer buying, except perhaps in the case of automobiles, probably because of individual debt paying and increased saving during the early stages of recovery. This should provide support to business on any setback, and become a more positive strengthening factor as recovery progresses. (3) The railroads next likely to offer more support to the steel industry in 1939 than in 1938, owing to a more favorable recent earnings trend, which has brought a marked upturn in railroad equipment buying in the past two weeks.

Current business news

The New York Times adjusted index for the week ended December 10 rose 1.2 points to a new high for the year at 101.8. The rise was due largely to an increase of 2.1 points in the adjusted index of electric power production. Since the seasonal factor for this index increases sharply during the following week, the upturn in the electric power index may be due partly or entirely to an imperfect seasonal adjustment. Gains were also recorded for automobile production, steel sheet production, and lumber production, while cotton mill activity and carloadings declined. For the week ending December 17, tentative data indicate a further rise of 2.0 points in the adjusted automobile index, and a decline of that amount in the steel index.

Copper consumption of copper during November, as measured by deliveries to consumers, dropped to 51,297 tons, compared with 59,527 tons in October. This decline of over 25 per cent was more extreme than had been looked for, and led American producers to make plans for reducing production. Lower operating rates for Kennecott are expected to take effect January 1, and other companies will probably follow. Foreign consumption of copper during November made a sharp drop, deliveries to foreign consumers being off only 10 per cent.

The decline in steel operations of 2.3 points this week — 57.6 per cent of capacity was more than seasonal, and represented more of a decline (in points) than in the corresponding week in any of the previous 5 years. Incoming orders of the U. S. Steel Corporation during the past week were at an even lower level, approximating 45 per cent of capacity.

Some falling off in cotton mill activity has been expected in the textile trade, according to newspaper reports early this week, owing to an accumulation of unsold stocks at mills. The New York Cotton Exchange Service reports that "sales of unfinished goods in recent weeks have run much below production, and some groups of mills have planned to curtail operations in the next few weeks". Our confidential reports from textile companies confirm the recent decline in sales. At the end of this week, however, mill sales took a distinct turn for the better. Print cloth sales during the week mounted to an estimated 44,000,000 yards, or more than double the weekly mill output, and trading expanded in other mill products. This upsurge in buying has stopped talk of mill curtailment, and no more than the usual holiday shutdowns are now expected.

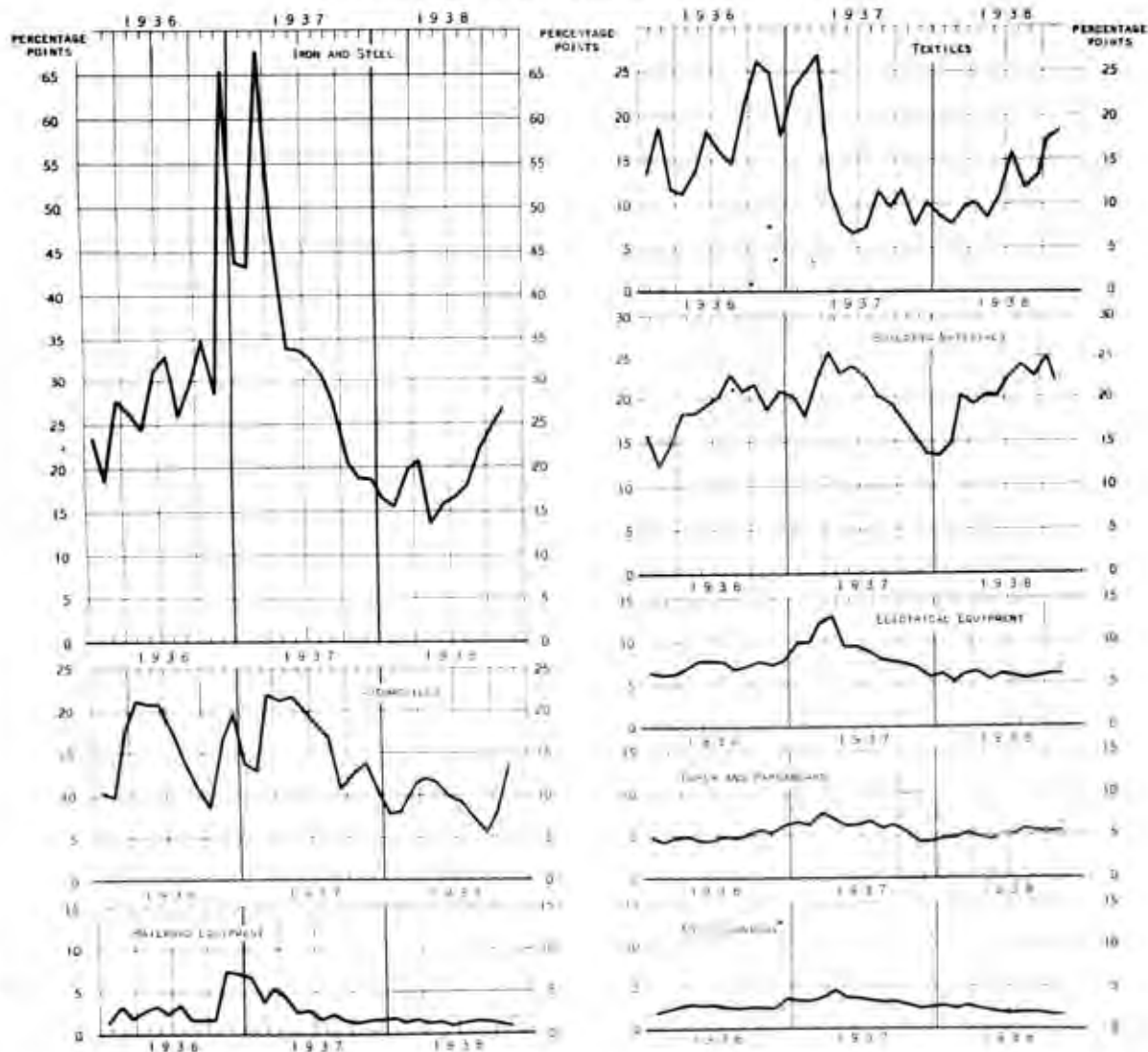
Department store sales for 264 reporting stores during the week ended December 10 totalled \$60,692,000, as compared with \$49,166,000 for the previous week. The rise due to Christmas buying was slightly more pronounced than last year, the total dollar volume showing a decline of 2.1 per cent from last year's corresponding figure, which compares with 2.4 per cent for the previous week. A further sharp rise in sales may be expected during the week ending December 17, particularly since Thursday was payday. Last year's reports for the corresponding week showed an increase of 13 per cent in total sales.

NEW ORDERS AND FACTORY OUTPUT



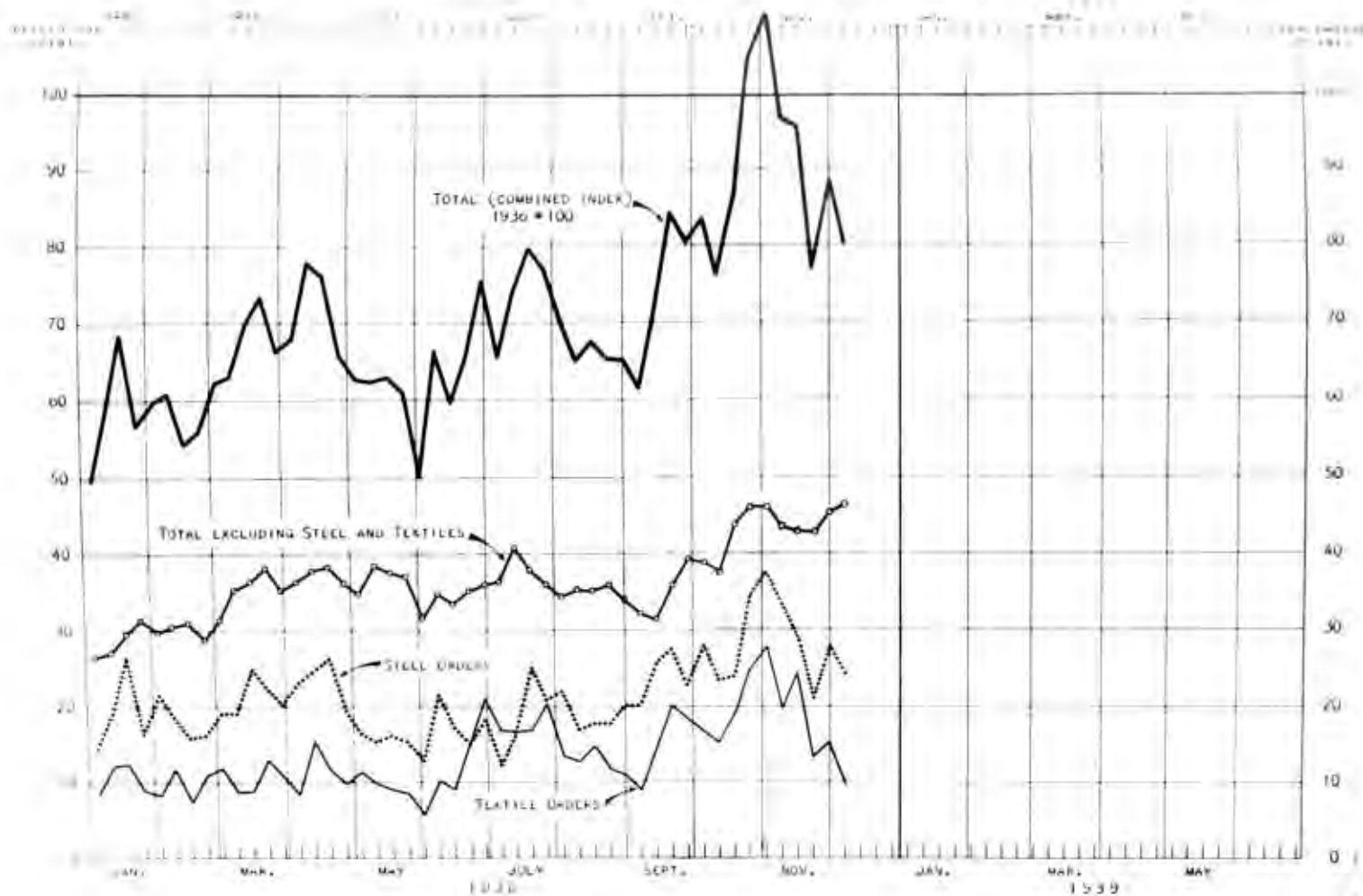
New Orders Grouped by Industries

WEIGHTED ACCORDING TO RELATIVE IMPORTANCE

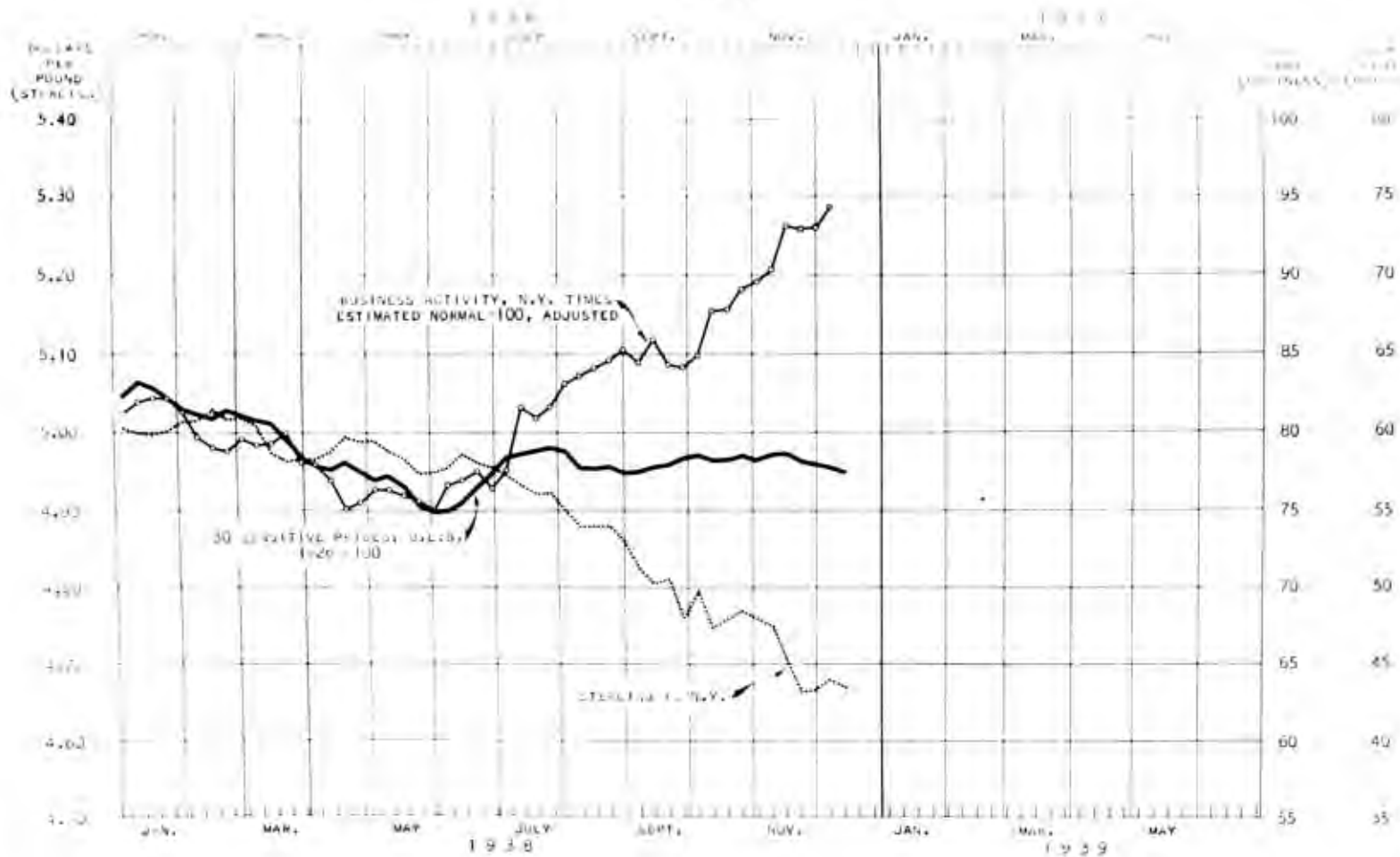


*EXCLUDES WHOLESALE TRADE, AMUSEMENT, EDUCATION, AND OTHER

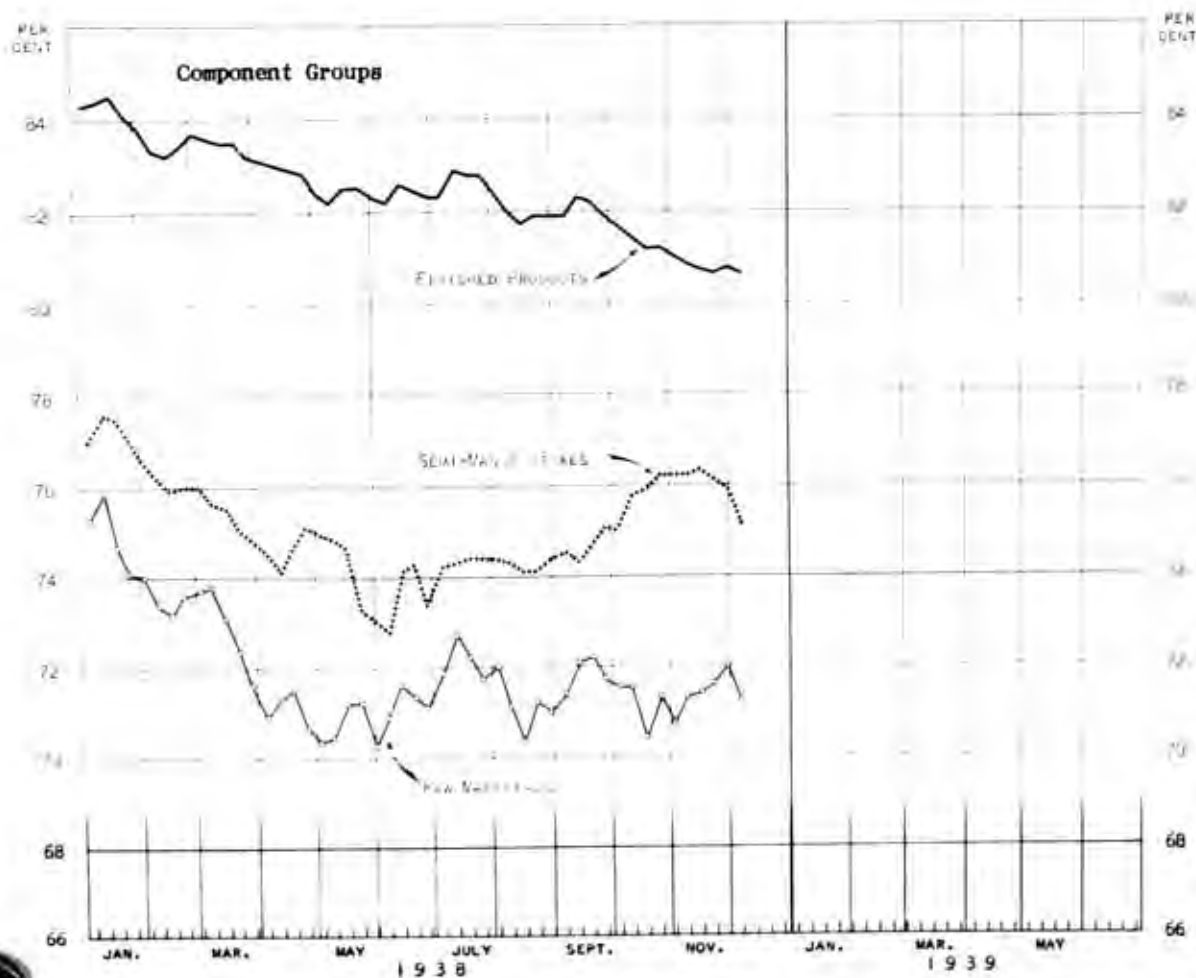
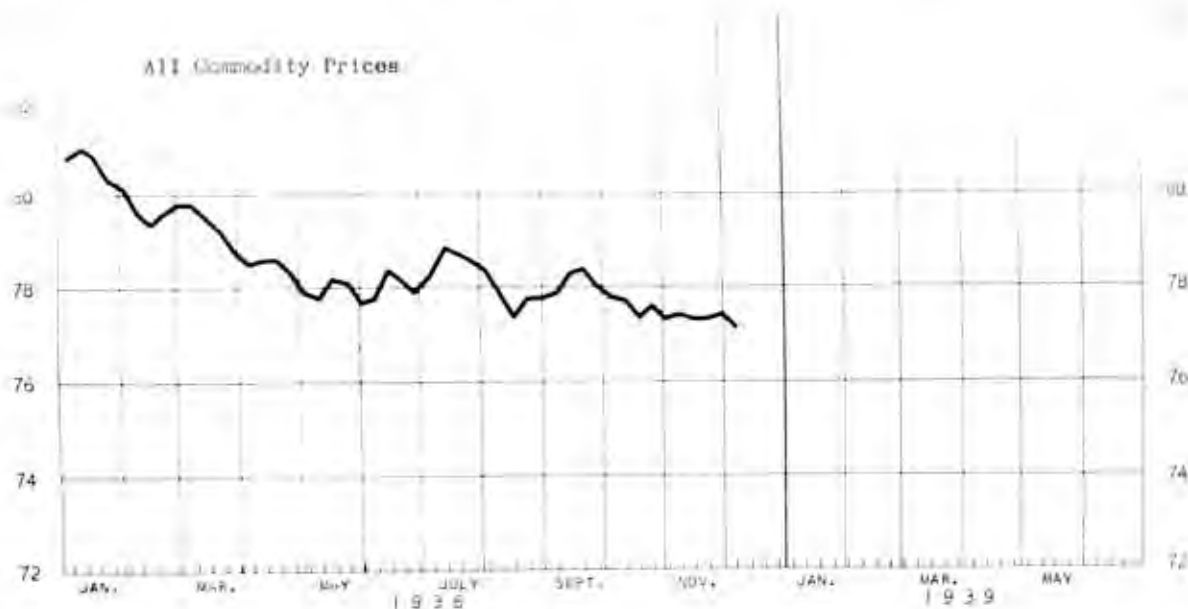
INDICES OF NEW ORDERS Combined Index of New Orders and Selected Components



COMMODITY PRICES, BUSINESS ACTIVITY AND STERLING EXCHANGE Weekly



U.S. ALL COMMODITY PRICE INDEX AND COMPONENT GROUPS
1926 = 100



December 19, 1938

I took this to the White House today for the conference with the President and the Fiscal and Monetary Advisory Board. I gave it to the President and he accepted it.

The Fiscal and Monetary Advisory Board has been advised by the experts of the Treasury, Federal Reserve Board and National Resources Committee that:

1. The 1938 national income is estimated at \$62 billion. For the calendar year 1939 it is estimated that the national income will be between \$65 and \$68 billion.
2. A national income of around \$80 billion would provide:
 - (a) substantial reduction of unemployment;
 - (b) Federal revenues sufficient to balance the current level of cash expenditures on the basis of the existing tax structure.
3. An income of \$90 billion or more is attainable through full utilization of our man power, plant and equipment, technology and natural resources, assuming the elimination of some important bottlenecks.
4. Also it is important for Federal fiscal policy to take into account:
 - (a) changes in the volume of capital expenditures being undertaken by private enterprise, and any hindrances or bottlenecks tending to restrict the expansion of private expenditures;
 - (b) the fact that available supply of credit is so great that present and prospective Federal borrowing will not create a shortage of credit available at reasonable rates for private enterprise.
 - (c) changes in the volume of the outstanding debt of State and local governments and changes in the volume and character of their expenditures and receipts.

In pursuit of the objective of attaining a higher national income we make the following recommendations with respect to fiscal policy for the next fiscal year:

1. If taxes are to be increased, those selected should be such as interfere least with additions to the aggregate income of the American people. These taxes, among others, are: estate taxes, gift taxes, lowering tax exemptions as personal income rises, higher income tax on middle brackets.

2. We advise against new taxes which operate to reduce substantially consumer purchasing power. These taxes, among others, are: processing taxes, sales taxes, taxes on payrolls, excise taxes.
3. The Board notes with approval the proposed changes in the budget presentation and recommends that the principles embodied in these changes be extended as rapidly as feasible. (See appended copy.)
4. (a) For the purpose of adding to the national income next year, and of preventing what promises to be a serious bottleneck within the next year or so, action should be taken to secure a large railroad equipment program.

(b) Recovery could be further stimulated by additional government activities financed through self-financing government corporations. These activities should be, in the main, such as will facilitate private investment and expansion of private industry. A special report on such activities will be later submitted.
5. That a comprehensive survey be started with the view of immediately setting up machinery to obtain all necessary detailed information with respect to the current receipts and expenditures of State, local and municipal administrative bodies and to changes in the volume and make-up of their outstanding debt.
6. Steps should be taken at once to provide for engineering and legal planning of various public works, such public works to be ready for immediate prosecution when required to give increased flexibility in the timing of public expenditures and increased assurance of value and utility of the expenditure itself.

This program is much needed not only because of the character of current Federal, State and local public works and relief, but even more especially because of the extensive rearmament being undertaken. To make certain that the rearmament program shall not be continued as a device to reduce unemployment or to stimulate business activity, it is essential to have such plans perfected as will permit a ready transfer of employment from armament industries into needed productive public and private works projects as soon as peak activity in rearmament is passed.

GROUP MEETING

December 20, 1938.
9:30 a.m.

Present: Mr. Hanes
Mr. Taylor
Mr. Oliphant
Mr. Bell
Mr. McKeynolds
Mr. Haas
Mr. White
Mr. Lochhead
Mr. Gaston
Mr. Duffield
Miss Chauncey

H.M.Jr: I haven't got anything for Mac these days.

McR: You wanted to know about this maid over there at the White House who wanted to go down to the Bureau.

H.M.Jr: Yes.

McR: As far as her status is concerned, she's eligible to go over there...

H.M.Jr: Yes.

McR: ... if you want her to go.

H.M.Jr: Certainly.

McR: Just be one more person to teach something over there.

H.M.Jr: That's all right. I forgot what I wanted for it, but I paid for it.

McR: Well, you got what you wanted for it.

H.M.Jr: I mean I got what I wanted from the White House; now I've got to pay for it.

McR: O.K.

H.M.Jr: O.K.?

McR: O.K. I've got a memorandum from the Bureau objecting

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to it. But then, they'll do what they're told with perfectly good grace.

H.M.Jr: This isn't for Grace, this is Marguerite.

Taylor: Whew!

H.M.Jr: Well, anyway, make it up for Marguerite, and I'll sign it. Tell her it's my Christmas present to her.
Dan?

McR: You mean - is that Miss LeHand?

H.M.Jr: Yes.

Dan?

Bell: Tennessee Valley Authority is in with a request for a million dollars for ten years. That's the one that you agreed to buy.

H.M.Jr: Oh.

Bell: The other million dollars

H.M.Jr: Pardon?

Bell: The other million dollars they'll get from Mr. Jones, as they did before.

H.M.Jr: What do you mean, a million dollars for ten years?

Bell: They want you to buy their obligations running for ten years. That's the matter I discussed with you five or ten days ago.

H.M.Jr: What do you charge?

Bell: They want two percent.

H.M.Jr: What's the last bond issue?

Bell: I told them I thought it would be two and a quarter. They want to split the difference, make it two and an eighth. The last bond issue, nine years, is selling on a 1.72 basis, and the 2½s '48 are selling on a 1.90 basis. Wayne and I felt - talked it over

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and we agreed that 2-1/8 is fair, although if you were selling it on the market it might have to go to 2 1/4.

H.M.Jr: How much you want to charge them?

Bell: 2 1/4.

H.M.Jr: Sold. What else?

Bell: The World's Fair people have been talking to us

H.M.Jr: I knew you just didn't come in to be sociable this morning.

Bell: ... have been talking about a display.

H.M.Jr: Go ahead. I knew it wasn't just a social meeting.

Bell: Should have taken this up with you yesterday. Everybody hollering for it. They've been talking about a display - it's a terrible example - that they've sent in, and you can't read it but I'd like you to go over it, maybe, after this meeting.

H.M.Jr: A display?

Bell: Yes, that is, a wall map or something with the United States Government lighted up; and then as these lights here go out each one of these blocks will light up. These will be dollar signs - I mean dollars; then, leading off from the dollars will be these little organizations - emblems of some kind - and they will light up: like Production Credit Corporation, and so forth.

H.M.Jr: Does it say anywhere: "Buy Baby Bonds"?

Bell: No, that's represented by the United States Treasury Building.

I don't know whether it's good or not, and it's so small that you can hardly tell just what it is going to look like.

H.M.Jr: Well, you and Gaston and I will take a look at it. You think you're "agin" it?

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Bell: I don't want you to go up there at the World's Fair and see this big display and say, "Who prepared that?"

H.M.Jr: What about getting that gold machine and putting that down there? You drop a quarter in one end and sterling goes up or down.

Oliphant: Have you seen that?

White: Hard to explain to anybody.

Oliphant: It's full of orangeade and pink lemonade.

Bell: All right.

H.M.Jr: Is that all?

Bell: That's all.

McA: Nothing stronger than that, Herman?

Oliphant: Nothing stronger than that.

White: One of the men in the Tariff Commission - research - called up and said they've been asked by the Tariff Commission to prepare a report on German trade; wanted to know whether we had any information we could give them with respect to the way in which it operates, and so forth. I told him we'd let them know. I had in mind that this report we're doing for you will probably be ready for you in a short time.

H.M.Jr: On what trade?

White: German trade.

Oliphant: Where did the request come from?

White: The Tariff Commission requested the research staff; the research staff called me.

H.M.Jr: Make them come through the Commission to me, the office of the Secretary, if they want it. From the Commission to the office of the Secretary.

White: All right, sir.

H.M.Jr: Will you?

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White: I'll do that.

H.M.Jr: Anything else?

White: There's a letter here received from somebody who is making an inquiry with respect to this newly named board about which there was a write-up, and asked some questions. Simple answer is required. I prepared it for your signature. I don't know whether you wanted that signed as ...

H.M.Jr: McReynolds is secretary of that board.

White: We'll turn this over to him, then.

Here's the Munitions Control Board's report.

McR: I talked to Dan about it.

H.M.Jr: What?

Bell: He walks out on every meeting.

H.M.Jr: Absolutely. That's why - it's terrible - that's why I'm going to make him secretary. That's why he'll stay. He gets bored and walks out. It's not fair.

McR: But after all, I have some things to do.

(Hearty laughter)

Haas: Where does that leave the rest of you?

H.M.Jr: God bless you. Bell must feel the same way about it.

White: One of the things you'd have to do is answer some of these letters.

H.M.Jr: What else, Harry?

White: There's the Munitions Control Board preliminary report that's come in. Went to the legal division. Anybody else besides Mr. Taylor?

H.M.Jr: Well, the legal division can report on it next year.

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Cliphant: We're asked to approve the report.

H.M.Jr: I understand.

White: That's all.

Lochhead: Sterling is holding quiet. Francs are continuing to steady up again after a pause last week. You notice yesterday on your charts there - well, you'll have these foreign charts - French rentes went up; and after the quieting down of Mussolini and the Monnet speech - seemed to have started a little enthusiasm in the bond market.

H.M.Jr: Triple confidentially, Mr. Monnet is back with an aviation commission and with the authority signed by Daladier, the Minister of Air, and some third person. They wanted to keep it secret and I said I wouldn't receive them unless Mr. Welles called me up and said it was all right.

Well, the President called up Welles Friday night and Welles called me, and they've asked me to go ahead, which we're doing. They want a thousand planes. They've got the cash. They want them before the first of July. And we'll help them all we can.

Of course, as I told them, it all gets down to a question, will the President tell them that they can really have the most recent planes. I mean if they buy something - the usual thing which is released isn't much good. So we'll see.

And what happened then - I got what I think is a nifty. Monnet, as you all know, is very much interested in China and Indo-China, and this cablegram came through showing that Hai-Phong - they got a log jam on that Chinese railroad. So when he comes in this morning to ask, "Will you please help the French?" I'm going to say, "How about helping our mutual friends the Chinese?" and remind them that the French board of directors dropped the rate on the Suez Canal twice in the same day last week just because Mussolini threatened to take Tunisia away from them. And why wait for any threats, why not do it voluntarily and help move the stuff up?

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I think it's a nifty. While they're around bothering me, taking up my time trying to find a thousand planes for them, why not get them to loosen up on that line? So I just thought I'd - I mean this is strictly unofficial, but I like it.

Leahman: Mr. Secretary, did you see the notice the other day - speaking about airplanes, they said Germany is turning them out so fast, you know, that they'll be willing to supply France and England.

H.A.Jr: Which? Germany?

Leahman: Yes - the other day. You'll probably run across that somewhere.

H.A.Jr: What Monnet told me was - it's very interesting; I guess you'll (Hanes) know - he said our people have these planes which have been turned out in competition for the Army, and that our plane factories just haven't got any orders. And they've got these model planes - they're there - one model of each, finished, completed, in competition; they have no orders. And this order comes in right now - it will be ahead of the Army appropriation, be out of the way. They said they just haven't got any business. The planes have been built, finished, already tested, and there they are. I mean one model of each.

Leahman: I know that's true about Sikorsky up there at Bridgeport. They haven't got any business.

H.A.Jr: And so maybe we can get these orders placed and get them delivered before Congress passes this bill.

Wayne, anything?

Taylor: Oh, did you get my memo about the Chinese conversation I had with Bewley?

H.A.Jr: Yes. That's all right.

Taylor: That's ...

H.A.Jr: You mean on our credit - help stabilize it.

Taylor: Yes.

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H.M.Jr: Don't you think I've done about enough for the last two days for China?

Taylor: That was my impression, and that was - I thought I - the general thing - the impression I gave him was that we were going to - we made a pretty strong gesture here, and we weren't closing the door to it, but let's just ease it along a little bit.

H.M.Jr: Well, that was all right.

Taylor: Yes.

On this Cuban banking report, I think I'd better talk to Welles about it to see where we go next on it. I think it's a - on the whole it's a pretty good job, but there are certain points in there I don't think we can handle by writing to ...

H.M.Jr: Well, will you carry the ball on it and let me know if and when you want me to get in on it?

Taylor: Yes.

H.M.Jr: Please.

Taylor: I don't think there's any occasion for your getting in on it.

H.M.Jr: I'm not up-to-date on it, as you know. But you'll carry it.

Taylor: Yes.

H.M.Jr: All right.

Taylor: Do you want to see Edwards?

H.M.Jr: About 11:45?

Taylor: All right, fine.

H.M.Jr: The power group, 11:15.

Anything else? Power - Eddie Bartelt?

Bell: (Nods affirmatively)

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H.M.Jr: I know you people would all like to know that Mrs. Klotz had a successful operation. She's up in New York. A very serious one, but it's been successful. She was operated on last Friday and she may be out at least a month. But everybody says she's getting along nicely. It may be two or three months. But it was a successful operation.

Duffield: Nothing.

H.M.Jr: Is it all right on that lawyer?

Duffield: Yes. I'm not asking him to see you.

H.M.Jr: I wanted to - I loved the way you tried to stop me yesterday. You're sure you don't - it's all right?

Duffield: It's all right.

Oliphant: Now, what's this?

H.M.Jr: I mean it's ...

Hanes: Talking about lawyers, we want to hear about it.

Duffield: It's all right.

Hanes: We want to hear about it - talking about lawyers.

H.M.Jr: He was so anxious that I didn't press the question yesterday, and I haven't seen him since then.

McR: John, Herman is the only one that's supposed to be teased by this conversation about the lawyers.

Duffield: Incidentally, he's gone about as far as he can.

Oliphant: What?

H.M.Jr: Has he been satisfactory?

Duffield: Well, just partially.

H.M.Jr: But you don't want to - you want to sort of let it rest.

Duffield: I'll let that depend on Mr. Oliphant, I think.

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Oliphant: Well, I'm enjoying all the bliss of complete ignorance.

H.M.Jr: George?

Haas: I haven't got anything.

H.M.Jr: Got it on the inside pocket.

Haas: Did you notice that?

H.M.Jr: Tax letter.

"Here are some of the significant speculative comments about them:

"1. Perhaps the Treasury is being conservative, playing safe once again, and showing minimum amount of revenue expected during next fiscal year. 'It is better to have to adjust revenue yield upward than downward.'

"2. Perhaps Treasury is placing its worst income picture before Congress, to discourage, if possible, the voting of numerous items of expenditures.

"3. Perhaps the Treasury is laying the groundwork for being in good position to ask Congress for additional taxes to support any added spending.

"Speculative view number three is getting most attention in tax circles. It is the one which has the greatest current significance for business. We shall report any new angles which develop, especially after the budget is released early in January."

Haas: The point I was making is, he's got a good imagination or he's got some information, but in any case he's not up-to-date.

Hanes: Partially good.

H.M.Jr: Well, that's - put it back in your pocket.

Haas: One of the boys brought it in to me.

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- H.S.Jr: (To Chauncey) He (white) gave me a special memorandum on the unemployment. It isn't there. I want to lay my hands on it.
- Herbert?
- Chauncey: Since Dan raised this request of the World's Fair, we have a request for one piece of literature about the Treasury Department to be distributed in large quantities free at the Fair. And we've - I've asked Birgfeld to find out whether they're going to - his letter doesn't state whether the World's Fair Commission is going to pay for it. We can give them the copy.
- H.S.Jr: Well, you fix it up with Dan. Dan's very liberal these days.
- Herbert: Give them a Baby Bond booklet.
- Lockwood: The only trouble, Mr. Taylor - I think they'll have to have a redemption bureau at the World's Fair; people will bring their bonds up to cash in.
- H.S.Jr: Herman?
- Oliphant: In anticipation of that annual report of the Munitions Committee, we have already done a great deal of work, and have the draft of a letter. We'll be glad to discuss it with you whenever you're ready, whenever you want to discuss it.
- H.S.Jr: Now, when are you and Hanes going to be ready - I want to fix my time-table - when are you two gentlemen going to be ready to talk about the codification of the tax laws?
- Oliphant: Guess some time today.
- H.S.Jr: Here's the thing. The President's having Cabinet tomorrow afternoon, so that's out. And I - I'm free; I have no appointments for tomorrow morning. But I want to know, when would you gentlemen like to see me?
- Oliphant: Any time tomorrow morning.

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H.A.Jr: 10:30.

Hanes: I haven't anything tomorrow at 10:30.

Oliphant: 10:30.

H.A.Jr: All right.

White: Herman, that formal meeting is the first week in January. Secretary ought to handle it before he goes away.

H.A.Jr: Now, the other thing - would you (Hanes) find out whether Preston Delano will be here Wednesday and Thursday, so that if - I mean if we get together and get this thing straightened out Wednesday - well, the latest we want to see him would be Thursday morning maybe, see? But I mean I've got Cabinet Wednesday afternoon. So if he did this thing, then allowing time to readjust our own position, we'd get to him, say, Thursday morning. But I'd rather have him go to bed Wednesday, if necessary, and be ready for us Thursday morning. I mean I'm being serious, not being funny. I'd rather have him go to bed Wednesday, be here Thursday and clean this thing up before both of us leave.

Hanes: Right. 10:30 in the morning.

H.A.Jr: For you and

Hanes: 10:30 tomorrow morning.

H.A.Jr: Tomorrow morning.

I'm figuring that, allowing time that he might want to do some more work - but we'd be definitely ready for him Thursday morning; and if he's not well and - or feeling well, let him go to bed tomorrow, so he would be there.

What else, Herman? How did your speech go last night?

Oliphant: Terrible.

H.A.Jr: What?

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Oliphant: Terrible.

H.M.Jr: Why?

Oliphant: Well, the thing I mentioned to you (Hanes).

H.M.Jr: What?

Oliphant: Do you want to take the time now to discuss that Munitions report?

White: You weren't changing the subject by any chance?

McR: He wasn't changing the subject.

H.M.Jr: Keep after Miss Chauncey. No, I'm not going to - I'm all booked today, will be with you two gentlemen tomorrow morning.

Oliphant: Well, I'll bring it up some time after that.

H.M.Jr: What was the matter with the speech?

Oliphant: I found it a little difficult because

Hanes: He's not telling the truth. I interrupted him, stopped him from preparing his speech. The last thing he said was, "Well, maybe I'll make a better speech if I don't know what I'm going to say."

H.M.Jr: Are you feeling well? Are you all right?

Oliphant: It would have gone all right.... Fine bunch of boys, just like an old law school class. Had a lot of fun. Room full of young fellows.

H.M.Jr: Fine. Hanes?

Hanes: I haven't got anything.

H.M.Jr: Swell. Now we'll do Danny Bell's electric sign.

RE GOVERNMENT POWER CORPORATION

December 20, 1938.
11:30 a.m.

Present: Mr. Taylor
Mr. Bell
Mr. Foley
Mr. Duffield
Mr. Bartelt

H.A.Jr: Now look, it says one billion 850. Is that net after fertilizer's out?

Duffield: No, fertilizer's in.

Foley: Operations.

Bell: You mean it's after taking care of the loss?

Duffield: No, it's not after taking care of the loss, because they have segregated those two operations in their report to you - fertilizer one category, power in another. There would be no net income there if fertilizer were included.

H.A.Jr: Can't fertilizer stand on its own feet?

Duffield: It's now bearing the cost of a lot of experimental work, and that was ... It should stand on its own feet.

H.A.Jr: But you don't set it up that way.

Duffield: I didn't set it up that way.

H.A.Jr: On.

Duffield: They didn't set it up that way in their report for the budget.

Taylor: This (newspaper article attached) completely disagrees with any of the figures that are here.

Duffield: We've just taken their figures, that's all. We haven't attempted to say whether their figures are phony or not.

H.A.Jr: On, I see. You mean you're taking T.V.A. figures.

Duffield: T.V.A. figures from the Budget Bureau.

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Foley: That's all we can do, is take it from these different agencies.

H.A.Jr: You take it from the Budget Bureau.

Duffield: That's right.

H.A.Jr: You think the Budget Bureau is accurate?

Duffield: That's right.

Taylor: Ought to read that (newspaper article); that's their own testimony.

Self: I think this man is talking about the project as a whole; you've got several millions of dollars down there - be run up to one, one fifty, two hundred million - probably be charged up to flood control and navigation.

Taylor: He isn't talking about that.

H.A.Jr: I think that's very mean, to bring up anything like that at this time. You don't expect Duffield to read the New York Times.

Foley: Too early in the morning.

Duffield: I don't read this until late at night.

H.A.Jr: Well, anyway, going on the figures of the Bureau of the Budget ...

Duffield: That's right.

H.A.Jr: ... that means that 235 million dollars could be bondable?

Duffield: That's right.

H.A.Jr: I see.

Duffield: That isn't - I didn't total the power cost column, because that last item isn't segregated; but I added it up if you want to know outside of that ...

H.A.Jr: This is the whole story?

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Duffield: That's the whole story, as far as we know. Now, the second table, at completion, is compiled at the year of maximum yield.

Now, Mr. Bartelt is planning to do it in another and probably more realistic way.

H.M.Jr: Well, have you gentlemen thought what kind of a bill would be necessary to form a power corporation, in order to get this thing started? Have you thought that far, Ed?

Foley: Only generally. We haven't put any ideas on paper.

H.M.Jr: Supposing you think about it.

Foley: Want a draft?

H.M.Jr: Yes.

Bell: But don't you want to make it broader than just power?

Duffield: Power and water and these things - power and irrigation.

Bell: You've got irrigation, fertilizer, power.

H.M.Jr: Well, don't sink it, don't make it too broad.

Bell: Some cases, it's very difficult to separate it.

H.M.Jr: Make it broad, you could take in anything; that doesn't mean we have to

Foley: No, just comprehensive, so that

H.M.Jr: Well, what I'd like to do is - I mean if you've got this thing through, which would be the one which could stand up in public the best?

Duffield: The one

H.M.Jr: Which one?

Duffield: You mean that ...

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H.M.Jr: But which one of these organizations?

Bell: Boulder Canyon.

H.M.Jr: Boulder?

Foley: Boulder first, yes.

Bell: Got contracts signed on the dotted line.

H.M.Jr: You mean you could go out - now take - for instance, Boulder includes amortization of payment. Would you include the irrigation project?

Bell: It isn't included here - the All-American Canal - but the All-American Canal will be repaid ...

Duffield: It's included on the second page. But, as Mr. Bell suggested last week, the way you might do that is include the amortization on the irrigation project, but just capitalize it part amortization, part interest.

Bell: This isn't the total cost of Boulder - 165, isn't it, Eddie?

Bartelt: Yes.

Bell: And it's all repayable.

Bartelt: I don't know whether the Secretary's attention has yet been called to the fact that the Treasury has made advances under the Boulder Canyon Act which carry four percent interest, and those advances now amount to 113 million dollars, on which there is 17 million dollars unpaid interest. In other words, you have an investment now of 130 million in the Boulder Canyon project. It's an interest-bearing account. It's true that bonds weren't issued, but it's equivalent to that.

Bell: The basic law provided for a capitalization of the interest on Boulder Canyon Dam during the construction period, so there's 17 million dollars of interest that's been capitalized on Boulder Canyon Dam.

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H.M.Jr: Which is

Bell: Which is part of the cost.

H.M.Jr: I see.

Bartelt: You have the authority to defer that interest, and that has been deferred over a period of years, and the entire investment now amounts to 130 million dollars, including the interest; it's drawing four percent interest.

H.M.Jr: Well, but can it pay four percent on 130?

Bartelt: Yes, the Boulder Canyon project is one of the projects which will actually pay out.

H.M.Jr: Well, that will be the first one. I want to take the easiest one.

Bartelt: It's the best one.

Duffield: Would you plan to segregate these bonds and say, "These are Boulder Canyon bonds," or would you say, "These are Power Authority bonds"?

H.M.Jr: They'd be Power Authority Bonds. But if I offer, say, a hundred million as the first, say, series, and they say, "What are these?" I say, "We've stuck Boulder Dam in this." In other words, as I see this thing - I'm thinking out loud - that when this corporation was formed, I'd take it that we would take over Boulder Dam, that is, the liabilities of Boulder Dam, and then we'd go ahead and explain to the public, "Now we've taken over Boulder Dam and this is what we've taken." And then this corporation would offer, say, a hundred million dollars worth of Power Authority bonds and explain to the public what it is, and - I mean because this would be the easiest one to explain. And then back of this is all of Boulder Dam, and then as time goes on we're going to take it over. But the first series we'd offer would be a hundred million dollars worth of bonds. I mean that's - I mean the way of - I think of it as of today.

And then after we have digested Boulder Dam and if the public received the thing well, then we could

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look into the next easiest. I know I'd take T.V.A. last, certainly, until Mr. Taylor got through reading the newspapers and bringing you fellows up to date.

But I mean that's - I mean I keep throwing out stuff as you bring me more information - that's the way I look at the thing. We won't sell, say, 500 million all at once.

But - and I - again I don't know whether I agree with Mr. Bell, but I just wonder if we'd have to take over the fertilizer works, inasmuch as that's experimental; whether we wouldn't just consider that experimental and leave it there and let Congress pay for that cost of experimenting with fertilizer. That's my hunch.

Bell: That might be one of the things you'd want to write off.

H.W.Jr: But isn't that a continuing cost every year?

Bell: No, I'm not so sure. This early experimentation may develop into a real revenue-producing thing. That's Muscle Shoals.

H.W.Jr: I understand. I didn't - I took it for granted it was.

Bell: Well, when this Muscle Shoals project was operated by the Army, as I recall, they turned in receipts of about a million or million and a half a year, didn't they - fertilizer sale. Since T.V.A. has taken it over, there's been a lot of experimentation going on, and that's costing a great deal of money.

H.W.Jr: Well, I think what we want to do is - we step into the thing - the President keeps mentioning Boulder Dam; we'll take that on, take on another one. If we get T.V.A., it's up to him to say how much of T.V.A. we want to take on and how much experimentation we want to write off publicly.

Bell: Well, Boulder should be first and probably Bonneville should be second.

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Curfield: Going to be slow to develop any net revenue.

Bell: Have it coming in in 1941, 1942.

Foley: How much of the transmission lines do you pile on? If you pile on the cost of tying in Grand Coulee and then cabling, etc., it's going to run it around '45 or '46 before she begins to get out from under that transmission load.

Bell: I'd capitalize that.

Foley: Capitalized item.

H. J. Jr: Do you want to use this in his message - the possibility we'd take over this ...

Bell: No.

H. J. Jr: I don't think we're ready.

Bell: I think our statement in the budget message has got to be rather general. The possibilities are there.

H. J. Jr: Do you want to raise anything at this point other than that the boys should continue and get it far enough - let's see what a bill looks like and then actually try to work out the machinery of how we would take over one. I mean what are the motions that we have to go through? See? To take over Boulder. See? I mean how would it be on the books, and everything else? Let's just go through the motions on a trial basis of taking over Boulder Dam through this new Authority.

Curfield: I'm wondering if any refinement of these figures will come out of the work of Mr. Bartelt.

H. J. Jr: Then also, on this Authority, somebody will have to run it - I mean we've got to have somebody.

Foley: You want it in the Treasury or independent of the Treasury?

H. J. Jr: In the Treasury, I think - definitely.

Foley: A corporation in the Department of the Treasury.

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- W.H.Jr: That's what I think.
- Ball: I should think, as long as it's going to be practically all financing, that you'd want it here. And you could use the Crop Control Corporation as a sort of a model.
- Taylor: Commodity Credit, you mean.
- Ball: No, I mean crop insurance; that's set up within the Agriculture Department, using Agriculture officials as directors, so forth. It's a pretty good set-up. And you use all of the other service machinery just as if it were a bureau.
- W.H.Jr: On crop control, do they have administrative officers?
- Ball: Yes, but they're usually administrative officers of the Department of Agriculture, use all the Department of Agriculture machinery.
- W.H.Jr: That's all right, don't you think so? I mean all this is subject to - I mean experimentation; but the thought that I have is that this ought to carry one good salary.
- Ball: Probably right. Half a dozen people, something like that, to take care of it.
- Wiley: Create the office in the Treasury, all the powers to be exercised by an administrator to be appointed by the Secretary.
- Taylor: Seems to me you have to lay down in your legislation and so on what the accounting principles are going to be; if you don't do that, why, you'll run up against this stuff (in newspaper article).
- Ball: I think you've got to give the Secretary the power to determine what value to carry them at on the books for the purposes of valuation, but not write in the legislation accounting principles.
- W.H.Jr: I've got a hunch - can you hold your thought a minute - I have this very unusual authority as

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Secretary of the Treasury, that the Farm Credit comes over when they want to write off a loss in the Cooperative Bank, ten, twelve million dollars, they come to me, state the fact, and I write off ten, twelve million dollars loss in the Cooperative Bank. Don't I? Well, I did it. You know what I'm talking about. They had a loan for the Farmers National. When they want to write off a loss over at Farm Credit, under the law they come to me, state the facts, say, "We want to write off a ten million dollar loss." They state the facts, and I sign it - no recourse to anybody. I just write it right off. Now, study how the hell did that happen.

Bell: I don't know how that happened. I never was in on it.

H.A.Jr: I mean if you sit around

Bell: Just happened, probably.

H.A.Jr: Governor Myers comes in and says, "Mr. Morgenthau, here's the facts. I recommend that we write off the books of Farm Credit a ten million dollar loss."

Bartelt: They didn't get any money, though, did they?

H.A.Jr: Pardon?

Bartelt: They didn't get any money, though.

H.A.Jr: No, but they write it off.

Taylor: The Commodity Credit principle is better, where you have an appraisal, which is exactly the same thing that you're talking about, which gives you the power to write it off; but it's an appraisal and then you

H.A.Jr: ... go to Congress to make up the difference. But on this thing - where this is different: we don't expect Congress to make this up; I don't want to go to Congress.

Bartelt: Well, the General Counsel's office is working on a bill in alternate forms to take care of those alternatives: one where Congress would reimburse and the other

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one to take care of it simply from an accounting standpoint.

H.S.Jr: Wayne, keep thinking about this. I'm just hitting it on high. But I do think in this particular case ...

I've got another one to bring up here, Dan?

Bell: Oh, have you?

H.S.Jr: My foot bothered me.

I do think in this case I want this in the Treasury, I don't want it set up - but I mean I'll argue or listen - as Commodity Credit, because that's an operating thing. Once, after all, we get this thing in here we're not going to operate these things.

Foley: Oh no. Just to finance them once and collect the interest, that's all; that's finished.

Taylor: Well, if you've got an obligation out which is based on certain, let's say, presumptions, or whatever it may be, you've got to keep those good with the public.

H.S.Jr: True.

Duffield: That's right.

Taylor: And the only way you can keep them good is to require a certain type of report, a certain principle back of the thing, and so on, so that if they come back the next year and say, "Boys, we've got to change that..."

Foley: Well, you give the Secretary the power to prescribe those rules and regulations, accounting procedures, and so forth.

H.S.Jr: Well, gentlemen, would you go in and see Mr. Taylor the next day or two and give yourselves a chance to talk this thing over with you (Taylor), because I'm kind of pushed. I want you to talk it.

Now one other thing which Bartelt gave me, which I asked

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That agreeable to you, Wayne?

Taylor: Right. No, I'm - this thing (newspaper article), why, is - which I was pretty sure was going to appear some time or another, is the damndest statement you ever saw, and it absolutely discredits every figure they've given you in the Budget. This is in public sworn testimony; I don't know whether that means anything or not, but I would think that it would.

H.L.Jr: By a T.V.A. representative?

Taylor: Yes.

Barfield: You've got to have some protection against that sort of thing in this law.

H.L.Jr: Every protection.

Taylor: That's just the kind of thing I'm worrying about.

H.L.Jr: In other words, I don't want a (words not understood)...

Taylor: I think I'd take that in preference to what this boy's been doing.

H.L.Jr: Did you see the one that the Post ran - copy from the cartoonist of the St. Louis Post-Dispatch - with a fellow walking off with the whole building.

"At the present time..." - this I think we may want to use in the budget message, because this.... - "At the present time the Government has a net proprietary interest in various governmental corporations and lending agencies of about \$4,100,000,000.

"Capital stock of one billion 988; surplus, 624; net assets in non-stock agencies, 758; special obligations held, 738. Total, four billion one. The details..." - and so forth and so on.

Now, of that - this is just on the so-called Commodity Credit type?

Barfield: The lending agencies, yes, sir.

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H.M.Jr: How much of that could we go to the public with - could we sell - is salable?

Bartelt: Well, you could take that 738 down here and begin with it.

H.M.Jr: Yes.

Bartelt: And create a corporation which would take over all these assets. It seems to me you could get practically all of it.

H.M.Jr: The whole four billion?

Bartelt: Yes. For instance, if the R.F.C. should be given authority to buy all of these assets and issue obligations

Bell: Well, wait a minute, you've got a lot of capital stock in there which isn't earning anything.

Taylor: Yes.

Bell: What's it worth from the capitalization standpoint?

Bartelt: Well, these are - most of these corporations are earning ...

Taylor: Yes, but they're not paying anything on the capital stock. That's another thing that we ought to be thinking about.

H.M.Jr: Well, there's two billion dollars worth of capital stock here.

Bell: We're not - getting nothing on it.

Taylor: Which we get nothing on. We're entitled to a dividend return on that stuff.

H.M.Jr: What interest, Wayne?

Taylor: Well, if it's capital stock there should be a dividend return, see?

Bell: You give Jesse Jones 500 million dollars in capital stock. We in effect have written it off. It's ...

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A. J. Jr: Are you going to use this?

Bell: Not in that form. I'm trying to get up a table in another form.

A. J. Jr: Bartelt, could you furnish Mr. Bell, Mr. Taylor, these two gentlemen (Duffield and Foley), each copies - so you see, you want one, two, three, four more copies.

But this is a good job, this is a swell job, because here it shows roughly two billion dollars worth of capital stock on which the Treasury gets nothing, and it gives the whole picture. And this comes under the head of what I call the Commodity Credit plan.

Bell: Those are the credit agencies.

A. J. Jr: There they all are. And this is my power corporation. We're making progress. I think we're making progress here. So if you will meet again and work with Mr. Taylor and get his ideas, anybody else's ideas, and - that's all.

Foley: But the first draft of the legislation you want limited to your so-called power program.

A. J. Jr: Well, I'd make it broad enough that you can take in power...

Bell: ... and the related ...

A. J. Jr: Yes.

Foley: Income from so-called power projects; but you don't want the legislation to cover the so-called Commodity Credit stuff.

A. J. Jr: That Mr. Bell is putting into his message. The Commodity Credit plan - you're taking care of that, aren't you? That goes into the President's message.

Bell: Oh yes.

Bartelt: Well, the General Counsel's office is also working on a proposed bill. They're putting it up in alternate

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forms, one to take care of it as an accounting proposition, the other on a Commodity Credit basis.

H.M.Jr: Ought to get together on both. That's good work.
We'll get together on both of them.

the company.

DEC 20 1938 CONTROLLER TAXED ON TVA ACCOUNTING

Two Congressmen Try to Have Him Say \$310,171 Was Year's 'Operating Loss' on Power

WASHINGTON, Dec. 19 (AP).—Congressional investigators heard a lively debate today on whether the Tennessee Valley Authority showed an "operating loss" or a "net expense" of \$310,171 on its power operations for the fiscal year 1938.

Representative Wolverton, Republican of New Jersey, contended that it was a loss, which would have been even greater had interest on government contributions been taken into account. E. L. Kohler, controller of the TVA, insisted that he had deliberately chosen the term "net expense" to distinguish TVA operations from those of private business. Both agreed, however, that the Authority's power expenses, exclusive of interest, exceeded income by \$310,171.

Representative Wolverton brought up the matter while examining Mr. Kohler, a witness before the TVA Investigating Committee, on the agency's financial statement for the year ended June 30, 1938.

"On a profit-and-loss statement," Mr. Wolverton asked, "would this item represent profit or loss?"

"No Computation" to Profit
"It is not a profit or loss statement," Mr. Kohler replied. "There is no computation for TVA ever to show a profit."

"There is a computation to show Congress a profit or loss," the Representative snapped.

"This confusion of terms exists because you are attempting to link TVA with a private enterprise," the witness responded.

"We would not be able to give a profit-and-loss to Congress because it is not a commercial venture," Mr. Kohler explained.

He added that in Government accounting any vacancy that showed an excess of income over outgo paid it into the Treasury. Conversely, he said, operating deficits were made up by Congressional appropriations.

"Am I justified in telling Congress that the Controller of TVA doesn't know whether TVA is making a profit?" Mr. Wolverton asked.

"I think you are," Mr. Kohler replied calmly, "since the act does not require it to make a profit and net expense must be provided by Congressional appropriation."

Mr. Kohler concurred under repeated questioning that if the TVA could be compared with private business the 1938 operations would show a loss of \$310,171 for 1938. Similarly, he said, the loss would be \$745,664 for the five years of TVA operation. This figure also was stated on his statement as a "net expense."

Congress's Aim Discussed

There followed a discussion of whether Congress intended that the TVA should be a profitable operation. Representative Jenkins, Republican of Ohio, contended that if it did not so intend, the TVA board could reduce its rates at will until ultimately it would be giving power away under a system of "complete socialism."

"You have distorted what I have said," Mr. Kohler shot back. "The law does require that so far as practicable TVA rates shall put power operations on a self-supporting basis that will liquidate part of the costs."

"Surely Congress didn't mean that you could run your accounts so we couldn't tell whether TVA was running at a profit or loss," Mr. Jenkins asserted.

"To end the argument," Mr. Wolverton said, "I'm willing to concede, if you want to use the term profit and loss."

Mr. Wolverton then brought up the subject of interest. Mr. Kohler said that the operations for the year would have shown an additional deficit of \$1,000,000, or a total of \$1,310,171, if interest had been computed at 3 per cent. He based this on an allocated cost of about \$23,000,000 to power.

"This would create a false picture of what I suppose you would call 'operating loss,'" Mr. Kohler asserted.

"Somebody is out the interest charge," Representative Wolverton replied. "I assume it is Uncle Sam."

Taxes the Source, Kohler Says

Mr. Kohler said he preferred to believe that Federal borrowing had been confined to relief and other emergency expenditures and that its long-range operations were financed through taxation.

"I consider that I have contributed as an income tax payer a small part of the cost of the dam, for which I get no return," he said.

Asked by Francis Biddle, counsel for the committee, if he felt that the committee should not take interest into account in determining a fair rate yardstick, Mr. Kohler replied that the yardstick "had nothing to do with accounting."

Previously, Chairman Donahoe, Democrat of Ohio, announced that the committee would ask Congress to give it more time in which to complete its investigation. He explained that it would be impossible to finish by Jan. 3, the specified date. The committee has voted to recess on Wednesday subject to call of the chairman.

REDACTED
The Hundred Needles

AT COMPLETION

	<u>Net Revenue</u>	<u>Bondable at 4%</u>	<u>Power Cost</u>	<u>Total Cost</u>
TVA (1946-50).....	\$ 9,400,000	\$ 235,000,000	\$ 279,141,200	\$ 494,092,864
Boulder (1945).....	7,563,000 ^{1/}	189,000,000	130,000,000 ^{2/}	130,000,000
Bonneville (1954)....	4,000,000	100,000,000	77,200,000	115,700,000
Irrigation projects (1966).....	28,773,000 ^{1/}	719,400,000	933,500,000 ^{2/}	933,500,000
River, harbor, flood control projects ^{3/}	400,000	10,000,000	(Not segregated)	
	<hr/> \$50,136,000	<hr/> \$1,253,400,000	<hr/>	<hr/>

- ^{1/} Includes amortization payments on irrigation costs; the estimate on irrigation project includes a conservative estimate of the Grand Coulee power sales.
- ^{2/} Includes irrigation costs which were to be amortized, but which are not required by law to pay interest.
- ^{3/} Power developments on pending and future projects of this character are indeterminate and, therefore, the estimate has been left about at its current size.

G
D
F
I

December 19, 1938

TO THE SECRETARY:

At the present time the Government has a net proprietary interest in various governmental corporations and lending agencies of about \$4,108,000,000, as follows:

1. Capital stock	\$ 1,988M
2. Surplus	<u>624M</u>
Sub-total	2,612M
3. Net assets in non-stock agencies	758M
4. Special obligations held by the Secretary of the Treasury	<u>738M</u>
Total	\$ 4,108M

The details of the foregoing are set forth in the attached statement.

In connection with our conference on Sunday, December 11, I have been in touch with the General Counsel's Office in the preparation of a draft of legislation for all corporations in accordance with general principles embodied in the Commodity Credit Corporation Act.



175

INTEREST OF THE UNITED STATES IN GOVERNMENTAL
CORPORATIONS AND LENDING AGENCIES

(In millions of dollars)

	Capital stock	Surplus	Total
<u>I. Stocks:</u>			
Reconstruction Finance Corporation	300	205	705
Commodity Credit Corporation	100	-	100
Export-Import Bank	21	1	22
Federal Crop Insurance Corporation	5	-	5
Federal Deposit Insurance Corporation	150	-	150
Farm Owners' Loan Corporation	200	46	246
Federal Savings and Loan Insurance Corporation	100	14	114
Federal Savings and Loan Insurance Associations	47	-	47
Federal Home Loan Banks	124	-	124
U. S. Housing Authority	1	144	145
Federal Farm Mortgage Corporation	200	-	200
Federal Land Banks	124	152	276
Federal Intermediate Credit Banks	70	46	116
Banks for Cooperatives	169	11	180
Production Credit Corporations	120	1	121
Regional Agricultural Credit Corporations	5	13	18
U. S. Housing Corporation	2	-	2
Disaster Loan Corporation	12	1	13
Federal National Mortgage Association	10	1	11
Federal Prison Industries Inc.	4	2	6
Island Interways Corporation	12	15	27
Panama Railroad Company	7	38	45
FPC Mortgage Company	25	-	25
	1,985	624	2,612
<u>II. Non-Stocks:</u>			
Tennessee Valley Authority			217
Public Works Administration			37
U. S. Maritime Commission			24
Rural Electrification Administration			35
Federal Housing Administration			113
Farm Credit Administration			4
Navy Department (Sale of surplus property)			177
War Security Administration			1
Interior Department (Indian loans)			2
Puerto Rican Reconstruction Administration			30
Railroad Loans (Transportation Act)			2
Securities received from FPC (Act Feb. 24, 1933) ..			
			798
<u>III. Special Obligations Held by Treasury:</u>			
Reconstruction Finance Corporation			712
Farm Owners' Loan Corporation			5
U. S. Housing Authority			14
			731
Total	2,985	624	3,612

* Deficit

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

DATE December 20, 1938.

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH
BANK OF FRANCE.

L. W. Knoke

I called Mr. Cariguel at 11:45 this morning. Things were still going "beautifully" he said, and he was gaining at the rate of over \$1,000,000 a day in gold or foreign exchanges. They now had the public in the market but even so he wouldn't venture an opinion for any length of time ahead. As regards Mussolini, nobody in France was paying any attention to him - he was a joke. Sterling had been weak this afternoon and this weakness was due, he thought, to the debate in the House of Commons yesterday. However, Cariguel agreed with me that if this explanation didn't seem plausible most any other might be just as good. Generally speaking there was practically nothing doing; everybody was getting ready for Christmas.

LWK:KW

December 20, 1938.
12:08 p.m.

WJr: Dr. Gruening, Morgenthau speaking.

Ernest
Gruening: How are you, sir?

WJr: Fine. We are thinking of taking on in the Treasury a man by the name of James H. Edwards.

G: Yes?

WJr: The President -- sort of a financial advisor to Nicaragua.

G: Yes.

WJr: And I wondered if you knew anything about him, or whether you could find out.

G: James H. Edwards?

WJr: Edwards.

G: No, I don't. I never heard of him. When was he down there?

WJr: He's down there now. I mean, he's -- he's here in Washington, but he's worked there -- he's worked with Sumner Welles in Cuba and -- and Ecuador, and different places like that.

G: What does Sumner Welles think about him?

WJr: He recommends him.

G: Well, I'll see if I can check on him. Do you know Long who was Minister down there until a few months ago? He's been here in Washington. I'll try to get ahold of him and through other sources.

WJr: Well, would you, because we are going to bring him in to help us in Central and South America with trade.

G: Oh, I see.

WJr: You see?

G: Yeah.

WJr: In Import-Export Bank and that sort of thing.

G: I will be delighted to find out what I can about him and let you know.

- 2 -

HMJr: Yes, because -- I want -- if there is any sour note anywhere I'd like to know about it.

G: Incidentally, do you remember a conversation we had one time, oh, over a year ago on Mexico?

HMJr: Yes, you were right.

G: Well, I -- I think we ought to cut it out.

HMJr: Cut what out?

G: What we are doing to help them.

HMJr: Well, we're not helping them.

G: Well, I mean I think we -- I think we've gotten the dirtiest, shabbiest deal from those people down there that any friendly people ever got.

HMJr: I agree with you.

G: I mean they just deliberately take advantage of our good nature and our generosity --

HMJr: I agree with you.

G: And they are going to blow the good name of policy sky-high unless we can somehow stop it.

HMJr: We are in complete accord.

G: Good.

HMJr: O. K.

G: O. K. I'll find out what I can about this other man.

HMJr: Thank you.

G: Thank you.

December 20, 1938.
12:11 p.m.

Operator: General Craig.

HMJr: Hello.

C: General Craig.

HMJr: Hello.

C: Go ahead.

HMJr: Hello.

Craig: Good morning, Mr. Secretary.

HMJr: How are you?

C: Pretty well, sir.

HMJr: General, we are thinking of taking on in the Treasury a man by the name of James H. Edwards to help us in Central and South America.

C: James H. --

HMJr: Edwards.

C: Yes?

HMJr: He's been in the Philippines. He's now financial advisor in Nicaragua.

C: Financial advisor for this Government?

HMJr: No, employed by Nicaragua.

C: Yes, sir.

HMJr: Ah -- and he's done work in Santo Domingo, and they tell me that your bureau of insular affairs knows all about him.

C: I'll find out for you, sir.

HMJr: Could you -- I mean whether there is anything back in his history which isn't all right.

C: I'll find that out, and may I telephone over a little later?

HMJr: If you would, please.

C: I would be very glad to, sir.

- 2 -

HMJr: Thank you very much.

C: And, Mr. Secretary --

HMJr: Right?

C: In case you need me within the next week or so, tell Marshall

HMJr: Right -- O.K.

C: You can count on him more than you can on me.

HMJr: I don't believe that.

C: Yes you can. He is a dandy.

HMJr: Well, I still don't believe it, but -- I -- I'm not ready to talk on the French because they are not ready.

C: All right, sir.

HMJr: We haven't had time.

C: All right.

HMJr: But when they know what planes they want, then I've got to go to the President and try to get a clearance.

C: All right, sir. You know what my ideas are on that. They haven't changed since I gave you that original memorandum.

HMJr: I know.

C: Personal one.

HMJr: I understand.

C: All right, I'll let you know reasonably soon, sir.

HMJr: Thank you.

December 20, 1938.
12:26 p.m.

HMJr: Hello.
General Craig: Mr. Secretary?
HMJr: Talking.
C: General Craig.
HMJr: Yes, General.
C: The case of James H. Edwards has been looked on. We have his full record in the insular bureau, and he started with General McIntyre.
HMJr: Yes.
C: They stated in recommending that he had had twenty years service and he had steadily gone from bottom to top and was a thoroughly qualified and increasing his qualification value right along. That's been repeated by the two succeeding bureau chiefs. There is nothing that is not good in his record as a reliable, ordinary well-informed man in the Philippines, Santo Domingo and Nicaragua.
HMJr: Fine. Thank you very much.
C: Does that cover it?
HMJr: Entirely.
C: All right, sir.
HMJr: Thank you.
C: Good bye.
HMJr: Good bye.

December 20, 1938.
3:50 p.m.

W: Hello.

Operator: Secretary Wallace. Go ahead.

W: Hello.

Henry A. Wallace: Hello, Henry.

W: I'm sorry I had somebody here before.

W: I just happened to recollect that the President threatened to lock us in a room together and we are going to be over there tomorrow afternoon. I wondered if he might maybe ask us a question.

W: Well, I saw him yesterday. He kidded some and I kidded some, but he still ought to put it in the form of a question, and --

W: Of course --

W: I don't think locking us in a room -- that we've been that naughty that we should be locked in a room.

W: You don't think that we ought to be locked in a room.

W: I don't think so.

W: Well, I wondered if we should get together before we met tomorrow afternoon is all.

W: Well, I got this stuff on for tomorrow. I don't -- I told him this again. We were over there -- this so-called Fiscal and Monetary Committee, which is giving recommendations to what we would call good taxes and what we think are bad taxes.

W: Yes.

W: I'm serious, and I said if Wallace wants to meet, why not let him meet with these people, because it isn't only the Treasury he needs. There's Ecoles, and there is no other group that has very definite ideas on this thing, and -- and -- I'm willing to meet and see if we can rub the edges off each other, but I couldn't do it between now and tomorrow because I'm working so hard on the budget.

W: Yeah. Well, if you can't do it you can't do it, and that's that, and if that --

W: But I don't see that the tax program will be coming up right away anyway.

- 2 -

W: Well, that's a good deal the way I'm inclined to feel about it.

HMJr: As a matter of fact, if the thing goes the way -- along the way it can, I mean, I'd be surprised if any tax bill went up before March.

W: Yeah.

HMJr: Now, when this budget is out of the way, frankly, I'm just sunk. We're so far behind.

W: Sure.

HMJr: But I'd love to sit down with you. You don't have to lock the room. I'll come to you or you come to me and we can sit down and talk it over.

W: Yeah.

HMJr: And I'm perfectly willing to tell the President, ^{tomorrow} / if he asks if we did it, I said I begged off until we got the budget out of the way and that then I'd be -- I'd be at your disposal. I'm willing to say that and take full responsibility for delaying it.

W: No.

HMJr: How's that?

W: Well, that's more than fair.

HMJr: Well, I mean, after all, he hasn't even -- he hasn't -- Henry, the amount for the Army and Navy hasn't even yet been decided.

W: Um-hm.

HMJr: So there isn't much use in talking about taxes until we know how much we have to raise.

W: Of course, it seems to me that a lot of fundamental work is to be done on what you can get out of increased taxes on the middle income bracket, and --

HMJr: Well, we've given him all that.

W: And all that kind of stuff that I don't know anything about. It's --

HMJr: Well, what I'd like to do is just as soon as I am physically able to do it -- and I'll tell him that I'm not able to do it now -- I'd like to put what we have

at our disposal, and give you what we've given him.

W: Well, that would be fine.

HMJr: And what we've given the Fiscal and Monetary Committee,

W: Yeah.

HMJr: Is that fair?

W: Well, that's more than fair again.

HMJr: I'll tell him tomorrow that I've asked for a postponement.
How's that?

W: That's -- that's grand.

HMJr: That'll take the curse off you.

W: All right.

HMJr: All right. I appreciate your calling me very much.

W: Thank you, Henry.

REB

GRAY

London

Dated December 20, 1938

Rec'd 3:41 p. m.

Secretary of State,
Washington.

1451, December 20, 6 p. m.

FOR TREASURY.

One. Answering a question in Parliament today, the Chancellor of the Exchequer stated that in view of present circumstances the foreign transactions Advisory Committee has come to the conclusion, in which he concurs, that the relaxations of restrictions on foreign lending announced on February 1 (reported in No. 81, February 1, 8 p. m.) should be immediately withdrawn. He then said "I have reason to think that the need for such restriction is generally acknowledged and I state accordingly that the temporary relaxations made in February have been withdrawn."

Two. The dollar opened at 4.57-5/8 and was 4.67-5/16 at fixing when the price of 148 shillings 10 pence gave 1 penny premium. Seventy-five bars were sold, thirty-five being married and forty furnished by the British fund. After fixing the rate remained steady until the Chancellor of the Exchequer's statement after which sterling was offered and the

REB

2-#1451, From London, Dec.20,6p.m.

the British authorities began selling dollars at $.66\text{-}3/4$ since which time the pressure has been fairly heavy the rate now standing at $4.66\text{-}1/2$ the three months forward dollar premium, however, remains unchanged around $2\text{-}1/4$.

The Bank of France is thought to have bought about two million pounds of sterling today letting the spot rate improve from 177.50 to .30. The three months forward franc is $9/16$ discount while the one month is around par but there is practically no dealing in forward franc.

JOHNSON

PEG

HPD

PARAPHRASE OF SECTION FIVE, TELEGRAM NO. 2135 of
December 20, 1938, 4 p.m., from Paris.

Such expenditures as budgetary revenue will not cover
will total about 40,000,000,000 francs; this does not
include advances to local bodies. The foregoing figure
is made up principally by the following:

	(millions of francs)
Special budget for armament and public works	27,000
Railways	6,000
Various subsidies	5,400
Postal administration	8

In the conclusion of the report it is stated that whatever
may be the condition of the investment market next year,
it will not be possible to undertake financial reconstruc-
tion unless ways and means of increasing the national income
are found, and that the French economic situation would
have to be transformed in order to accomplish this. The
Financial Committee expresses the view that the true rem-
edies lie in a national organization of French production,
in a well-planned national economy, and in the development
of the wealth of French colonial possessions.

END MESSAGE.

WILSON.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 20, 1938, 4 p.m.

NO.: 2135

FOR THE TREASURY.

There was a quiet market today, with continued demand for francs. A large amount of sterling was obtained by the fund, which offered francs at 177.52 at opening, and gradually brought it down to the official closing rate of 177.38. Firm dollar, around 37.98. There was improvement in the belga. On the security market a fair amount of profit was taken, which in view of recent substantial gains was considered normal. However, the undertone was good, and there were only slight irregular gains or losses in rentes today as compared with the closing yesterday.

I give below the essential features of the 1939 budget report of the Finance Committee of the Chamber -

There is a deficit of 10,000,000,000 francs in the 1938 budget. Public indebtedness amounts to a total of 580,000,000,000 francs. This figure includes the following:

	(billions of francs)
Domestic public debt	410
Foreign debt	16
Railway debt	102
Departments and communes debt	40
Colonies and Govt. Institutions debt	12

An accounting surplus of about 25,000,000 francs is shown in the 1939 ordinary budget of 68,146,000,000 francs. There is an increase in appropriations in this budget of

about

- 2 -

about 11,500,000,000 francs over the 1938 budget. This increase is due for the most part to the following -

(millions of francs)

Increase in cost of public debt	1,272
Increase in cost of supplies and services, approximately	4,200
Increase in armament appropriations, about	2,520

Additional expenditures of about 3,005,000,000 francs are called for in the recent decree laws.

It is pointed out in the report that the success of the reconstruction plan of the Government will depend upon very substantial repatriation of capital so that there may be a reduction in rates for borrowing, and so that costs of production can be reduced by industry. However, it is emphasized that there can be a continuation of repatriation of capital only if political and social peace is maintained at home and if the coming months do not bring danger or menace from the outside. The Finance Committee observes in its report that next year the Treasury will have to borrow.

END SECTIONS ONE TO FOUR, INCLUSIVE.

WILSON.

EA:LWW

160

TO: Mrs. Cheney

This was all handled
by phone & matter
has been disposed

8

Gmc

1/4/39

MR. MOREYNOLDS

Shaw
20
1938

THE JOHNS HOPKINS UNIVERSITY
BALTIMORE, MARYLAND

Elder 181
Green
mark

OFFICE OF THE PRESIDENT

December 20, 1938

Dear Mr. Morgenthau:

We have now received the promised support for the further study of settlement in relation to present day problems that you and I have discussed.

The contribution has been made with the understanding that it is to date from December 16th. That leaves us with the necessity for taking care of the expenses up to and including the 15th. Not having received the check for \$1000.00 which you mentioned, I am wondering if there has been some misunderstanding about it. While the matter is not of immediate urgency, I ought, before the end of the year, reimburse Dr. Pelzer for his expenses and provide him the promised salary.

I shall be in New York on December 23rd and at that time will confer with the representatives of various agencies in order to see what we can do to speed the issue. I have just heard of the astounding conditions which Germany has imposed upon those who wish to leave.

Sincerely yours,

Isiah Bowman

The Honorable Henry Morgenthau, Jr.
2211 30th Street
Washington, D. C.

December 20, 1938

My dear Mr. President:

I am sending you herewith the latest report of Admiral Waeche on the proposed construction of a Coast Guard Air station and base for Coast Guard vessels at Kodiak, Alaska.

Sincerely,

The President,
The White House.



THE COMMANDANT OF THE UNITED STATES COAST GUARD

WASHINGTON

19 December 1938.

C-O-N-F-I-D-E-N-T-I-A-L

MEMORANDUM FOR - The Secretary of the Treasury

With further reference to the constructions of a Coast Guard Air Station and base for Coast Guard vessels at Kodiak, Alaska, I have conferred with Admiral Cook, Chief of the Bureau of Aeronautics, and Admiral Moreell, Chief of the Bureau of Yards and Docks, Navy Department, relative to combining the facilities of the Coast Guard and Navy, as far as practicable to do so. The results of these conferences have been most satisfactory, and the Navy Department will cooperate to the fullest extent, so as to provide the facilities desired by the Coast Guard, at the lowest total cost for the combined services.

Further conferences between the technical people of the Coast Guard and of the Navy will be held, so that, within a week or ten days, a revised estimate will be submitted as to the cost to the Coast Guard for this base.

Medical, recreational, and docking facilities, as well as communication facilities (both radio and telephone), power, heat, light, water, cold-storage, and sewage disposal, will be incorporated in the Navy plans to take care of the Coast Guard - so that, the only separate units, exclusively for the use of the Coast Guard, will be: Coast Guard hangar, with necessary auxiliaries, including ramp; and quarters and barracks for Coast Guard officers and men. Each Navy hangar will have its own ramp, as well as the Coast Guard hangar.

R. R. Waesche
R. R. WAESCHE
Rear Admiral, U.S. Coast Guard,
Commandant.

Confidential

P A R A P H R A S E

A telegram (No. 1486) of December 20, 1938, from the American Consul General at Shanghai reads substantially as follows:

Horiguchi of the Domei News Agency informed the representative of the NEW YORK TIMES (Abend) on December 20 that it had been decided that the principal retaliatory action by the Japanese against British and American interests would be in Shanghai and that in the Shanghai area British and American trade will be subject to more severe restrictions. The Japanese Embassy spokesman in Shanghai and the First Secretary of the Japanese Embassy (Kita) also gave Abend confidentially similar information. In this connection reference is made to the Consul General's telegram No. 1485 of December 19.

893.51/6744

(COPY)

December 20, 1938

To: The Secretary

From: Mr. Hanes

I telephoned Ambassador Spruille Braden, who had called you earlier in the afternoon. He had seen the President and had been requested by him to see you before going back to Columbia in order to discuss some matters that had arisen during their conversation. Mr. Braden will call you tomorrow to ask for an appointment.

J W H.

AT COMPLETION

	<u>Net Revenue</u>	<u>Bondable at 4%</u>	<u>Power Cost</u>	<u>Total Cost</u>
TVA (1946-50).....	\$ 9,400,000	\$ 235,000,000	\$ 279,141,200	\$ 494,092,864
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- ^{1/} Includes amortization payments on irrigation costs; the estimate on irrigation project includes a conservative estimate of the Grand Coulee power sales.
- ^{2/} Includes irrigation costs which were to be amortized, but which are not required by law to pay interest.
- ^{3/} Power developments on pending and future projects of this character are indeterminate and, therefore, the estimate has been left about at its current size.

AT PRESENT (1938-39)

	<u>Net Revenue</u>	<u>Bondable at 4%</u>	<u>Power Costs</u>	<u>Total Costs</u>
TVA.....	\$1,850,000 ^{1/}	\$46,250,000 ^{1/}	\$ 61,424,200	\$116,189,700
Boulder.....	3,750,000 ^{2/}	93,750,000	113,500,000 ^{3/}	113,500,000
Irrigation projects.....	3,500,000 ^{2/}	87,500,000	140,000,000 ^{3/}	140,000,000
River, harbor flood control projects.....	379,165	9,480,000	(Not segregated)	
	<hr/>	<hr/>	<hr/>	<hr/>
	\$9,479,165	\$236,980,000		

- ^{1/} Inclusion of fertilizer operations, which lost \$1,859,000, would eliminate bondable income.
- ^{2/} Includes amortization payments on irrigation projects.
- ^{3/} Includes irrigation costs which were to be amortized, but which were not required by law to pay interest.



COMMISSIONER OF
ACCOUNTS AND DEPOSITS

TREASURY DEPARTMENT

OFFICE OF THE SECRETARY

WASHINGTON

December 19, 1938

TO THE SECRETARY:

At the present time the Government has a net proprietary interest in various governmental corporations and lending agencies of about \$4,108,000,000, as follows:

1. Capital stock	\$ 1,988M
2. Surplus	624M
Sub-total	2,612M
3. Net assets in non-stock agencies	758M
4. Special obligations held by the Secretary of the Treasury	738M
Total	\$ 4,108M

The details of the foregoing are set forth in the attached statement.

In connection with our conference on Sunday, December 11, I have been in touch with the General Counsel's Office in the preparation of a draft of legislation for all corporations in accordance with general principles embodied in the Commodity Credit Corporation Act.

INTEREST OF THE UNITED STATES IN GOVERNMENTAL
CORPORATIONS AND LENDING AGENCIES

(In millions of dollars)

	Capital Stock	Surplus	Total
<u>I. Stock:</u>			
Reconstruction Finance Corporation	500	205	705
Commodity Credit Corporation	100	—	100
Export-Import Bank	21	1	22
Federal Crop Insurance Corporation	5	—	5
Federal Deposit Insurance Corporation	150	—	150
Home Owners' Loan Corporation	200	48*	154
Federal Savings and Loan Insurance Corporation ...	100	14	114
Federal Savings and Loan Insurance Associations...	47	—	47
Federal Home Loan Banks	124	—	124
U. S. Housing Authority	1	144	145
Federal Farm Mortgage Corporation	200	—	200
Federal Land Banks	124	182	306
Federal Intermediate Credit Banks	70	46	116
Banks for Cooperatives	149	11	160
Production Credit Corporations	120	1	121
Regional Agricultural Credit Corporations	5	13	18
U. S. Housing Corporation	2	—	2
Disaster Loan Corporation	12	1*	11
Federal National Mortgage Association	10	1	11
Federal Prisons Industries, Inc.	4	2	6
Inland Waterways Corporation	12	13	25
Panama Railroad Company	—	38	45
WFO Mortgage Company	21	—	25
	<u>1,988</u>	<u>624</u>	<u>2,612</u>
<u>II. Non-stock:</u>			
Tennessee Valley Authority			217
Public Works Administration			37
U. S. Maritime Commission			94
Rural Electrification Administration			34
Federal Housing Administration			38
Farm Credit Administration			119
Navy Department (Sale of surplus property)			4
Farm Security Administration			177
Interior Department (Indian Loans)			2
Puerto Rican Reconstruction Administration			4
Railroad Loans (Transportation Act)			30
Securities received from WFO (Act Feb. 24, 1938) ..			2
			<u>758</u>
<u>III. Special Obligations held by Treasury:</u>			
Reconstruction Finance Corporation			719
Home Owners' Loan Corporation			5
U. S. Housing Authority			14
			<u>738</u>
Total	<u>1,988</u>	<u>624</u>	<u>4,108</u>

ACCOUNTS AND DEPOSITS
December 13, 1938

Dec 13, 1938.

4.00 P.M.

ROUGH EXPENDITURE ESTIMATES FOR 1939 AND 1940.

170

(In millions of dollars)

	1939	1940
Regular Departments.	\$ 884	\$ 947
National Defense	1,033	1,155
Veterans Administration	539	546
Agricultural Adjustment (Inc. parity carry over)	700	800
Civilian Conservation Corps.	275	285
Social Security (Grants)	338	377
General Public Works	556	611
Other (inc. Old Age Reserve - R.R.A/C ,	643	842
Emergency (from 1939 and prior appns.)	3,041	833
Interest on Public Debt	976	1,030
	8,985	7,426
W.P.A. (President's figure)	- -	1,500
	8,985	8,926
Treasury revenue estimate (revised) . .	5,510	5,462
Deficit	3,475	3,464
Additional W.P.A. program	250	- -
Additional National Defense	- -	250
New deficit	3,725	3,714

Excluded

Rough Expenditure Estimates for f.y. 1940

Regular Depts	\$ 947 M ✓
National Defense	1.155 ✓
Veterans Administration	546 ✓
Agricultural Adjustment (Inc. partly carry-over)	800 ✓
Civilian Conservation Corps	285 ✓
Social Security (Grants)	377 ✓
General Public Works	611 ✓
Other (Inc. old agv reserve) RRA acct)	842 ✓
Emergency (Carry-over from 1939)	833 ✓
Interest on the public debt	<u>1.030</u> ✓
	7.426
R.P.A. (President's figure)	<u>1.500</u>
	\$ 8.926
	5462
	<u>4.850</u>
Treasury tentative revenue estimate	\$ 4,076 M
Deficit	3,464
	500 M
Does not include	
Supplemental national	3,964 M
defense: only	<u>1,500</u>
	2,464 M

These figures are subject to change in line 15-808.

Rough estimate

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PUBLIC WORKS EXPENDITURES — 1940

Agriculture (Roads)	\$213,000,000
War (Rivers & Harbors, Flood Control, Housing)	200,000,000
Interior	70,000,000
Treasury (Public Buildings)	50,000,000
Navy	25,000,000
Tennessee Valley Authority	42,000,000
Other	<u>11,000,000</u>
	\$611,000,000

5-1178

December 21, 1938

My dear Mr. President:

Some of the changes which are being proposed in the Social Security Act involve very broad future burdens upon the Federal Treasury and should, therefore, be given the most careful examination. These matters are now under consideration by the Treasury and I should like to bring them to your personal attention at your convenience.

I hope that in the meantime you will not commit yourself definitely to any specific changes in the present Social Security system.

Faithfully yours,

Secretary of the Treasury

The President,
The White House.

By Hand
L. B. G. per
12-21

OFFICE MEETING

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

Present: Mr. Hanes
Mr. Taylor
Mr. Bell
Mr. Gaston
Mr. Gibbons
Mr. Lochhead
Mr. Duffield
Mr. White
Mr. Haes
Mr. McReynolds
Miss Chauncey
Mr. Oliphant

H.M.Jr: Good morning.

Gibbons: Good morning.

H.M.Jr: There's one thing I want to bring to you people's attention. I had the darndest time trying to locate it, but Miss Chauncey was a good detective. When Bullitt wanted to bring over this French mission to see me, I knew there was some memorandum around that said we couldn't see foreign missions until they cleared the thing with the State Department. We had a terrible time finding it; Miss Chauncey finally found it. It's a memorandum from Hanes in which he said that the President instructed members of the Cabinet that in case any foreigners came to the Department with any letter of introduction, no matter from whom, that before acting on such request the Department should submit the matter to the State Department to check on the individual. So if everybody would bear that in mind

Hanes: He said, "Even if they have a letter from the President of the United States."

H.M.Jr: But I could not find it. We called Sumner Welles and we called - I kept that French mission back until I got a clearance. But I couldn't find it, and I know that Bullitt thinks I was lying. I couldn't find the thing. Finally Miss Chauncey found it.

Wells: I asked Miss Lehend, Rudolph Forster. None of them saw anything; knew nothing about it. Nothing came

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from the White House. Welles said nothing came from the State Department. I began to think the boss had had a dream.

H.M.Jr: It was funny - when we called Welles he must have been at Cabinet.

Hanes: He was at the meeting. Welles brought up the discussion, he brought the thing to the President, about some German who was trying to get a release of a moving picture in order to take back to Germany, who had a letter from the State Department - with a letter from some member of the Government.

Mohr: I asked him personally about it. He said nothing had gone from State Department to the Treasury or any place else.

Hanes: He brought it to the Cabinet meeting and the President said, "Every Department here take these instructions." He said, "No matter who brings a letter of introduction to any Department, refer him to the State Department; and even if he has a letter from the President of the United States, check him with the State Department."

H.M.Jr: Well, I know Bullitt thought I was lying like hell. When Bullitt comes back, I'll show him that; at least I went through with it. As a result of which Welles for the first time heard about it and was very appreciative.

Bell: Mr. Secretary, it's always been the rule; I mean as long as I've been here, it's always been the rule.

H.M.Jr: But nobody - evidently nobody followed it.

Bell: Nobody followed it.

Taylor: Once identified, why, that's - that's all right, huh?

H.M.Jr: I would say yes. Yes. I mean once identified. But I think as good a case in point as any is this present French mission, which the State Department did not know about. Huh? Well, you know the case

-3-

here two years ago; a man up here - over at Anacostia said he was head of an airplane mission from Chile or Peru, something like that, and would like to be shown the planes. So they said if he'd wait a few minutes, they'd get him an officer to take him around. They went to the phone and called up the State Department to find out whether there was such a mission. By the time they came back, the man had disappeared. I mean it's that kind of a thing; I imagine it's that sort of thing he has in mind.

Herbert, I wish you'd call up somebody over at the Washington Post...

Gaston: Yes.

H.M.Jr: ... and tell them that I personally appreciate the story in the Post today on the Japanese, the aid that we've given Japan.

Gaston: Felix Cotten wrote the story; called me up last night about 11:30 about it.

H.M.Jr: Why, was he bothered?

Gaston: Well, he wanted to check on his impression on the amount of the Chinese silver, and I helped him a little.

H.M.Jr: Then will you tell Felix Cotten I think it's a swell story.

White: Called me yesterday afternoon and I helped him along a little bit on it.

Gaston: Yes.

H.M.Jr: Now, another thing. You talk about people ... I may be all wrong on this, and maybe I'm going too far, but last night while we were waiting on the President, Tommy Corcoran went by and he said just as he went by - hardly stopped at all - he said, "I want to see White about South America. Is it all right?" And I said, "No. I want to know more about it." He let it go at that.

White: Perfectly all right with me.

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H.A.Jr: Well, maybe I'm wrong; if I am, I wish somebody would tell me.

Alignment: Well, I think that sort of thing that Alsop and Kintner had last night - that it's very, very dangerous, very damaging; it can kill the thing if that sort of publicity gets out before we've laid the ground for it. I think it ought to be corralled.

H.A.Jr: Well, I don't particularly agree with you there. But I'd just like to know again: if the President of the United States says to me that he wants Mr. Corcoran and Mr. Smith and Mr. Jones to study South America for him, O.K., but why should Tommy Corcoran be studying South America and getting all this information out of the Treasury? For whom? That's what I want to ask him. Maybe I'm wrong.

Taylor: Absolutely right.

Gaston: You're a hundred percent right. It's destructive of any kind of organization.

H.A.Jr: As he walked by he said, "You know, I've been trying to get you, to get permission to talk to Harry White." He says, "Is it all right?" I said, "No."

So, as I say, if you people think I'm wrong, that I'm too stern..... All I want to ask him is, "Whom is this for? Why do you want it? Is it for the President?"

Do you people think I'm wrong?

Gaston: You're absolutely right.

Sibbons: You know, that thing you asked me about the other day - I saw a guy in the lobby of the Washington the other day at lunch. He just mentioned - "Well, I'm not going to let Tommy run my shop." That's the reaction.

H.A.Jr: I'm not complaining about Tommy. If he's useful to the President, that's the President's business. But when he starts trying to get the Secretary of

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the Treasury into ward politics in New York - I'm just not going to do it. And I referred it over to Helvering, and I knew Helvering could take care of himself. Guy Helvering just smiled. He said, "All right. I'm not just going to let Tommy run my shop."

"Guy," I said, "you're a hundred percent right."

Hanes: I think it gives added protection to the men too. If they don't get clearance, why, that's something that they

H.M.Jr: Sometimes it works all right, but in one case - usually they end up by blaming me, and that's where the blame belongs.

Johnny?

Hanes: Only thing I have is the Social Security Board wants to get some indication from us by tomorrow, if they can, as to how we're going to go on these recommendations that they're making, how we're going to consider the financing them, and so forth.

H.M.Jr: Well, you and Herman and I go into a huddle at 10:30; I go to the White House at two.

Hanes: Well, personally, I don't know whether it's necessary for us to express an opinion at this time or not. It may be the President might ask you whether or not the Treasury has made up its mind as to the

H.M.Jr: Well, when you say "the Social Security" who do you mean? Altmeyer?

Hanes: Altmeyer, yes.

I want a little bit of guidance, because I think if I'm going to pinch-hit for you again at this meeting tomorrow, then I'd better either keep my mouth shut or if we've got any indication to give them

H.M.Jr: What time is the meeting?

Hanes: They haven't informed me yet. I think it's 11

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o'clock tomorrow morning. But they haven't given me a definite date yet - time.

H.W.Jr: Let's see how we get along.

Hanes: You don't want to go to this meeting?

H.W.Jr: I wouldn't go for the world. I don't know anything about it.

Wallace called me up yesterday afternoon, said, "When are you and I going to get together on the processing tax? The President's going to ask us at two."

"Henry, I'll tell the President that from now until the first of January I can't do anything other than I'm doing. I just can't take on anything more." And I'll tell him so.

And I said, "The tax bill, if it comes up next March - will be the earliest, and I'm going to suggest we let it go until I can get a breath of fresh air."

So he said, "That's all right."

I said, "We won't have any tax bill before March."

Hanes: But if I understand - the President said to the newspapers, if that has - what I read - if that has any bearing on the situation -; he's not going to recommend anything specific on these recommendations in his message to Congress - any specific way to either increase the benefit or to raise the money for paying it.

H.W.Jr: That I don't know.

Hanes: He said that to the press. I just read that in the paper.

H.W.Jr: Are you in on this, Bell?

Bell: No, I haven't heard anything about it except what I've read in the papers. From what I read in the papers, I should think the Treasury would be much opposed to it.

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- H.M.Jr: Johnny, I'd love to get this bank thing straight, and if we get the bank thing straight - what did I say I'd do for you (Oliphant)? Something you were pressing me on. What was that?
- Oliphant: I don't remember.
- H.M.Jr: Yes, what was it yesterday that Herman said? What was it Mr. Oliphant said?
- Oliphant: I haven't anything.
- H.M.Jr: You had something.
- Oliphant: Well, the thing Eddie mentioned.
- H.M.Jr: Well, something. Well, anyway, if we get the bank thing - this isn't a bribe - I'll take up Social Security.
- Hanes: I don't think the Treasury is prepared to give any final answer on this thing. I certainly am not, and I've studied the thing now for some length of time. And I'm not prepared to give an answer on this; it's an awfully complicated
- McR: I should like to participate in any conference you have with respect to Social Security, before you arrive at a position on some of these new things.
- Gaston: Will you let me in too?
- H.M.Jr: O.K. George wants to get in and Wayne will want to get in.
- McR: Something to talk about. If the President isn't going to make any specific recommendation, I'm perfectly willing for those things to go up - let it go. But if we've got to tie ourselves down to some of those things they said in there, we ought to know what we're doing anyhow.
- H.M.Jr: We'll get together, and if we're not satisfied I'll write the President a letter and simply say that the Treasury - that I, speaking for the Treasury, hope he will not commit himself until we have a chance to sit down and talk with him about it.

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- James: Then my one there would be to stall, because I don't think we're ready to say anything.
- H.M.Jr: Well then, if - Mac, if you'll write a letter for me to the President simply saying that the Treasury - that I hope that he will not say anything in his message which will commit him on the Social Security program, because some time in the middle of January we'd like to have - the Treasury and the Treasury experts would like to have a chance to sit down.
- James: I don't think anyone but the Social Security crowd can criticize us for that attitude, because they're not together - the Council and the Social Security Board - they're just five and four and six and eight.
- H.M.Jr: Well, something happened on Molly Dewson - that resignation - the President was quite snotty about it: no "Dear Molly" stuff or anything else.
- Chaiken: They didn't give out anything. Well, he announced that Miss Ellen Woodward had been appointed to the Social Security to take the place of Miss Mary Dewson and then somebody said, "Well, what about Miss Dewson? We didn't know she had resigned. Has that been announced?" And he turned to Steve and Steve said no, it hadn't been announced. And they said, "Well, why is Miss Dewson leaving?" and he said, "Oh, she just couldn't stand it any longer." And then he realized what that implied and he said, "I mean she couldn't stand the pace any longer. The work is too heavy. There wasn't any disagreement or anything of that sort."
- H.M.Jr: Well, let's - if we're all - I think something like that - if you'd like to be included
- Bell: I'll consider that includes me.
- H.M.Jr: What?
- Bell: It's all right.
- H.M.Jr: I'll use the word "Treasury."
- Bell: I assume that before any legislation goes up that it would go through the regular channels - the Budget ...

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Oliphant: Yes. Our shop would like to take a look at it. Affects us very materially.

H.M.Jr: You know what's driving Altmeyer; he's trying to beat the gun on Vandenberg, that's what he's trying to do.

Gaston: Well, from the fiscal standpoint it's the most menacing thing that's ever been proposed in this whole Administration.

McR: Just as well have the Townsend plan.

H.M.Jr: Well then, all the more reason that I write a letter to the President and tell him - I'll put it up that the Treasury isn't ready, or we'll think about it very carefully. The point we want to do is to keep him - that I want to ask him - that I hope that he won't commit himself, you see ...

Hoopes: Yes.

H.M.Jr: ... in either his budget message or his message to the nation. Without revealing what it is, I understand in his message to the nation he doesn't go into any economic thing at all; it's purely - I mean there is nothing that has to do with economics.

Oliphant: That is, on the Social Security the Treasury will have views to present the middle or latter part of January - isn't that it?

H.M.Jr: Yes. As for the budget message, if it isn't right it's Danny Bell's fault.

Bell: What did you say?

H.M.Jr: If the budget message isn't right, it's Danny Bell's fault.

Bell: Even though I didn't write it.

H.M.Jr: Oh well, didn't you write it?

Bell: I'm going to write one. I don't know if it's accepted.

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H.W.Jr: At least you see it before it goes to the printer.

Bell: I don't think there will be anything in the budget message about Social Security. If there is, it'll be quite general.

H.W.Jr: And I don't think there will be anything about kinds of taxes, unless he uses that thing that his "Peaks and Valleys" Committee sent him.

All right?

Hanes: That's all I have.

H.W.Jr: Does that take care of that?

Hanes: Yes, sir.

H.W.Jr: Herman, how do you feel?

Oliphant: Fine.

Here are those pictures of those \$900 houses out in Fort Wayne. Ed thought you might want to look at those. I hadn't seen them. You've already seen them?

H.W.Jr: Oh yes. And I took it to the President - that same thing. Tell him I'm two weeks ahead of him. And I met the fellow, Watson, who did it.

Oliphant: Nice boy.

H.W.Jr: For a lawyer he's good.

Oliphant: He's a persistent fellow, hangs onto things. They tell me out at Fort Wayne that they're quite some houses.

H.W.Jr: I've been interested in this for a long time, and McDonald brought Watson over here and introduced me and gave me that.

Oliphant: Very significant in connection with that thing we were working on a long time ago in Idaho.

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H.M.Jr: This is better yet. And I took that photo along two weeks ago.

Oliphant: That

Gaston: That looks like your new industry that's going to provide your economic kick that you were talking about.

H.M.Jr: They can build a million of these houses. That's the best thing that's come into this office in a long time. Tell Ed I'm two weeks ahead of him.

Oliphant: All right.

Gaston: What the President said yesterday on the Social Security recommendations in connection with the general message on the state of the nation was that he would probably approve the general objectives of the Advisory Council report in his message, but "don't go out on a limb as to any details of the thing."

H.M.Jr: Well, I think as long as you were there - if Gaston and McReynolds would collaborate on a letter for me to the President, you see - please.

Gaston: Yes.

H.M.Jr: Let's get it over today.

Gaston: Yes.

H.M.Jr: All right, Herbert?

Gaston: Yes.

H.M.Jr: George?

Maas: (Brings up a chart) Could give you - get a lot more figures on it. I think that does it.

H.M.Jr: Gentlemen, I'm going to stop on this thing a minute. I want you all to listen to this thing, particularly Harry. I wonder - too bad they can't see this. Explain, George, will you? I don't want to put too much feeling into it. Stand back here, will you, so

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they can see it. Want a pencil? I think if each person was given one of those ...

ALCO: I don't know if this is visible.

A.A.Jr: Explain the thing.

ALCO: At the top up here are our excess reserves, and these drops here are the different changes which are made by the Federal Reserve Board in excess reserves. This is the one made in the middle of 1936, the first one, which had no material effect, because excess reserves were at a very high level. Over here is where they made these two steps which reduced excess reserves still further, very drastically. Both steps were announced at the same time, cracked the Government bond market wide open, very sharply.

Down here this black line is an index of new orders, which is a rather broad index representing new business. And it's the basis for the index of industrial production, the physical volume index.

You will note here that - and this red line is a net cash deficit, a three months moving average - you will note here that the net cash deficit over here, about eight months prior to the break in new orders, was going down; during that period while it was going down, you had a very sharp increase in new orders, a sharp increase in the physical volume of business. The new orders didn't break. And the new orders as a basis for industrial production didn't break until the excess reserves were announced - broke the Government bond market, broke the new orders.

H.W.Jr: To the day?

ALCO: Practically.

Alignment: That was also the day of the price statement at the White House, wasn't it?

ALCO: Right in that neighborhood, Herman.

A.A.Jr: I wish you'd give everybody here a copy of this who's interested.

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The President made the statement last night - he said until somebody shows him to the contrary, that we have to have these large expenditures to keep going. I asked George to do this for me. I don't know that I'm going to use it, but it certainly is very significant, and I'd like some of these other people to take it and see if they can tear it apart.

Bell: I thought it was due to a reduction in Government expenditures that business went off.

H.M.Jr: That's the point I wanted to see - whether it was or wasn't. Huh? I thought it might be we'd want to put that in the budget message.

Bell: Suits me.

H.M.Jr: What?

Bell: Suits me.

H.M.Jr: But this whole school of - that you need bigger deficits for more prosperity, has frankly got me worried, and I asked George to take a look at this thing and see if that was true or not.

White: Well, are you going to give an opportunity to examine it before you give it to the President? I take it ...

H.M.Jr: What?

White: ... there will be an opportunity.

H.M.Jr: Oh sure, anybody can take a look at it. We've all taken a look at the other stuff.

White: And found so many errors in it that it was very unfortunate that that was handed in.

H.M.Jr: What was handed in?

White: That previous chart.

H.M.Jr: Which one?

White: The relationship of foreign trade to - well, I didn't

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mean to raise that. I just didn't want this to go in to him until we had a chance to examine it.

H.M.Jr: As I say, you'll have a chance. And I'd like you to show it to Currie, see? But I'm just - no, show it to Currie, will you, Harry?

White: I'll do that. If it's sound, it's important, of course.

H.M.Jr: Right. And I just want it in my vest pocket as a life-saver.

Anything else, George?

Wes: I have nothing else.

H.M.Jr: Incidentally, you might label that place where the break took place as the "ants in the pants" era.

White: The what?

H.M.Jr: The "ants in the pants" era.

Cliphant: That's - "ants in the pants" era - that's when they opened the window.

H.M.Jr: That's when I called the President up five times in five days at Warm Springs. He said, "What's the matter, Henry, got ants in your pants?" I said, "I'm worried." That was in March '37 - March '36 or '37?

Wes: March '37.

Taylor: March '36 is what you mean.

H.M.Jr: No, March '37 is the date I mean. If you remember, Marriner was out in Salt Lake. Remember? It was when the big break took place in the bond market.

Taylor: I remember it very well.

H.M.Jr: Well, wasn't it March '37?

Taylor: Well, yes, the break in the bond market was '37.

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H.M.Jr: That's what I called the "ants in the pants" era.

Oliphant: That's when we were having too much recovery.

H.M.Jr: Then April first came, and that statement.

Wayne?

Taylor: On China, I talked to Sumner Welles, and he's giving the same information that I gave to Bewley, that we were ...

H.M.Jr: Commercial ...

Taylor: A different subject.

H.M.Jr: Oh.

Taylor: On this joint stabilization fund action - that we weren't closing the door to it, but we felt that our gesture had been a very important one and so on. He's going to give that to Mallet and repeat it.

I also told Hornbeck about that delightful forty minutes I had with Mr. Ukawa, and he wants to give me all that business. I said no, I would just talk to official members of the Japanese missions, carrying out that theory.

I'd like, oh, about two minutes with you before your banking thing on this correspondence with the Rublee committee.

H.M.Jr: Do it right after this meeting, Wayne.

Now, Wayne, I'm sending Commander Thompson to Hai-Phong, and I wish you'd let Mr. Welles know, and I'd like letters from him to the various consuls, asking their cooperation. The purpose - I cleared this last night with the President - the purpose of Commander Thompson's trip is - now look me in the eye when I say this, please - to accelerate tung oil coming out of China.

Taylor: (Smiling) Yes, sir.

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Lockwood: You know, I was reading back some of the reports of that road, and one of the difficulties they're having with the chauffeurs running on the road is smuggling of opium; so that's also a perfectly logical thing for Thompson to be doing.

H.M.Jr: But to accelerate the tung oil coming out. And ask me afterwards some of the other things that I've done to accelerate the tung oil coming out - which is only for me; it isn't ready yet for the State Department. What?

Taylor: All right.

H.M.Jr: Will you?

Taylor: (Nods yes)

H.M.Jr: Anything else?

Taylor: No. I'll cover that other one later.

Duffield: The stockholders of the Anglo California meet on December 28 to vote on the change in capital stock and to elect new directors. Just a question of whether we - how long we want to wait to be informed on what the R.F.C. is going to do.

H.M.Jr: Is it true, that rumor I heard, that they're thinking of electing a new director by the name of Giannini?

Duffield: I hadn't heard that one.

H.M.Jr: You hadn't heard that one. You know, that would be a swell idea.

Duffield: Nuh, nuh, nuh.

H.M.Jr: You don't think so. All right.

Duffield: But at some time, I think, as the - along about the 24th, if we don't know what they're going to do, maybe we'd better ask.

H.M.Jr: Well, keep after Preston Delano. He's the man. Will you?

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McFarfield: I will.

H.M.Jr: Keep after Preston Delano.
Harry?

White: There's a note from the War Department that I think ought to go to the S.E.C. Really relates to them. Regards the flotation of Japanese bonds in Hawaii.

H.M.Jr: Well, that's in today's paper.

White: Well, we got it yesterday, last night.

H.M.Jr: Well, will you give it to McReynolds, to write a letter for me of transmittal, please?

White: And here's a memo on silver.

H.M.Jr: Silver? It's all settled.

White: That's why I thought you ought to have a memo to digest it.

H.M.Jr: God, these people who want to put themselves on record! What do you say: how much should we increase it?

White: (Laughs)

Taylor: Left that up to you.

H.M.Jr: All right.

White: No change.

H.M.Jr: What?

White: No change.

H.M.Jr: No change - three o'clock, Saturday afternoon, December 31.

Oliphant: Give us time enough for our paper work.

H.M.Jr: What do you mean?

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Oliphant: Well, if there is paper work involved.

H.M.Jr: Well, it's like how many New Yorkers go into the Cabinet, see? When you know that, you know the answer, see? You know who's going to be Attorney General.

Oliphant: That's right.

Lochhead: There's a little more paper work on it this time.

Oliphant: More paper work this time than before.

Lochhead: The six months proposition.

H.M.Jr: How much time you want on this thing?

Oliphant: Like to have a couple days.

H.M.Jr: O.K.

Oliphant: Tell Bernie and me; you needn't tell the rest of these fellows.

H.M.Jr: All right. What else, Harry?

White: That's all.

H.M.Jr: I could tell you now; it's settled.

Gibbons: I got a call yesterday - request to make a Jackson Day Dinner speech somewhere - from the National Committee. I said I'd have to check with you. I didn't think that the Treasury should get mixed up in it. I don't want to do it.

(Hearty laughter)

Not passing the buck to you.

McR: Please tell him "No."

H.M.Jr: I think it would be a swell idea.

Gibbons: I told Herbert if I could get up and say that, give them my ideas about raising money, see - I got an idea on that.

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H.M.Jr: By God, you stand on your own feet on this one. I'm so tired of being cussed up and down the Hill. If you don't want to do it, you go to Havana or something.

Gibbons: What can you say?

Hanes: I was going to ask you to give me instructions not to do it.

H.M.Jr: It's money-raising, isn't it?

Gibbons: I think so. Just simply couldn't be on the level with them.

H.M.Jr: No, no.

Gibbons: Have to be like a parrot and say what they want you to say. That's one thing ...

H.M.Jr: Money-raising dinner - no.

Gibbons: I'm not going to pass the buck to you.

H.M.Jr: That's all right, I'm just kidding. Treasury policy: no treasury officials speak at money-raising dinners unless it's Baby Bonds.

Taylor: Raising money for the Treasury - it's something else.

Gibbons: They must be pretty hard up for speakers.

Hanes: Thanks, Steve.

(Hearty laughter)

H.M.Jr: This is good today.

Gibbons: I was merely referring to myself, Johnny.

H.M.Jr: All right.

Gibbons: If it included Herman or Mac, that could go, but not ...

Loganhead: The pressure on sterling both yesterday afternoon

-20-

late and this morning - it's down to about 4.65 3/4. There are two things: first of all, that talk about the split in the Cabinet over there, the fight in the Cabinet; and secondly, putting back the ban on foreign lending. You saw that article in the paper; they put back the ban on foreign lending. That's been interpreted as a sign of weakness rather than a corrective force.

Taylor: Well, their answer to that is that it is intended to strengthen sterling.

Lochhead: But the market interprets it in its own way. On the other hand, the francs have been very strong both yesterday and today. When they called up Carigeul yesterday, the French had gained over a million pounds in the morning. Feeling quite happy, thought that the movement had spread to the people, the general public was in on the market; but wouldn't want to make any predictions until after the first of the year.

H.M.Jr: O.K. All right.

Bell: I have nothing.

McR: There was a memorandum from Dr. Parran.

H.M.Jr: Not Doc Townsend.

McR: Certain commodity people in Agriculture talking about nutrition again. He wants to talk to you. But I don't believe you can get any place on it. I think you might just as well let them do what they can. Probably make it an experimental proposition out here in Maryland.

H.M.Jr: I'd like Taylor and Hanes and Oliphant and Mac to stay for a minute, please.

DEC 21 1938

Secretary Morgenthau

Herman Oliphant

Re: Authority of the Export-Import Bank of
Washington to make loans to foreign governments.

A question has been raised as to the authority of the Export-Import Bank of Washington to make loans to foreign governments as such. A study of this matter indicates that the Export-Import Bank of Washington has authority to make loans to foreign governments for the purpose of aiding in the financing and facilitating exports and imports and the exchange of commodities between the United States and other nations.

The Export-Import Bank of Washington was created as a banking corporation, under the laws of the District of Columbia, pursuant to Executive Order No. 6581, dated February 2, 1934. The Executive Order recites the expediency and necessity of organizing a banking corporation with power "to aid in financing and to facilitate exports and imports and the exchange of commodities between the United States and other nations or the agencies or nationals thereof" (underscoring supplied), and the certificate of incorporation of the Bank expressly states that the Bank is formed for that purpose. In connection with and in furtherance of such purpose, the certificate of incorporation authorizes the Bank:

"To do a general banking business (except that of discount or circulation); to receive deposits; to purchase, sell and negotiate, with or without its endorsement, or guarantee, notes, drafts, checks, bills of exchange, acceptances, including bankers' acceptances, cable transfers, and other evidences of indebtedness; to purchase and sell securities, including obligations of the United States or of any State thereof, but not including the purchase with its funds of any stock in any other corporation; to accept bills or drafts drawn upon it; to issue letters of credit; to purchase and sell coin, bullion, and exchange; to borrow and to lend money; and to do and to perform the necessary functions permitted by law to be done or performed in conducting said enterprise or business."

By Section 9 of the Act of January 31, 1935, 49 Stat. 1, the Bank was authorized to continue to be an agency of the United States, and, in

addition to existing charter powers, and without limitation of the total amount of obligations of any borrower, was authorized and empowered:

"to discount notes, drafts, bills of exchange, and other evidence of debt for the purpose of aiding in the financing and facilitating exports and imports and the exchange of commodities between the United States and any of its territories and insular possessions and any foreign country or the agencies or nationals thereof, and, with the approval of the Secretary of the Treasury, to borrow money and rediscount notes, drafts, bills of exchange, and other evidences of debt for the purposes aforesaid." (Underlining supplied.)

From the annual report of the Export-Import Bank of Washington for the year 1937, dated January 10, 1938, it appears that the activities of the Bank have centered in three major fields, namely, "short term accommodations to facilitate exportation of agricultural commodities; medium term loans or credits to assist in financing the exportation of industrial products; and advances to exporters against obligations issued by foreign governments in settlement of claims arising out of blocked exchange". It is to be noted, however, as indicated in such report, that the Bank has made advances of approximately \$21,000,000 in financing for the Government of Cuba the purchase of silver bullion and its minting into 50,000,000 standard Cuban pesos. During the course of the debate on the Act of January 26, 1937, 50 Stat. 5, extending the functions of the Bank until June 30, 1939, Mr. Stengall of the House Committee on Banking and Currency in describing the activities of the Bank mentioned these transactions referring to them as "loans to the Republic of Cuba to finance the purchase of silver bullion and the minting thereof into standard Cuban pesos". (1937) 81 Cong. Rec. 359, 360.

In view of the foregoing, it appears that if it can reasonably be said that the purpose of a loan by the Export-Import Bank of Washington to a foreign government is "to aid in financing and to facilitate exports and imports and the exchange of commodities between the United States and other nations" such loan is within the authority of the Bank.

It seems clear that loans by the Export-Import Bank of Washington to foreign governments are not within the purview of the Johnson Act, 48 Stat. 574 (U. S. C., title 31, 804a), which prohibits certain financial transactions with foreign governments in default on their obligations to the United States. Section 2 of that Act defines "person" (subject to the prohibitions of Section 1) as including individuals, partnerships, corporations, or associations "other than a public corporation created by or

- 3 -

pursuant to special authorization of Congress, or a corporation in which the Government of the United States has or exercises a controlling interest through stock ownership or otherwise". The Bank was created pursuant to congressional authorization; its common stock is held by Federal officials "for the use and benefit of the United States"; its preferred stock was purchased by the Reconstruction Finance Corporation. During the course of the debate on the Johnson Act Mr. McNamara of the House Committee on Foreign Affairs, in response to inquiry, indicated that Section 2 would permit the Government or its agencies to loan money to any foreign government. (1934) 78 Cong. Rec. 6049. It is of interest to note that during the debate one of the members specifically stated that Section 2 would permit Export-Import Bank to loan money to foreign nations, particularly Russia. (1934) 78 Cong. Rec. 6050.

(Signed) Herman Oliphant
~~Director~~

JBF:dm 12/19/38

TREASURY DEPARTMENT

197

INTER OFFICE COMMUNICATION

DATE: December 21, 1938

TO: Secretary Morgenthau

FROM: W. H. Hadley

Subscriptions for Own Account
by 100 Largest Commercial Banks

The accompanying tabulation covers subscriptions both for cash and exchange on the December, 1938 Treasury offering for the 100 largest commercial banks. These 100 banks entered 34% of the total exchange subscriptions and 25% of the total cash subscriptions as shown in the following table:

(dollars in millions)

Subscriptions to December 15, 1938Treasury Offering

<u>Cash Subscriptions</u>	<u>Total for Country</u>	<u>100 Largest Banks Amount</u>	<u>Percent of Total</u>
2-3/4% Treas. bonds 1960/65	\$5,732	\$1,089	19%
1-1/8% Treas. notes 12/15/43	3,647	1,272	35%
Total	\$9,379	\$2,361	25%

<u>Exchange Subscriptions</u>			
2% Treas. bonds 1947	\$701	\$244	35%
2-3/4% Treas. bonds 1960/65	188	68	36%
1-1/8% Treas. notes 12/15/43	39	-	1%
Total	\$928	\$312	34%

On the cash subscriptions, only one bank failed to subscribe, four subscribed to one issue only, and six others subscribed on one or both issues considerably below the limitation set by their capital and surplus. However, 85 of the banks subscribed for the maximum permitted them and the remaining 5 applied for amounts only slightly under the maximum allowed.

On the exchange subscriptions, 33 banks made no subscriptions while 24 others had subscriptions totaling less than 2% of the total for the 100 banks. Eight banks, with exchange subscriptions of over \$10 million each, placed \$201 million of the \$312 million total, or 65%. The following table shows the breakdown of these exchange subscriptions:

Analysis of Exchange Subscriptions
of 100 Largest Commercial Banks

<u>Size of Subscription</u>	<u>Number banks</u>	<u>Subscriptions</u>	
		<u>Dollar Amt.</u>	<u>Percent of Total</u>
\$ 45 - 30 million	4	\$146,859,000	47.0%
20 - 10 "	4	54,622,000	17.5
10 - 5 "	7	43,239,000	13.8
5 - 4 "	5	21,705,000	5.9
4 - 3 "	3	9,031,000	2.9
3 - 2 "	8	16,657,000	5.3
2 - 1 "	12	14,572,000	4.7
Under 1 million	24	5,915,000	1.9
No subscription	33	0	0
Total	100	\$312,600,000	100.0%

	Amt. Entitled to Subscribe (Cap. & Surplus)	Cash Subscriptions		Exchange Subscriptions		1-1/8% 12/15/43	Total Exchanges	199
		2-3/4% 1960/65	1-1/8% 12/15/43	2-3/4% 1960/65	2% 1947			
Chase Natl. Bank, N.Y.	200 500 000	0	100 000 000	0	0	0	0	
National City Bank, N.Y.	123 500 000	61 750 000	61 750 000	0	6 000 000	0	6 000 000	
Security Trust Co., N.Y.	260 000 000	50 000 000	130 000 000	3 000 000	33 700 000	0	36 700 000	
W. of America N.Y. & S.A., San Fran.	92 000 000	46 000 000	46 000 000	0	4 313 750	30 000	4 343 750	
Continental Illinois N. B. & Tr. Co., Chi.	93 500 000	46 750 000	46 750 000	0	92 800	0	92 800	
First Natl. Bank, Chicago	60 000 000	30 000 000	30 000 000	2 500 000	1 588 650	0	4 088 650	
Bankers Trust Co., N.Y.	75 000 000	37 500 000	37 500 000	0	44 600 000	0	44 600 000	
Central Savings Bk. & Tr. Co., N.Y.	81 000 000	40 500 000	40 500 000	0	2 000 000	0	2 000 000	
First Natl. Bank, Boston	67 000 000	33 500 000	33 500 000	0	0	0	0	
Manufacturers Trust Co., N.Y.	75 233 480	37 600 000	37 600 000	0	100 000	0	100 000	
Security-First N. B., Los Angeles	46 000 000	23 000 000	23 000 000	0	84 800	0	84 800	
Spring Trust Co., N.Y.	105 000 000	50 000 000	50 000 000	0	0	0	0	
Cleveland Bank & Trust Co., N.Y.	65 000 000	30 000 000	30 000 000	0	0	0	0	
Bank of Manhattan Co., N.Y.	40 000 000	20 000 000	20 000 000	0	8 000 000	0	8 000 000	
First Natl. Bank, N.Y.	110 000 000	55 000 000	55 000 000	0	5 000 000	0	5 000 000	
National Bank of Detroit	25 000 000	12 500 000	12 500 000	0	15 061 200	0	15 061 200	
J. F. Morgan & Co., Brexol & Co., N.Y.- Phila.	43 533 000	21 000 000	21 000 000	0	0	0	0	
Phila. Natl. Bank, Phila.	30 000 000	15 000 000	15 000 000	0	0	0	0	
Cleveland Trust Co., Cleve.	31 620 000	15 000 000	15 000 000	0	1 386 000	100 000	1 486 000	
New York Trust Co., N.Y.	37 500 000	18 750 000	18 750 000	0	10 500 000	0	10 500 000	
Northern Trust Co., Chi.	9 000 000	4 500 000	4 500 000	0	0	0	0	
Wm Exchange Bk. Trust Co., N.Y.	30 000 000	15 000 000	15 000 000	18 500 000	0	0	18 500 000	
Wells Natl. Bank, Pittsburgh	30 000 000	5 000 000	15 000 000	1 917 700	1 083 000	0	3 000 700	
America Trust Co., San Fran.	19 000 000	9 500 000	9 500 000	0	4 658 000	0	4 658 000	
Union Trust Co., Pittsburgh	80 000 000	40 000 000	40 000 000	2 224 150	5 005 000	10 200	7 239 350	
Secum. Co. for Insurance, etc., Phila.	20 400 000	10 200 000	10 200 000	0	400 000	0	400 000	
First Natl. Bank, St. Louis	13 435 000	5 000 000	5 000 000	0	4 564 000	0	4 564 000	
Wells Fargo Bk. & Union Tr., San Fran.	15 000 000	5 000 000	2 500 000	0	97 000	0	97 000	
Barrie Trust & Savings Bank, Chi.	13 000 000	6 500 000	6 500 000	50 000	0	0	50 000	
Anglo Calif. Natl. Bank, San Fran.	19 050 000	9 525 000	9 525 000	0	100 000	0	100 000	
First Wisconsin Natl. Bk., Milwaukee	17 500 000	8 750 000	8 750 000	0	0	0	0	
Bank of New York, N.Y.	15 000 000	7 500 000	7 500 000	0	0	0	0	
National Chautau Bank, Boston	30 000 000	15 000 000	15 000 000	0	0	0	0	
Marine Trust Co., Buffalo	15 000 000	7 500 000	7 500 000	0	1 500 000	0	1 500 000	
Public Natl. Bank & Tr. Co., N.Y.	14 000 000	7 000 000	7 000 000	0	1 000 000	0	1 000 000	
San Francisco Bank, San Fran.	10 000 000	5 000 000	5 000 000	0	0	0	0	
Commerce Trust Co., Kansas City	8 400 000	4 200 000	4 200 000	0	4 050 000	0	4 050 000	
Newcastle-Commerce Bk. & Tr. Co., St. Louis	13 000 000	6 500 000	6 500 000	0	700 000	0	700 000	
First Natl. Bank, Palto.	8 000 000	4 000 000	4 000 000	0	35 000 000	0	35 000 000	

	Amt. Entitled to Subscribe (Cap. & Surplus)	Cash Subscriptions		Exchange Subscription			Total Exchanges
		2-3/4% 1960/65	1-1/8% 12/15/43	2-3/4% 1960/65	2% 1947	1-1/8% 12/15/43	
Fidelity Union Tr. Co., Newark	13 500 000	6 750 000	6 750 000	0	0	0	0
Seattle-First Natl. Bank, Seattle	10 200 000	5 100 000	5 100 000	150 000	107 000	55 000	312 000
Detroit Bank, Detroit	6 610 000	3 305 000	3 305 000	0	0	0	0
National City Bank of Cleveland	10 750 000	5 375 000	5 375 000	1 200 000	1 200 000	0	2 200 000
Central Natl. Bk. of Cleveland	14 050 000	7 000 000	7 000 000	120 000	80 000	0	200 000
First Natl. Bk. & Tr. Co., Minneapolis	12 000 000	3 000 000	3 000 000	0	2 452 900	0	2 452 900
Banker First Natl. Bk., San Fran.	12 000 000	6 000 000	3 000 000	0	33 000	0	33 000
Farmers & Merchants N. B., Los Angeles	7 500 000	3 750 000	3 750 000	0	48 000	0	48 000
First Natl. Bank, St. Paul	12 000 000	6 000 000	6 000 000	0	5 000 000	0	5 000 000
City Natl. Bk. & Tr. Co., Chi.	6 000 000	3 000 000	3 000 000	0	0	0	0
Whitney Natl. Bk., New Orleans	7 000 000	3 500 000	3 500 000	0	1 000 000	0	1 000 000
United States Natl. Bk., Portland, Ore.	7 150 000	3 575 000	3 575 000	0	720 000	0	720 000
Marine Midland Trust Co., N.Y.	10 000 000	5 000 000	5 000 000	0	0	0	0
Citizens Natl. Tr. & Svcs. Bk., Los Ang.	8 155 000	4 000 000	4 000 000	0	0	0	0
Brooklyn Trust Co., Brooklyn	12 500 000	6 000 000	6 000 000	0	0	0	0
Manufacturers Natl. Bk., Detroit	6 000 000	0	3 000 000	0	0	0	0
First Natl. Bank, Kansas City, Mo.	4 000 000	2 000 000	2 000 000	0	1 000 000	0	1 000 000
Industrial Trust Co., Providence	11 500 000	1 000 000	0	902 600	500 000	0	1 402 600
Guard Trust Co., Phila.	13 000 000	6 500 000	6 500 000	500 000	0	0	500 000
Indiana Natl. Bk., Indianapolis	9 000 000	4 500 000	4 500 000	25 556 500	5 003 000	0	30 559 500
Northwestern N.B. & Tr. Co., Minneapolis	12 000 000	5 000 000	5 000 000	4 000	1 999 500	0	2 003 500
Bank of Calif., N.A., San Fran.	14 000 000	0	7 000 000	0	1 000 000	0	1 000 000
Fidelity-Phila. Trust Co., Phila.	21 700 000	10 000 000	10 000 000	35 300	0	0	35 300
California Bank, Los Angeles	7 500 000	3 750 000	3 750 000	0	0	0	0
First Natl. Bank, Dallas	10 600 000	5 300 000	5 300 000	0	500 000	0	500 000
Corn Exchange N. B. & Tr. Co., Phila.	11 350 000	4 000 000	2 000 000	0	1 500 000	0	1 500 000
First Natl. Bank, Portland, Ore.	6 000 000	3 000 000	3 000 000	0	0	0	0
Savings Banks Trust Co., N.Y.	32 497 000	16 000 000	16 000 000	0	6 000 000	0	6 000 000
Riggs Natl. Bank, Washington, D.C.	6 600 000	3 300 000	3 300 000	0	530 000	0	530 000
Fifth Third Union Tr. Co., Cinn.	10 000 000	5 000 000	5 000 000	8 000	3 000	10 200	21 200
Peoples-Pittsburgh Trust Co., Pitts.	13 000 000	6 500 000	6 500 000	0	0	0	0
Commercial Natl. Bk. & Tr. Co., N.Y.	14 000 000	7 000 000	7 000 000	0	0	0	0
First Natl. Bank, Pitts.	9 800 000	4 900 000	4 900 000	10 000	0	0	10 000
Manufacturers & Traders Tr. Co., Buffalo	12 500 000	6 250 000	6 250 000	0	0	0	0
Mississippi Valley Tr. Co., St. Louis	7 432 000	3 716 000	3 716 000	0	2 000 000	0	2 000 000
First Natl. Bank, Atlanta	8 420 000	4 210 000	4 210 000	0	2 000 000	0	2 000 000
United States Trust Co., N.Y.	28 000 000	10 000 000	0	0	0	0	0
Toledo Trust Co., Toledo	7 225 000	3 612 500	3 612 500	10 561 000	0	0	10 561 000
Merchants Natl. Bank, Boston	6 000 000	3 000 000	3 000 000	500 000	0	0	500 000

	Amt. Entitled to Subscribe (Cap. & Surplus)	Cash Subscriptions		Exchange Subscriptions			Total Exchanges
		2-3/4% 1960/65	1-1/8% 12/15/43	2-3/4% 1960/65	2% 1947	1-1/8% 12/15/43	
State Street Trust Co., Boston	8 471 700	4 225 000	4 225 000	500 000	500 000	0	1 000 000
First Natl. Bank, Phila.	7 111 000	3 555 500	3 555 500	0	1 000 000	0	1 000 000
Farmers Deposit Natl. Bank, Pitts.	12 000 000	6 000 000	6 000 000	0	200 000	31 000	291 000
Citizens & Southern Natl. Bk., Savannah	7 300 000	3 650 000	3 650 000	20 000	1 048 650	0	1 068 650
Empire Trust Co., N.Y.	6 000 000	3 000 000	3 000 000	0	0	0	0
Wilmington Trust Co., Wilmington, Del.	14 000 000	7 000 000	7 000 000	0	0	0	0
Second Natl. Bank, Boston	6 000 000	3 000 000	3 000 000	0	2 000 000	0	2 000 000
Meritoric Bk. & Tr. Co., Winston-Salem	5 650 000	2 825 000	2 825 000	0	1 561 500	52 200	1 613 700
City Bank Farmers Trust Co., N.Y.	20 000 000	10 000 000	10 000 000	0	0	0	0
Commercial Tr. Co. of N.J., Jersey City	6 440 000	0	0	0	0	0	0
Lincoln-Alliance Bk. & Tr. Co., Roch.	6 780 900	3 390 000	3 390 000	0	300 000	0	300 000
Natl. Bank of Commerce, Seattle	5 000 000	2 500 000	2 500 000	0	0	0	0
First Natl. Bank, Cinn.	9 440 000	4 700 000	4 700 000	21 500	183 950	40 000	245 450
Ohio Natl. Bank, Columbus	6 207 000	250 000	2 000 000	0	3 031 600	0	3 031 600
Republic Natl. Bk. & Tr. Co., Dallas	7 100 000	3 550 000	3 550 000	0	0	0	0
Central Trust Co., Cinn.	6 550 000	3 275 000	3 275 000	35 000	10 000	0	45 000
State Bank of Albany, Albany	5 370 000	2 685 000	2 685 000	0	3 000 000	0	3 000 000
Commonwealth-Comm'l. State Bk., Detroit	4 700 000	2 350 000	2 350 000	0	6 000 000	0	6 000 000
Hartford Natl. Bk. & Tr. Co., Hartford	7 300 000	3 650 000	3 650 000	0	0	0	0
Union Planters N.B. & Tr. Co., Memphis	6 750 000	3 375 000	3 375 000	0	0	0	0
First Natl. Bank, Noranton	8 205 000	4 000 000	4 000 000	0	0	0	0
First & Merchants N.B., Richmond	5 800 000	2 900 000	2 900 000	0	2 000 000	0	2 000 000
TOTALS	2,615,045,080	1,089,299,000	1,272,540,000	68,115,750	24,156,300	328,400	312,600,650

C A B L E

From: Hong Kong

Date: December 21, 1938

To: Federal Reserve Bank of N. Y.

178.

Please accept expression of thanks from His Excellency Kung and the Board of Directors for extension of credit against gold to June 30, 1939 which we hereby confirm. Please convey most sincere appreciation to Secretary Morgenthau.

(Signed) Central Bank of China

for 12/21/38

203

J. Lossing Buck
American Consulate
Yunnanfu, Yunnan, China

204



AIR MAIL TO LONDON ONLY
BOAT FROM LONDON TO U.S.A.

CORREO AEREO  VIA AIR MAIL

The Honorable

Secretary Henry Morgenthau, Jr.

Treasury Department

Washington, D. C.

U.S.A.

R HONG KONG
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JR

Confidential

Peiping via N. R.

Dated December 21, 1938

Rec'd 11:59 p.m.

Secretary of State,
Washington.

735, December 21, 5 p.m.

Embassy's 702, December 2, 1 p.m.

One. The press has announced that the Federal Reserve Bank is to issue subsidiary paper notes to the amount of dollars four hundred thousand in denominations of one-half, one, two and five cents. At the same time the press states that a total of one hundred fifty million dollars will be the value of the Federal Reserve Banknotes in circulation by the end of the year.

Two. An American banking source in discussing the currency situation stated that this subsidiary note issue is of no great importance as these notes are intended to replace the subsidiary copper coins which are rapidly disappearing from circulation. He added that the amount is small and presumably will have no effect on the financial market which remains virtually unchanged as to rates and in future dealing no value.

Three.

-2- #735, December 21, 5 p.m., from Peiping via N. R.

Three. The same source commented upon the value of banknotes which are expected to be in circulation by the end of the war: approximately four hundred million is the currency requirements of North China and since currency loss 1938, only about one hundred and thirty million appears put in circulation; consequently even if one hundred and fifty million are in circulation by the end of the year it is difficult to see how an additional 250 million can be put in circulation by March 10, 1939 without seriously upsetting the financial market.

Four. An intensified program of import restrictions may well be the remedy adopted by the Japanese to solve this question and the source of information then mentioned a list of some 90 items which it is currently rumored will be placed upon the restricted importation list. (Embassy's 698, November 30, 3 p.m.).

Five. Insofar as the exchange position of the Federal Reserve currency is concerned, as from March 10, 1939, when it is announced that only such currency will be legally in circulation, the American banker expressed his opinion that, regardless of any suppressive measures towards free exchange, a type of bootleg exchange will necessarily

-3- #735, December 21, 5 p.m., from Peiping ~~to~~ N. R.
necessarily continue to function at a lower rate than
the official one.

Six. In connection with this matter of exchange
it is reported that the German bank here is reputedly
dealing in Federal Reserve banknotes at a lower rate
than the official one.

Repeated to Shanghai and to be forwarded by mail
to Tokyo and Tientsin.

LOCKHART

CSB

REB

PLAIN

Amembassy, Peiping

Chungking via N. R.

Dated December 21, 1938

Rec'd 4:44 p. m.

Secretary of State,

Washington.

609, December 21, 10 a. m.

Following are pertinent extracts from Central News release Chungking dated December 20:

"The contention made by Mr. Arita, Japanese Foreign Minister, the provisions of the nine power treaty are no longer applicable due to changed circumstances is entirely unfounded both factually and juridically, declared the WAICHIAOPU spokesman when interviewed this afternoon. -- --

The changed circumstances referred to by Mr. Arita, continued the spokesman, were brought about by Japan's forcible encroachments upon China's integrity in recent years and by her closing of the open door in certain areas of China.

These were exactly circumstances which the nine power treaty was designed to prevent but which had been brought about by Japan in violation of the treaty, said the spokesman, adding that a treaty could not be considered inapplicable simply because of violations by one of its signatories. -- --

Commenting

REB

2-#609, From Chungking, Dec.21,10a.m.

Commenting on Japan's objection to the British and American loans to China, the spokesman said Japan had no ground for raising any objection in this matter.

Even if the American and British loans were intended as political gestures against Japan, as Mr. Arita thought they were, such gestures were justified and represented the minimum of action open to the powers, said the spokesman after referring to Japan's 'treaty-breaking activities and destruction of foreign rights and interests in China'.

Commenting on Mr. Arita's avowed solicitude for the welfare of third-party nationals in China, the spokesman said the 'embarrassments and inconveniences' caused to them by the hostilities were directly attributable to Japan's aggression in China. Consequently, if Mr. Arita were really sincere in his professed anxiety to third-party nationals regarding 'embarrassments and inconveniences', he should move to stop his country's aggression.

Concerning the third point made by Mr. Arita that the establishment by so-called economic bloc between Japan, China and 'Manchukuo' would not hamper foreign interests in China, the spokesman contended that this was disproved by the whole train of events since 1931.

Inasmuch

REB

3-#609, From Chungking, Dec.21,10a.m.

Inasmuch as the Japanese proposal of such a tripartite bloc of 'new order' in eastern Asia was aimed at the establishment of Japan's hegemony in eastern Asia, said the spokesman, it was in direct conflict with foreign rights and interests in eastern Asia."

PECK

EMB

ROW

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

211

DATE December 22, 1938

TO Miss Chauncey

FROM Mr. White

SUBJECT: Report of conference held at the Secretary's home Sunday afternoon, December 18, 1938. Present: the Secretary, Mr. L. P. Chen, Mr. White.

The Secretary explained to Mr. Chen that he was of the opinion that there was a possibility that Senator Vandenberg might attack in Congress the recent extension of credit by the Export-Import Bank to China. The Secretary thought that Senator Vandenberg might be discouraged from so doing were he made thoroughly cognizant with the economic benefits that accrue to the people of Michigan from the expenditure by the Chinese Government on trucks, etc. The Secretary suggested to Mr. Chen that he might get in touch at once with Mr. Mooney and convey to Mr. Mooney the thought that it would help the trade relations between China and General Motors if Mr. Mooney were to explain to Senator Vandenberg (and possibly the other Senator from Michigan) the economic benefits Michigan was deriving from the Chinese purchases. Mr. Chen thought it was an excellent idea and said that he would get in touch with Mr. Mooney at once.

The Secretary also suggested to Mr. Chen that he (Mr. Chen) arrange to secure an invitation through Mr. Chrysler from some public organization such as the local Chamber of Commerce etc., to make a speech in Detroit (and possibly elsewhere in Michigan) describing the commercial benefits of the recent arrangements made with the Export-Import Bank. The publicity departments of the large automobile companies that were receiving orders from Mr. Chen for trucks could arrange to have the speech receive favorable publicity throughout the country, and thus help prevent unfavorable comment of the export credit, and prepare the ground for continuation of favorable commercial relations between China and the United States. The Secretary also suggested that, after they had made their large purchases of tires, Mr. Chen might do the same thing in Ohio. Mr. Chen stated he thought it an excellent plan and would go to work on it at once.

The Secretary also asked Mr. Chen to cable at once to China and ascertain whether the French were doing all they could to assist in the shipment of goods over the Yunnan Fu railway from Hai Phong and whether reasonable rates for the shipment of goods were being charged. The Secretary stated that if the French were not expediting the shipments and were charging excessive rates he would be glad to see what could be done about it here. He said that the French were under sufficient obligation to warrant his belief that something definite could be done in securing for the Chinese Government good service at reasonable rates on the Yunnan Fu railway. Mr. Chen said he would cable at once.

HDW

DEC 22 1938

Dear Sir:

You are hereby designated to act as General Counsel for the Department of the Treasury during the absence of Herman Oliphant, the General Counsel, with the operating title of Acting General Counsel.

Very truly yours,

(Signed) H. Macmillan, Jr.

Secretary of the Treasury.

Mr. Edward H. Foley, Jr.,
Assistant General Counsel,
Treasury Department.

CTE:bjs
Typed: 12/22/38



TREASURY DEPARTMENT

UNITED STATES COAST GUARD

WASHINGTON 22 December, 1938.

From: Mr. Campbell.
To : Mr. Nicholson. *Secretary*

Message from Professor Buck.

Chen, Kansu Commissioner Reconstruction reports:

Sinkiang not red, not being Sovietized. Chief Russian activity there trading company with branch Lanchow, but China will not permit establishment branches elsewhere. Beginning July '39 Central Bank notes will be circulated. Two million Central notes already shipped. Another million soon. I should think Russian help could be valued around two hundred million yuan. U. S. dollar basis computing exchange at yuan official rate. Five hundred Russian trucks purchased, not thousands. Not liked as gas consumption high. American trucks preferred. Changsha destroyed by Chinese so Japanese will have no building. America and other powers should take action to curb Japan. Friends from Kiangsu tell of terrible suffering Chinese women Japanese raping.

17 dear Mr. President:

The Secretary of the Treasury at the meeting of the Fiscal and Monetary Advisory Board on November 21, 1938, presented material to the Board which related to the program of W.P.A. expenditures scheduled for the next three months.

We pointed out that in the spring of 1938 when you recommended to Congress comprehensive recovery legislation of which the appropriation for work relief formed an important part, the possibility was envisaged by Congress that a situation might arise which would call for expenditures beyond those anticipated at that time.

Although there has been a marked increase in industrial production, and, we believe, a sound foundation for the continuance of recovery has been established, nevertheless the level of unemployment remains higher than was anticipated. It was naturally very difficult to predetermine accurately when expenditures on the heavier type of projects represented by the public works and public housing programs would become fully effective. We find that from July 1st to November 18, 1938, the total withdrawal from the Treasury by the U. S. Housing Authority was less than \$4 million and by the Public Works Administration, exclusive of Federal projects, only about \$80 million, of which \$34 million was withdrawn under the 1938 Relief Act. Whereas, the total withdrawal by the Works Progress Administration amounted to approximately \$882 million.

In addition to the foregoing, the New England hurricanes dislocated industrial production over a wide area and also imposed additional burdens on the Works Progress Administration. Private re-employment has been and is being further retarded by the depressing effects on American trade and industry of the extremely critical international political situation. Finally, there has been an unanticipated lag in private employment despite the sharp increase in industrial production. Combination of these circumstances has thrown most of the recovery burden on the W. P. A. portion of the recovery program during the last five months.

It would now be necessary to cut the W. P. A. rolls by almost one million workers if we are to remain within the apportionments of funds by months hitherto made pursuant to the Emergency Relief Appropriation Act of 1938.

FILE COPY

Mr. President - 2

It is our opinion that, from the standpoint of a proper timing of government expenditures with the requirements of the general economic situation, it would be exceedingly unwise to cut work relief expenditures drastically at this time. Therefore the Fiscal and Monetary Advisory Board respectfully recommends that you both release all present reserves and also modify the apportionments by months hitherto made by reducing the period of apportionment from eight to seven months.

Respectfully submitted,

The Fiscal and Monetary Advisory Board

(Sgd) H. Morgenthau, Jr Chairman

(Sgd) D. W. Bell

(Sgd) M. S. Eccles

(Sgd) Frederic A. Delano

P.S. Appended are two charts showing the lag in private employment despite sharp increase in industrial production.

Chart 1 - Industrial Production and Total Non-Agricultural Employment.

Chart 2 - Total Labor Supply - Not Classified by Regular Employment, Emergency Employment and Unemployment.

11/22/38

FILE COPY

Regraded Unclassified

THE WHITE HOUSE
WASHINGTON

My dear Mr. Bell:

Reference is made to the provisions of Section 2 of the Emergency Relief Appropriation Act of 1938. I find that although there has been a marked increase in industrial production and a sound foundation for the continuance of recovery has been established, the following unforeseen extraordinary emergencies and unusual circumstances have supervened since the enactment of that Act:

- (1) Reemployment in private industry has not, to the degree expected, kept pace with the increase in industrial activities.
- (2) The critical foreign situation has had an adverse effect upon American business and industrial employment in this country. Moreover, it has been an unexpected deflationary force adversely affecting the prices of commodities entering into world markets, such as certain of our important agricultural commodities. This has accentuated relief problems in important areas of the country.
- (3) The hurricane seriously dislocated industry and trade in the Northeastern section of the country and added to the relief burden in that area.

Because of these emergencies and circumstances, I direct that the apportionment, distribution, and administration of Works Progress Administration funds be, pursuant to the provisions of Section 2 of the Emergency Relief Act of 1938, modified by reducing the total period of apportionment from eight to seven months.

I further direct that all reserves hitherto set up against the appropriations in question be released.

Sincerely,



Honorable Daniel W. Bell,

Acting Director of the Budget.

FEDERAL RESERVE BANK
OF NEW YORK

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OFFICE CORRESPONDENCE

Date December 21, 1938.

CONFIDENTIAL FILES

SUBJECT: TELEPHONE CONVERSATION WITH
BANK OF ENGLAND.

L. W. Knoke

Mr. Bolton called me at 9:55 a.m. today and unburdened himself somewhat as follows: "I am principally occupied in trying to keep you posted of what is going on. We have been sending you warning cables that the undertone of sterling is worrisome. At the moment the sterling rate is simply being maintained by means of the squeeze which we have engineered and money rates are rising. Over the turn of the year, that is from December 30 to about January 3, the exchange market is ready to borrow sterling against dollars at between 7 and 10 per cent per annum. That is just a measure of their conviction that sterling is bound to go down and of their determination to maintain their long dollar position. The best we have been able to do during the last three weeks by the squeeze was to keep some sort of stability in the rate. Now, with the news of some dissension in the Cabinet, the situation will become much more difficult for us and there is very little likelihood that this matter of Cabinet dissension will be cleared up before the middle or the end of January. Over the turn of the year there will be a large scale raid on sterling and unless there is some improvement in the political situation from January 3 on, I think we are going to find ourselves in an untenable position. On January 3 we shall have to give up the sterling squeeze because it will be impossible to maintain a money squeeze. At the moment it is effective simply because the banks are

FEDERAL RESERVE BANK
OF NEW YORK

OFFICE CORRESPONDENCE

CONFIDENTIAL FILES

L. W. Knoke

Date: December 21, 1938.

SUBJECT: TELEPHONE CONVERSATION WITH
BANK OF ENGLAND.

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window dressing. In the long run it is impossible politically and economically. I am still discussing all these things with Governor Norman and, of course, he is discussing them with the Treasury. What will come of it I don't know but there will be a very heavy pressure against sterling from the end of the year onward; so heavy I am afraid that we will have to let the rate go down a bit more. Personally I don't want to see the rate drop below the present level which I think is low enough already. We shall resist to the extent of our resources but we shall probably be up against an impossible movement which may well carry us below 4.81. I shouldn't doubt if in the first week in January we shall lose £50,000,000 of gold. The more we stick at any particular level the worse it will be for us as everybody in the London and also the Continental markets is convinced that sterling will depreciate. Unless there is some political improvement our position is going to be very very difficult. I am just speaking what is going through my mind and am trying to warn you as to what might happen and exchange views with you. We have a fortnight before anything is likely to happen. I think what we shall certainly do at the turn of the year is to drop the sterling squeeze. In addition we may put an embargo on dealing in forward gold although that would only force those who are bent on acquiring gold for forward delivery into the Paris or Amsterdam markets. Furthermore we may have to go into the dollar forward market going short of future

OFFICE CORRESPONDENCE

DATE December 21, 1938.

CONFIDENTIAL FILES

SUBJECT TELEPHONE CONVERSATION WITH

L. E. Knoke

BANK OF ENGLAND.

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dollars by means of swap operations which will be necessary for us to get spot dollars in defense of sterling. Our present short position is about \$50,000,000 which we can liquidate with the gold that we now have in New York (\$32,000,000). The remaining \$18,000,000 we can, of course, likewise use in defense of sterling. The present pressure on sterling is, of course, in part due to the repatriation of French funds from London now accelerated by Reynaud's success in getting his budget through the Chamber. The movement of capital back into France is coming primarily from London. There is practically nothing returning from New York. On the contrary, I think there will soon be a new flight of capital from Europe to New York. Taking it all around I don't view the New Year with any optimism at all, and all I want to do is give you material for discussion and keep you fully in touch with our own thoughts. I may be exaggerating the dangerousness of the situation and if I am I shall be only too glad to be wrong. Everybody is convinced that Hitler is going to make a move early in 1939. Hope is low that Chamberlain's meeting with Mussolini will bear fruit. Domestically there is very strong objection against Chamberlain's foreign policy. There is also the belief that certain of our defense ministers have not done their job very thoroughly. In addition there is a growing movement in the Conservative Party to make major changes in the Government. I repeat I am giving you my personal opinion but

FEDERAL RESERVE BANK
OF NEW YORK

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SUBJECT: TELEPHONE CONVERSATION WITH

L. W. Knobe

BANK OF ENGLAND.

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what I am telling you is necessarily for free discussion. I am putting you under no obligation to keep it to yourself."

LWK:KW

December 21, 1938. 221
10:38 a.m.

WMJr: Hello.

Operator: Mr. Bell. Go ahead.

WMJr: Dan?

Daniel
Bell: Yes?

WMJr: Just as I can refresh my memory -- was it you, or Colonel
whatever his name is -- the W.P.A. -- what's his name?

B: Hank Harrington.

WMJr: Told us that when -- that he saw Hopkins, and that Hopkins
would be satisfied with six fifty. Did I get that from
you or from --

B: You got that from me. Hopkins called me here -- ah --
Sunday, and asked me what figure I had in mind, and I said
I didn't have any figure in mind, and he said that he was
bound and determined to recommend six hundred and fifty
million dollars, and I said, well I'd sign on the dotted
line for that, and what's happened in the meantime, I --
I don't know, but I suppose Harry hasn't been in on it
very much.

WMJr: But that's what he said?

B: Yes.

WMJr: Well, I just -- I -- I thought that, because you notice
I said that to Harrington last night and he snapped at me.

B: Yeah.

WMJr: Incidentally, that fellow Harrington -- I'm going to teach
him a little manners. I think he's pretty rude.

B: Really?

WMJr: Yes.

B: But I just thought it was the Army style.

WMJr: Well, yes, but he ought to take a few lessons from General
Craig.

B: He ought to what?

WMJr: Take a few lessons from General Craig as to manners.

B: O. K. Well, he's -- he's -- I think he's got his feet on the ground over there, and he knows a lot of things are being done that shouldn't be done. As a matter of fact, I think they got yesterday about a hundred million dollars more than they expected.

HMJr: Yes.

B: That's the way I figured.

HMJr: Right.

B: All right.

HMJr: Thank you.

December 21, 1938.
4:35 p.m.

Mr.: Hello.

Operator: Mr. Knoke.

Mr.: Thank you.

Mr.: Go ahead.

Mr.: Hello.

L. W.
Knoke: Mr. Secretary?

Mr.: Yes.

Mr.: Mr. Knoke.

Mr.: How are you?

Mr.: Quite well, thank you, sir. Mr. Secretary, I'm sending tonight copy of a telephone conversation, ah --

Mr.: Yes.

Mr.: Which is by all odds the most pessimistic we have received in a long while.

Mr.: Right.

Mr.: And I thought I'd mitigate the shock by telling you beforehand.

Mr.: What's the matter with it?

Mr.: Oh, he's -- he thinks that there are just -- by the end of the year they can't hold sterling, and he thinks it is going through four sixty-one. - after

Mr.: Um-hm.

Mr.: And -- uh -- the thing is just too big for them.

Mr.: I see.

Mr.: The pressure is there and the determination on the part of the short element to see this thing through and they stay short of sterling and are willing to pay as high as ten percent for a few days over the end of the year but they want to maintain their long position in dollars. So altogether it is very unsatisfactory, but I -- I gave it just very nearly the way word by word the way he gave it to me over the phone.

MMJr: Right.

K: And I think you will find it unpleasant reading.

MMJr: Everything's unpleasant these days, Knoke.

K: How's that?

MMJr: Everything's unpleasant these days.

K: Yes.

MMJr: That has to do with outside this country.

K: Check.

MMJr: Well, I'll wait for it.

K: All right, sir.

MMJr: Thanks for softening the shock, but I -- anything today in Europe you can't frighten me.

K: Yes, I see. Well, that may be the right -- the right --

MMJr: I just can't -- well, thanks Knoke.

K: All right, sir.

MMJr: Good night.

JR

GRAY

London

Dated December 21, 1938

Rec'd 1:55 p.m.

Secretary of State,
Washington.

1454, December 21, 1 p.m.

FOR TREASURY.

Summary of press comment on the reimposition of foreign loan restrictions follows:

The FINANCIAL NEWS in an editorial characterizes the step as desirable but belated and points out that "it is obviously a measure calculated to check a depreciation of sterling and it seems clear that the motives for such a policy have been strengthened by the conclusion of the Anglo-American Trade Agreement. Unlike the Tripartite Agreement the trade pact fixes a definite datum line by which a depreciation of sterling can be measured, namely the rate of about 4.70 prevailing at the time it was signed. And in view of the exchange clause in the treaty the Treasury may well be anxious to convince the American authorities that all reasonable steps have been taken to maintain the exchange value of the pound".

The Lombard Street column of the same paper further asserts that the first of the relaxations of July 19, 1934

(reported

-2- #1454, December 21, 1 p.m., from London.

(reported in No. 428, July 20, 1 p.m.) in favor sterling area countries for increasing their sterling assets to stabilize increasing exchange should also be withdrawn: "It would be absurd if acting upon the old rules the Foreign Transactions Advisory Committee were to authorize loans which would strengthen the sterling reserves of sterling bloc countries which have recently repatriated their funds from London."

The FINANCIAL TIMES editorial mentions the recent decline in the dollar value of the pound and also suggests the possible motive of "keeping the market sweet" for possible rearmament borrowing.

The TIMES city column refers to recent comments included therein on the "continuous strain on sterling caused by the steady withdrawal of foreign balances from London" and to the fact that "It is no secret that the exchange accounts gold holding has declined seriously since the beginning of August and although it remains at a satisfactory level it is not so large, in relation to London's foreign liabilities, that the authorities could cheerfully contemplate unnecessary inroads into it." This article also refers to the need of husbanding capital for domestic needs, in particular the British Government's

necessary

-3- #1454, December 21, 1 p.m., from London.

necessary heavy borrowing during 1939.

The DAILY HERALD congratulates the Chancellor of the Exchequer on his decision. The NEWS CHRONICLE city editor describes the announcement as a "definite signal of distress" indicating the authorities' concern at the pressure on sterling. The city column of the DAILY TELEGRAPH'S comment is that "nobody will deny that the authorities are merely following the path of prudence in affording some relief to sterling by tightening the foreign loan screw."

Still under the influence of Sir John Simon's statement reported in No. 1451, December 20, 6 p.m., the dollar was strongly bid this morning going quickly to 4.65-5/8 when the British fund intervened. The market reacted to 3/4 but the pressure is reported as fairly heavy now. There was a large turnover of gold at the fixing, 358 bars being sold but most of the whole was market transactions and the British fund is reported to have given only about fifty bars. The dealings are thought to be largely the covering of maturing forward positions. The price was 149s 3d and was quoted as giving 1/2 d premium at 4.65-3/4 but the market

-4- #1454, December 21, 1 p.m., from London.

market calculates that the price was really at shipping parity.

The estimate quoted for the Bank of France's purchase of sterling yesterday as two million pounds is now considered in the market to have been nearer three million pounds and the French authorities are thought to be buying sterling at about the same rate as yesterday, around 177.18 while the one month forward franc stands at a premium of $1/32$ and the three months discount is down to $1/2$.

JOHNSON

DDM:PEG

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 21, 1938, 4 p.m.

NO.: 2142

FOR THE TREASURY.

The franc was again favored today, and we are told that approximately \$2,500,000 were obtained by the fund. At opening the rate was 177.26 with the fund offering francs and the rate was gradually lowered to 177.08 which is the present level. For one month the forward rate is par; for three months, 50 centimes. Today there was strength in the belga.

Very strong and active security market, with gain of 3 to 4 francs in rentes. In market circles it is believed that Reynaud might undertake a conversion operation in the early part of January, but confirmation of this has not been possible.

A Belgrade press report states that the Central Bank President is on his way to Paris, but there is no indication of the purpose of his visit.

WILSON.

HA:LWW

GROUP MEETING

December 22, 1938.
9:30 a.m.

Present: Mr. Hanes
Mr. Taylor
Mr. Bell
Mr. Gaston
Mr. Gibbons
Mr. McReynolds
Mr. Lochhead
Mr. Haas
Mr. White
Mr. Foley
Mr. Duffield
Miss Chauncey

H.M.Jr: Good morning.

Gibbons: Good morning.

G.M.Jr: I suppose you people know about Oliphant. During the night he had this very, very serious heart attack, and we got him into the Naval Hospital and he's under an oxygen tank; and he has this blood clot and they won't know for a couple hours whether he will or won't live. They won't know for a couple hours. Dr. McIntire just talked to me and said in a couple hours they'd know.

Gaston: Is it a blood clot?

G.M.Jr: A blood clot in the heart proper.

(Foley comes in)

Come in, Ed. Ed, I guess you'll have to carry on, because it will be three months before Mr. Oliphant will be with us - at least three months - and they said maybe - well, we don't know.

Foley: Terribly sorry to hear it.

Hanes: What's the matter with him, Mr. Secretary? Do you know?

H.M.Jr: He's got a blood clot. He's under oxygen. Won't know for a couple hours whether he will or won't live.

Haas: What time was it, Mr. Secretary?

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Hed: About half past five this morning. They called me a little after six.

Hanes: Wasn't feeling very well last night when he left here about 6:30; wasn't feeling too well then.

H.M.Jr: I'm going to make you (Foley) Acting General Counsel. Do the best you can.

Foley: Yes, sir.

H.M.Jr: Now the only thing important I've got is that letter. Now where is that?

Foley: The letter to Giannini?

H.M.Jr: Yes.

Foley: Here's a copy of it.

H.M.Jr: I want to give it back, if you don't mind. No, but where is the original? Is it there, Miss Chauncey?

(Miss Chauncey hands letter to H.M.Jr)

H.M.Jr: Thanks.

Chauncey: There's another piece to it.

H.M.Jr: Thank you.

Now we'll go through those motions this morning, see?

Hanes: Was - this was all right?

H.M.Jr: Fine. Now, let's see - S.E.C. 11:15.

Hanes: What'll I do about that meeting? Couldn't get the Secretary of Labor any other time except 10:30. What'll I do about that?

H.M.Jr: Well, let it go.

Hanes: Just say I can't go.

H.M.Jr: You say there's an emergency matter.

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HANES: send somebody?

H.M.Jr: I wouldn't send anybody. Just let it ride.

HANES: I tried every other time in the day, and the Secretary of Labor couldn't go on any

H.M.Jr: Well, just call her up and say that an emergency matter has arisen and it needs your attention here, and that's all. I mean let this be a lesson to all of us: not try to do four things at the same time. I mean for obvious reasons I want you here at 11:15. Huh?

HANES: I just wondered how I should do that. I'll just call her up and tell her I won't be there.

H.M.Jr: Just tell her - no sense of sending anybody else. And will you see that the same people are here who were here last Saturday?

HANES: Yes.

H.M.Jr: Will you? The same people.
You got anything?

HANES: I've got these forms for the income tax.

H.M.Jr: My God, I just got through paying my December one.

HANES: This is not for you. This is the corporation tax, which we've cut down to a very short form which will be used by 400,000-odd corporations under \$25,000 a year. If anybody's interested in seeing it - I don't know whether you've seen them or not, have you?

OSGUTH: Yes, we got out a release on it.

H.M.Jr: What else have you got?

HANES: I haven't got anything else. Got that letter prepared for Senator Harrison and Congressman Doughton on the codification of the Internal Revenue law, and which is written for your signature; and there's quite a long memorandum with it. I've been over the memorandum, but it doesn't do exactly what the

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Joint Committee wanted to do. They want ...

H.V.Jr: Has Ed seen it?

Hanes: I assume that Ed has seen plenty of it.

Foley: I was just present when Mr. Oliphant was talking to you about it last night.

Hanes: Mr. Oliphant drew this letter himself, or had it drawn, with a long memorandum, and there is some disagreement between us and the Joint Committee, because this letter recommends that the codes not be enacted into absolute law, but *prima facie*.

H.V.Jr: Well, look, old man, if you and Ed will get together and tell me you're together, I'll sign the darn thing.

Hanes: Well, I'm thoroughly incapable of being together with anybody on the thing, because it's a matter of law which I'm not capable of answering. I just know there's a difference of opinion between us and the Joint Committee. Stam wants it enacted into absolute law and we do not wish it enacted into absolute law, but *prima facie*. There's a difference between us and the Joint Committee, and the Joint Committee has asked - they're going to get a letter from the Department of Justice to go into the front part of the code, and they want a letter from us, and since we're in disagreement with them, I don't know whether we ought to send this letter before we have a conference with them and talk to them, rather than just sending a letter which is not the kind of a letter that they want.

I think we ought to perhaps - the easiest way to do would be to have a conference with Stam, find out if this letter would be acceptable. I wouldn't like to have us send a letter up there which is something that they didn't want to ask for.

H.V.Jr: Is it agreeable that Ed take it and carry it?

Hanes: Absolutely. I'll be glad to get rid of it if I can.

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Stam: That's something Phil Wenchel ought to handle.

Hanes: It's been handled by the Department all the way up - studied it, corrected it. It's been in the Department four months. We've been working on the correction of this enormous thing; it's a big enormous book we've had for about four - I think it's all of four months, and it's been in the legal department for about four months.

H.A.Jr: How do you want to leave it? You say what you want.

Hanes: I tell you the way

H.A.Jr: Well, say what you want.

Hanes: I'd like to have Ed sit down with Stam and me and see if we can't get the thing ironed out between ourselves and the Joint Committee. I'd hate to have us go out on the line opposing something that the Joint Committee has set its heart on. And old man Doughton said this is his last term in Congress and he wanted to leave it as a memorial to himself; and I hate to go out into opposition to him. That's rather selfish, because I've got to work against him.

H.A.Jr: Now we're leaving it that - who signs this, you or me?

Hanes: You, and it goes as a record - as a matter published in the Record.

H.A.Jr: Well, I'll take anything you fellows give me.

Hanes: If Ed will meet with Stam and me when I get Stam, I'll appreciate it.

Foley: I'll check up on it and talk to Phil Wenchel; we'll get together.

Hanes: He's thoroughly familiar with it.

H.A.Jr: Mac, see that Ed gets in touch with Monnet. I'd do it tomorrow, wait until I get out of town, so he can take care of me today, take care of Hanes before he goes out of town. But tomorrow let him see Monnet

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and see if he can fix him up.

Henes: That's all I have.

H.W.Jr: Herbert?

Costan: I have nothing. I suppose there will be some questions at the press conference this morning about the announcement by Aubrey Williams yesterday that they had funds to last until February 7.

H.W.Jr: Well, I'm largely responsible for the fact that there was an announcement. I don't know whether I did right or wrong. But Bell was there, and I suggested that they put the thing out to prepare the country for this, didn't I?

Costan: I think it's a good thing. I was glad to see it get out.

Bell: As I recall, the President said, "Just let it gradually leak out that"

Costan: No let it leak.

Bell: ... that they were going to be out of funds on February 1. Might as well make a formal statement. Then he backed it up with Lewis's statement that they wanted a billion.

H.W.Jr: As a matter of fact, he didn't tell them the truth, did he?

Bell: I didn't read the paper.

H.W.Jr: The truth of the matter is they'll be out of funds on the 22d of January - of - yes, that's the truth.

Bell: Well, just as to some parts of it, not all of it.

H.W.Jr: Well, that's what he said there that night.

Bell: Said that he wouldn't be able to obligate the payrolls for the second - for the two weeks after January 22 - those that are paid on January 22. Now, there will be many of them paid on February 1, and those will have been obligated at the end of that time.

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- H.R.Jr: I think it's better to have it out and have the country know about it. I think it's too big a secret to be carrying around alone. What?
- Gaston: I'm amazed that the boys haven't made some analysis of the figures and got this dope before.
- H.R.Jr: As I say, I made the suggestion. And as Bell says, the President said, "Let it leak out" - and some leak!
- Gaston: There's all kinds of leaks.
- H.R.Jr: Then the President checked up with Wallace and Miss Perkins yesterday as to my statement that I made to him night before last that consumption was catching up to production and they confirmed what I said. And Wallace went further and said he thought they were beginning to build up inventories again.
- And then I see that today's labor figures for New York - number of employees fell off. And Colonel Harrington said there would be a million and a half jobs provided - did he say six months or three months - a million and a half.
- Bell: Six months.
- H.R.Jr: He also used the figure of eleven and a half million unemployed - that they were taking care of 23 percent of them, which I thought was a new way of putting it, to me; I'd never heard it put that way before: eleven and a half million unemployed, U.P.A. takes care of 23 percent of them.
- Gaston: Could we see if that checks with George's figures?
- H.R.Jr: What?
- Gaston: I don't believe that checks with George's figures, does it?
- Hubb: Well, the figures on unemployment - the estimates vary. That eleven is a little higher than some of the figures.
- Gaston: I see.

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Hess: But it's pretty hard to argue, the basis is so vague.

Duffield: I have nothing. I'm available if you want me to do anything.

H.M.Jr: Available?

Duffield: Uh-huh.

H.M.Jr: Aren't you busy?

Duffield: I'm current.

H.M.Jr: Well, I congratulate you. I wish we all were. Aren't you helping on the - aren't you helping Bell?

Duffield: I'm current.

Bell: I haven't got to that point yet; today or tomorrow I'll be finished with it.

H.M.Jr: If he has nothing to do for half a day, then he can work all Sunday.

Bell: Fine, that's a good idea.

Duffield: I'll have something for you this afternoon, so ...

Bell: All right.

H.M.Jr: Wayne?

Taylor: Here's a picture of the stamp for Savings Bonds. Thought you might want to use it for the fourth anniversary. Pretty good looking stamp, if you want to do it.

H.M.Jr: Swell. Oh, that's grand. You mean a regular stamp.

Gaston: Postage stamp.

H.M.Jr: Oh, swell.

Taylor: Nice-looking job.

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H.M.Jr: Yes. Well, I'll see what I can do with the President. (To Chauncey) See that I take that over when I see him Monday.

Anything else?

Taylor: (Nods no)

Bell: Celebrating anniversaries now with stamps?

Taylor: It's an idea.

Bell: Next year will be the tenth of the deficits, so we might ...

Taylor: This is a blue one, but make that one a red one.

Bugest: Whose anniversary is it, Wayne?

Bell: It's the - this red-headed girl looks like she got a little plumper in the last four years.

Taylor: We can change that.

H.M.Jr: Commonly known as a "Jeff Coolidge girl."

McR: Talking about the "baby blond."

H.M.Jr: "Baby blond"?

Gibbons: Did you see the current issue of LOOK? - the women lobbyists, including F. B. Roberts....

H.M.Jr: Good.

Gibbons: ... a whole page of them - Mrs. O'Connors of Kentucky...

H.M.Jr: McReynolds is fixing up an order to give you (Foley) authority. If you stay behind, I want to talk to you a couple minutes.

(McR hands H.M.Jr. order referred to)

H.M.Jr: What a men!

Now that doesn't - in the absence of Herman Oliphant, that doesn't mean he won't continue to draw his salary.

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MAN: doesn't affect that status at all. Ed gets no more salary and Herman gets no less.

H.M.Jr: I wasn't worrying about Ed getting more.

Banton: Think of the perquisites.

McK: Doesn't affect the salary status at all.

H.M.Jr: You (Poley) stay behind.

White: A couple memos here on trade that you asked for.

H.M.Jr: what's this?

White: why, you asked about

H.M.Jr: Oh.

Chauncey: For the farm?

H.M.Jr: No, not for the farm. I'm not taking anything to the farm.

Lochhead: The markets are quiet but steady. Francs continuing to gain. I have the written-up conversation that I referred to yesterday. I think you should read it over - that very pessimistic statement of Bolton.

H.M.Jr: Knoke called me up, said, "I want to cushion the shock for you."

Lochhead: I spent some time with Monnet yesterday evening working up - nothing you need to bother about.

H.M.Jr: I can't.

Lochhead: Misunderstood that anyway.

H.M.Jr: He said he'd see me next week. The point is he's got these various papers incorporating the Canadian corporation, so forth and so on - get the story

McK: He'll have him in tomorrow.

H.M.Jr: Yes. And Oliphant was to tell him informally whether it was outside the Johnson Act.

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- Gibbons: I got in a row with this Committee; they won't take no for an answer, that Johnny or I won't make a speech. They say it's the President's benefit ...
- H.M.Jr: Oh, don't bother me. You fellows are all of age. You get together; whatever you do is all right with me.
- Gibbons: I told them that Johnny is ...
- H.M.Jr: You fellows all have been around as long as I have.
- Hanes: I told them I wouldn't go; you weren't going to be here.
- Gibbons: They say you've got to go. Just over-night - they'll send you to Pittsburgh or Chicago.
- H.M.Jr: Who's "they"?
- Gibbons: Both Jim and Quayle. That the President is back of this thing... Here's the story: that these different localities can't get up a dinner unless they have a speaker who
- H.M.Jr: Well, the Treasury Department is the only department where a Treasury employee can't be a National Democratic Committeeman. The President's back of that.
- Gibbons: I kept you out of it.
- McR: It's obvious that Johnny Hanes can't go.
- Gibbons: I'll talk to Johnny about it.
- Hanes: I just said I wouldn't go.
- H.M.Jr: Well, I won't approve your going; I won't approve your going. And if Farley wants the President to direct me to do it, all right - in writing. O.K. But we've got all these rules and regulations and we've crossed this bridge about keeping the Treasury out of collecting money. Now, whether you do it in the Treasury Building or whether you do it over a dinner table - I can't see any difference.

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Gibbons: I didn't quote you at all. I said ...

-Buncey: Got a telegram this morning asking you to permit Mr. Gibbons... I was going to give it to Mr. Mac.

H.M.Jr: Gibbons will handle it. You take it, Steve.

Gibbons: Sure. I hate to annoy you with it this morning.

H.M.Jr: It doesn't bother me a bit. When Jim gets bothered about anything, he never hesitates to call me. Whenever Jim really wants something, he calls me; he knows ... - and he hasn't called me.

Gibbons: No. but that's ...

Bell: I suggested that five-minute meeting around eleven - Mr. Taylor sit in - and if they want to continue for the purpose of confirming past action, that they go into Mr. Taylor's room after the five minutes is up.

H.M.Jr: Library of Congress.

Bell: Trust Fund.

H.M.Jr: Well, Taylor's got to be here at 11:15.

Bell: I don't think - it will take only a few minutes. What they want to do is put in a formal record action of the Board during the past year; purpose of the 11 o'clock meeting is to accept a gift of the property right across from the Carlton Hotel, 16th and L. Good piece of property. That is being given.

H.M.Jr: Well, if it lasts more than five minutes, can't we just confirm them and can't they adjourn up to ...

Bell: O.K.

H.M.Jr: You better be here at 11. One of these many trust funds of which I am custodian.

Bell: That's all I have.

H.M.Jr: Mac?

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McR: (Nods nothing)

H.M.Jr: What?

McR: (Nods nothing)

H.M.Jr: All right. Ed, would you stay a minute?

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December 22, 1938.
11:53 a.m.

HMJr: Hello.

Senator
Glenn: All right.

HMJr: Ah -- Henry Morgenthau, Jr.

G: How are you, Mr. Secretary?

HMJr: I'm pretty well. How are you, Senator?

G: I'm fairly well. I've got a bad cold.

HMJr: Ah -- Senator, talking about this bank holding legisla-
tion --

G: Yes?

HMJr: Ah -- from the standpoint of the Treasury --

G: Yes?

HMJr: Ah -- we would a little bit rather, if it is feasible,
to hold off until the first of February.

G: Well, I'll try and do it as I told you I would.

HMJr: Fine, but you remember you raised the question the other
day.

G: Yes, it's my own judgment that it would facilitate matters
by introducing the bill the first thing and then making
any amendments that your hearing would suggest, but if
you think otherwise, why, all right.

HMJr: Well, it would be a little bit better for us, but I -- I
-- I'm just going that far.

G: Yes.

HMJr: And, of course if the situation changes, why -- we are
here and I'd be glad to come to see you at any time that
you want me to.

G: Very well, we'll talk about it later.

HMJr: But, thank you so much.

G: All right.

HMJr: Thank you.

c/o Board of Trustees,
Liang Lu Kou, CHUNGKING,
22nd December 1938.

Secretary Henry Morgenthau, Jr.,
United States Treasury Department,
Washington, D.C.

Dear Mr. Morgenthau,

My secretary was suddenly taken ill with appendicitis and had to fly from Kunmin to Hongkong for an operation, and for this reason there is a delay in one week's report which I had already sent her but which she could not forward.

It looks now as though I could make the trip to Burma by the first of January. T. L. Soong has just come over the road with twenty trucks of war materials. Up until this time the only information from people who attempted to travel the road indicated great difficulty in making the trip in any reasonable length of time. Mr. S. M. Ling of the Southwest Transportation Company left on November 5th and was not able to complete his return trip from the Burma border until December 11th. A representative of the Central Aircraft Company attempted the trip and did not complete it because of landslides. According to his report which was confidential landslides are continuous and are likely to occur during the dry season because some of the cuts are at steeper angle than at the angle of repose of the soil above the cuts. He also reports that some of the fills are very narrow and in some places have fallen away taking the road with it. T. L. Soong

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22/12/58.

Secretary Henry Morgenthau, Jr.

in his interview with me gives a more favorable report.

It is because of these unfavorable reports that I have not made the trip earlier, but now it seems possible to attempt the journey without undue delay, although I should judge that the matter of getting through depends upon whether or not one meets a slide of considerable magnitude or whether the road falls away in some places with narrow fills. I have felt some little concern about not making the trip earlier, but I felt that a report on the road when more nearly completed would be of greater use to you, especially since I have had direct information from time to time from people who have travelled the road.

I am enclosing some memoranda on various subjects of possible interest to you.

Respectfully yours,

J. Lossing Buck
J. Lossing Buck.

Encls:

JLB:MG

LOCAL SZECHUAN OFFICIALS AND LOCAL LEADERS
IN CHENG TU, SZECHUAN.

Chungking, December 19, 1938.

After my return from Lanchow, I stayed about three weeks in Chengtu to become better acquainted with the situation in Szechuan and to make contacts with representative people. I met most of the officials and I have already informed you of the interview with the Governor who later invited me to dinner, as also did General Teng Hsi-hou.

The Commissioner of Reconstruction is quite an active man and apparently considers agricultural improvement one of the most important problems in Szechuan. He has some plans in mind for carrying out an extensive agricultural extension program along a few lines.

The Commissioner of Education is a man who has been termed by those who are acquainted with him as a type "who knows it all", and therefore is not susceptible to suggestions. There is a plan on foot now to give vocational education to many high school students who did not pass their examinations for college entrance. College entrance examinations were rather stiff since the capacity of the universities is greatly limited.

The Commissioner of Civil Affairs seems to be a man of more ability than most of the other Commissioners and is working on a definite program. He is emphasizing extension of the bao chai system which has been put into effect in some of the other provinces and in the training of police throughout the province.

I had a good talk with S. C. Liao who is an important local leader of considerable influence and who is also a go-between between the Central Government and local officials. The local leaders in Szechuan still apparently have considerable influence and are, therefore, an important factor in the situation. Mr. Liao states that Szechuan is loyal to the Central Government and that the few local uprisings are of no real significance. There are various reports as to the reasons for these local troubles in two or three hsien. One report is that one magistrate recruited 2000 soldiers instead of the 200 he was supposed to recruit; others state that local gentry whose interests are affected have enlisted the aid of secret societies in staging some uprisings, and it is true that members of such societies marched through one hsien to another to riot. Apparently the situation is not really serious, but is an indication of some of the difficulties in bringing about reforms and in enlisting complete support to the Central Government regime.

I also had the good fortune to meet Marshal Chow, another local leader of great influence. He also makes the statement that Szechwan can be depended upon.

REACTIONS TO THE AMERICAN LOAN

Chungking, December 20, 1938.

The public and official reaction to the American loan is very favorable and its effect on the morale is excellent. I had dinner with Mr. Sun Fo, head of the Legislative Yuan and Dr. Wang Chung-hui, Minister of Foreign Affairs, on Sunday evening. Both seemed pleased with the loan and the Foreign Minister was in an unusually happy mood. Chengtu papers announcing the loan also announced the possible loan from England for railway construction and the headline was worded "English and American Loans to China Are of Great Assistance". Editorials are very favorable to the loan and speak of it as of great political significance and importance to China because of the definite stand taken in favor of China and that it is a beginning which will lead to other concrete steps aiding China. A number of individuals have referred to the smallness of the loan but at the same time with the recognition of its significance.

INTERVIEW WITH DR. H. H. KUNG

Chungking, December 19, 1938.

Dr. Kung appeared satisfied with the progress of American loans. I mentioned to him the matter of the interest of Mr. Chen, the Commissioner of Reconstruction of Kansu, in credits for a railroad from Russia to Lanchow. Dr. Kung stated he had asked Mr. Chen to look into the matter but that it cannot be built now, and as for American investment in it, America has never yet built a railroad in China.

INTERVIEW WITH MR. HSU MO, VICE-MINISTER OF
FOREIGN AFFAIRS

Chungking, December 20, 1938.

"The loan from America is most welcome and while it is not great, it is of considerable political significance and is a beginning most probably of further aid. It will also lead England to follow suit. There was consideration being given to a change in our foreign policy as we had about given up hope of assistance from America and England and it was thought that we would have to follow the opinion of many and seek a closer alliance with Soviet Russia. Now it seems unnecessary to reconsider our foreign policy. We want increasing aid from America and England and with it, we can win the war; without it, we cannot.

"We are utterly disappointed with the attitude of the French Indo-China authorities. They have notified us that they must now enforce their decree of October 1937 prohibiting shipment not only of munitions but of all supplies for Chinese factories. This is in violation of all treaties with China. The order was issued to the French Indo-China authorities by the French Government with the admission that it was so done because of Japanese threats. They even admitted that the Japanese had occupied one of their small islands as a base. We have made representations but to no avail. They have even closed the port of Kwanchowwan to us for the same reason. The French are also raising some objection to British capital building a railroad from Suifu, Szechwan, to Kunming, on the

ground of previous rights. Examination of the old contracts leads to the conclusion that those rights have now expired.

"Of all the countries we have dealt with diplomatically, the Japanese are the worse and the French only second. ||

"Japanese will probably attack Sian next and if successful, it will deal a severe blow to us, even worse than Canton. It will threaten our base in Szechwan so that the capital may have to move again and it will cut our supplies from Russia."

Mr. Hsu Mo seemed to attach more influence to the Russians than I was able to discover in the Northwest. He also feels the Chinese communist influence is strong. This reflects in part, apparently, his own very anti-communist feeling.

THE KUNMING (YUNNANFU)-BURMA ROAD
(Interview with Mr. T. L. Soong, Manager of the South-
west Transportation Co.)

Chungking, December 20, 1938.

"I have just come from Rangoon with twenty trucks of munitions. It took eleven days from Rangoon to Kunming as I stopped along the way for inspection and consultation. The trip would be seven days without such stops. The road is good, and excellent in parts. The landslides will not cause much difficulty - much less than along the Yunnan Indo-China Railway, and can be easily cleared. I plan to build rest houses and to have missionary doctors at five or six stations for truck drivers, travellers and for the local populace. The agricultural and mineral resources are excellent and a railroad should prove an economic investment. There is one unfinished bridge at Waitung and a temporary bridge is being constructed for the passage of the Ambassador. I recommend that you wait until the bridge is completed after the first of the year. At that time we are sending a caravan of 400 trucks to Rangoon to take out exports and bring in supplies. You may go with this caravan, or with Mr. Ling, on his second trip. I am going over the new direct road from Szechwan to Kunming the end of this month. You can go with me if you wish." (I accepted the suggestion and Mr. Soong will let me know definitely within a few days.)

This road will save considerable time over the other one via Twelyang and I am glad to have an opportunity to go over it. It is supposed to be completed by the end of the month. Mr. Soong is pushing Dr. Kung and the Ministry of Communications to hurry up the railroad building in Southwest China.

TRANSPORTATION

(Interview with Mr. Chang Kia-ngau, Minister of Communications)

Chungking, December 20, 1938.

"I have now changed my profession from building and managing railroads to building and maintaining highways. However, we are pushing the building of the Yunnan-Burma Railway and the Yunnan-Szechwan Railway. We are trying to use rails from old railways to complete the railway from Kweilin to Liuchow in Kwangai. No attempt will be made at present to extend this line to Nanning to connect with the line from Indo-China. (on account of Japanese threat and probably on account of non-cooperation of French in transporting material. J.L.B.)

"Our attention is confined to building railroads in Southwest China as we consider this more important than to build railroads to the north into Kansu. We are not interested in a line connecting with the Russian railways as it is long and only opens with Russia rather than with an open port.

"It is more important to maintain the roads we have than to build new roads. We have just taken over the Kweichow provincial roads and will give attention to their maintenance. The Yunnan-Burma road has also been placed under the supervision of this Ministry. It is a fair road, but we are investing another million yuan to improve it and make it a first class road. Work to eliminate landslides is to be completed before the rainy season late next spring. I advise you to wait and go over the road after it is completed, especially since your Ambassador has just gone over it in its present condition.

I am going over it about the middle of February when the first stage of its completion will be finished, and I would like you to travel with me.

"We are organizing transportation by native methods - carrying and by carts over the Suifu, Szechwan -Kunming old road which we are improving for this purpose and over the new direct motor road from Luchow, Szechuan, to Kunming. (Coolies and cart transportation will be organized in stages with rest houses and food for men and with doctors and veterinarians. J.L.B.)

"P. W. Tsou of the Foreign Trade Commission tells me it is my job to see that the American loan is repaid." (There is every evidence that this Ministry and the Foreign Trade Commission are on their toes to get the products out. J.L.B.)

"I was the last of my staff to leave Hankow. When the Changsha trouble occurred, I flew there and urged the staff to remain. I do this to keep up the morale. I encourage them not to become downhearted but to take the trials as a challenge."

Minister Chang's secretary of General Affairs told me he is now faced with the problem of finding employment for 50,000 railroad staff thrown out of work. Many of them will be transferred to highway management of transportation.

FOREIGN EXCHANGE AND CURRENCY SITUATION
(Interview with Dr. Arthur Young, Advisor to the Central Bank)

Chungking, December 21, 1938.

"With the fall of Hankow exchange weakened, but the talk of peace following, firmed the market so that we purchased back more than our sales. The exchange market has been steady and firm and is in a good technical position, although we need a larger stabilization fund."

Dr. Young showed me a message just prepared to be sent by Dr. Kung to the American, British and French governments urging them to assist the Chinese government by all means to prevent expected revived attempts on the part of the Japanese in the occupied areas to force their new currency on the people.

I have been informed by an official that Japanese are now depositing their personal funds in Chinese banks in Shanghai as they fear confiscation by Japan later, especially after the war.

SOME GENERAL OBSERVATIONS

Chungking, December 20, 1938.

One hears of a great deal of dissatisfaction with the Kuomintang because there are so many people in it who have little real ability and who are often more interested in their "rice bowl" than in anything else. The Youth Movement of the Kuomintang has been started in order to offset the trend of the young towards the communist areas, but apparently the people in charge of this movement do not have the qualifications to give it the practical direction which is needed for its success. Students who attended the summer military training classes have returned greatly dissatisfied because of the inadequate training received. The difficulty apparently is one of qualified officers to train the large number of students. The matter of thorough training in all types of activities is of first importance in China and the absence of it is all too evident.

A representative of the Central Aircraft tells me of the bombers they repaired only to have them smashed by incompetent pilots after a few hours or less of flying. In other words, apparently the pilots are given responsibility of flying these bombers before they are sufficiently trained. All the B-17 bombers shipped over a year ago were almost immediately smashed up. These are now being repaired at Chengtu and at least three or four were again smashed immediately after being put into use. Of course, it is inevitable that accidents should occur but it

seems to be the general opinion of trained observers that attention needs to be given to the thoroughness of training.

There seems to be much less interest in the possibility of peace than early in November. The talk about the necessity of much closer co-operation with Russia has also subsided somewhat.

Chungking, December 20, 1938.

The type of co-operation extended by Curtiss Wright with China through the Central Aircraft Company is a good illustration of how American industrial enterprises can invest in China for the purpose of helping China develop industries and at the same time obtain reasonable profits. Some Chinese have expressed to me the importance of American enterprises taking the initiative in negotiating for industrial opportunities in China rather than waiting for China to initiate such enterprises. The statement was made that such type of co-operation would be welcomed by the Chinese and that Americans should not hesitate to push the idea. I have talked with an American in the Central Aircraft representing Curtiss Wright who states that he believes out of his experience that this type of co-operation is essential for industrial development in China and that it is one way by which Chinese can be given thorough and practical technical training to carry on the enterprises themselves.

SECRET
REF ID: A66542

December 23, 1938.

MEMORANDUM FOR THE PRESIDENT
Submitted through the Secretary of the Treasury.

The second meeting of the Committee on Purchases of Blind-made products, created by the Act of June 23, 1938, (Pub. No. 739, 75th Cong.) was held in the office of the Director of Procurement on December 21, 1938, with the following members present:

- W. C. Mical, representing the American Foundation for the Blind, New York City.
- Augustus B. Warfield, representing the Department of War
- Arthur E. Mayo, representing the Department of the Navy
- Maurice I. Tynan, representing the Department of the Interior
- Alex McC. Ashley, representing the Department of Agriculture
- Fletcher H. Davis, representing the Department of Commerce
- Christina Joy Peoples, Chairman, representing the Department of the Treasury

There were also present Major H. Feldman, Assistant to General Warfield; W. B. Irwin, Executive Director, American Foundation for the Blind; C. C. Kleber, General Manager, National Industries for the Blind; Peter J. Salmon, Technical Advisor to Mr. Mical, and Robert LeFevre, Secretary to the Committee.

At this meeting General Warfield presented a draft of the regulations prepared by the sub-committee that was appointed at the initial meeting. These were discussed and after adoption of two amendments offered by Captain Mayo, were approved.

There were also presented suggested prices and related data to apply to corn brooms and cotton mops, the two items which the National Industries for the Blind propose for purchase from agencies for the blind. After discussion prices for the various sizes of these two items were agreed upon.

The regulations and the prices appear in the attached schedule which has been issued to ordering offices.

The meeting was adjourned with the understanding that future meetings would be held upon call by the Chairman.

C. J. Peoples,
Director of Procurement.

cc/L
Inclosure.

SCHEDULE OF BLIND-MADE PRODUCTS

JANUARY 1, 1939

Prepared under the direction of
COMMITTEE ON PURCHASES OF
BLIND-MADE PRODUCTS

Issued by
TREASURY DEPARTMENT
PROCUREMENT DIVISION
BRANCH OF SUPPLY
WASHINGTON, D. C.

Committee on Purchases of Blind-made Products

Chairman

Christian Joy Peoples, representing the Department of the Treasury

M. C. Migei, representing the American Foundation for the Blind

Augustus B. Warfield, representing the Department of War

Arthur H. Mayo, representing the Department of the Navy

Maurice I. Tynan, representing the Department of the Interior

Alex McC. Ashley, representing the Department of Agriculture

Fletcher H. Hawis, representing the Department of Commerce

Robert LeFevre, Secretary.

REGULATIONS PRESCRIBED BY THE COMMITTEE ON PURCHASES OF BLIND-MADE PRODUCTS

The following Rules and Regulations are prescribed for carrying into effect the Act of June 25, 1938, 52 Stat. 1408 (U.S.C. Title 41, Sec. 41-43), which provides as follows:

"Sec. 1. It enacted by the Senate and House of Representatives of the United States of America in Congress assembled, that there is hereby created a Committee to be known as the Committee on Purchases of Blind-made Products (hereinafter referred to as the "Committee") to be composed of a private citizen convenient with the problems incident to the employment of the blind and a representative of each of the following Government Departments, the War Department, the Navy Department, the Treasury Department, the Department of Agriculture, the Department of Commerce, and the Department of the Interior. The members of the Committee shall be appointed by the President, shall serve without additional compensation, and shall designate one of their number to be chairman.

"Sec. 2. It shall be the duty of the Committee to determine the fair market price of all brooms and mops and other outdoor commodities manufactured by the blind and offered for sale to the Federal Government by any non-profit-making agency for the blind organized under the laws of the United States or of any State, to revise such prices from time to time in accordance with changing market conditions, and to make such rules and regulations regarding such commodities, time of delivery, authorization of a central non-profit-making agency to facilitate the distribution of orders among the agencies for the blind, and other relevant matters of procedure as shall be necessary to carry out the purposes of this Act. Provided, that no change in price shall become effective prior to the expiration of fifteen days from the date on which such change is made by the Committee.

"Sec. 3. All brooms and mops and other outdoor commodities heretofore produced in accordance with applicable Federal Specifications by or for any Federal Department or Agency shall be produced from such non-profit-making agencies for the blind in all cases where such articles are available within the period specified in the price determined by the Committee to be the fair market price for the article or articles so produced. Provided, that this Act shall not apply in any case where brooms and mops are available for procurement from any Federal Department or Agency and procurement therefrom is required under the provisions of any law in effect on the date of enactment of this Act, or in cases where brooms and mops are produced for an outside Federal United States."

1. (a) The National Industries for the Blind hereinafter referred to as "National Industries" is designated as the agency to facilitate the distribution of orders among the agencies for the blind.

(b) The Procurement Division, Treasury Department, is designated to consolidate purchases by the Federal Government of the Blind-made products specified by the Committee on Purchases of Blind-made Products hereinafter referred to as the "Committee".

2. The Committee will issue schedules, through the Procurement Division, to all Departments and agencies of the Federal Government hereinafter referred to as "ordering offices", setting forth details as to descriptions of blind-made commodities to be purchased by ordering offices in accordance with said Act, including the amounts determined by the Committee to be the fair market price thereof, time of delivery, applicable Federal Specifications, etc. These schedules will be revised from time to time, the effective date of any changes in price to be indicated in such revised schedules.

3. Any ordering office receiving any commodity which is listed in said schedule (or was within the Continental limits of the United States), shall transmit a request for allocation covering its requirements to the Procurement Division. These requests for allocation shall be addressed to:

Committee on Purchases of Blind-made Products,
Procurement Division, Treasury Department,
400 and 5th Streets, N.E.,
Washington, D. C.

4. (a) The Procurement Division will advise all necessary agencies from Federal Prison Industries, Inc., and hereafter provided that the request for allocation to National Industries, provided that in the schedule of the Procurement Division, any item listed in the schedule of blind-made products may be subject to clearance by Federal Prison Industries, Inc., be handled by the Procurement Division as a stock item for delivery to ordering offices in Washington, D. C., at the schedule price plus any applicable Procurement Division charges.

(b) National Industries will maintain a record of all non-profit-making agencies for the blind organized under the laws of the United States or of any State, and statistical data showing their respective monthly production of the commodities specified in the schedule of blind-made products available for sale to the Federal Government, so that there may be equitably distributed among such agencies.

(c) Each request for allocation shall bear the stamp of approval of the Procurement Division showing that it was there the required action with respect thereto, and any request for allocation received by National Industries without such stamp of approval shall be forwarded to the Procurement Division for approval of the allocation.

(d) National Industries shall determine, immediately upon receipt of such request for allocation, whether any agency for the blind is in a position to furnish the requirements, and if not, it shall promptly refer the request directly to the ordering office with notice in that effect, transmitting to the Procurement Division a copy of such notice. The said notice shall constitute a clearance to the ordering office to effect the purchase elsewhere.

(e) As soon as National Industries determine which agency for the blind is to furnish the requirements, it will furnish the ordering office the name and address of the agency. The ordering office will, thereupon, issue a purchase order to said agency, forwarding copies thereof to National Industries and the Procurement Division.

(f) The Procurement Division may give any ordering office such clearance as may be necessary to effect the prompt procurement of material in short emergency needs.

5. Items for which orders for blind-made products will be transmitted by the agencies for the blind, as directed by the ordering office, and if the regulations of a particular ordering office require the use of vouchers, such vouchers will be transmitted by such ordering office directly to said agencies for completion by such agencies to the ordering office. Each item shall be submitted in triplicate and the original copy shall be held by the ordering office. An authorized representative of the particular agency for the blind, whose orders are filled from stock of the Procurement Division for delivery to ordering offices in Washington, the Procurement Division will accompany the shipments.

6. Payments will be made by the ordering offices to the Procurement Division on stock items delivered in Washington, and directly to the agencies for the blind in all other cases.

7. No commodity shall be delivered by any agency for the blind, under a purchase order issued by any ordering office, unless at least 75% (or other percentage with respect to a particular item that may be specified in the schedule of blind-made products) of the direct labor of production of such commodity shall have been performed by the blind; and unless the agency for the blind offering such commodity shall have produced it for private sale for at least six months prior to the receipt of such an order. Each certified invoice shall contain a certificate duly executed by an authorized representative of the agency for the blind showing that such agency is a non-profit-making organization; that the percentage of direct labor of production by the blind is within the prescribed limit for the particular commodity, and that such agency has produced the commodity for private sale for the said six month period.

8. Beginning April 1, 1939, National Industries shall furnish to the Procurement Division quarterly reports of Government purchases of blind-made products, showing all transactions concluded prior to the fifteenth day of the previous calendar month. These reports will include a list of all purchase orders filled, with the quantity, shipping and delivery points, and price received under each order. The Procurement Division will then submit these reports to the Committee with any recommendations it may deem appropriate with respect to the fair market price of any article or articles contained in the schedule of blind-made products.

9. (a) "Non-profit-making agencies for the Blind" shall mean any institutions operated in the interest of blind persons, the net income of which institutions does not inure in whole or in part to the benefit of shareholders or individuals, as evidenced by affidavits which shall have been filed with National Industries establishing such status.

(b) "Ordering office" shall mean any executive department, independent establishment, board, commission, bureau, agency, or division of the United States, and any corporation, all the stock of which is beneficially owned by the United States.

10. These rules and regulations shall be effective on and after the date of approval by the Committee; provided, however, that the Committee may, subject to the provisions of said Act, amend these regulations from time to time. Notice of any such amendment and the effective date thereof will be given to ordering offices through the Procurement Division.

APPROVED BY THE COMMITTEE

December 31, 1938.

C. J. Forster
Chairman

Procedure for purchase

Prior to placing orders, departments and establishments will forward requests for allocation to

Committee on Purchases of Blind-made Products
Procurement Division, Treasury Department
7th and D Streets, SW.
Washington, D. C.

Requirements will be immediately allocated by the National Industries for the Blind and the ordering office notified of the name and location of the agency or agencies designated to manufacture the material. Purchase order and bills of lading should then be prepared and forwarded direct to the designated agency, forwarding copies of the order to the Committee on Purchases of Blind-made Products and the National Industries for the Blind.

Orders for delivery in Washington will continue to be placed with the Procurement Division as heretofore for filling from stock maintained in the Procurement Division Building.

ITEM NO.	ARTICLE	QTY	PRICE PER UNIT
	Brooms, corn; shall be in accordance with Federal Specification No. BB 51 Amendment 3:		
36-B-100	28 pounds to dozen	dozen	\$1.17
36-B-105	32 pounds to dozen	dozen	1.80
36-B-110	36 pounds to dozen	dozen	5.34
	Mops, cotton; shall be in accordance with Federal Specification No. TM 561A:		
36-M-162	12 pounds to dozen	dozen	2.64
36-M-165	15 pounds to dozen	dozen	3.70
36-M-170	20 pounds to dozen	dozen	5.40
36-M-175	24 pounds to dozen	dozen	5.28

Above prices are f.o.b. cars at point of manufacture for shipment on government bill of lading.
The point of manufacture will be the location of the particular agency for the blind to which an order is allocated.

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 22, 1938, 9 a.m.

NO.: 2146

Re telegram No. 870 of November 19 from the Department and telegram No. 1966 of November 21 from the Embassy; Cochran has returned and this morning he resumed his duties in the Embassy.

WILSON.

EA:LWW

JR

GRAY

London

Dated December 22, 1938

Rec'd 1:22 p.m.

Secretary of State,
Washington.

1460, December 22, 4 p.m.

FOR TREASURY FROM BUTTERWORTH.

I arrived last evening.

It may be noteworthy that the market has now become aware of the action taken by the British authorities as indicated in the following excerpt from yesterday's press.

"Very few operators who had bought gold forward three months ago are taking up the metal because London banks are again showing great diffidence in advancing money against gold. This is partly because of the approach of the end of the year and the increasing seasonal stringency of credit.

An even more important factor however is the request which was made to the London banks a short while ago by the Bank of England to discourage loans against gold. A complete ban on these loans has not been reimposed but the familiar 'request' has been made".

JOHNSON

RR:CSB

REB

Yunnanfu via Hong Kong & N.R.

Dated December 22, 1938

Rec'd 1:29 p. m. 23rd

Secretary of State,
Washington.

13, December 22, 1 p. m.

Local reaction to American Commercial credits loan to China has been universally favorable. Comment is usually to the effect that the amount of the loan is immaterial; it is the sentiment behind the loan that makes it important. In an article in one of the local Chinese newspapers neighbor Hsu Po Yuan manager of the Yunnanfu branch of the bank of Communications materialization of world sympathy for China, and it is the result of China's efforts in continuation of the war for the past 17 months. He stated that one of the indirect results would be the strengthening of China's currency and that China should be solemnly confident now in the ultimate defeat of Japan. The recent British and American loans indicate absolute confidence on the part of those countries in the soundness of China's economic structure. The soundness of the loans indicates that their attitude towards China is identical. This

REB

2-#13, From Yunnanfu, Dec.22,1p.m.

This is representative of the local reaction to both the
British and American loans.

Copy to Chungking by air mail.

Repeated to Peiping.

MEYER

CSB

REB

PLAIN

London

Dated December 22, 1938

Rec'd 4:35 p. m.

Secretary of State,
Washington.

1462, December 22, 6 p. m.

FOR TREASURY FROM BUTTERWORTH.

One. Although I am of course unable at the present time to report on the general economic situation in Great Britain I feel I should record in connection with the significant effect of the armament program on the trade position last night's announcement by Sir John Anderson that the British Government is to place orders for light steel for air raid shelters amounting to £20,000,000. When to this sum is added the cost of the requisite labor and other materials the total resultant employment will be very considerable. The plate section of the steel industry in which unemployment is relatively heavy because it has so far been little affected by the armament program will be the main beneficiary.

Two. The exchange market was quiet. The dollar opening at 4.66-1/2 bid until fixing when the rate was 4.66-5/8, 97 bars were sold, 47 being married and the remainder

REB

2-#1462, From London, Dec.22,6p.m.

remainder supplied by the British fund. The price of 149 shillings gave a premium of $1/2$ pence. When the New York market came in, dollars were offered around 4.66- $3/4$ and towards the close the rate went to 4.67.

The franc was steady around 177 $1/8$ and bid until rumors that the French Government had received only a small majority on one of its decrees at which time the franc became offered and the rate went to 3/16.

JOHNSON

NPL

RECEIVED

DEC 23 1917

RECEIVED - AMERICAN

RECEIVED - AMERICAN

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 22, 1938, 8 p.m.

NO.: 2153

FROM COCHRAN.

At 5:00 p.m. I visited at the Bank of France, where I learned that this morning's exchange market was favorably affected by the speech which Reynaud made yesterday before the Chamber in defense of his reconstruction program and in which he pointed out the improvements which had resulted therefrom. The French stabilization fund by noon had acquired about £ 1,600,000. When it became known that the Government won today's fight by the narrow majority of seven votes on the 2 percent tax in the financial program, there was a reaction for a time and 600,000 pounds were lost by the fund. This movement had quieted down by evening, however, and the market was again offering sterling on the belief that the severest test had been passed by the Government and its financial and budgetary legislation would shortly be completed. Therefore 1,000,000 pounds was the net gain for the day.

This morning at the opening of business the French stabilization fund contained gold in the amount of 11,585,000,000 francs. If it had not been for the severe set-back suffered on the twelfth of December, when about

- 2 -

400,000,000 francs were lost, the amount now in the fund would have been approximately 12,000,000,000 francs. Thus the stabilization fund is in good condition. The outlook is promising for further gradual augmentation of the resources of the fund through some short covering but to a larger desired result through actual capital repatriation made more confident by the program of the Premier and the Finance Minister and anxious to take advantage of the rise which French securities are experiencing.

The French fund, I was told, used the dollar proceeds of the 8,000,000 dollars worth of gold sold from New York a few days ago to buy sterling. The idea was to help check the decline of sterling, and it is said that the British officials warmly appreciated the move. I am informed that the French took this action despite their desire to keep intact and even augment possibly by further shipments soon the supply of gold which is held in the United States. The officials who have charge of the French fund are anxious to see sterling firmer. With this purpose in mind they are to some extent trying to divert sales of dollars on this market to London. The fund at the same time is buying dollars for the purpose of meeting its own requirements on future contracts therein. In addition to the sterling mentioned above, it thus acquired today 600,000 dollars. Yesterday

- 3 -

Cobbold, of the Bank of England, was here in Paris conferring with officials of the Bank of France regarding the exchange situation, and it was reported that he was somewhat defected(defeated?). I was told he telephoned me, but I had not yet arrived here.

END SECTIONS ONE, TWO
AND THREE.

WILSON.

EA:LWW

PARAPHRASE, SECTION FOUR, TELEGRAM NO. 2153 OF
DECEMBER 22, 1938, FROM PARIS.

I am told that at the meeting last week of directors of the Bank for International Settlements, the Governors of the Belgian, Swiss and Dutch National Banks had confidential talks of their worries over sterling. It is said they even intimated among themselves that they might permit their currencies to be based on sterling if the rate should go lower, or even perhaps if in a reasonable length of time the present level should not be improved. This possibility is the result of economic consequences of the depreciation of sterling rather than the result of any criticism of recent management of the British equalization fund. It was suggested when I was in Washington that upon my return to Europe I might visit the three central banks above mentioned. It might be advisable for me to make these calls during the first week in January, particularly in view of the above report. I shall immediately try to make the required arrangements if telegraphic instructions to this end are forthcoming.

END OF MESSAGE.

WILSON.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 22, 1938

TO Secretary Morgenthau
FROM Mr. White
SUBJECT: Recent trends in our foreign trade.

SUMMARY

(1) Our balance of trade of almost \$1 billion for the first ten months of 1938 is the highest favorable balance this country has had since 1921. This exceptionally large favorable balance of trade during this year is due to the partial maintenance of the gain in exports achieved during 1937, while at the same time our imports dropped to the depression level of 1934.

(2) In the past few months our exports have been increasing (the low point was reached in July 1938), but the increase is less than seasonal. The trend of our exports has been downward throughout the whole of the year 1938, but the decline has not wiped out the increases achieved. A lower level of exports this year compared with last year has also been true of the exports of the leading countries of the world with the exception of France and Switzerland.

(3) Our exports to Europe and South America have been maintained better than our exports to other continents, while our exports to Africa and Asia show the most substantial declines. Since July, however, our exports to South America have declined sharply from the 1937 levels, but that is due to the fact that our 1937 levels were so high.

(4) Our exports of agricultural products during this year were \$100 million greater than last year, while our exports of non-agricultural products decreased by \$220 million. The increase in exports was spread throughout the list of agricultural products, but the major changes were an increased exports of grains of \$145 million, while our cotton exports declined by \$100 million. Of the non-agricultural commodities, the largest declines were for automobiles and iron and steel products which accounted for a loss of \$150 million. The largest increase occurred in the export of aircraft which doubled from \$30 million in 1937 to \$60 million in 1938.

Secretary Morgenthau - 2

(5) Our imports were \$1 billion less during the first ten months of 1938 compared with the same period in 1937. We reduced our imports from all major countries of the world with the exception of the Union of South Africa and the Netherlands West Indies. Canada lost \$133 million in sales to us in 1938 compared with 1937. Imports from British Malaya declined \$100 million, Argentina \$95 million; imports from the United Kingdom declined \$80 million, and from Japan \$75 million.

(6) Our import of agricultural commodities dropped by \$600 million out of the total decline of \$1 billion. The chief agricultural products which were reduced were grains, unmanufactured wool, hides and skins, and coconuts. The chief non-agricultural items which were greatly reduced were tin, furs, and diamonds. Unmanufactured tobacco was the only major item of import which was increased in 1938 as against 1937.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 21, 1938

TO Secretary Morgenthau - 3
 FROM Mr. White
 Subject: Recent trends in our foreign trade.

(1) Our balance of trade for 1938 promises to be the greatest we have had since 1921.

For the first ten months of 1938 our excess of exports over imports totals about \$1 billion. This excess has been large notwithstanding a substantially lower level of exports this year than last year. (Last year's favorable balance of trade for the first ten months was only \$60 million.) The explanation for our large excess of exports has been the drastic decline in our imports we have experienced this year. Our imports during this year have dropped to the depression level of 1934.

(2) Our exports have been increasing since July but the increase has been less than seasonal.

	Exports 1938
January	289
February	263
March	276
April	274
May	257
June	233
July	228
August	231
September	246
October	278
November	
December	

Secretary Morgenthau - 4

The quarterly totals below show the declining trend in 1938.

	1937 (In millions of dollars)	1938
1st quarter	713	828
2nd quarter	824	764
3rd quarter	843	705
4th quarter	968	785 (est.)
October	333	
November	320	
December	315	

Our fourth quarter exports will show, we estimate, about a 13 percent increase over the third quarter. This increase is somewhat less than the seasonal increases taking place in the past few years.

(3) The level of our exports is less than last year's not that is true of all the leading countries except France and Switzerland.

Exports of Leading Countries
Percentage Change 1938 from 1937

	<u>January through October</u>	<u>October</u>
France	+ 26.2	+ 19.7
Switzerland	+ 2.7	+ 11.8
<u>United States</u>	- 5.1	- 16.5
Sweden	- 6.8	- 17.8
Germany	- 8.8	- 14.2
Netherlands	- 9.3	- 10.5
United Kingdom	- 11.4	- 9.5
Canada	- 13.0	- 7.4
Japan	- 18.8	- 8.1
Argentina	- 43.1	- 26.6

If, however, we compare the last month alone instead of the whole ten months, the decrease in this year's exports as compared with last year is greater for the United States than for all the leading countries except Sweden and Argentina. The explanation is not so much that all exports are now falling as it is that exports rose very sharply last fall.

The downward trend in value of total exports began about May, but the physical volume has been downward from the beginning of the year. The physical volume is now about one-fourth lower than last October.

(4) Our exports to Europe and South America have kept up better than to any other continent for the ten months of 1938, while our exports to Africa and Asia show substantial declines.

Since July, however, our exports to South America have fallen off sharply from the level of exports in the same month of 1937.

Percentage Change in 1938 over 1937

	<u>January through October</u>	<u>July through October</u>
Total United States exports	- 5%	- 17%
Europe	- 4	- 9
South America	- 3	- 24
Oceania	- 3	- 17
North America	- 11	- 19
Asia	- 13	- 20
Africa	- 23	- 35

(a) Our exports to the following important European countries have increased this year.

	<u>Percentage change January through October</u>
Ireland	235%
Spain	152
Czechoslovakia	134
U. S. S. R.	83
Greece	50
Denmark	48
Netherlands	8
United Kingdom	6
Sweden	2

Secretary Morgenthau - 6

(b) Our exports to the following European countries are lower this year than last.

	<u>Percentage change</u> <u>January through October</u>
Germany (including Austria)	- 12%
Belgium	- 15
France	- 16
Portugal	- 20
Italy	- 25

(c) Latin American countries to which United States exports have increased this year over 1937:

	<u>Percentage increase</u>
Venezuela	13%
Chile	8

(d) Latin American countries to which United States exports have declined this year from 1937:

	<u>Percentage decline</u>
Uruguay	- 58%
Mexico	- 44
Cuba	- 16
Brazil	- 7
Peru	- 5
Argentina	- 4
Colombia	- 2

(e) Some other countries to which United States exports have increased this year over 1937:

	<u>Percentage increase</u>
Hong Kong	49%
Kwantung	45
Turkey	3
Netherland Indies	9

(f) Some other countries to which United States exports have declined this year over 1937:

	Percentage decline
China	- 36
Japan	- 34
Union of South Africa	- 21
British India	- 7
Canada	- 3
Philippine Islands	- 3
Australia	- 1

(5) Exports of agricultural items increased by 15 percent in 1938, but exports of non-agricultural items decreased by 10 percent.

Our cotton exports declined by \$100 million while our total exports declined \$130 million in the first ten months of 1938. Exports of all other agricultural products increased by almost \$200 million over the previous year, of which the increased export of grains accounted for \$16 million.

Non-agricultural commodities decreased by \$220 million compared with last year, or 10 percent. The items with the largest declines were automobiles, and iron and steel products, which declined a total of \$150 million. The largest increase occurred in the exports of aircraft which rose from \$30 million in 1937 to \$60 million in 1938.

(6) Imports from all countries were \$1 billion less for the first ten months of 1938 than for the first ten months of 1937.

Canada led the list with a reduction of \$133 million in sales to us in 1938 compared with 1937. Our imports from Cuba declined \$36 million. In South America, the country of largest decline was Argentina, losing \$95 million in the first ten months, out of a total reduction of imports from South America of \$160 million.

Imports from Asia declined \$350 million, or 43 percent, and imports from Europe declined \$260 million, or 36 percent. In Asia, British Malaya alone lost \$100 million in sales to us; Japan lost \$75 million, and China \$55 million. In Europe, the United Kingdom lost \$80 million in sales to us, Belgium \$34 million, Germany \$30 million and France \$20 million.

Secretary Morgenthau - 8

Our imports increased from only two major countries in the world, the Union of South Africa and the Netherlands West Indies.

United States imported from	Percentage decline in imports January - October 1938 com- pared with 1937
Australia	- 84%
Argentina	- 75
New Zealand	- 74
Uruguay	- 69
China	- 59
Belgium	- 50
British Malaya	- 51
United Kingdom	- 47
Netherlands	- 45
Japan	- 43
Chile	- 42
India	- 41
Netherland Indies	- 41
Canada	- 39
Germany	- 36
France	- 32
Sweden	- 25
Czechoslovakia	- 25
Brazil	- 22
Mexico	- 21
Cuba	- 21
Italy	- 12
Colombia	- 7
Netherlands West Indies	7 3
Union of South Africa	6

(7) Our imports of certain agricultural commodities practically disappeared, such as unmanufactured wool which dropped from \$91 million to \$16 million, hides and skins from \$63 million to \$22 million, grains from \$100 million to \$5 million, cocoa from \$48 million to \$18 million. Agricultural commodities as a whole accounted for a loss of \$600 million out of the \$1 billion decline. Of the non-agricultural commodities the most severe decline came in tin which declined from \$86 million to \$37 million, furs which declined from \$81 million to \$41 million. Unmanufactured tobacco was the only major class of imports which increased.

December 22, 1938

To: The Secretary
From: Mr. Hanes

I attach hereto a letter to Chairman Doughton from the Honorable James W. Morris, Assistant Attorney General, dated January 18, 1938. Chairman Doughton and Senator Harrison are extremely anxious to have a letter signed by you along these general lines for incorporation in the Codification of Internal Revenue Laws, which they hope to enact by resolution of Congress as absolute law.

The letter prepared for your signature by the General Counsel's office suggests that we recommend the codification be not passed as absolute law, but as *prima facie* evidence of the law. I discussed this matter with Mr. Oliphant and he feels that it would be a mistake to pass the codification as absolute law and he has written a clear-cut memorandum giving his reasons therefor. As I see it, knowing very little about legal matters, Herman's position makes good sense to me, but does not answer the practical question as to your position and mine should we decide to refuse them our active support by writing such a letter. I have been told repeatedly by Chairman Doughton that he is desirous of enacting this code into absolute law as one of the first steps of the new Congress, and further that this has been one of his long cherished ambitions. Had Herman not been taken suddenly ill this morning, I think he and I together could have straightened this matter out without worrying you with it, but as matters now stand it would seem to me to be a question of whether or not we wished to cast our lot with the Joint Committee in their effort or to let them go it alone and pass it without our support.

I find myself somewhat embarrassed by the conversations which took place between Ros Magill, Stam, and myself before I took over the duties of this office, in which I gathered the impression that Ros was sympathetic with the effort of the Joint Committee. I have left the matter in Ed Foley's hands to take up with you on Tuesday as Stan is extremely anxious to have your letter appear in the book and I believe December 27th is the deadline. Ed Foley has discussed this matter with Mr. Morris of the Department of Justice, who has been asked by the Joint Committee to bring his letter of January 18, 1938, down to date. Mr. Morris told Foley that he did not wish to take a position inconsistent with the one taken by the Department last year and I have advised Mr. Foley that in my opinion it would be a mistake for us to urge any different course upon the Department of Justice. I believe Mr. Foley indicated to Mr. Morris that the General Counsel's office were more favorable to *prima facie* rather than enactment into absolute law.

J. W. H.

December 22, 1938

To: The Secretary
From: Mr. Hanes

I have been informed further by Messrs. Foley and Wenchel that in discussing this matter over the telephone Mr. Morris told Mr. Wenchel that he would be willing to hold up his answer to the Joint Committee until the Secretary had made up his mind whether or not he would send such a letter. Since I do not believe we should be in the position of trying to get the Department of Justice to oppose the enactment of the Code, I have asked Mr. Wenchel to tell Mr. Morris that the Department of Justice should use their own best judgment in making an answer to the Joint Committee irrespective of the position which the Treasury may ultimately take.

J. W. H.

LETTER TO THE CHAIRMAN FROM JAMES W. MORRIS,
ASSISTANT ATTORNEY GENERAL

DEPARTMENT OF JUSTICE,
Washington, January 18, 1938.

Hon. R. I. DOUGHTON,
Chairman, Joint Committee on Internal Revenue Taxation,
Room 1336, House Office Building, Washington, D. C.

MY DEAR CONGRESSMAN DOUGHTON: I am in receipt of your letter of January 15, 1938, requesting the views of this office relative to the proposed codification of internal-revenue laws and the enactment of such codification into law. In your letter you quote the statement contained in the report of the subcommittee of the Committee on Ways and Means of January 14, 1938, dealing with this proposal.

The Tax Division of the Department of Justice, in the performance of its function of handling revenue litigation, has been impressed with the need of a codification of the revenue laws which will be recognized as the law rather than as being merely prima facie evidence thereof. We believe that much confusion exists by reason of the number of revenue acts, containing in many instances the same basic provisions, to which reference must be made in the handling of cases arising under the various acts. This confusion constitutes a burden for courts and counsel alike.

Also, several of these statutory provisions were amended by Executive order. Since the changes thus made have not appeared on the face of the statutes, it has been necessary to refer to the Executive order to ascertain the nature and extent of these changes. I am glad to see that this situation has been taken care of. It will also be helpful and lessen confusion.

It is the opinion of this office that the enactment of a codification of the revenue statutes will be a definite step toward clarity, certainty, and simplicity. Such a codification will bring the substantive and procedural provisions together and will be most helpful.

In doing this work I feel that the staff of the joint committee has made a valuable contribution to the tax law which will be a substantial aid to this division in the handling of litigation involving Federal Revenue.

Very truly yours,

JAMES W. MORRIS,
Assistant Attorney General.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

December 22, 1938

Dear Henry:

In accordance with my conversation with the President at Warm Springs and with reference to the subject of my memorandum, of which you have a copy, I have today sent to him through Mac a suggestion as to what he could say on the subject in his message. I doubt if he intends making any reference to it at this time but wanted him to have this suggestion before him for consideration.

For your own confidential information,
I am enclosing a copy.

Sincerely yours,

M. S. Eccles
M. S. Eccles,
Chairman.

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

Enclosure

BY HAND

Rehabilitation of the American banking system, which has been brought about since the declaration of the bank holiday by Presidential proclamation on March 6, 1933, has been a notable achievement in which both the Congress and the Executive can justly take pride. The proclamation has remained in effect but, in view of national recovery and of the great improvement in the condition of our banks, I feel that it would be appropriate to remove the restrictions of the bank holiday.

In considering the termination of the bank holiday, I would like to suggest that the Congress, through appropriate committees or through a joint committee specially named for that purpose, undertake a review of Federal banking statutes and a careful study of our banking system and of the agencies established by the Federal Government to supervise and regulate banking. Such a study will disclose what additional legislation may be desirable in order to strengthen still further the banking system, so that it will be fortified as completely as possible to meet changing economic conditions and to meet adequately the credit needs of commerce, agriculture and industry, while protecting the rights of bank depositors and the public interest.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE December 23, 1938

TO Secretary Morgenthau
FROM Mr. Taylor

When Bawley called on you yesterday he first read from a message which he had received for transmission to you, which took almost the identical position maintained by Bolton in his conversation with Knoke on the previous day, namely, that after the year-end squeeze had been terminated that the British Treasury anticipated considerable pressure on the pound and that they were not sure of their ability to resist a movement of major proportions, and that they had no specific plans directed towards dealing with the situation at cetera. You told Bawley that as a result of Bolton's message news of the the/situation which he described did not come to you as a complete surprise, and that whereas you had no specific suggestion to make, you wished to emphasize the fact that you would cooperate in any way possible with his Government in order to help meet the situation; that naturally his Government was in better position to determine what the specific measures might be. Bawley then stated that it might be necessary for the British Treasury to discuss the question with some one on the ground prior to communicating again with you after the holidays. You told him of Butterworth's arrival and suggested that they get in touch with Butterworth immediately as Butterworth could undoubtedly throw considerable light on the Treasury's attitude, as he had just spent several weeks reviewing various aspects of the situation here.

You then referred to your surprise as to the course of French developments and stated that it was extremely difficult to evaluate situations of

this character, that you had felt that the French position would probably deteriorate, whereas it appeared to be doing the opposite, and you rather implied that the British situation was not developing according to any logical pattern.

Bewley then spoke of a message about balance of trade positions which he would like to discuss with you later when you had more time. You indicated that Tuesday would be a good time to take this up.

W.F.

LMS

GRAY

London

Dated December 23, 1938

Rec'd 2:40 p. m.

Secretary of State,
Washington.

1464, December 23, 5 p. m.

FOR TREASURY FROM BUTTERWORTH.

From such cursory observations as I have been able to make since returning it is evident that sterling is tight and will probably continue so until the year end. The market is generally aware of the action taken by the British authorities with the joint stock banks both as regards gold and renewing three months' dollars swaps but is not entirely certain as to the Bank of England's motives. The recent prohibitions have not been fully effective inasmuch as some of the merchant banks, American banks and even bankrupted subsidiaries of the joint stock banks have been bidding for three months' sterling deposits. With a $2\frac{1}{2}$ cent spread between the spot and three months forward rate they could offer as much as $2\frac{1}{2}\%$ per annum and obtain the kudos of a new deposit. The ordinary prevailing rate

LMS 2-No. 1464, December 23, 5 p. m., from London

rate for three months money is 1-3/8.

In the circumstances the expectation seems fairly general that after the year end when window dressing is over and money normally cheaper sterling will weaken, and on a longer view I have thus far met no one who is a bull of sterling but of necessity my contacts have not yet been numerous.

The pound fluctuated within the range 4.66 $\frac{1}{2}$ -7/8 with the volume small. The steady flow of funds from London to Paris continues with the franc at 177.10. Gold was fixed at 148s 11d with reserves supplying all but 8 bars which were given by the British fund.

All markets in London will be closed on Tuesday as well as Monday.

JOHNSON

CSB

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Paris, France

DATE: December 23, 1938, 5 p.m.

NO.: 2159

FROM COCHRAN.

Early this morning the Chamber approved the 1939 budget in its first reading. The vote for it was 336 against 229. The budget of 66 billion francs as it goes to the Senate shows an estimated surplus of 26 and a half million francs; on December 27 the Senate will take the bill under consideration, and it seems possible that it will be passed by the end of the year without important changes.

This morning the exchange market here reacted favorably to the above vote. A good amount of sterling at around 177.10 was gained by the French stabilization fund. There was a turn in the market later, partly due possibly to concern over Italian denunciation of the Laval agreement of 1935. There was a sharp drop in rentes, and some sterling had to be yielded by the French control. Quieter situation this evening. This morning dollars were bought by Chase for the French control.

WILSON.

PARAPHRASE OF TELEGRAM SENT

TO: American Embassy, Paris, France

DATE: December 23, 1938, 4 p.m.

NO.: 960

Visits by Cochran to Central Banks of Belgium, the Netherlands and Switzerland are approved by Secretary Morgenthau; reference last sentence of telegram of December 22, 6 p.m., No. 2153, from the Embassy. If the Embassy perceives no objection, the Department is agreeable.

WELLES

ACTING.

EA:LWW

CONFIDENTIAL

AMERICAN CONSULATE

Rangoon, Burma, December 23, 1938.

STRICTLY CONFIDENTIAL

SUBJECT: Activities in behalf of China.

THE HONORABLE

THE SECRETARY OF STATE,
WASHINGTON.

SIR:

I have the honor to report that two representatives of the Central Aircraft Manufacturing Company (Curtiss-Wright) are now at the site selected for the proposed new aircraft factory near Panhkan, or Panghkan, just across the Burma frontier in China, about 70 miles southeast of the Irrawaddy River port of Bhamo. They are C. E. Hunter, an American official, and H. F. Gourlie, a British subject. They traveled from Rangoon by car, via Lashio, to inspect road conditions from Lashio to the connection with the new Chinese highway, and from that point through Muse and Namkhan in the direction of Bhamo. Any use by the company of the Chinese highway, or of the Burma railways, would involve transport over the roads inspected.

The Intercontinent Corporation, a subsidiary of the Central Aircraft Manufacturing Company organized in Hong Kong, is being registered here to carry on operations in Burma. Wallace Pawley, a brother of W. D. Pawley, president of the parent company, is in Rangoon to establish an office here, which will be required

-2-

required in connection with the entry at this port of equipment and materials, and the shipment of the supplies in transit through Burma. Equipment and materials formerly at Hankow and now at Hong Kong and Yunnanfu, and additional equipment and materials from the United States, will be brought in, and the first shipment of supplies is expected to reach here early in January.

Factory to be Permanent.

The representatives of the company assert that the new factory will be a permanent establishment, and will continue to be operated at the site selected regardless of the duration of the hostilities in China. In the event of the termination of hostilities, the manufacture of aircraft for commercial purposes, and for peace-time military purposes, will be carried on, they say, under arrangements with the Chinese Government. They indicate that the cost of the transfer of all equipment and materials to the new factory site will be borne by the Chinese Government. It is suggested that arrangements might be made for independent transport services on the Irrawaddy River from Rangoon to Bhamo under the Anglo-Chinese Agreement of 1894, which contains a clause permitting such a service by the Chinese or through Anglo-Chinese co-operation. The Irrawaddy Flotilla Company, Limited, a private British concern, now has a practical monopoly of river transport.

The Burma Government has announced its decision to grant a drawback of fifteen-sixteenths of the duty payable

-3-

payable on all goods passing through Burma in transit to China, and crossing the frontier from Miamo, or from Lashio over the new road. This is the same drawback as recently granted in connection with transit shipments of war materials for the Chinese Government.

Sales of American Trucks.

Mr. Dewey W. Smith, Vice President of the Studebaker Export Corporation, and Mr. Frank B. Appelbee, special representative of the Indian Division of the Chrysler Export Corporation, have been in Rangoon in connection with possible further sales of Studebaker and Dodge motor trucks to the Chinese Government. Mr. Appelbee has been making inquiries concerning the possibility of shipping boxed trucks through Burma in bond, without payment of any duty. Mr. Smith has reported that although the Southwest Transportation Company, of which T. L. Soong is the recognized head, has established an office in Rangoon, purchases by that organization are still made in Hong Kong. He has also reported that he sold 200 trucks to that organization in Hong Kong before coming to Rangoon. He has estimated that in point of numbers the several thousand American motor trucks in China rank as follows: Ford, Dodge, Studebaker, General Motors, White, others.

Bank of China Branch.

The Bank of China has leased ground-floor premises in Rander House, 55 Phayre Street, Rangoon, and will

open

-4-

open its local agency on January 3, 1939. The building is that in which the Consulate has quarters, and the premises leased are part of those formerly occupied by Dawson's Bank, an agricultural banking institution. It is said that agencies may be opened later at Mandalay, Rhemo, and Lashio.

Respectfully yours,

AUSTIN C. BRADY
Austin C. Brady
American Consul

Distribution:

Original and four copies to the Department;
Copy to Embassy, London;
Copy to Consulate General, Calcutta.

800

ACB/ama.

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1939

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WAR DEPARTMENT
WASHINGTON D C.

- 23 1238

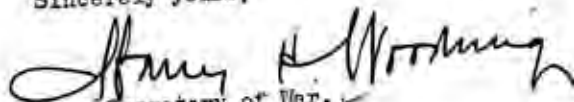
The Honorable,

The Secretary of the Treasury.

Dear Mr. Secretary:

Thank you for your kindness in making available to me the copy of a cable sent Mr. Chen by Dr. H. H. Kung on December 17. With reference to its last paragraph, the latest information at my disposal indicates that the Yunnan--Burma highway is still not practicable for large and systematic shipments of munitions to China.

Sincerely yours,


Secretary of War. ✓

REB

PLAIN

Shanghai via W. H.

Dated December 23, 1938

Rec'd 1:42 p. m.

Secretary of State,
Washington.

1493, December 23, 2 p. m.

In commenting editorially upon the Japanese Foreign Minister's latest statement regarding Japanese policy, the NORTH CHINA DAILY NEWS observed that "The Japanese Foreign Minister deceives himself if he believes for a moment that his latest statement concerning Japanese policy with regard to China carries any real conviction. His declaration consists of words rendered entirely meaningless by the facts which are all too well known, facts which eloquently deny the statements he makes". The paper continues "whatever may be the declared intention of the Japanese Government the facts show that they or their agents are bent upon a policy of definite exploitation of China, its people and its natural resources. Mr. Arita has signally failed to explain away any of the very real grievances which foreign neutrals have against his Government and his policy. He cannot hope for success in this direction until there has been a very decided change in Japanese behavior in China."

The

REB

2-#1493, From Shanghai, Dec. 23, 2p.m.

The SHANGHAI EVENING POST and MERCURY says "If Mr. Arita thinks that Britain and America recognize any right for a country other than China to dictate restrictions he deceives himself. Other powers have long recognized the right of China to have a free hand in governing herself and they have joined in treaties safeguarding such right -- treaties to which Japan has subscribed her signature."

The SHANGHAI TIMES, on the other hand, in referring to the statement asserts that "It is obviously the desire in Tokyo to remain on friendly terms with Washington and London but if any nations of the west are going to finance one side in this eastern quarrel against the other because of what they believe to be their own injury, it is as Mr. Arita said 'very dangerous' and might have far-reaching historic consequences". This paper asks "Can a policy of bolstering up a regime which has been driven out of east China best serve those interests without which such a show of protest is now being made."

Repeated to Chungking and Paiping, by mail to Tokyo.

GAUSS

CSB

17-7 3-18

Federal Surplus Commodities Corporation
Summary of Commodities Procured -
Fiscal Year 1938 and Fiscal Year 1939 to date

(Figures in thousands)

Commodity	Unit	Total fiscal year ended 6/30/38	Total 7/1/38 to 3/29/39	9/30/38 to 10/5/38	10/6/38 to 10/12/38	10/13/38 to 10/19/38	10/20/38 to 10/26/38	10/27/38 to 11/2/38	11/3/38 to 11/9/38	11/10/38 to 11/16/38	11/17/38 to 11/23/38	11/24/38 to 11/30/38	12/1/38 to 12/7/38	12/8/38 to 12/14/38	12/15/38 to 12/21/38	Total fiscal year 1939 to date	
Apples (Dried)	Pounds	14,557	-	-	-	-	-	-	-	-	-	-	-	-	-	548 (2)	
Apples (Fresh)	Bushels	5,625	-	3	110	195	166	70	1	-	-	-	-	-	-	80 (7)	
Apples (Dried)	Pounds	2,990	-	-	-	-	-	-	-	-	-	-	-	-	-	16,840 (1)	
Beans (Dried)	Pounds	56,800	-	-	-	-	-	-	-	-	-	3,430	5,360	2,670	4,380	38 (5)	
Beans (Snap)	Bushels	33	38	-	-	-	-	-	-	-	-	-	-	-	-	328 (6)	
Beets (Fresh)	Bushels	11	119	65	11	40	67	20	-	-	-	-	-	-	-	80 (7)	
Blackberries (Canned)	Cases	-	80	-	-	-	-	-	-	-	-	-	-	-	-	35,613 (8)	
Butter	Pounds	15,035	6,188	5,109	3,783	3,804	1,719	2,469	1,936	924	576	1,773	1,618	2,794	2,718	2,691 (9)	
Butter	Bushels	990	1,127	370	234	216	194	133	124	89	100	47	43	14	-	270 (10)	
Cane Syrup	Gallons	237	107	-	-	-	-	-	36	25	45	30	22	5	-	153 (11)	
Caryophyll	Bushels	-	101	6	1	16	17	5	1	2	1	2	1	-	-	21 (12)	
Carrots	Crate	-	21	-	-	-	-	-	-	-	-	-	-	-	-	163 (13)	
Celery	Bunches	1,174	178	-	-	-	-	-	-	-	-	-	-	-	-	- (15)	
Celery (Whole wheat)	Sacks	408	-	-	-	-	-	-	-	-	-	-	-	-	-	- (16)	
Cheese	Pounds	3,446	-	-	-	-	-	-	-	-	-	-	-	-	-	449 (17)	
Corn	Sacks	-	8	-	-	-	-	-	-	-	449	-	-	-	-	25 (18)	
Corn Meal	Barrels	-	10	-	-	-	-	15	28	15	16	-	250	-	20	526 (19)	
Cotton	Bales	-	-	-	-	-	-	30	-	-	-	-	-	-	-	650 (20)	
Cotton Fabric	Yards	1,133	147	-	-	-	-	-	-	-	-	-	-	-	-	- (21)	
Cotton Mesh Bags	Bags	-	-	-	-	-	-	-	-	-	-	-	-	-	-	- (22)	
Cottonseed Oil	Pounds	9,780	-	-	-	-	-	-	-	-	-	-	-	-	-	- (23)	
Cotton (Shell)	Cases	270	-	-	-	-	-	-	-	-	-	-	-	-	-	273 (24)	
Flax	Pounds	3,677	-	-	-	-	-	-	-	-	-	-	-	-	9	9 (25)	
Flour	Barrels	2,699	279	-	-	-	-	-	-	-	-	-	-	-	-	- (26)	
Grapefruit	Boxes	401	-	-	-	-	-	-	-	-	-	-	-	-	75	1,303 (27)	
Grapefruit Juices	Cases	552	471	-	-	214	-	-	227	132	-	55	-	-	-	15,560 (28)	
Grapes	Tons	8	-	-	-	-	-	-	-	-	-	-	-	-	-	2,550 (29)	
Labels	Labels	-	15,560	-	-	-	-	-	-	-	-	-	-	-	-	8,961 (30)	
Latexes Ticking	Yards	-	2,550	-	-	-	-	-	-	-	-	-	-	-	-	- (31)	
Wine (Dry skin)	Pounds	21,520	8,961	-	-	-	-	-	-	-	-	-	-	-	-	40,453 (32)	
Milk (Fluid)	Quarts	12,497	6,672	534	551	580	631	652	2,947	4,823	3,042	4,559	4,107	5,185	6,170	979 (33)	
Onions	Pounds	3,000	674	76	153	74	44	35	12	-	-	-	-	-	-	531 (34)	
Oranges	Boxes	1,932	639	54	47	-	-	-	-	-	-	-	-	-	-	9,075 (35)	
Paper Bags	Bags	21,825	9,075	-	-	-	-	-	-	-	-	-	-	-	-	11,100 (36)	
Peaches (Dried)	Pounds	2,534	3,523	-	4,791	1,873	913	-	-	-	-	-	-	-	-	6 (37)	
Peaches (Fresh)	Bushels	8	-	-	-	-	-	-	-	11	1	-	-	-	-	286 (38)	
Pears (Fresh)	Boxes	318	229	-	-	-	-	-	-	-	-	-	-	-	-	3 (39)	
Pears (Canned)	Cases	862	-	-	-	-	-	-	-	-	-	-	-	-	-	- (40)	
Pears (Dried)	Pounds	6,000	-	-	-	-	-	-	-	-	-	-	-	-	-	- (41)	
Pears (Fresh)	Bushels	-	3	-	-	-	-	-	-	-	-	-	-	-	-	378 (42)	
Potatoes (Sweet)	Bushels	440	-	-	204	122	36	8	-	-	-	-	-	-	-	2,367 (43)	
Potatoes (White)	Bushels	4,315	2,069	232	45	19	-	-	-	-	-	-	-	-	-	- (44)	
Potato Starch & Flour	Pounds	2,562	-	-	-	-	-	-	-	-	-	-	-	-	-	13 (45)	
Prunes (Dried)	Tons	55	13	-	-	-	-	-	-	-	-	-	-	-	-	11 (46)	
Prunes (Fresh)	Bushels	-	-	-	-	-	-	-	-	-	-	-	-	-	-	- (47)	
Raisins	Tons	15	11	-	-	-	-	-	-	-	-	-	-	-	-	678 (48)	
Rice (Milled)	Pounds	73,190	-	-	-	-	-	-	-	-	-	-	-	-	-	145 (49)	
Tobacco	Cases	3,500	145	-	-	-	-	-	-	-	-	-	-	-	-	114 (50)	
Tomatoes (Canned)	Bushels	50	114	-	-	-	-	-	-	-	-	-	-	-	-	- (51)	
Tomatoes (Fresh)	Bushels	282	-	-	-	-	-	-	-	-	-	-	-	-	-	- (52)	

December 23, 1938

December 23, 1938.

Treasury Department, Division of Research and Statistics.

* Weekly figures reported by Federal Surplus Commodities Corporation are based on telegraphic reports and are unrevised.
Fiscal year 1938 totals have been revised to include all contract cancellations and other adjustments.

Regraded Unclassified



HEADQUARTERS

146
RECEIVED THE COMMANDANT OF U. S. COAST GUARD
AND FERRY TO BE

TREASURY DEPARTMENT

UNITED STATES COAST GUARD

WASHINGTON 23 December, 1938.

From: Spagent, Hongkong, China.
To : Secretary of the Treasury.

Message from Professor Buck.

Foreign and Chinese visitors to northwest provinces only allowed by official permit as Russians desire secrecy and Chinese want control extension Chinese Soviet influence. Chinese here welcome Russian help but not her political faith and Russian Aviation Corps kept in supervised guest houses. Russians feel China not giving enough in return. Average number of Russians in Lanchow one hundred forty and six guest houses gives credence to this number. Russians only allowed to trade with Chinese government. Kuomintang three months political schools, Kansu, have trained twentyfive hundred teacher students. Generalissimo's blue shirt organization very active here. Kansu is battlefield of political faiths with Kuomintang apparently well in lead. Commissioner, Kansu Foreign Affairs, states that the former plottings of the British turned Governor of Sinkiang to favor Russians and Russian influence Sinkiang apparently is very great. Governor of Sinkiang permits no foreign or Chinese visitors with exception of Chen, Kansu Commissioner, Reconstruction Bureau, who visits Sinkiang often, and who negotiated Sino-Russian barter agreement. Chen urging Chinese government to build railroad Russia to Lanchow and possibly Czechuan and Paochi terminus Lunghai Railroad, distance Russian railroad to Paochi, two thousand seventy miles. Chen suggests China supply labor, Russia material, and the U. S. A. equipment on credit to Russia. Mine concessions possible. Commissioner Foreign Affairs also desires American investment Northwest China to advance influences and states Russians are not in position to oppose. I have been warmly welcomed and was only foreigner present and on platform at Sun Yat Sen's memorial ceremony on November 12. Am favorably impressed with new Kansu officials all from the south. Central government's control silver and gold collection and prices evident here.

Handwritten: 21
Handwritten: 97

**FEDERAL RESERVE BANK
OF NEW YORK**

December 23, 1938.

Dear Mr. Secretary:

Corporate security flotations this week totaled \$41,900,000, of which about \$4,700,000 was for new capital. A \$10,168,000 additional issue of Consumers Power Company first mortgage $3\frac{1}{4}\%$ of 1966 was offered this morning at 104 $\frac{1}{2}$, to yield about 3.01 per cent. The same company offered first mortgage $3\frac{1}{2}\%$ of 1967 last January to yield about 3.39 per cent. \$16,000,000 of Railway Express Agency serial notes of 1939-48 to yield $3\frac{3}{8}$ to $2\frac{1}{2}$ per cent was sold yesterday. Two issues of preferred stock - for Beneficial Industrial Loan Corporation and Pennsylvania Power Company - totaled \$11,700,000. All four of the above issues met with a good reception and apparently have been entirely sold. A \$4,000,000 private sale by a manufacturing company was also reported.

Comparatively large amounts of the recent \$30,000,000 Chesapeake and Ohio and \$48,000,000 Central Illinois Public Service Company issues are reported to be still in the hands of underwriters. Including these two issues, the total of undigested securities on dealers' shelves appears to be greater now than at any time since the autumn of 1937, when most of the \$48,000,000 Bethlehem Steel Debenture and \$44,000,000 Pure Oil preferred stock issues fell back on the underwriters. The Chesapeake and Ohio issue is of Aa grade, however, and \$38,000,000 of the Central Illinois financing is rated A by Moody's, and during the next few weeks, when almost no new offerings are scheduled, and when there is normally a considerable augmentation of funds seeking investment, it should be possible to dispose of these bonds, with or without some concessions from the syndicate prices. The largest issue now in process of registration for public offering is \$4,500,000 Central Maine Power Company bonds, which may reach the market the second week in January. Aside from that, there are no corporate flotations in sight for January.

During the past week, municipal bond awards amounted to about \$20,000,000, and the \$50,000,000 Federal National Mortgage Association $1\frac{5}{8}\%$ per cent 5-year notes were heavily oversubscribed.

According to preliminary figures, corporate issues in December totaled about \$205,000,000, of which about \$40,000,000 was for new capital and \$165,000,000 for refunding. These figures approximate the averages for the final quarter of the year, when new capital averaged \$43,000,000 a month and refunding issues \$188,000,000. The accompanying chart shows these averages by quarters for the last three years. Refunding increased in each successive quarter of 1938, but new capital in the last quarter was lower than at any time since the first quarter of 1936, with the exception of the January-March, 1938 period.

During 1938, issues for 10 companies account for over half of the new capital raised through the new security market. They might have appeared in one quarter just as well as in another, as the market has been quite receptive to attractive offerings at least since the second quarter. Consequently, it seems incorrect to attach much importance to the changes during the last three quarters.

12/23/38

Corporate new capital issues in 1938 (using preliminary figures for December) amount to about \$780,000,000 as against \$1,116,000,000 in 1937, and \$907,000,000 in 1936. The following table gives as nearly comparable figures as are available for the years 1929, 1934-38, classifying as refunding all issues whose proceeds did not finance new plant, equipment, inventories, and other direct income-creating expenditures:

Domestic Corporate Security Issues
(000,000 omitted)

	<u>New Capital</u>	<u>Refunding</u>	<u>Total</u>
1929	\$2,001.6	\$7,375.0 (mainly investment trusts, holding cos., etc.)	\$9,376.6
1934	178.3	311.6	489.9
1935	403.6	1,863.9	2,267.5
1936	906.8	3,672.2	4,579.0
1937	1,116.3	1,276.7	2,393.0
1938 (preliminary)	782.0	1,271.3	2,053.3

The steel and oil industries were the chief borrowers of new capital in 1938, with the chemical and public utility industries also taking substantial but smaller amounts.

Despite the two issues on underwriters' hands at the moment, the reason for the current slump in borrowing is not deemed to be any difficulty in the machinery for distributing securities. At the moment, businesses with an outlook for earnings, sufficient to command investor confidence, do not seem to be able to put more capital to profitable use. It is significant, in this connection, that well over 90 per cent of the new capital borrowed during the year was in the form of bonds and less than 10 per cent in the form of common stock.

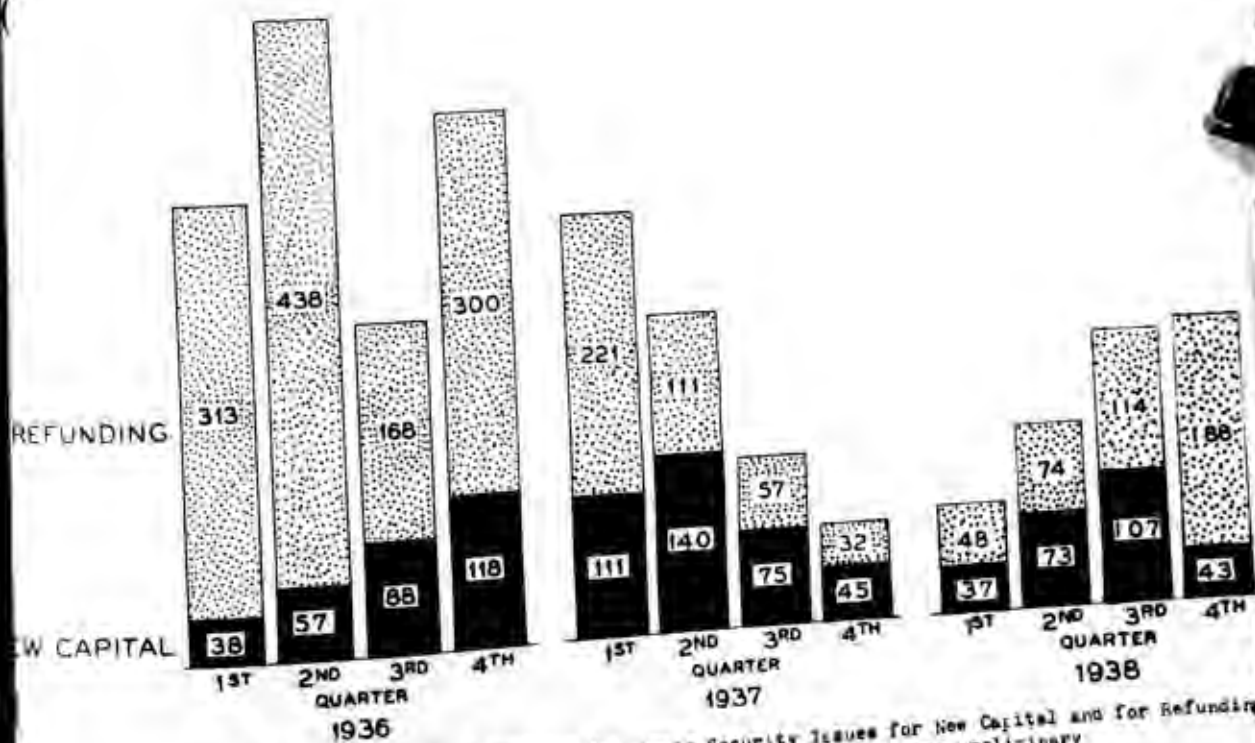
Yours faithfully,



Alan Sprout,
First Vice President.

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

Enc.



Average Monthly Volume of Domestic Corporate Security Issues for New Capital and for Refunding
 In millions of dollars. December, 1938 figures are preliminary
 (Source: Federal Reserve Bank of New York)

ADDRESS THE COMMANDANT, U. S. COAST GUARD
AND REFER TO HIM

HEADQUARTERS

TREASURY DEPARTMENT

UNITED STATES COAST GUARD

WASHINGTON

December 23, 1935

From: Mr. Campbell, Hongkong, China.
To : Secretary of the Treasury.

Message from Professor Buck.

General Wu, former head peace preservation corps of thirty
hailens South Kansu and who declared Kansu in favor Central Government
at time Sian coup, says Japanese can easily cut communications west
of Lanchow to approach through South Mongolia. He was told by member
Kansu government that Russia asking for control of Kansu by Eighth
Route Army in return for one thousand planes. He thinks Chiang Kai
Shank will not accept unless hard pressed by Japanese. He states China
must either lose country or become sovietized and believes latter
course will be chosen. Contrary to Chen, he states Sinkiang is being
sovietized. He and chief inspector police state Eighth Route Army
branch office Lanchow is permitted secretly to spread soviet propa-
ganda in Kansu and secret agents are at work in every hailen. He says
Kuomintang strongly organized here to combat such propaganda.



DEPARTMENT OF STATE
WASHINGTON

In reply refer to
RA

December 23 1938

STRICTLY CONFIDENTIAL

My dear Mr. Secretary:

For your information, the following strictly confidential telegram dated December 20, 1938, has been received from the Embassy at Rio de Janeiro:

"In compliance with the Department's instruction no. 251, December 10, I discussed the matter of exchange treatment of United States commerce at length with Aranha and later presented to him the note supplied by the Department concerning this matter. Instead of commenting on the note itself, he at first mentioned Secretary Morgenthau's letter to Souza Costa transmitted in the Department's telegram no. 145 of December 18, 7 p.m., and indicated, with disappointment, that he felt it did not demonstrate a willingness on the part of our Government to cooperate to the extent of extending credits to solve the exchange problem as suggested in Souza Costa's letter. I informed Aranha that I believed Secretary Morgenthau's letter provided a definite opportunity for Souza Costa to lay before him a concrete program both as regards exchange and the other matters dealt with, but I urged Aranha to treat the exchange question as an immediate problem and not to permit it to become involved in other matters dealt with in the exchange of correspondence between Mr. Morgenthau and Souza Costa.

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury,

Washington, D. C.

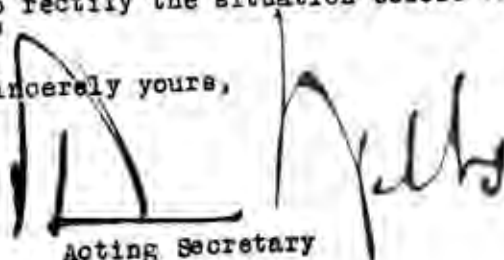
-2-

Costa. After some discussion, he consented to do this and said that with a view to making concrete suggestions as to a method of improving the exchange situation, he will discuss the note with the President this afternoon."

A further strictly confidential telegram dated December 22, 1938, from the Embassy at Rio de Janeiro states:

"I have been informed by Aranha that he has discussed the question of exchange treatment with the President and with the Minister of Finance, and that the latter requested 48 hours to study the matter. Aranha assured me, however, that steps would be taken to rectify the situation before the end of the year."

Sincerely yours,



Acting Secretary

PARAPHRASE OF TELEGRAM RECEIVED

FROM: American Embassy, Rio de Janeiro

DATE: December 23, noon, 1938

NO.: 297

Reference my 293 of December 17, 11 a.m.

I am informed by the Director of Exchange that the Bank of Brazil will close exchange for maturities and daily quotas from November 15 to November 23 inclusive, during the week of December 26.

Will you inform the Department of Commerce please.

SCOTTEN

EA:DJW

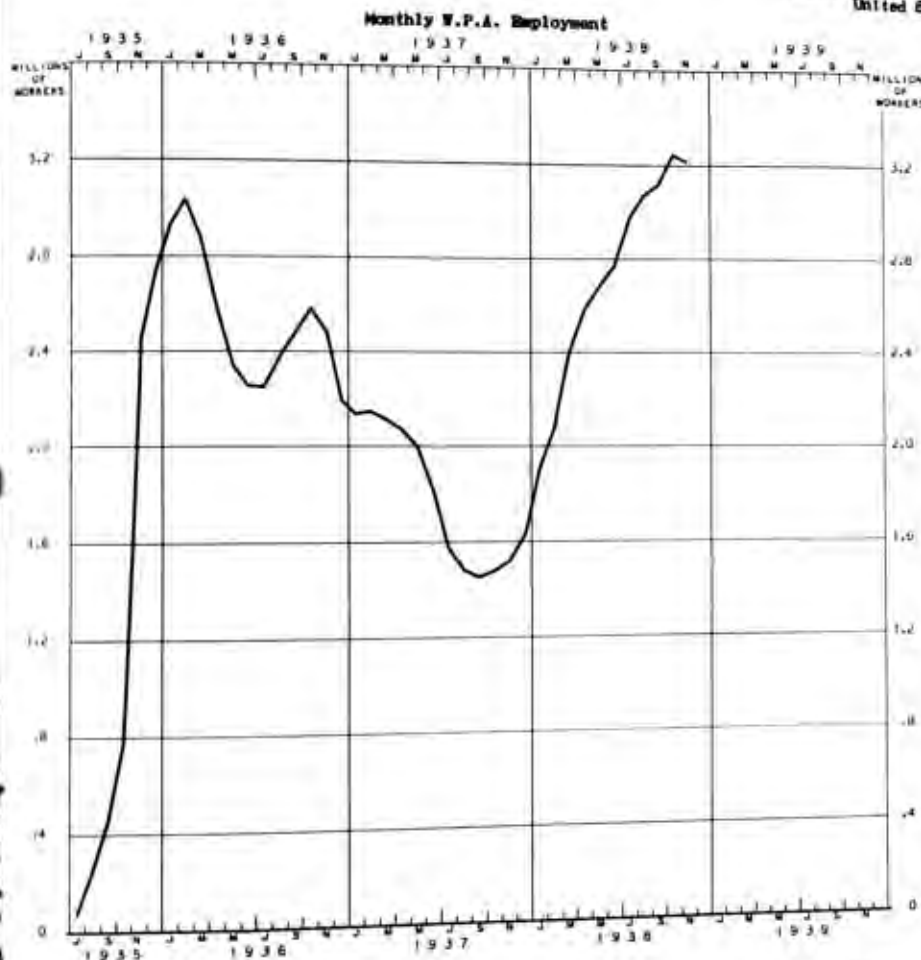
December 23, 1938

To: The Secretary
From: Miss Lonigan *el*

The total number of WPA workers
on December 17, 1938 is 3,083,249.

BA
The decrease during the week from
December 10 to December 17 was 55,796
workers. However, WPA employment is
still higher in December of 1938 than
in December of any previous year.

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed
United States



SOURCE: WORKS PROGRESS ADMINISTRATION

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Weekly
United States

306

Week ending 1938	Number of Workers (In thousands)
March 5	2,167
March 12	2,244
March 19	2,357
March 26	2,395
April 2	2,445
April 9	2,504
April 16	2,531
April 23	2,544
April 30	2,582
May 7	2,607
May 14	2,626
May 21	2,650
May 28	2,678
June 4	2,693
June 11	2,712
June 18	2,736
June 25	2,767
July 2	2,807
July 9	2,853
July 16	2,899
July 23	2,938
July 30	2,967
August 6	2,993
August 13	3,017
August 20	3,039
August 27	3,067
September 3	3,086
September 10	3,102
September 17	3,114
September 24	3,120
October 1	3,129
October 8	3,137
October 15	3,167
October 22	3,201
October 29	3,245
November 5	3,263
November 12	3,258
November 19	3,244
November 26	3,216
December 3	3,185
December 10	3,139
December 17	3,083 a/

Source: Works Progress Administration
a/ Confidential

WORKS PROGRESS ADMINISTRATION
Number of Workers Employed - Monthly
United States

307

	Number of Workers (In thousands)
1936	
January	2,926
February	3,036
March	2,872
April	2,570
May	2,340
June	2,256
July	2,249
August	2,377
September	2,482
October	2,581
November	2,483
December	2,192
1937	
January	2,138
February	2,146
March	2,115
April	2,070
May	1,999
June	1,821
July	1,569
August	1,480
September	1,451
October	1,476
November	1,520
December	1,629
1938	
January	1,901
February	2,075
March	2,395
April	2,582
May	2,678
June	2,767
July	2,967
August	3,067
September	3,120
October	3,245
November	3,216 a/

Source: Works Progress Administration
a/ Confidential
Monthly figures are weekly figures for the
latest week of the month.
They include certified and non-certified
workers.